Agri Commodity Markets Research

July 2019: Summer arrives in US, corn bulls overheat

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After months of rain and cold, US midwest summer in July brought welcome reprieve to corn, soy and wheat fields and restored river transport. The benign weather pattern tamed the bull in G&O, however major risks remain for poorly conditioned US summer crops, while forward weather in Central America, Indonesia and Australia still looks on the dry side. Amid a relatively tight corn balance sheet and with geopolitics still at play we can expect some volatility over the coming months. On the softs side, a rather strong Brazilian real will likely provide support.

WHEAT

CBOT Wheat forecast slightly lowered despite production cuts

- Global wheat production revised down, on hot and dry weather in Europe, the Black Sea and Australia.
- Corn volatility to translate to wheat.

SUGAR

ICE #11 Sugar to trade in a range, but likely going to recover some ground

- Large Thai delivery resulted in downward pressure, but surprisingly did not depress the white premium.
- A strong Brazilian real is likely to support sugar prices ahead.

CORN

CBOT Corn's engine overheated in July, as US Midwest weather returned to normal and crop conditions improved

- A competitive global corn export market, replenished global grain supplies, US 2018/19 carry-in at a 31-year high.
- Funds bought back 450,000 lots in nine weeks and were burnt twice Any extension of the net long position will require a significant weather downgrade.

COFFEE

Arabica to be supported by a strong BRL

- Higher demand for certified stocks to support futures prices.
- Frost in early July only had limited damage, of ~1% to 3% of 2020/21 arabica potential.
- Adverse weather ahead for Central American and Ethiopian crops.

SOYBEANS

CBOT Soybeans eased last month

- The China-US rumor mill continues to spin, but a deal remains elusive.
- US farmer support payments – and potential US production cuts in 2019 – help limit CBOT downside.

SOYMEAL & OIL

CBOT Soymeal fell on improvements in US weather, and weak export and feed demand

- Falling domestic feed demand and South American competition are weighing on US soymeal
- CBOT Soy Oil, conversely, should see supply-side upside from continued decline in US crush volumes.

PALM OIL

Seasonal production increase to result in higher palm oil inventories in Indonesia and Malaysia in 2H 2019, compared to 1H 2019

- Palm oil inventories in Indonesia remain high despite higher year-on-year disappearance.
- Malaysian palm oil production to reach 21mmt in 2019.

COTTON

Short covering and weather risks remain in the short term, followed by bearish fundamental pressure

- Improved 2019/20 supply prospects, coupled with increasing demand concerns, drove ICE #2 Cotton further into the low USc 60/lb region.
- Speculators deepened their net short position across the ICE #2, to fresh record levels as of July 16.

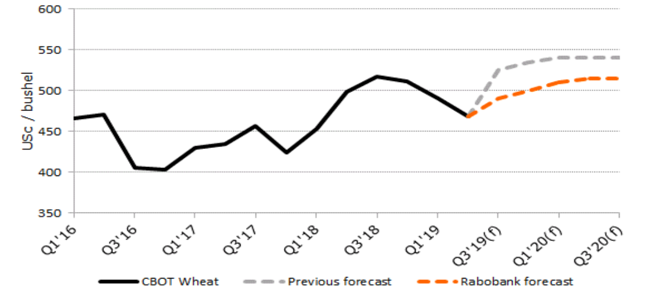
Wheat

CBOT Wheat forecast slightly lowered despite production cuts

- CBOT Wheat prices fell -9.7% this month, mainly following corn.
- Global wheat production revised down, on hot and dry weather in Europe, the Black Sea Region, and Australia.
- Corn volatility to translate to wheat.

CBOT Wheat outlook lowered, but neutral at these levels

	unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
CBOT	USc/bu	512	492	469	490	500	510	515	515
Matif	EUR/mt	202	198	182	178	181	183	181	181



Source: Bloomberg, Rabobank 2019

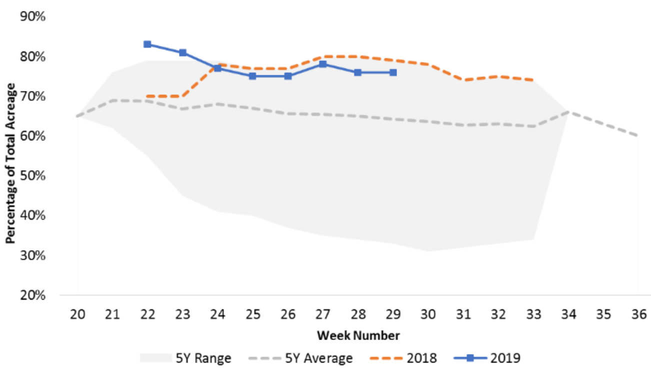
USDA 2019/20 global wheat production was reduced 9mmt, or 1.2%, from June to July. With major exporter production reduced by 10mmt amid a modest increase in production in the US, hot and dry weather across Europe, the Black Sea Region, and Australia has pushed yields down. Russia, the leading wheat exporter, has seen 2019/20 production estimates repeatedly cut since April. Despite trimmings in a few geographies, global 2019/20 production remains up by 40mmt. Global (excl. China) 2019/20 stocks-to-use is therefore also seen lower, at 22%, vs. 24% a month earlier.

The winter wheat harvest should continue to progress well throughout August, with good weather in the forecast. The winter wheat harvest is progressing well in many major exporting countries, bringing some harvest pressure on prices, as lots of wheat comes to the market throughout August. The US winter wheat harvest continues to be behind schedule, at 69% complete, compared to a five-year average of 78%. But with warm and dry weather in the forecast for the US Midwest, there should be some good opportunities to catch up. Weather in the northern plains also appears favorable to spring wheat development, with US crop ratings stable at 76% Good/Excellent as of July 23, compared to 64% on a five-year average. Europe is forecast to be hot and dry, with France likely to experience temperatures above 40°C. Currently, French soft wheat crop ratings remain higher than previous years and steady, at 73% Good/Very Good as of July 15. Russia and the Black Sea Region are forecast to be cooler than normal, with light showers, causing no issues for harvest progression. Romania and Russia continue to dominate the FOB market, suggesting there are no major issues with the supply there for the time being. However, production estimates for Russia declined slightly further in recent weeks, mainly due to lower yields in spring wheat. With the bulk of the harvest coming to market in August, they are likely to continue to dominate the FOB market for the month ahead.

The Matif Wheat/CBOT Corn ratio declined by 5.6% this month, after reaching lows not seen since June 2016, down 26% YTD. We expect EU wheat (excl. durum) production to increase by 11mmt YOY, a reversal from the situation this time last year, when European wheat was in short supply due to drought. As a result of the bumper 2019/20 EU wheat crop, EU feed demand for corn is set to fall by 6mmt, while feed demand for wheat is expected to increase by 4.5mmt.

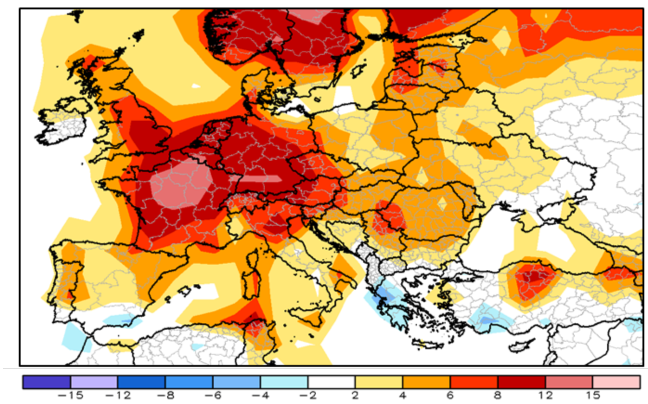
Bullish price risk may come to wheat markets from corn. For now, we do not expect the corn market to show a large rally. However, it is likely to stay volatile throughout the next months, and this volatility will be transferred onto wheat. Any rally in wheat that is not supported by higher corn prices will have limited upside.

US spring wheat ratings continue to be exceptional at 76% Good to Excellent as of July 21



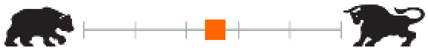
Source: USDA, Rabobank 2019

EU weather: extreme heat expected, but wheat crops should cope well at this stage. One-week anomaly forecast in °C:



Source: NOAA, Rabobank 2019

Corn



CBOT Corn's engine overheated in July, as US Midwest weather returned to normal and crop conditions improved. Uncertainty on yield justifies a supply risk premium, though high US carry-in, soft global demand, and large global supplies should prevent a CBOT Corn breakout to USD 5/bu

- A competitive global corn export market, replenished global grain supplies, and protracted feed slowdown have all left US 2018/19 carry-in at a 31-year high. These factors will mitigate the 2019/20 US stock cut.
- Funds bought back 450,000 lots in nine weeks and were burnt twice (short before weather market, long before acreage change). Any extension of the net long position will require a significant weather downgrade.

US Corn emerged last month cold, wet, and vulnerable. From 20,000 feet, the US Corn Belt landscape appears visibly pockmarked, particularly to the east and north, reflecting patchwork, frenzied planting by farmers taking advantage of surging CBOT prices. Rabobank maintains its view of 7.4m corn acres left unplanted. Meanwhile, the planted crop has seven-year-low crop ratings of 56% Good/Excellent and faces significant yield risk from a rain-delayed season, 'degree day' deficits, lack of inputs, weak stands, and frost risk before harvest. The USDA will likely revise 2019/20 acreage and carry-out estimates downwards in August, after having resurveyed the Midwest, with 2019/20 YOY stocks-to-use declining sharply, from 16.4% towards a six-year low of 10%.

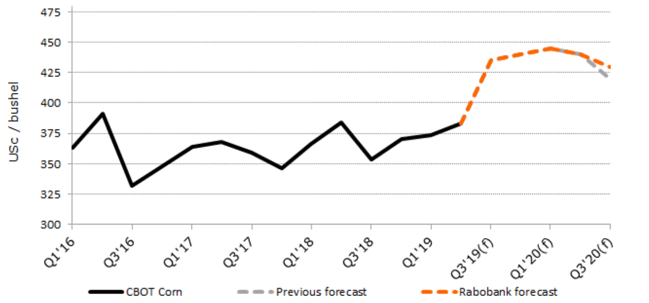
Supply-fueled concerns for US Corn reached a fever pitch in June, with CBOT touching its highest level in five years, behind speculative short-covering/length of 450,000 lots (or almost half the annual seaborne volume of corn). In the last month, though, a widely derided USDA acreage report combined with the arrival of more typical (hot, humid) summer weather that accelerated development – excl. the 2018 anomaly, the national crop is 'only' ten days behind the 2012-2017 average – to knock some wind out of CBOT's sails, with prices down 6% from their peak. Without further deterioration in weather or a US-China trade resolution, it will be difficult for Non-Commercials to reengage further on the long side.

The greatest obstacles to further near-term CBOT Corn breakouts are the US 2019/20 carry-in (31-year high of 2.3bn bu) and world exporter grain supplies (+90mmt YOY), particularly in South America. Brazil and Argentina corn production likely surpassed 100mmt and 50mmt, respectively, for the first time – and farmers are aggressively marketing their crop to the world, spurred on by a record harvest, weak currency, and high CBOT prices. Brazil has seen back-to-back record monthly corn exports, and that trend could continue through year-end. Meanwhile, US corn is priced out of the world market, and commitments are running about 9% behind pace. Aside from exports, there's scope for the USDA to cut US domestic use further amid high corn basis, abundant wheat supplies, low ethanol margins, and muted feed demand.

The US corn crop continues to face an uphill battle to improve, but the recent improvements in weather and feed grain abundance provide some margin for supply. Substantial risks ahead remain to justify a weather premium in CBOT Corn, but unless the weather worsens, expect corn to remain range-bound at the mid-USD 4/bu level.

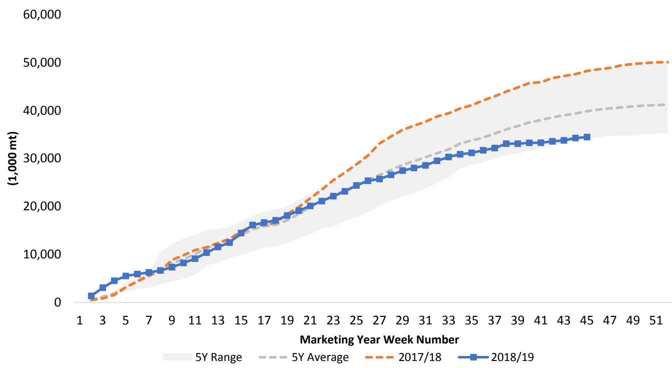
US Corn is highly vulnerable to weather risks, otherwise ample global supplies will keep CBOT from further breakouts

	Unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
CBOT	USc/bu	370	373	383	435	440	445	440	430



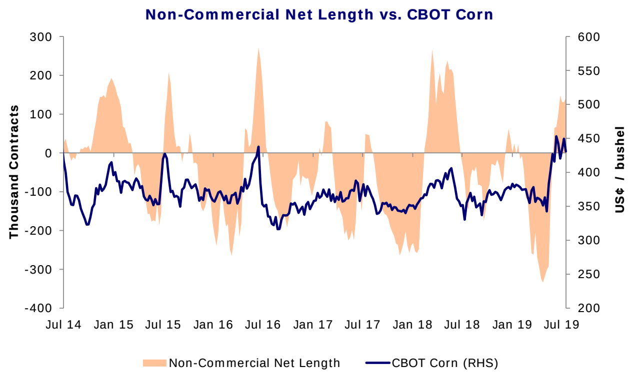
Source: Bloomberg, Rabobank 2019

High US corn prices have caused export sales to lag behind USDA's target, raising likelihood of higher stocks in 2018/19



Source: USDA, Rabobank 2019

Non-Commercials' record purchase program has stalled and will require additional catalysts to regain momentum



Source: CFTC, Bloomberg, Rabobank 2019

Soybeans

CBOT Soybeans eased last month, in solidarity with corn. There are increasing supply risks for US soy, but these remain secondary to the multi-year supply burden and trade war/ASF-hit demand. US supply risks, MSP, and China purchase hopes will keep sellers sidelined, but prices are expected to stay range-bound near USD 9/bu

- The China-US rumor mill continues to spin, but a deal remains elusive. Meanwhile, ASF is cutting Chinese 2018/19 soybean imports to three-year lows.
- As China aims to source its ASF-lowered soybean requirements almost exclusively from South America, farmers are scaling back sales. Meanwhile, US farmer support payments – and potential US production cuts in 2019 – also help limit CBOT Soybean downside.

CBOT Soybean YTD gains of 1% – and the 13% move off 11-year lows of USD 8/bu seen two months ago – come largely thanks to spill-off from the weather risk premium in US corn and widespread G&O Non-Commercial buybacks of 750,000 lots. Last month, the US Midwest weather pattern shifted, from saturated and cool to humid and warm conditions, which aided summer crop development and eased CBOT Soybean prices 3% last month. US soy record 2018/19 stocks (1.1bn bu, 2.6x the previous record), trade war-reduced export demand, and ASF-slowed global feed demand growth present bearish fundamentals for CBOT Soybeans.

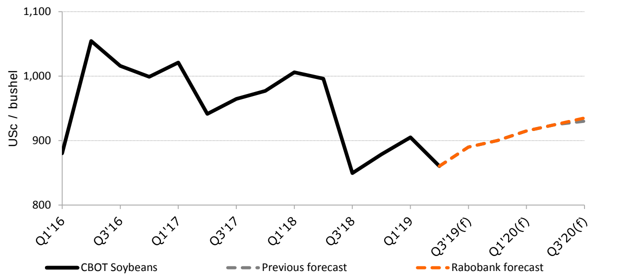
US production concerns are still relatively minor, but have been growing due to the challenging planting season and the poorest Good-Excellent conditions (54, -16 points YOY) since 2012. The USDA's June US planting survey, wide of the mark on corn, is far closer to reality on soybeans (80m acres, vs. Rabobank's 82m-acre projection, down from 89.2m acres last year). In 2019/20, lower US yields (a likely outcome, given current crop conditions) will combine with lower acreage to cut production by 10% to 15%, lowering 2019/20 US ending stocks below 1bn bu, and bringing stocks-to-use from 26% closer to 20%. Meanwhile, the economics (soy-corn ratio of 2.25) support further acreage shifts and supply-side cuts in soy in 2020/21. In short, absent a US-China trade deal or severe weather issues, the US will undergo gradual supply-side rebalancing over the coming two years – which encourages us to maintain our gradual price increases to USD 9.35/bu in 2020.

The smaller 2019 US crop is but a step in a multi-year drawdown project. In the interim, CBOT's attention is on adverse global demand dynamics and market positioning. South America's record soybean production and exports are expected to be +10% YOY, reflecting fierce export competition to ASF-weakened global demand. Amid recent strength in the BRL and ARS, along with relatively stronger offers for their nascent corn harvests, Rabobank expects the record pace of South American farmer soybean sales to slow in the coming months. In the US, meanwhile, crop uncertainty and the Market Facilitation Payment will also limit farmer selling, and offset weak US crush (in decline for three consecutive months) and weak US export demand.

Rabobank expects China to import at best 84mmt soy in 2018/19 (-8mmt YOY) and take until 2021 to return to pre-ASF levels. China's ASF epidemic has left a 10mmt animal protein deficit, and – together with similar issues in Vietnam – is widely anticipated to drive higher animal protein imports and prices. The silver lining for US soybean demand lies in China's animal protein imports, which have begun to rise to address the domestic deficit. The US has a large pork surplus that China could use to close the gap; however, the trade war and associated tariffs have limited procurement to date. In case Chinese procurement of US pork and soybeans occurs in earnest later this year, it would shake US domestic soybean demand and CBOT prices from their lethargy.

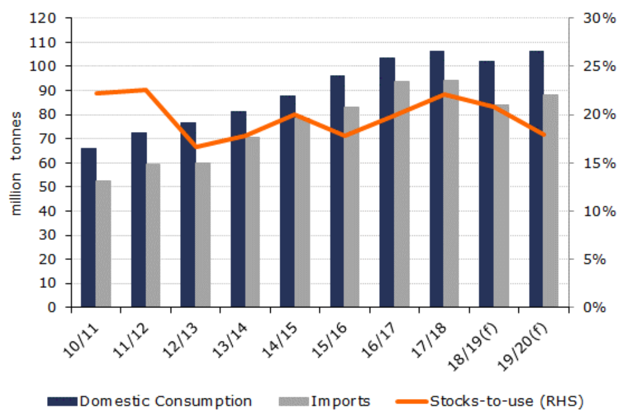
US Corn production issues provide knock-on support for CBOT Soybeans, though stocks, low demand restrain upside

	Unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
Soybeans	USc/bu	879	905	860	890	900	915	925	935



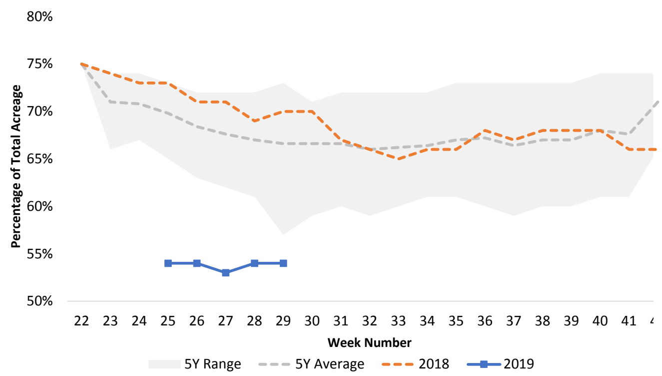
Source: Bloomberg, Rabobank 2019

China's imports will be at 3-year lows in 2018/19 allowing it to source mainly from South America and to eschew the US



Source: USDA, Rabobank 2019

US soybeans Good-Excellent ratings are at seven year lows; supply risks have raised export prices above competition



Source: USDA, Rabobank 2019

Soymeal and Soy Oil

CBOT Soymeal fell 4% last month, on improvements in US weather, and weak export and feed demand. Heavy cuts to NOPA crush and lower soy oil supplies led to more moderate losses of 1% on CBOT Soy Oil

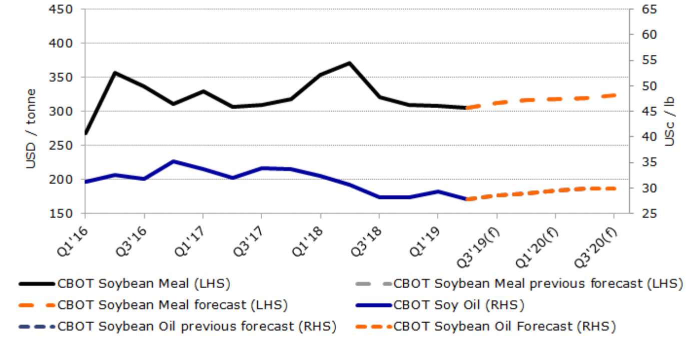
- Falling domestic feed demand and South American competition are weighing on US soymeal; US soy crop concerns have further pushed US crush margins down to their lowest levels of 2019.
- China is expected to import more meat to address its animal protein deficit, and a major question for CBOT Soymeal will be if China will buy from the US. CBOT Soy Oil, conversely, should see supply-side upside from continued decline in US crush volumes.

US crush margins last month touched 2019 lows of USD 5/mt, a 70% decline from June, as US soybeans enjoyed a weather premium that contrasted strongly with weakening soymeal demand fundamentals in exports and domestic feed. In the past three months, NOPA crush has shown consecutive declines; the June print of 148.84bu was the lowest since September 2017. Even so, the cuts in soymeal production have not been sufficient to offset demand weakness, and soymeal fell 4% MOM, the most of the complex. On the export front, US meal is showing a USD 20/mt-USD 30/mt premium to replenished South America (soy production +10% YOY), and US export commitments are running 10% behind pace to achieve the USDA's target of 13.9m short tons in 2018/19. Meanwhile, the USDA cut domestic feed 150,000 short tons in its July WASDE, on the back of oversupplied CBOT Lean Hogs' 25% decline from early April and contrasting higher, weather-driven feed costs that squeezed hog producer margins. That trend reversed considerably this month with the hotter Midwest weather and warming US-China relations, raising the possibility that US feed demand will rise, but exports will remain under pressure by the US weather premium. For CBOT Soymeal, much will depend on China's decisions to plug its +10mmt animal protein deficit, with imports from Europe, South America, or the US. Rabobank sees prices in the low-USD 300s if trade wars and tariffs continue.

Lower US crush has pushed soy oil supplies to 2019 lows, offsetting biodiesel and export demand weakness. CBOT Soy Oil fell 1% MOM, but remains the best soy complex performer, up 2% YTD. FOB Midwest Biodiesel's discount to on-highway diesel declined in June, leading the USDA to cut 2018/19 US biodiesel demand by 2%. Compounding the emerging weakness in domestic demand, US soy oil is relatively expensive compared to South American, trading at a hefty, USD 135/mt premium to palm oil. Export commitments are running -9% behind pace to reach the USDA's 2018/19 target, raising the possibility of further cuts. Still, the lower crush output and US weather premium will be positive catalysts for soy oil going ahead, and Rabobank's forecast is maintained, with expectations for CBOT Soy Oil to reach USc 30/lb by 2020 – with potential downside risk coming from a possible animal protein export demand-driven CBOT Soymeal rally that would result in strong crush and excess soy oil.

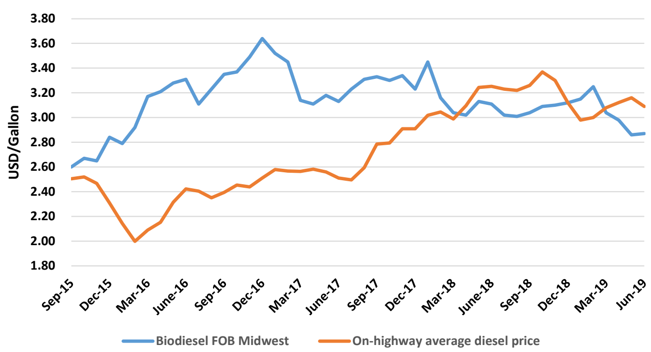
CBOT Soymeal, Soy Oil face demand concerns that could keep prices somewhat range-bound

	unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
Soymeal	USD/mt	309	309	305	312	316	318	320	324
Soy Oil	USc/lb	28.3	29.4	27.8	28.5	29	29.5	30	30



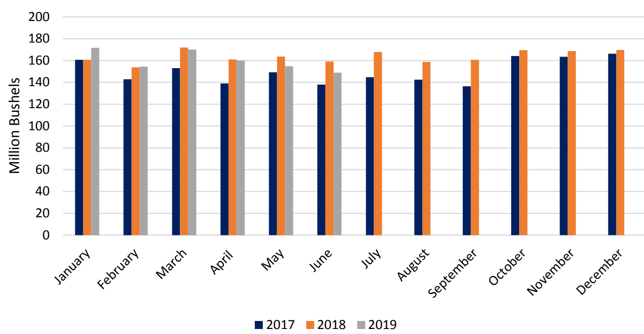
Source: Bloomberg, Rabobank 2019

US on-highway diesel's premium to biodiesel narrowed last month which could curb domestic biodiesel/soy oil demand



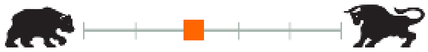
Source: USDA, ERS, DOE, Rabobank 2019

US NOPA crush slowdown continued for a 3rd month, in line with declining crush margins, raising demand concerns



Source: NOPA, Rabobank 2019

Palm Oil



Seasonal production increase to result in higher palm oil inventories in Indonesia and Malaysia in 2H 2019, compared to 1H 2019

- Palm oil inventories in Indonesia remain high despite higher year-on-year disappearance.
- Malaysian palm oil production to reach 21mmt in 2019.
- Indian palm oil import demand is expected to remain healthy throughout Q3 2019.

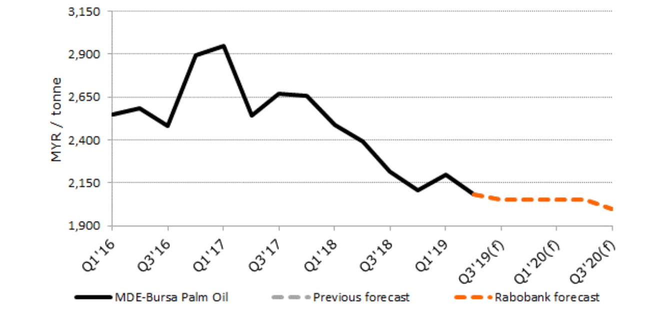
Palm oil inventories in Indonesia remain high despite higher year-on-year disappearance. The implementation of the B20 mandate in Indonesia and a favorable palm oil/gas oil spread – for discretionary palm oil-based biodiesel blending – helped to increase demand for Indonesian palm oil in the first five months of 2019. According to GAPKI, total Indonesian palm oil exports and domestic consumption increased by 23%, or 4mmt YOY, to 21.7mmt in the first five months of 2019. Despite this significant increase, Indonesian palm oil production during the same period also increased by 19%, or 3.5mmt YOY, to 21.9mmt. Consequently, at 3.5mmt, Indonesian palm oil inventories in May 2019 were up 17%, compared to January 2019.

Malaysian palm oil production to reach 21mmt in 2019. According to the MPOB, Malaysian palm oil production decreased by -9% MOM in June 2019, to 1.5mmt. This production decrease, however, is within expectations, due to fewer harvesting and milling activities during Eid al-Fitr celebrations in June 2019. Despite this decrease, Malaysian palm oil production in 1H 2019 grew by 10% YOY, to 9.8mmt. Moving forward and assuming a normal weather situation, we expect Malaysian monthly palm oil production to increase from July 2019 towards the end of Q3 2019/beginning of Q4 2019, on the back of the resumption of normal plantation activities and seasonal production increases. Due to this, we have revised our forecast for Malaysian palm oil production in 2019 upwards, from 19.9mmt previously to 21mmt.

Indian palm oil import demand is expected to remain healthy throughout Q3 2019. As of early July 2019, Indian edible oil inventories at port and in the pipeline decreased by 2% MOM, to reach 2.2mmt. This decrease occurred on the back of healthy domestic edible oil demand and lower month-on-month Indian edible oil imports in June 2019. During this period, Indian edible oil imports decreased by 9% MOM, to reach 1.1mmt. We expect Indian palm oil imports to pick up in Q3 2019, due to edible oil inventory restocking activities and preparation for Diwali's seasonal edible oil demand increase. Meanwhile, Indian Q4 2019 edible oil imports could still be affected by Indian 2019/20 soybean production, of which the outlook remains uncertain. Due to the delayed monsoon, 2019/20 soybean sowing activities in India lagged, compared to last year. According to the provisional statistics from the Indian Ministry of Agriculture & Farmers' Welfare, sowing of soybeans in India only reached 5.2m hectares as of July 12, down from 6.4m hectares during the same period last year.

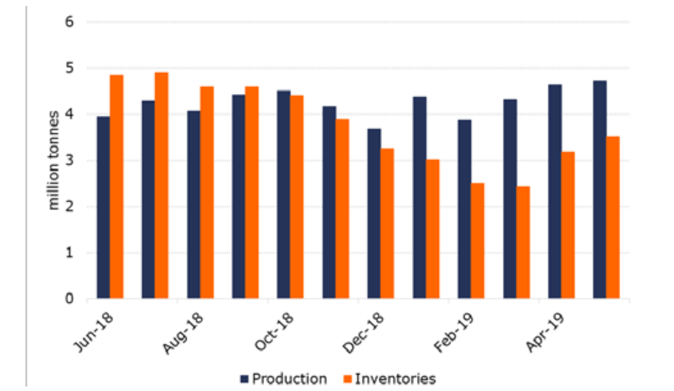
Palm Oil price forecast is maintained as per last month

	Unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
Palm Oil	MYR/mt	2,108	2,200	2,085	2,050	2,050	2,050	2,050	2,000



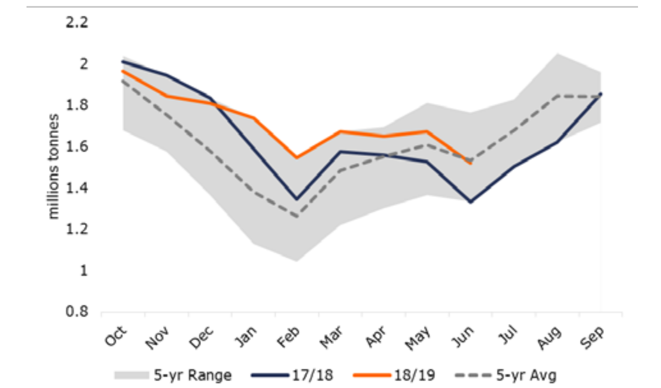
Source: Bloomberg, Rabobank 2019

Palm oil inventories in Indonesia increased in Q2 2019, after decreasing in Q1 2019



Source: GAPKI, Rabobank 2019

Malaysian palm oil production grew by 9.2% YOY in 1H 2019



Source: MPOB, Rabobank 2019

Sugar

ICE #11 Sugar to trade in a range, but likely going to recover some ground

- Range-trading likely, for now.
- A large white Thai delivery resulted in downward pressure, but surprisingly did not depress the white premium.
- A strong Brazilian real is likely to support sugar prices ahead.

ICE Sugar #11 October prices declined by 8% in the first three weeks of July. In the latest CFTC report, Non-Commercials sold an impressive 30,264 lots WOW, despite the steady appreciation of the Brazilian real during the CFTC week and most of July. The weather has been quite good, with the monsoon bringing rather good rainfall levels to India. Meanwhile, we have seen dry weather in the South of Brazil, where the harvest is progressing at full speed and there was a significant – and to some extent expected – recovery in the sugar mix. Ethanol sales have been very strong so far in 2019, and this should continue to support the ethanol parity going forward.

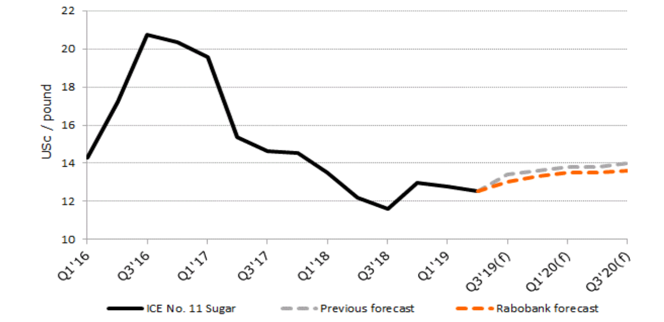
The raw and white sugar price will continue to be driven by the availability of Indian sugar for the international market. On the one hand, the Indian government will have fewer incentives to subsidize sugar exports this coming season, given that there will be no major elections in 2019/20. On the other hand, the stocks as of end September 2018 will be significantly higher than those a year ago, creating an impossible situation if left to the market alone. With this in mind, ISMA is asking for export subsidies for up to 7mmt and for the policy to be announced in July – not at the turn of the season. Any announcement could bring surprises.

A white plight. The August white contract saw the largest delivery in more than a decade, at 0.8mmt, all Thai. There was a downard market reaction to the news, as it was read as a sign that Thailand is struggling to place its sugar ahead of the next harvest and has turned to contract delivery as a last resort. There is also a risk of Thailand participating in the October delivery, so there may be more downward pressure ahead. Inexplicably, despite the large delivery of whites, the Oct/Oct white premium has strengthened since the delivery, jumping from USD 50/mt to nearly USD 60/mt, prompting a few toll refiners to restart operations – a clear sign that demand must not be too weak.

Getting out of the range is unlikely in the short term, but not impossible. The range of the first contract so far in 2019 (USc 13.4/lb to USc 11.6/lb) has been the narrowest since 2005 in the Jan-Jul period. But we have to go back all the way to 1971 to find a year when prices kept such a narrow range for the whole year. Usually, well-supplied markets – like the current situation – display low price volatility. But sugar is a volatile commodity: A surprise change in the Indian export subsidy policy (either way), or sharp movements in the Brazilian real or energy prices in Brazil will likely result in sugar regaining its usual volatility. Also, the weather in Brazil CS is likely going to be drier than usual in the coming quarter, and the same applies to the weather in Australia and Indonesia, according to IRI forecasts. With a Brazilian real strengthening, we believe there is some room for upside.

ICE #11 Sugar price forecast lowered, but still bullish

	Unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
Sugar	USc/lb	13.0	12.8	12.5	13.0	13.3	13.5	13.5	13.6

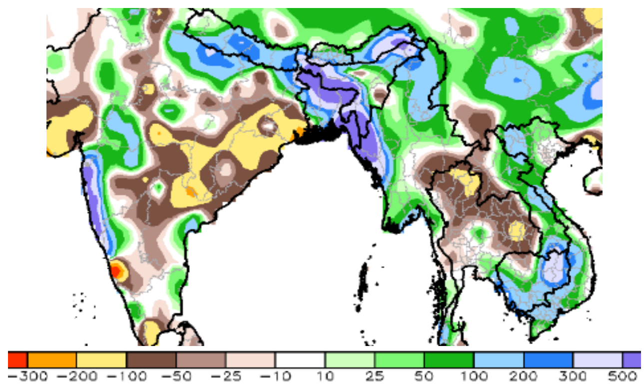


Source: Bloomberg, Rabobank 2019

Oct/Oct white premium has strengthened despite a very large Thai delivery

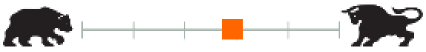
Source: Bloomberg, Rabobank 2019

Indian weather has become more normal, but rainfall still disappoints over Thailand. 30-day rainfall anomaly (mm):



Source: NOAA, Rabobank 2019

Coffee

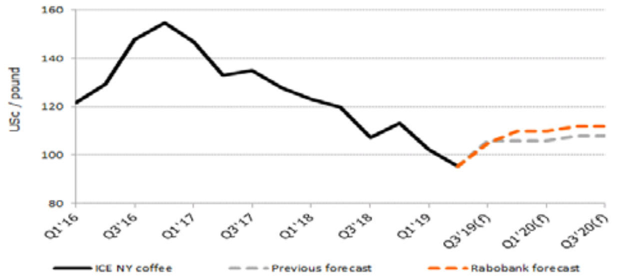


Arabica to be supported by a strong BRL

- Higher demand for certified stocks to support futures prices.
- Frost in early July only had limited damage, of ~1% to 3% of 2020/21 arabica potential.
- Adverse weather ahead for Central American and Ethiopian crops.

ICE Arabica forecast largely unchanged

	unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
ICE Arabica	USc/lb	113.1	102.8	95	**105**	**110**	**110**	**112**	**112**
ICE Robusta	USD/mt	1,627	1,534	1,402	**1,520**	**1,530**	**1,550**	**1,560**	**1,560**



Source: Bloomberg, Rabobank 2019

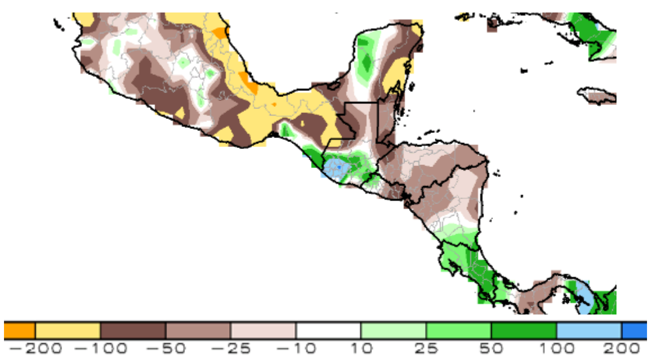
We are slightly increasing our price forecast. We see a few good reasons to be friendly to arabicas, both in unwashed and washed coffees. The BRL is now stronger, trading at 3.74 vs the USD, 3% stronger MOM. Also, we estimate that the light frost Brazil saw in early July reduced next year's arabica potential by around 1% to 3%. This should still potentially allow for a record arabica crop, together with another possible record robusta crop. But for the time being, it is too early to bet on it, and the question still stands as to whether some trees, without visible damage, could still see consequences from the frost. At the moment, we assume there are no non-visible consequences. In the more immediate term, the lower quality of the current Brazilian arabica harvest will increase the demand for ICE Arabica-certified coffees, quite likely resulting in further drawdown of stocks. We are not seeing much flow into certified stocks, given the current differentials and crop levels, except perhaps for financing reasons. But total stocks in destination countries are increasing and may continue to do so. This is in part due to the saturation of the pipeline.

We are keeping a close eye on 2019/20 mild washed crops. As anticipated in our last report, Central America has turned a little drier than usual. At the moment, it is not a major concern, but it is enough – in light of lower fertilizer usage – to make us trim some of our estimates in the area, especially considering that the forecast is for lower-than-normal rainfall going forward. We also see Ethiopia very dry. Even though the amount of freely available weather stations in Ethiopia is limited, we believe the weather maps show such a rainfall shortage that there must be an underlying issue.

Robustas to stay subdued. We maintain our view that strong robusta production in the main three key origins (Vietnam, Indonesia, and Brazil) will likely continue to put pressure on the market and keep a contango structure for most of 2019. The availability of low-quality Brazilian arabica coffee from the current harvest will also help keep a relatively wide arbitrage. For the time being, weather in Brazil's conillon areas has been good, and reservoir levels must be rather decent. The same can be said of the weather in Vietnam's main robusta areas and parts of Indonesia. Even if the weather turns drier in Indonesia, as is likely to happen, there will be significant amounts of robustas around the world to satisfy demand.

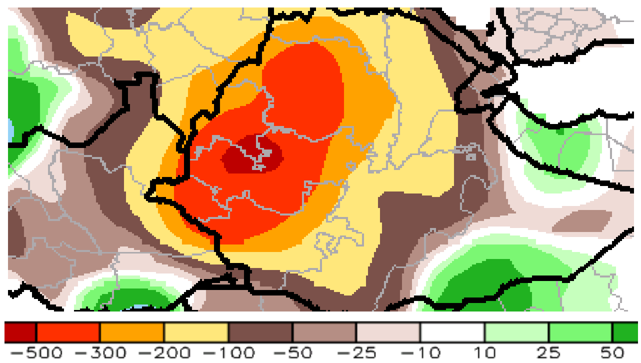
Demand could temporarily disappear. Roaster coverage with futures remains at very high levels, and pipeline stocks are large. US port stocks started to increase, going up by 0.21m bags MOM to end June, and stocks are also increasing in Europe (preliminary data). But in our view, the stock-build was due long ago, given record-high Brazilian exports in the season just finished. But for the market to return and stay below USD 1/lb, we believe funds will need to resume selling large clips. That is unlikely to happen while the BRL is strong and there is no increase in certified stocks.

Weather in Central America looks drier than normal. 30-day rainfall anomaly (mm):



Source: NOAA, Rabobank 2019

Ethiopia looks particularly dry. 90-day weather anomaly (mm):



Source: NOAA, Rabobank 2019

Cotton

Short covering and weather risks remain in the short term, followed by bearish fundamental pressure

- Improved 2019/20 supply prospects, coupled with increasing demand concerns, drove ICE #2 Cotton further into the low USc 60/lb region.
- Speculators deepened their net short position across the ICE #2, to fresh record levels as of July 16.
- 22m-23m bale US crop prospects exist, despite a slow season start, but weather risks remain as bolls open.

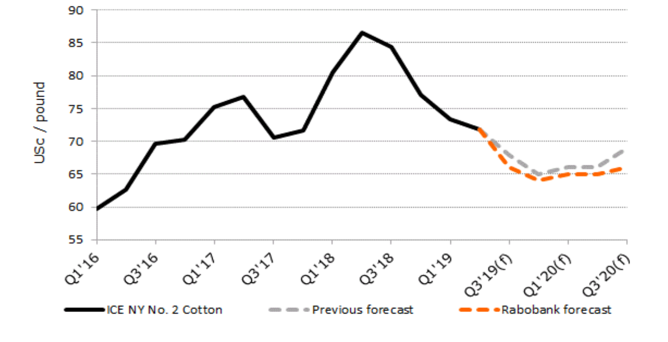
Improved 2019/20 supply prospects, coupled with increasing demand concerns, drove ICE #2 Cotton further into the low-USc 60/lb region – sailing through Rabobank's June forecast. The weakness was deeper than anticipated, on the back of two key developments: 1. diminishing US weather risks, and 2. further concerns over 2018/19 global demand prospects. The prevailing bearish sentiment undoubtedly caught the fund's attention, with Managed Money deepening their net short position to a record –44,270 lots as of July 16 – a 13,885-lot increase over the month. With such significant volume of speculative shorts – plus incoming weather and trade risks for US cotton – Rabobank maintains a risk premium in our near-term price expectations, forecasting USc 66/lb in Q3 2019. However, with a potential 22m-23m bale 2019/20 crop being picked – alongside a >12m bale Brazilian crop – Rabobank remains bearish in the medium/long term, with prices forecast at USc 64/lb in Q4 2019 and USc 65/lb in Q2 2020.

Strong US crop prospects, despite a slow, wet start to the season. Despite the rainy, cold start to the US season (plus the uneventful tropical storm Barry), crop conditions have improved rapidly over the past six weeks – now 60% rated Good to Excellent, the highest weekly rating for this time of year since 2010. This comes amid a largely drier weather pattern, along with heavy soil moisture profiles. NOAA's three-month outlook brings above-normal heat, along with more normal precipitation. With this in mind, Rabobank forecasts US 2019/20 abandonment at 10% – allowing production to reach 22m-23m bales, the largest year since 2005/06. Moreover, the scope for building domestic stocks is considerable next season. While the USDA forecasts new season stocks at 6.7m bales, this accounts for a 17m-bale export forecast – up 17% YOY and a new record if realized. Amid US-China trade tensions, this figure is very optimistic. Rabobank sees the likely revision of US exports lower, with additional supplies falling onto US ending stocks – potentially pushing new crop stocks to 7m-8m bales and weighing heavily on prices.

Declining demand prospects extend past Turkey and China, and, worryingly, into Southeast Asia. Latest USDA estimates saw Chinese 2018/19 consumption cut deeper – now down 3.7% YOY, driven by the ongoing US-China trade war. More worrying still is declining Bangladeshi use, forecast 5% lower YOY in 2018/19. It raises questions over broader Southeast Asian demand and marks the first yearly fall in Bangladeshi consumption since 2011/12. Given the bearish price environment, mills have largely adopted a hand-to-mouth mentality, with purchases being delayed until really necessary.

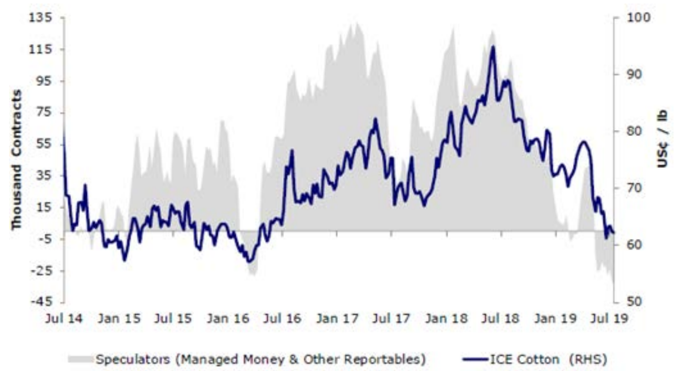
ICE #2 Cotton forecast revised marginally lower

	unit	Q4'18	Q1'19	Q2'19	Q3'19f	Q4'19f	Q1'20f	Q2'20f	Q3'20f
Cotton	USc/lb	77	73	72	66	64	65	65	66



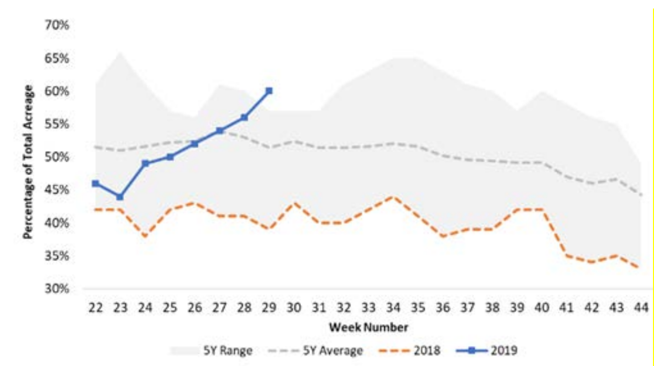
Source: Bloomberg, Rabobank 2019

Speculators (Managed Money & other reportables), as of July 17, held a record net short position across ICE #2 Cotton



Source: CFTC, Bloomberg, Rabobank 2019

US crop conditions have improved rapidly, to 60% rated Good to Excellent, despite a slow, wet start to the season.



Source: USDA, Rabobank 2019

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Methodology note: For ICE Sugar (raws and whites), ICE Arabica, ICE Robusta, and ICE Cocoa (NY and London), we aim to forecast the second rolling contracts, whereas for Palm Oil, we aim to forecast the third rolling contract. We have also used these contracts in the price diagrams. For all other contracts, we focus on the front month.

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