Rabobank

# Agri Commodity Markets Research

## May 2019: Heavy Rains, Buoyant Prices

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Excessive rainfall across the US has caused an impressive price rally of over 20% in CBOT Corn and Wheat, as funds rushed to cover short positions which were running at record net short in G&O before the rains. While corn plantings in the world's largest producer and exporter are severely delayed and will likely result in an unprecedented record number of unplanted acres, wheat markets globally are expected to see strong supplies out of the Black Sea that can cap the price rally. US soybean plantings also face delays, but prices have not risen much from their decade lows – as the US faces an export demand issue with the renewed escalation of the US-China trade war and African swine fever in China.

### WHEAT

**CBOT Wheat forecast up, on heavy rainfall across the US, but bearish off these levels.**

- CBOT Wheat has risen on the back of excessive US rainfall
- The Black Sea Region will remain key for price development

### CORN

**CBOT Corn rose to three-year highs, as a US weather supply shock took record short funds by surprise.**

- Acreage and yield impact uncertainties will drive price volatility
- Soft demand, and large South American and Black Sea supplies will limit the 2019/20 stock cut

### SOYBEANS

**CBOT Soybeans emerged from 11-year lows, on wet weather and planting concerns.**

- US-China trade deal hopes are slipping away, while ASF is wreaking havoc on animal feed demand
- Initial harvest results for Brazil indicate the crop recovered with late rains, to above 117mmm
- USDA decides to support farmers with cash payments

### PALM OIL

**Weak Malaysian ringgit to limit bearish pressure on palm oil prices.**

- Palm oil inventories in Malaysia and Indonesia remain higher year-on-ear
- Uncertainties around US-China trade war to provide volatility to palm oil prices

### SUGAR

**ICE #11 Sugar prices likely to see some support ahead.**

- Ethanol prices are lower in Brazil, due to low energy prices, but still much firmer than sugar prices.
- The weather has been price supportive in major sugar-producing countries

### COFFEE

**Limited price recovery ahead.**

- A cold front in Brazil had a disproportionate effect on prices, even though there was no damage
- Concerns mount on the 2019/20 mild washed crops.
- A potentially low arabica quality in Brazil will likely result in more demand for Peru and Honduras

### SOYMEAL & OIL

**Last month, ASF, trade wars, and South American competition briefly pushed CBOT Soy Oil and Soymeal to three and four-year lows.**

- ASF weighs on soymeal demand
- Softening demand fundamentals suggest that CBOT Soy Oil's direction will be driven from the supply-side, and depend on China's response to ASF and trade wars

### COTTON

**Prices range-bound ICE #2 futures prices are forecast to touch mid-year highs in Q2 2019.**

- The ICE #2 fell a staggering 14% through May, as both the US and China announced fresh trade tariffs
- World ex. China stocks to reach fresh records

# Wheat

**CBOT Wheat forecast up, on heavy rainfall across the US, but bearish off these levels**

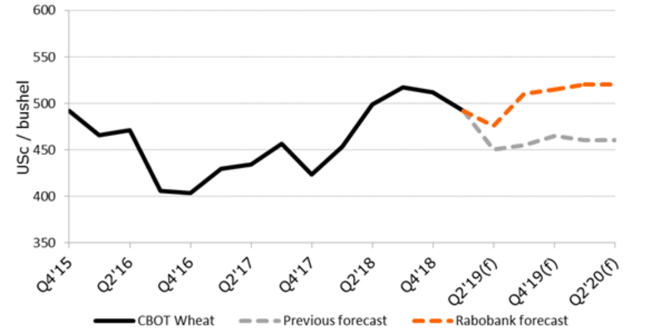
- CBOT Wheat has risen over 20% so far in May, on the back of excessive rainfall, and quality concerns across the US and Matif Wheat, followed by a 10% rise.
- The wheat rally will have shorter legs than the corn rally, as long as supplies from other producers meet demand.
- The Black Sea Region will remain key for price development. So far, expectations are high for that region, but some adverse weather risk is emerging.

**Excessive US rainfall has resulted in a +20% price increase in Chicago Wheat prices so far in May**, while Matif followed with 10% upside. Funds narrowed their sizeable CBOT net short positions. Kansas and Oklahoma received up to 400% of normal precipitation in the last 30 days, and both continue to face a higher probability of wetter and cooler weather ahead. Winter wheat protein content will likely suffer, and chances of crop infection from fungi and mycotoxins have increased. North and South Dakota also received a several times their normal rainfall, but a few dry days were enough to keep spring plantings progressing to 84%, which is just shy of the 91% on average at this point of time. The amount of US spring plantings that are prevented by the rainfall is likely going to be very small, compared to corn. As rains continue in the US this week and funds still hold large short positions in wheat – especially in KCBT Wheat – we will likely see continued price volatility. But soon the market will again shift its attention to production forecasts for other key producing regions

**The Kansas/Chicago spread has recovered a little from its sharp inverse.** The front spread went from -USc 50 in mid-May to -USc 40 towards May 29. Indeed, Kansas could be more affected by the heavy rains and flooding in a large portion of the state: quality – and possibly also yields – will be lower, pushing futures prices higher. CBOT Wheat has been impacted

**CBOT Wheat outlook bearish**

| | unit | Q3'18 | Q4'18 | Q1'19 | Q2'19(f) | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| CBOT | USc/bu | 517 | 512 | 492 | 476 | 510 | 515 | 520 | 520 |
| Matif | EUR/mt | 199 | 202 | 198 | 183 | 180 | 183 | 184 | 180 |

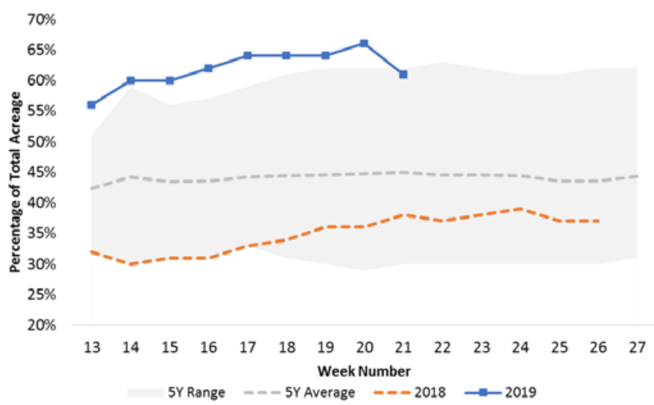



Source: Bloomberg, Rabobank 2019

by the poor Australian 2018/19 crop for months, and the outlook for the recently planted 2019/20 crop is again calling for a dryness-related subdued harvest. Australia has needed to import wheat this month, for the first time in more than a decade.

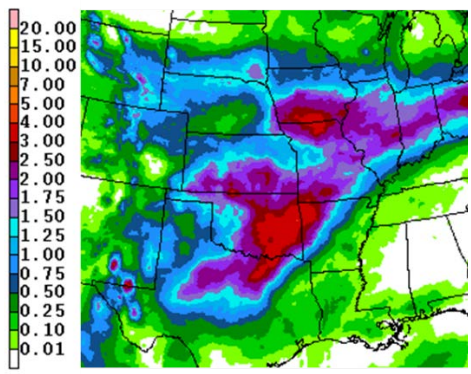
**The Black Sea will soon take center stage in pricing.** With weather woes in the US, along with poor planting and growing conditions in Australia, the wider European region is key to global supplies. The European Commission has raised its 2019/20 EU soft-wheat production estimate to 143.8mmt, from 141.3mmt last month (excl. durum). The weather has been a little drier than normal in France and parts of Germany so far this season, but rains there are forecast for next week. Production and export estimates for Russia have also continued to trend upwards, due to relatively good weather and sufficient soil moisture. The weather outlook for Russia and Ukraine needs to be monitored closely now, as hot weather has prevailed and is expected to continue for at least another two weeks. There is limited rain in the forecast for the Russian wheat belt and eastern Ukraine in the next two weeks – if rains don't return soon in this region, the wheat rally might continue. However, we still expect a strong supply out of the region that could add price pressure on CBOT and Matif wheat.

**US winter-wheat crop ratings started to come down slowly, but from very high levels**




Source: Macrobond, USDA, Rabobank 2019

**The US total precipitation forecast until June 4 across Kansas, Oklahoma, Missouri, and Iowa continues to be wet**




(rainfall in inches)

Source: NOAA, Rabobank 2019

# Corn

**CBOT Corn rose 20%, to three-year highs, as a US weather supply shock took record short funds by surprise. With rainy, cool conditions forecast in the Midwest through early June, Rabobank sees potential risk for a 1bn-bu cut to the USDA's supply projections and a CBOT melt-up, to USD 4.40/bu in 2019/20, juiced by fund short-covering. Further upside is capped by slowing domestic demand and strong export competition.**

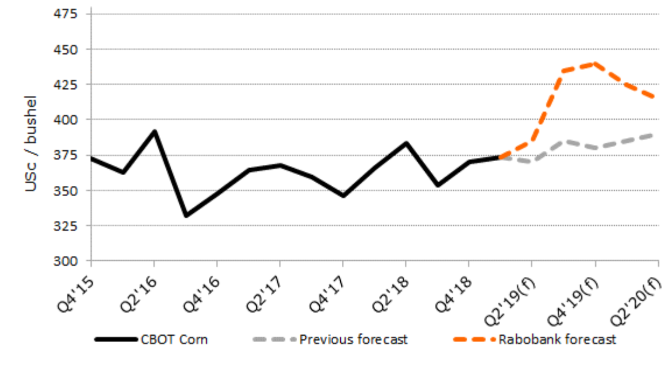
- We noted last month that the record fund short in CBOT Corn ahead of the US weather market was vulnerable to a supply shock and short-covering.
- Acreage and yield impact uncertainties will drive price volatility. Soft demand, and large South American and Black Sea supplies will limit the 2019/20 stock cut.

**CBOT Corn caught a US weather lifeline last month and climbed from contract lows to a three-year high**, above USc 430/bu. Persistent, heavy rainfall and cool temperatures over the central US have paralyzed corn plantings to their slowest pace on record: As of May 29, they were at 58%, vs. a five-year average of 89%. Notably, the worst-affected US states – Ohio 22%, Indiana 22%, South Dakota 25%, Michigan 33%, and Illinois 25%, which make up one-third of US corn acreage – had until recently been pegged by the USDA for a 1m acre YOY net increase in corn plantings. The supply-side implications for US corn – in acreage reduction and yield penalty – are severe and have firmly pushed eroding feed demand fundamentals into the rearview mirror.

**US farmers are grudgingly on the sidelines and facing tough decisions.** The CBOT soy/corn ratio is hovering above 2, the lowest in six years; absolute price and demand prospects also strongly favor planting corn, but weather won't permit it. From early May, the yield penalties for late-planted corn accelerate – and absent a sudden weather shift, we will likely see a record of at least 4m acres shifted to 'prevent planting'

**CBOT Corn price forecast pushes to USD 4.40/bu as US supply cuts outweigh high global production prospects**

| | unit | Q3'18 | Q4'18 | Q1'19 | Q2'19(f) | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| Corn | USc/bu | 353 | 370 | 374 | 385 | 435 | 440 | 425 | 415 |

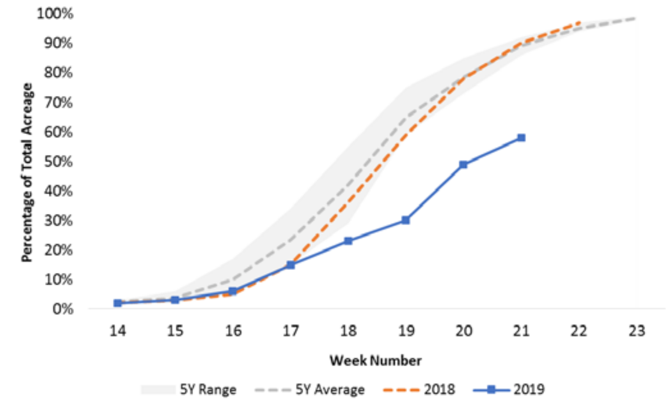



Source: Bloomberg, Rabobank 2019

(which provides an insurance payment to farmers), or to heavily subsidized and later-planted soybeans. Rabobank's US production estimate could easily fall further, but currently projects 88.5m acres of corn at 170bpa – which would result in a ~800m bu, or 5%, cut from the USDA's 2019/20 May supply estimates and, allowing for lower demand, would drive carry-out from a 30-year high to a four-year low, near 1.6bn bu.

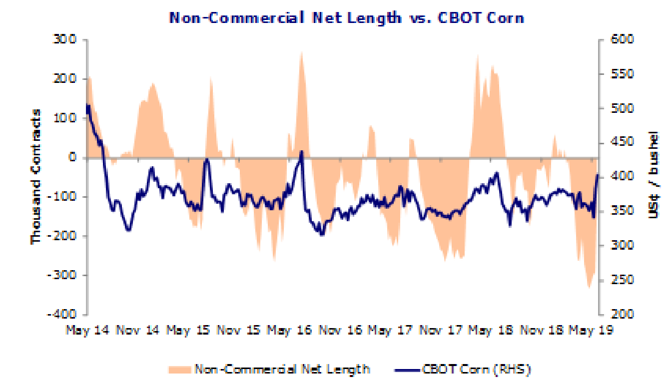
**Funds entered the US weather market with a record net short position on CBOT Corn** (near -350,000 lots), along with a two-dimensional focus on bearish trends of falling feed demand and growing export competition. Complacency with regard to emerging supply issues and commercial interest for corn (net long for the first time ever) made funds vulnerable to the recent price rise and has driven subsequent coverage (including a one-week record net purchase of 170,000 lots), in turn adding fuel to the rally. In response to the sharply lower US production outlook, Rabobank is raising its CBOT Corn price target to USD 4.40/bu in 2019 and declining into 2020, ahead of a larger planted crop. CBOT Corn price risk remains skewed to the upside, but price gains will be capped by softening (feed grain and ethanol) demand, and large South American and Black Sea supplies that, together, could absorb nearly half of US supply losses. US stocks should see a constructive fall, but remain at comfortable levels in 2019/20.

**US corn planting progress is the slowest on record, raising the prospect of sharply lower acreage and yield**




Source: Macrobond, USDA, Rabobank 2019

**Non-Commercials' record net short gave way to weather market liquidation and could reverse entirely to a net long**




Source: CFTC, Bloomberg, Rabobank 2019

# Soybeans

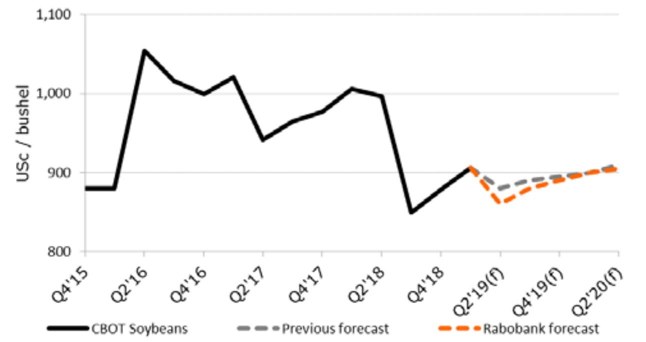
**CBOT Soybeans emerged from 11-year lows, on wet weather and planting concerns. Prices remain under pressure below US farmer cost of production, on bearish confluence of ASF-hit global feed demand and China turning to South American supplies for import needs. Rabobank sees potential for further price support from US government payments and G&O fund short-coverage.**

- US-China trade deal hopes are slipping away, while ASF is wreaking havoc on animal feed demand growth.
- Initial harvest results for Brazil indicate the crop recovered with late rains, to above 117mmt, enabling China to source its ASF-lowered soybean requirements entirely from South America and other non-US origins.
- The USDA's decision to support farmers with cash payments on 2019 production will exacerbate the supply glut, but will also limit farmer selling below cost of production.

**CBOT Soybeans enjoyed brief respite last month, on the back of slow US plantings and an extension of farmer assistance**, but longer-term prospects are as overcast as the US Midwest. In China, the historical demand engine for soybeans is grappling with the loss of 25% to 35% of pork production. A negative-demand environment (soymeal demand is projected down 4% YOY) will continue until 2020, when breeders cautiously begin rebuilding hog populations; it may take until 2021 for soybean imports to return to 2017 highs of 94mmt. Compounding the demand blow, China froze its goodwill US soybean purchases at 15mmt to 20mmt in response to the US trade war escalation and shifted procurement to Brazil, whose rain-stabilized crop of 117mmt can almost exclusively cover China's ASF-lowered 85mmt import requirement. Demand for US soymeal has been a rare bright spot for the complex, with crush margins rising 30% last month, on growing US pork sales and feeding to replace China's ASF-hit supplies. Still, the latest NOPA report showed a decline in crush, and meal demand could moderate if expectations dim for an animal protein export boost. If China takes a patriotic, rather than pragmatic route to filling its animal protein deficit, and limits its procurement of both soybeans and animal protein to outside the US, it will likely further raise prices for its consumers.

**Eroding feed-demand fundamentals and large stocks overshadowed by poor weather and lack of farmer sales**

| | Unit | Q3'18 | Q4'18 | Q1'19 | Q2'19(f) | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| Soybeans | USc/bu | 849 | 879 | 906 | 860 | 880 | 890 | 900 | 905 |

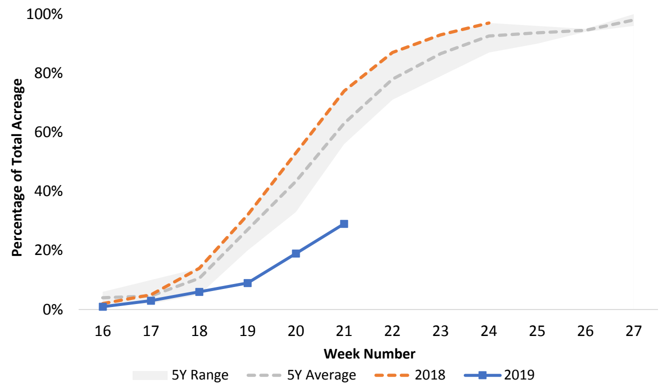



Source: Bloomberg, Rabobank 2019

**The shift south of Chinese soybean origination has once again turned the US into the cheapest origin**, but that is no panacea for demand. China historically accounts for ~55% of both world imports and US exports; even if the rest of the world bought exclusively from the US (unlikely), it would not fully replace 25mmt to 30mmt in lost annual demand from China. US export commitments are 17% behind the USDA's 2018/19 target of 1,775m bu, and we are likely to see carry-out revised higher, to 1,050m bu (+240% YOY).

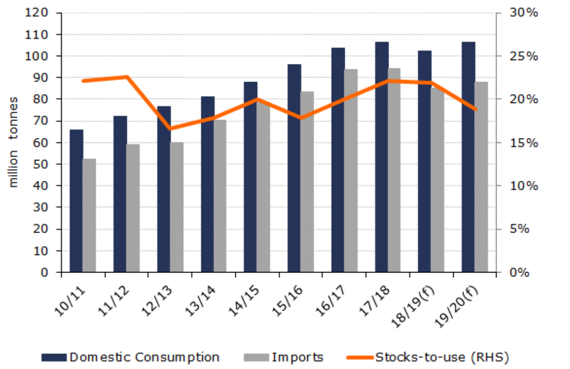
**In the short term, adverse US weather and expected supply cuts are taking the driver's seat** and led CBOT from sub-USD 8/bu levels last seen in 2008. A confluence of events will help lead to lower US soy plantings year-on-year. They include: wet, cool Midwest weather; prices below cost of production; record stocks; disillusionment about a China trade deal; and soy/corn ratio at six-year lows. Still, due the US government payments announcement last week that encourages 2019 plantings, the scale of soybean reductions will likely be lower than the 6m acres needed to keep stocks rising absent a trade deal. We expect cash flow to limit farmer selling, while weather risk will drive short-covering, but stubbornly high US stocks will keep prices in check, below USD 9.10/bu.

**US soybean plantings are well behind pace, at 29%, driving supply fears and price risk upside, with rain in the forecast**




Source: USDA, Rabobank 2019

**China, typically the engine of soybean trade, is facing a decline in import demand that will take years to fully recover**




Source: USDA, Rabobank 2019

# Soymeal and Soy Oil

**Last month, ASF, trade wars, and South American competition briefly pushed CBOT Soy Oil and Soymeal to three and four-year lows, respectively. Since mid-May however, poor US weather and promises of US support payments have supported the entire complex, though upside is capped by structural demand issues.**

- ASF weighs on soymeal demand, creating an animal-protein deficit and shifting supply to lower-intensity proteins. Still, reports that China is, to some extent, replacing US soybean purchases with pork, if confirmed over time, will support CBOT Soymeal.
- Softening demand fundamentals suggest that CBOT Soy Oil's direction will be driven from the supply-side, and depend on China's response to ASF and trade wars.

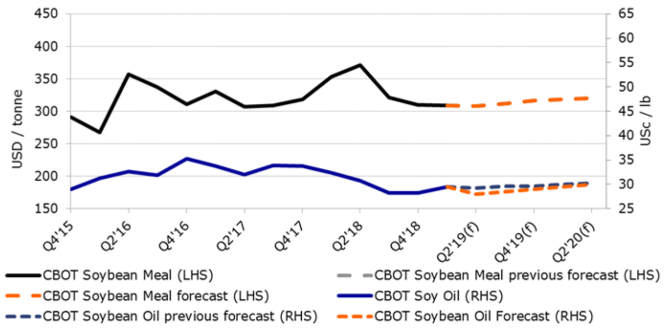
**The ASF-imposed animal protein deficit in China, the world's largest consumer, is precipitating structural changes** in the sector that will be bearish for global animal feed demand growth. Pork production in China will decline by at least 25% to 35% this year, and hog populations will remain constrained next year, as breeders weigh the risk of reinfection. Meanwhile, China's supply deficit will raise animal protein prices, and encourage consumer switching from pork to less feed-intense alternatives like seafood and poultry. Against the fading global feed-demand backdrop, the 2018/19 South American production recovery (+10% YOY) and FX-supported (peso -16% YTD, real -4% YTD) export competition were catalysts to briefly push CBOT Soymeal prices to their lowest in three years, at USD 281/short ton in mid-May.

**In the last two weeks, two potential lifelines have emerged to lift CBOT Soymeal 9% higher**, above the USD 300/short ton support level. The primary drivers are poor US weather, acreage, and yield expectations that have supported the entire soybean complex. The second element is a tenuous, but growing expectation that pork and poultry exporters, including the US, will see a surge in demand later this year from China to fill its supply deficit, which may boost domestic feed demand. Recent Chinese purchase commitments for US pork carcasses, combined with a freeze in US soybean purchases, drove crush margins up 25% in the last month, to seven-month highs, and are likely to reverse declines in NOPA crushing. If large-scale Chinese purchases of US pork are confirmed, US crush will test national capacity and trigger higher prices for CBOT Soymeal. If, however, China's mercurial qualities prevail and it switches from practicality (filling its protein deficit) to patriotism (eschewing US goods), then overenthusiastic US crushers will end up sitting on a soymeal glut.

**CBOT Soy Oil slipped below USc 26.5/lb last month, to four-year lows**, on complex weakness, before staging a partial recovery alongside the broader complex. Early 2019 export demand-driven optimism for CBOT Soy Oil is a distant memory: Expectations of Chinese soy oil imports (to cover a large domestic shortfall) and Brazilian soy oil export constraints (higher biodiesel mandates) have moderated or been delayed, and US export commitments are running 20% behind last year. Still, US domestic soy oil demand remains resilient, thanks to the biodiesel-Brent Crude discount and rising food demand. In May, WASDE even projected 2019/20 domestic demand to drive stocks -415m lb YOY, to six-year lows. Rabobank expects CBOT Soy Oil's recovery in 2019 to hinge on supply fundamentals. We'll see high crush margins drive a reversal from recent weak NOPA crush reports that will keep US soy oil supplies high and prices below USc 30/lb in 2019/20.

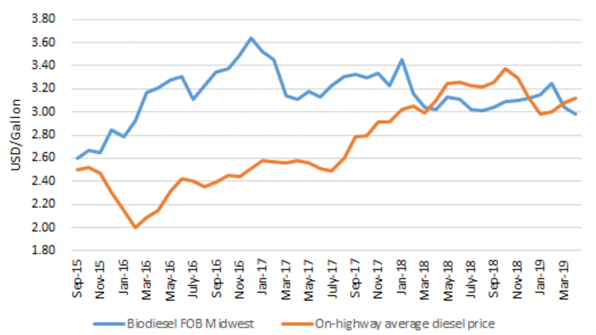
**CBOT Soy Oil, Soymeal enjoy US soy complex weather support, but fortunes hinge on China's ASF choices**

| | unit | Q3'18 | Q4'18 | Q1'19 | Q2'19(f) | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| Soymeal | USD/mt | 321 | 309 | 309 | 308 | 312 | 316 | 318 | 320 |
| Soy oil | USc/lb | 28.2 | 28.3 | 29.5 | 28.0 | 28.5 | 29.0 | 29.5 | 30.0 |



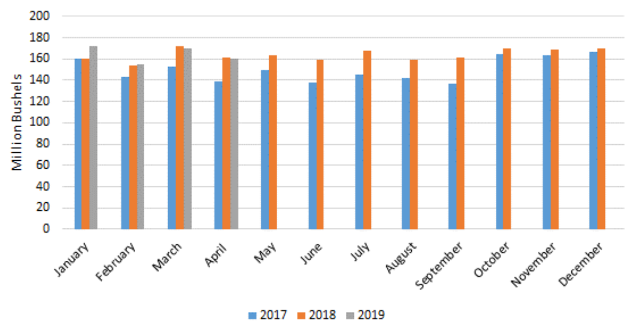

Source: Bloomberg, Rabobank 2019

**US on-highway diesel's expanding premium to biodiesel will encourage domestic biodiesel/soy oil demand**




Source: USDA, ERS, DOE, Rabobank 2019

**US crush slowed in early 2019, but last month's 30% rise in crush margins on hog export expectations will raise output**




Source: NOPA, Rabobank 2019

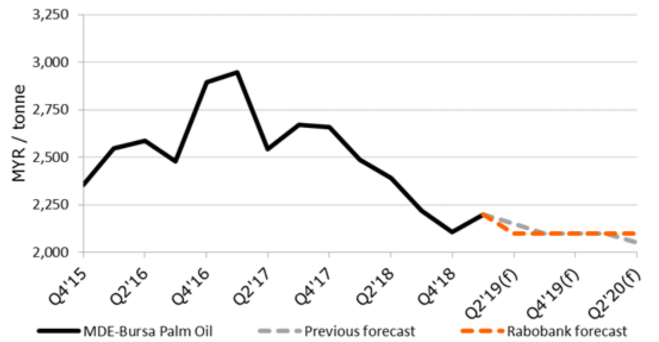
# Palm Oil

**Weak Malaysian ringgit to limit bearish pressure on palm oil prices.**

- Palm oil inventories in Malaysia and Indonesia remain higher year-on-ear.
- Uncertainties around US-China trade war to provide volatility to palm oil prices.
- India's edible oil imports decreased by 14% MOM in April 2019, as domestic inventories remain high.

**We largely maintain our 2019 palm oil price forecast**

| | Unit | Q3'18 | Q4'18 | Q1'19 | Q2'19 | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| Palm Oil | MYR/tonne | 2,219 | 2,108 | 2,200 | 2,100 | 2,100 | 2,100 | 2,100 | 2,100 |




Source: Bloomberg, Rabobank 2019

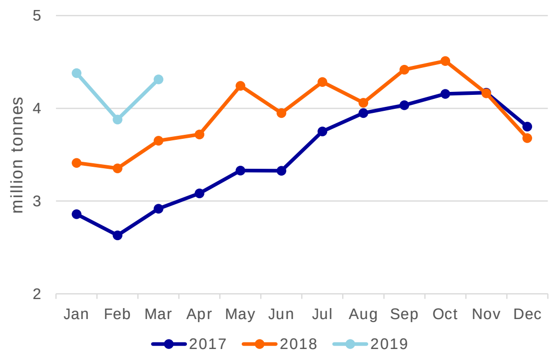
**Palm oil inventories in Malaysia and Indonesia remain higher year-on-year.** According to MPOB, Malaysian April 2019 palm oil production decreased by 1% MOM, to 1.65mmt, and Malaysian palm oil exports for the same month increased by 2% MOM, to 1.65mmt. This resulted in the decrease of Malaysian April 2019 palm oil inventories. Even though Malaysian April 2019 palm oil inventories decreased by 7% MOM, to 2.7mmt, they were still higher by 25% YOY. Meanwhile, according to GAPKI, Indonesian March 2019 palm oil production increased by 11% MOM, to 4.3mmt, while inventories decreased by 3% MOM, to 2.43mmt. We expect Malaysian and Indonesian May 2019 palm oil inventories to decrease further month-on-month, but to remain higher year-on-year. Palm oil production in Southeast Asia normally decreases during the Ramadan period, which is accompanied by higher domestic palm oil demand. Ramadan 2019 began on May 5 and will end on June 4.

**Uncertainties around the US-China trade war will provide volatility to palm oil prices.** The MDE-Bursa palm oil active contract price closed at MYR 1,983/mt on May 10, the lowest point in 2019. The sell-off happened on the back of the CBOT Soybean complex's prices decline due to uncertainties around the US-China trade war. Even though the combination of lower palm oil production and higher palm oil consumption during the Ramadan period will provide fundamental support for palm oil prices in June 2019, the ongoing US-China trade escalation will play a major part in determining the movement of palm oil prices.

**India's edible oil imports decreased by 14% MOM in April 2019, as domestic inventories remain high.** According to SEA India, Indian palm oil and soft oil imports decreased by 12% and 17% MOM, respectively, in April 2019, to reach 707,450mt and 491,313mt. As of early May 2019, Indian edible oil inventories at port and in the pipeline were flat month-on-month, at 2.4mmt. We expect Indian palm oil import activities to be similar month-on-month in May 2019, as high edible oil import volumes throughout Q1 2019 have resulted in high domestic edible oil inventory levels.

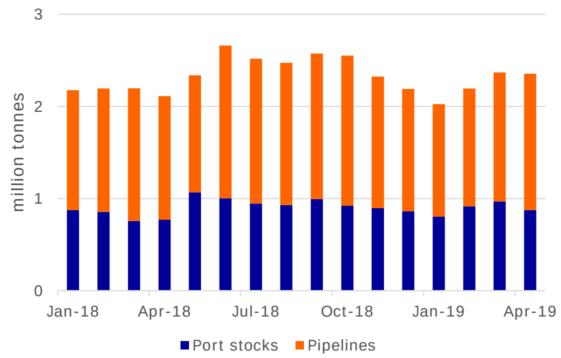
**A weak Malaysian ringgit will limit bearish pressure on palm oil futures prices.** Depreciation of the ringgit against the US dollar typically results in higher BMD palm oil futures prices, as palm oil will become more affordable for importing countries that buy palm oil in USD terms. The MYR has depreciated against the USD by 3.3% since late March, to reach a USD/MYR level of 4.19 as of the third week of May 2019. At the time of writing, the market is still pricing for the MYR to depreciate further in three months' time. This will help provide support for palm oil prices in the short term.

**Monthly 2019 palm oil production in Indonesia has been higher YOY due to higher matured oil-palm plantation areas**




Source: GAPKI, Rabobank 2019

**High Indian edible oil import volumes throughout Q1 2019 have resulted in high domestic edible oil inventory levels**




Source: SEA India, Rabobank 2019

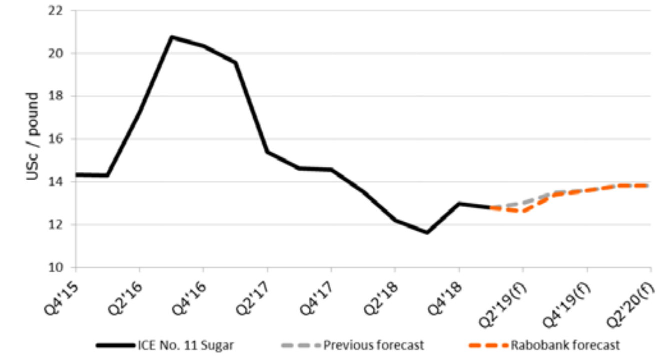
# Sugar

**ICE #11 Sugar prices likely to see some support ahead.**

- Ethanol prices are a little lower in Brazil, due to low international energy prices, but much firmer than sugar prices.
- The weather has been adverse in major sugar-producing countries, underpinning our bullish forecast.

**ICE #11 Sugar price forecast largely maintained**

| | unit | Q3'18 | Q4'18 | Q1'19 | Q2'19(f) | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| Sugar | USc/lb | 11.6 | 13.0 | 12.8 | 12.6 | 13.4 | 13.6 | 13.8 | 13.8 |



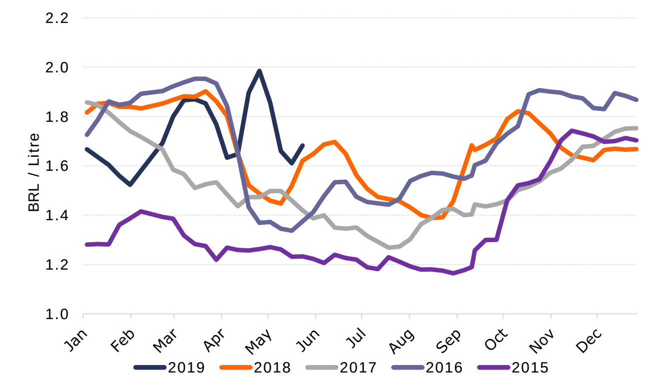

Source: Bloomberg, Rabobank 2019

**ICE Sugar #11 prices are likely trading near the bottom, and we expect some upside off of these levels.** At the time of writing, ICE Sugar #11 is trading at USc 11.9/lb in the front month. That continues to be significantly below Brazil ethanol parity, at around USc 12.6/lb. As the wet weather and economics incentivize Brazilian mills to maximize ethanol, availability of raws will be on the low side going into the intercrop season. The October 2019-March 2020 spread, at over USc -1/lb, is a sign of some shortage in raws ahead, as Brazil continues to focus on ethanol.

**Weather has been adverse in most major sugarcane areas.** While wet weather in Brazil continues to incentivize a low sugar mix, the dry weather pattern over Thailand is intensifying, with many parts of the country receiving 50mm less than normal over the last month. The area grown to cane is also expected to drop in favor of cassava. The cane areas in Yunnan, China, have also been suffering from dry and hot weather, with part of the region receiving 100mm less rainfall over the last month. The weather has also been worrisome in India, where rainfall has been below normal over the last year, and where the monsoon is expected to be delayed and to bring below-normal levels for a second consecutive year. Even though India is likely to have another exportable surplus in 2019/20, internal prices in India are climbing on the back of adverse weather, making exports less likely for the time being. The re-election of President Modi was largely expected, but it does not necessarily guarantee a renewal of export subsidies in the coming season. With the EU likely to export less in the foreseeable future, the fate of the white premium will depend even more on Indian export subsidies.

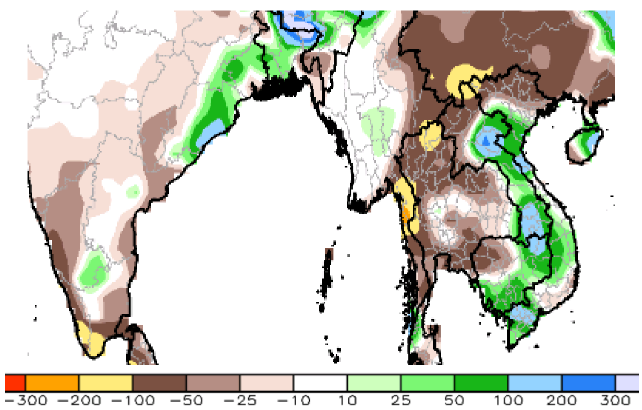
**With the developments in Brazil, Europe and Southeast Asia, the latest drop in the market seems unjustified**, which underpins our bullish sugar forecast. The main factors that accompanied the sugar price drop during the first three weeks of May were the depreciation of the Brazilian real – from USD/BRL 3.9 to over 4.0 – and the drop in Brent prices, on the back of global trade and growth concerns – from USD 72/barrel at the end of April to USD ~68/barrel as of May 24. Even though these factors are bearish, we believe sugar prices will have to trade very close, or above, the ethanol parity in Brazil at some point during the peak of the harvest, to avoid a shortage of raws going forward. Furthermore, NOAA expects the current weak El Niño event to continue through the northern summer with 70% likelihood, and through the fall with a 55% to 60% chance. Given the length of the current El Niño event, even though it's a weak one, we would expect the adverse weather to continue.

**Brazilian hydrous ethanol prices have been very strong, despite a high ethanol output**




Source: Cepea, Bloomberg, Rabobank 2019

**Thailand, China and India continued to be drier than normal, likely related to El Niño. 30-day rainfall anomaly (mm):**




Source: NOAA, Rabobank 2019

# Coffee

## Limited price recovery ahead.

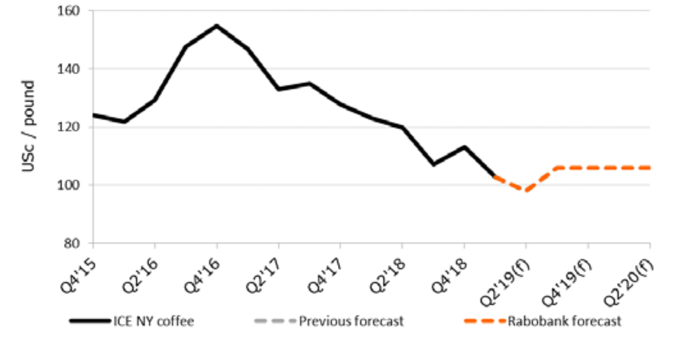
- A cold front in Brazil had a disproportionate effect on prices, even though there was no damage.
- Concerns mount on the 2019/20 mild washed crops.
- A potentially low arabica quality in Brazil will likely result in more demand for Peru and Honduras, and less for robustas.

**ICE Arabica prices are likely to see weather support ahead.** The weather in many arabica regions has been less than perfect. In the key producer Brazil, wet weather during the harvest has been less than ideal for the quality of the crop. Even though the weather has been drier in the last week, more rain is forecast. The unseasonal rainfall will exacerbate the quality issues already present in about 15% of the cherries in the western part of South of Minas during our February crop survey, and this will likely result in a lower proportion of fine cups and a more significant quality premium in the domestic market. That premium is likely to translate into more demand for Peruvian and Honduras coffee going forward, and possibly for certified coffees sitting in exchange-certified warehouses. The weather has also not been great in India and China, but for now, it has been very good over most key growing areas of Vietnam and (at least until recently) Indonesia. However, it was a relatively minor cold front, without any mentionable damage, that lifted the market by simply reminding players that the weather can be unpredictable. Could this be read as a sign of a colder Brazilian winter ahead? It is maybe too early to speculate, but certainly El Niño seems to be playing tricks.

**The outlook for 2019/20 crops in mild washed producers looks a bit grim.** The USDA has recently released a myriad of reports showing strong 2019/20 mild washed coffee crops. We tend to believe Peru will have a rather strong crop, but we have our reservations with regard to crops in Central America and Ecuador, as well as in most African and Asian mild arabica-

### ICE Arabica forecast unchanged, but lower robustas

| | unit | Q3'18 | Q4'18 | Q1'19 | Q2'19(f) | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| ICE Arabica | USc/lb | 107.1 | 113.1 | 102.8 | 98 | 106 | 106 | 106 | 106 |
| ICE Robusta | USD/mt | 1,587 | 1,627 | 1,534 | 1,430 | 1,520 | 1,550 | 1,550 | 1,580 |

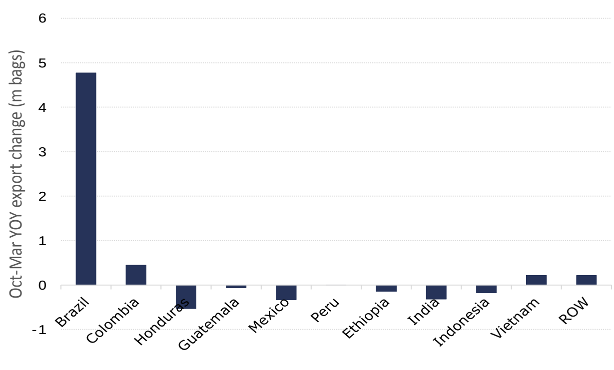



Source: Bloomberg, Rabobank 2019

producing origins. The reports about farmers abandoning farms in Central America are now widespread, and visitors to the area are surprised about the lack of young workers, who have joined recent caravans heading north. Fertilization use will almost certainly be lower in most mild producers, and it is a reasonable assumption that there will be one round less of fertilization for the crops coming from October onwards in most washed arabica-producing countries. Lower fertilization will not necessarily translate into lower production everywhere, but the production effect of any adverse weather will be exacerbated.

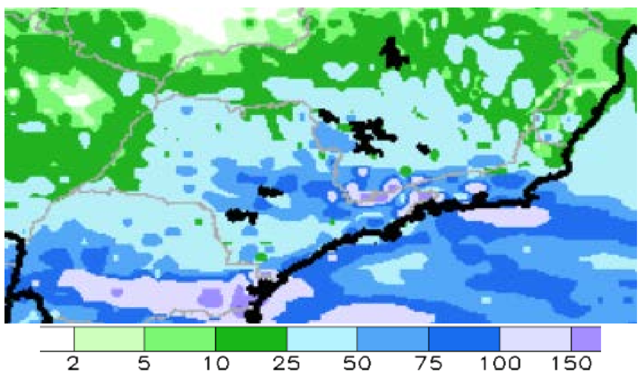
**On the robusta side, strong production meets potentially weaker demand.** Strong robusta production in the main three producing countries (Vietnam, Indonesia, and Brazil) will likely continue to put pressure on the market and generate a contango structure for most of 2019. If the wet weather during the Brazil arabica harvest continues, a high availability of low-quality arabica beans will pose strong competition for robustas. We remain bullish regarding robustas in the longer term, as consumption continues to increase, and we see issues in some countries outside of the top three. But for the time being, a low arbitrage and the quality issues in Brazil arabicas are likely to keep price upside limited.

### Exports out of Brazil have been overwhelming, which will lead other countries to use lower inputs




Source: ICO, Cecafé, customs data, Rabobank 2019

### Weather is looking wet in Brazil, lowering the quality of the arabica crop. 7-day forecast (mm):




Source: NOAA, Rabobank 2019

# Cotton

**Deteriorating US-China trade relations sent shockwaves through ICE #2 Cotton futures.**

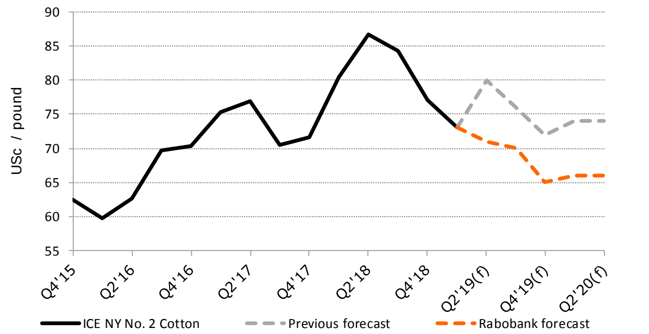
- The ICE #2 fell a staggering 14% through May, as both the US and China announced fresh trade tariffs – the scale and speed of the slump was widely unforeseen.
- World ex. China stocks to reach fresh records in 2019/20, as global new crop delivers another 7.7m bales YOY.
- Slow planting progress across the US Delta raises early concerns, as do the USDA's reported soy subsidies.

**Deteriorating US-China trade relations sent shockwaves through ICE #2 Cotton futures**, with a staggering 14% price drop through May. The scale and speed of the slump was unforeseen, as markets largely anticipated a positive conclusion to US-China trade negotiations. In contrast, the US announced additional Chinese import tariffs, totaling USD 200bn, which was met by USD 60bn of retaliatory tariffs from China – the US cotton tariff (25%) was kept unchanged. A prolonged US-China trade war raises major concerns over US export demand which, in turn, threatens significant domestic 2019/20 stock-building. This will drive a bearish tone through the ICE #2 in the medium term, severely limiting price action above USc 72/lb. Rabobank holds a bullish view from current levels, forecasting USc 70/lb in Q3 2019, on weather risks and non-China demand inquiry. Prices in the USc 60/lb to USc 70/lb region – for the first time in 14 months – should heighten nearby US export inquiry, particularly from Southeast Asia. However, Rabobank sees swelling global stocks weighing on the exchange in late 2019, taking prices back to USc 66/lb by 1H 2020.

**World ex. China stocks are set to reach record levels in 2019/20**, as global new crop output delivers another 7.7m bales YOY. This follows Brazil's emergence as a +12m-bale annual producer, while the US and India see relative margins and conditions drive output up 23% and 5% YOY, respectively. This higher supply availability should keep price surges limited in the

### ICE #2 Cotton forecast revised lower, following escalation in the US-China trade war

| | unit | Q3'18 | Q4'18 | Q1'19 | Q2'19(f) | Q3'19(f) | Q4'19(f) | Q1'20(f) | Q2'20(f) |
|---|---|---|---|---|---|---|---|---|---|
| Cotton | USc/lb | 84 | 77 | 73 | 71 | 70 | 65 | 66 | 66 |

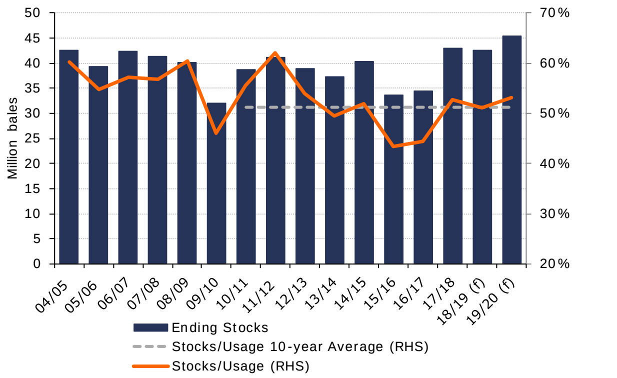



Source: Bloomberg, Rabobank 2019

presence of steady demand growth – Rabobank continues to forecast global demand growth in 2018/19 and 2019/20 at 2% and 3%, respectively, above the corresponding USDA estimates. The US 2019/20 balance sheet sits in a precarious position, as a combination of strong acreage, favorable conditions (hence low abandonment), and threatened export demand point towards considerable stock-building. Rabobank forecasts new crop US stocks to reach 6.9m bales, assuming 16.7m bales in exports. Without Chinese demand, there are real risks of US exports flattening year-on-year, at 15m bales, which could take stocks close to 9m bales. Non-US exporters will take relief in China's improving appetite for new season cotton, which should maintain export premiums – and grower margins – for Brazilian and Australian exports.

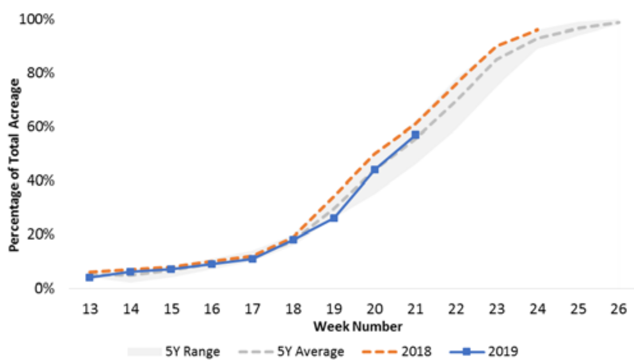
**Slow planting progress across the US Delta raises early concerns**, as persistent rainfall proves a major challenge for field operations. As of May 29, Arkansas, Louisiana, and Mississippi saw plantings 10% to 20% behind their respective five-year averages – 17% of annual US production stemmed from these states in 2017/18. While growers can plant surprisingly quickly during a break in the weather, Rabobank highlights that weather risk remains high as we enter the northern hemisphere spring. Furthermore, latest reports of USDA subsidies to US soybean growers have the potential to shift planted acres away from cotton – another factor threatening US area estimates.

### World ex. China stocks reach record levels in 2019/20, as stocks/usage ratio breaks above the ten-year average




Source: USDA, Rabobank 2019

### National US planting progress is on pace at 57% complete, despite rain delays across AR, LA, and MS




Source: USDA, Rabobank 2019

# Imprint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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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A summary of the methodology can be found on our website www.rabobank.com

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