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## **Sugar, Not Oil, Bonds or Stocks, May Be Best Investment in 2006**

March 20 (Bloomberg) -- Sugar, the best-performing commodity the past 12 months, may beat bonds, stocks and oil for a second straight year.

``Sugar could quadruple from here and it would still be below its all-time high," said former George Soros partner James Rogers, 63, who founded Lausanne, Switzerland-based Diapason Commodities Management SA, which oversees \$3.5 billion. ``The rally hasn't even started yet. And the fundamentals are changing dramatically in a positive way."

Prices are soaring as record gasoline costs prompt Brazil, the world's biggest sugar producer, to devote more than half of its crop to ethanol production to meet a goal of eliminating gas-fueled cars in four years. A drought in Thailand, the second-biggest exporter, and a 50 percent rise in Chinese sugar demand the past decade are compounding the supply squeeze.

``Sugar will definitely outperform bonds and equities this year, primarily because of supply constraints," said Andreas Meyer, 39, who helps manage \$130 million at Vienna-based Merit Alternative Investments GmbH and set up the Commodities Opportunities Fund two months ago.

Sugar climbed 60 percent in 2005 and is up 12 percent this year. By comparison, the Standard and Poor's 500 Index of stocks has gained 4.7 percent since Dec. 31, and U.S. government bonds have dropped 0.44 percent, according to Merrill Lynch & Co.

### Outpacing Bonds

``It's a meager year for bond returns compared to what may be in the offering in other asset classes," said Jack Malvey, chief global fixed-income strategist at Lehman Brothers Inc. in New York. Bonds globally may return as little as 2 percent this year, Malvey said.

Raw sugar for May delivery closed last week at 16.44 cents a pound on the New York Board of Trade. It may rise 52 percent this year to 25 cents a pound, according to Meyer at Merit Alternative Investments. Christopher Wyke, director of commodities for Schroders Plc in London, says prices will top 19.30 cents a pound. The record was 66 cents a pound in 1974.

Sugar is a top pick for Rogers, who co-founded the Quantum fund with Soros in 1970 and has been urging investors to buy commodities rather than stocks or bonds for the next 10 to 15 years. Rogers says producers of raw materials failed to invest in their business when prices were low, so they will be unable to keep pace with rising demand.

Rogers, author of ``Investment Biker: Around the World With Jim Rogers," and ``Hot Commodities," says he gets his investment ideas from countries he visits. His Beeland Interests manages the Rogers International Commodities Index, which fell 5.5 percent in February amid losses from its dealings with bankrupt broker Refco LLC. The index has more than tripled since inception in 1998, Rogers International says on its Web site.

### Rising Costs

Sugar's rally has boosted costs for companies such as cereal maker Kellogg Co., based in Battle Creek, Michigan, and candy maker Hershey Co., based in Hershey, Pennsylvania. Hershey's cost of sales last year rose 11 percent, and Kellogg's rose 5.9 percent. Sugar accounts for 10 percent of Hershey's cost of goods sold, JPMorgan Securities Inc. analyst Pablo Zuanic said.

Global sugar production will fall short of demand this year by twice as much as initially expected as world stockpiles dwindle and consumption grows, the London-based International Sugar Organization said in a March 8 report. The shortfall will be 2.225 million metric tons in the 2005-2006 crop year, up from a November forecast of 1.015 million tons, the ISO said.

#### China, India

The booming economies of China and India, the world's most populous nations, contribute to the shortfall. India, the No. 2 producer and biggest consumer of sugar, became an importer last year after two years of falling harvests, shipping in 2 million extra tons of the commodity. China, the world's second-biggest user, is trying to stem price gains by selling almost its entire 1 million tons of sugar reserves at auctions this year.

Consumption of sugar in China increased almost 50 percent in the past 10 years, according to the U.S. Department of Agriculture. Inventories of the sweetener halved as rising demand for the commodity in food and soft drinks outpaced production.

People in China increased consumption of sugar-containing soft drinks by 16 percent in 2005, said Chen Jing, an analyst at Beijing Orient Agribusiness Consultant Ltd. Atlanta-based Coca-Cola Co. and Purchase, New York-based PepsiCo Inc. are the two biggest sugar buyers in China, Chen said March 17.

#### 'Bull Run'

Sugar is "entering a bull run," said Richard Lucas, a soft commodities and renewable energies analyst at London-based natural-resources brokerage Ambrian Partners Ltd. "China is reorganizing its agricultural sector. Farm workers are moving to the cities, meaning there will be less people to work on the land, and the population is getting richer."

Disposable incomes in Chinese cities and towns are expected to rise 6 percent in 2006, according to Ma Kai, chairman of the country's top planning agency.

On the other side of the world, a new generation of vehicles in Brazil is deepening the sugar shortfall. So-called flexi-fuel cars, which allow motorists to switch to ethanol when it's cheaper, may account for all the nation's cars by 2011 under government plans. Such cars currently account for 48 percent of the nation's automobiles.

"We were enthusiastic about being able to cut our costs with this fuel," Fabiana Bueno, a 28-year-old fashion designer from Sao Paulo who bought a flexi-fuel car in December, said in an interview. "It certainly saves money." Ethanol costs her 1.99 reais (\$0.92) a liter, and gasoline 2.79 reais, she said.

#### 'Biggest Challenge'

Brazil is the world's biggest user of ethanol, devoting almost half its sugar to making the fuel, or about a 10th of the world's annual 148 million tons of production. A 1 percent increase in Brazilian ethanol production removes as much as 1 million tons of sugar from world supplies, according to Sergey Gudoshnikov, a senior economist at the International Sugar Organization.

"Brazil's biggest challenge this year would be to juggle between meeting the growing domestic ethanol demand and the increased attractiveness of world sugar prices," the organization said in its March 8 report.

The next best performers to sugar in the past year are copper, which has gained 50 percent, and silver, up 38 percent. Crude oil futures have climbed 13 percent.

#### Sweeteners and Fuels

Oil, at \$64 a barrel this week, will have to fall to \$35 before demand eases for sugar used as fuel, "and that's not going to happen anytime soon," said Stephan Wrobel, 33, chief executive officer of Diapason Commodities.

Prices are rising so fast, global sugar consumption growth may slow as some developing countries cut imports, according to Ratzeburg, Germany-based F.O. Licht, which has provided sugar data to refiners and traders for 130 years.

Some nations that depend on sugar from other countries to meet domestic demand may go without, Licht said on March 15. Reduced demand from importers may erode growth in worldwide consumption to 1.6 percent in the year ending Sept. 30 from 2.2 percent the previous year, it said.

``This could prove to be the Achilles heel of the market in 2005-06," said Licht.

Raw sugar production in Brazil in the crop year ending in April will be 28.5 million tons, compared with 26.7 million tons the year before, according to the ISO. Output may rise to 30.4 million tons next year.

``Brazil is ordering mills back to work early to crush cane to meet demand for ethanol," said Michael Coleman, who runs the \$60 million Merchant Commodity Fund in Singapore. ``Harvesting cane early damages the yield, even without bad weather. Anything that happens to the Brazilian crop would be explosive."

#### Producer Gains

Shares of Sao Paulo-based Cosan SA Industria e Comercio, the world's largest combined sugar and ethanol producer, have risen 96 percent since an initial public offering Nov. 17, compared with a 19 percent gain on the benchmark Bovespa index in the same period.

``It's amazing that this stuff is still given away for free at restaurants," said Wyke, 51, who's also director of emerging-market debt at Schroders, the 202-year-old London-based fund manager. His commodity fund has risen 5 percent since it was started Oct. 31.

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