

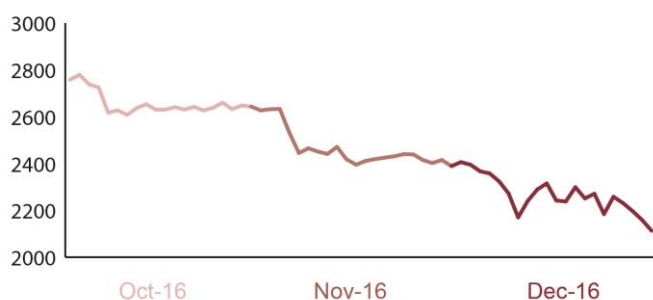
Market Report

January 2017

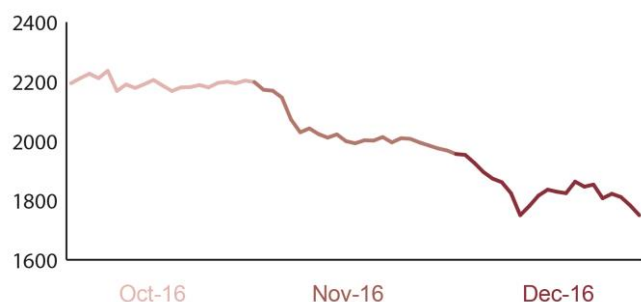
Cocoa Beans Continued lower prices

In December cocoa prices continued to move lower. Compared to the end of November where the second future month closed at £ 1956, prices lost about ten percent settling at the lowest level since almost 3 years at £1750. This was mostly driven by speculators extending their short positions, and a consensus that there is ample supply of cocoa leading to a large surplus this crop season. The downtrend that we entered in November was aggressively followed by technical analysis traders and system funds (see article on the backside). From a fundamental point of view we continue to see strong arrivals, and good arrival volumes are still expected ahead of us, which also aided prices to go down the path of least resistance. Origins weren't overly active during the month, with main producer Ivory Coast even announcing to hold back on selling 17/18 at least till the end of the calendar year, but at the same time chocolate industry participants were able to be picky on their buying given the solid forward price coverage they already hold. We saw some hopefully short lived unrest in Ivory Coast this week. The political developments in the IVC, the flow of arrivals, the intensity of the harmattan, coming grind numbers and the extent of forward origin selling will be the short term events to watch determining the market's next move.

New York close, 2nd month USD/Mt



London close, 2nd month GBP/Mt



Cocoa Butter Buying opportunity

The market has come to realize the crops will be good this year. As prices started to ease in November we have seen a continuation of that trend in December. Despite the tight physical supply of cocoa butter the prices of butter are down on the back of the expectation that the supply will improve. That is good news! But does that mean there is nothing to be worried about anymore? Well in cocoa you can never get complacent. Last week the market was confronted with unrest in Ivory Coast. Since Ivory Coast is the second largest grinding country of the world any disruption in local processing or exports will impact availability of raw material. Let this be a warning for the ones that want to buy the 'low' of the market.

Cocoa Powder On a steady pace

In a downwards terminal market, cocoa powder prices remained supported and moved sideways during the month of December. At the same time, powder buyers across the globe were very active, stepping in to cover their needs further into 2017.

In a context of supportive demand combined with historically attractive prices, it is favorable to consider covering remaining needs of 2017.

Cocoa Liquor Preparing for Easter

The year 2016 ended with fireworks as liquor demand was strong and availability remained tight. On the pricing side the bean futures market slide made liquor prices more attractive. While the liquor market remains tight and availability is expected to improve slowly towards the low season after Easter flat prices are attractive and buyers take market dips as opportunity to extend their cover. For ratio buyers a lower market means firmer levels.



Barry Maas

Manager Customer Price Risk
Cargill Cocoa & Chocolate

Speculators Participation

The commodity market as a whole, and the cocoa market as part of it, has seen a significant increase in speculators participation in the past decade.

In this month's Market Report we give insight in the types of speculators that can be identified, the role they play in the market, what information is available on their positioning and the conclusions that could be derived from it.

Speculators analyze and forecast price movements and are buying and selling futures- and option-contracts in order to make a profit. Most speculators have no intention to be involved in the physical underlying asset, and most of the time have no more exposure at the expiration of the contracts.

Type of speculators

We can identify different types of speculators which display different behavior and strategies;

- Index funds; these are more passively managed funds who hold on to their positions for a longer period of time. Examples are pension funds who can invest in a commodity basket or index with cocoa being part of that basket
- Discretionary funds; funds that manage money coming from investors, and which trade based on technical and fundamental analysis (like supply and demand)
- System funds; funds applying systematic trading. This could be full or partial automation of trading using computers and algorithms. Although systematic trading is more common to be based on chart patterns or correlations for example, there are also systems using fundamental data as trading input, or a combination of both.

Role of speculators

These different type of speculators can bring large volatility to the market, also if there is not a direct fundamental driver for it. At the same time, speculators can help to enable a fair price discovery as they provide liquidity at times when natural buyers and sellers are not active simultaneously. The chocolate industry is the natural buyer and origin countries are the natural sellers of cocoa. Speculators come as third party into the equation and can operate from both sides. This means that the speculator community can be competition for either industry, when buying,

or for origin, when selling. Through the futures markets, speculators bridge the gap between the potential mismatch in behavior between the chocolate industry and origin countries. Due to their size, speculators can at times also distort prices beyond what other market participants perceive as fundamentally justified fair value. This dynamic provides trading opportunities for all market participants.

Commitment of Traders

The US Commodity Futures Trading Commission (CFTC) publishes the Commitment of Traders (COT)-report on a weekly basis. They publish the weekly total and change of the positions that different categories of market participants hold in futures and options. Out of that data the position of speculators can be derived, and what they have done that specific week. So from this COT-report one can derive - what is called - the paper flow or order flow of futures. If speculators on a net basis have sold, that automatically means that the chocolate industry has been buying those volumes, potentially on top of volumes that origins have sold. By making an assumption on the origin sales and using this COT data, participants can make an estimate of the average futures price cover from the chocolate industry.

Managing exposure to price risks in the cocoa market

As said, on one hand speculators provide liquidity to the market, but on the other hand they can drive large and unexpected price swings. To support you in navigating through these uncertainties Cargill Cocoa & Chocolate offers several Price Risk Solutions. Please connect with your Sales Manager to find out more on what Cargill can do for you.

