Brazil Macro | August 2023

Commodities

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SUMMARY

Since our last scenario revision, commodity prices have risen on the back of a geopolitical shock and aided by a macro backdrop of a weak USD. The renewed geopolitical shock coming from Eastern Europe is a risk that could once again bring supply-demand imbalances in some commodities (e.g., grains, fuels, fertilizers). In macro, despite the monetary tightening promoted by the main central banks, fears of a potential recession have eased at the margin as U.S. data has improved. The appreciation of the CNY also helped drive the recent surge in commodity prices, and fiscal and monetary stimulus could come from the Chinese Government in the coming weeks, though we expect the impact on metal prices to be short-lived. As a result, we are slightly upgrading our aggregate commodity index forecast for YE2023, while maintaining it for YE2024. Our forecast for Brent oil is at USD 85/bbl for YE2023 and USD 95/bbl for YE2024. Worth noting, supply issues persist for many materials, with the CRB Index still 36% above pre-pandemic levels. Going forward, we expect a gradual drop in global material costs in the coming years, as global demand softens and aggregate supply gradually catches up.

OVERVIEW

01

Materials: A geopolitical shock amid a gradual drop in the coming years

- Since our last scenario revision, commodity prices have risen on the back of a geopolitical shock and aided by a macro backdrop of a weak USD.
- As a result, we are slightly upgrading our aggregate commodity index forecast for YE2023, while maintaining it for YE2024. Our forecast for Brent oil is at USD 85/bbl for YE2023 and USD 95/bbl for YE2024.

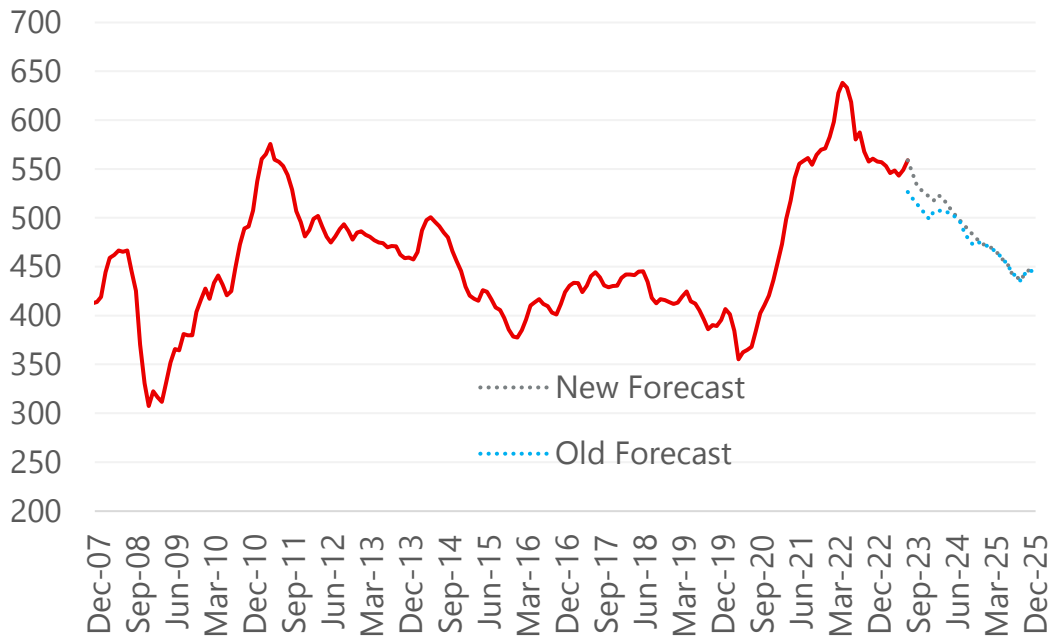
Our Forecasts for CRB Index – End of Period

YE	2021	2022	2023e	2024e	2025e
CRB Food	483	539	453 ↑	395 →	371 →
CRB Energy	1521	2078	1761 ↑	1724 →	1619 →
CRB Metal	1259	1010	1113 ↑	977 →	918 →
CRB	571	558	528 ↑	474 →	445 →

YE YoY	2021	2022	2023e	2024e	2025e
CRB Food	36%	12%	-16%	-13%	-6%
CRB Energy	31%	37%	-15%	-2%	-6%
CRB Metal	42%	-20%	10%	-12%	-6%
CRB	29%	-2%	-5%	-10%	-6%

Sources: Santander.

Our Forecasts for CRB Index – Monthly Averages



Sources: Bloomberg, Santander.

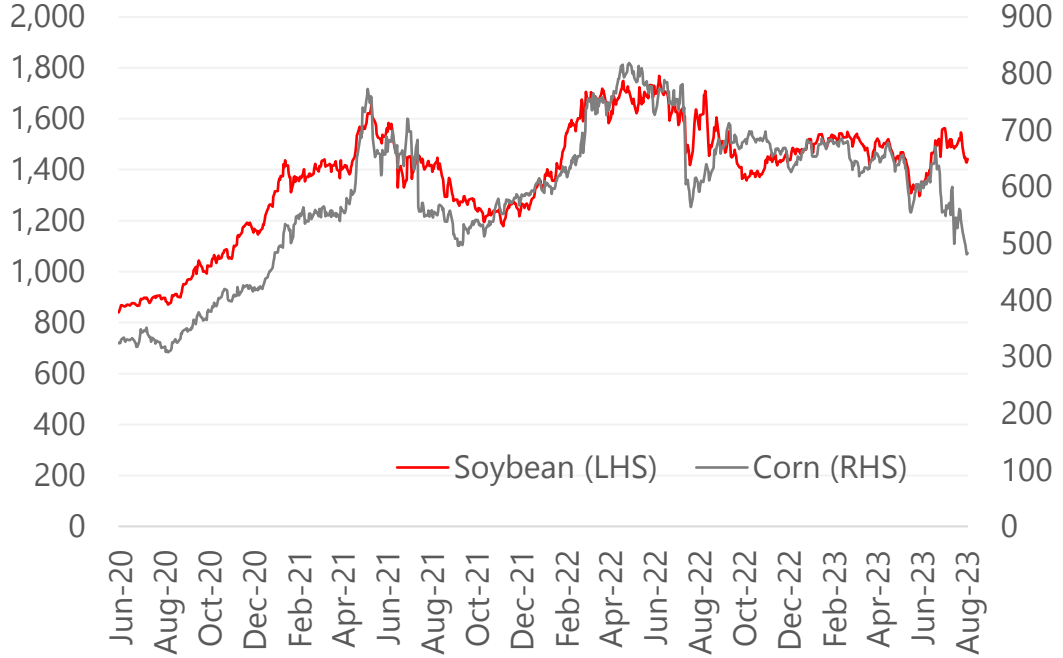
AGRICULTURE

02

Agri: A record brazilian grain output

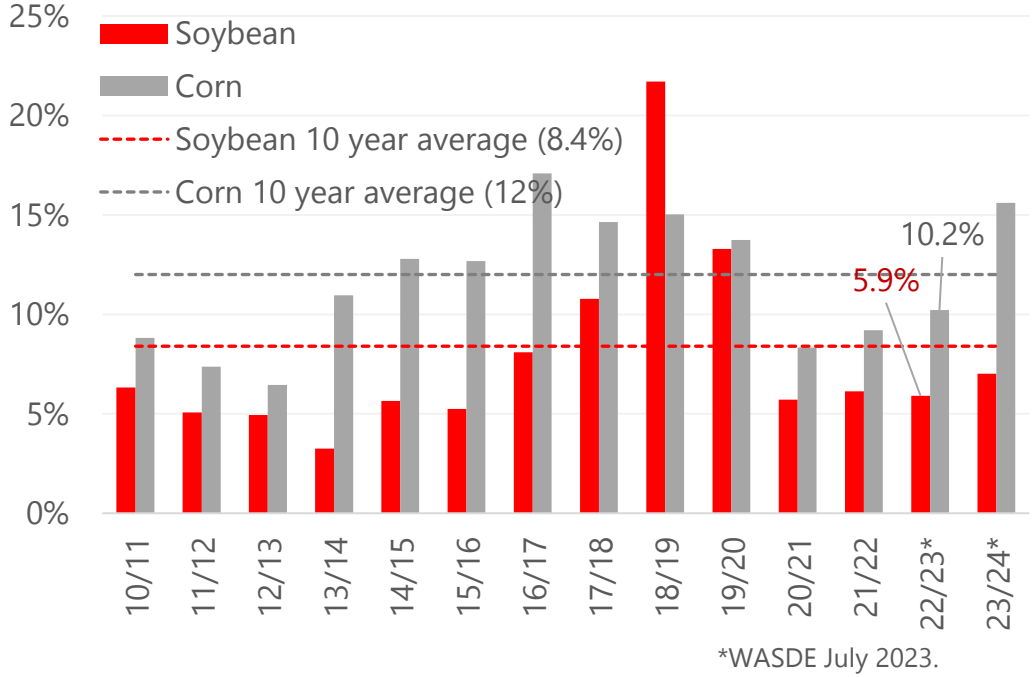
- Brazil is set for record soybean and corn output as a result of favorable growing conditions across most of the country. **We expect this to be a key factor dampening food inflation over time.**
- On July 17, Russia pulled out of an agreement that allowed Ukraine to export its grains. The renewed geopolitical shock coming from Eastern Europe is a risk that could once again bring supply-demand imbalances in some commodities (e.g., grains, fuels, fertilizers).

Chicago Board of Trade - Grains (USD cents)



Sources: Bloomberg, Santander.

US: Stock-to-Use Ratio in Grains (%)

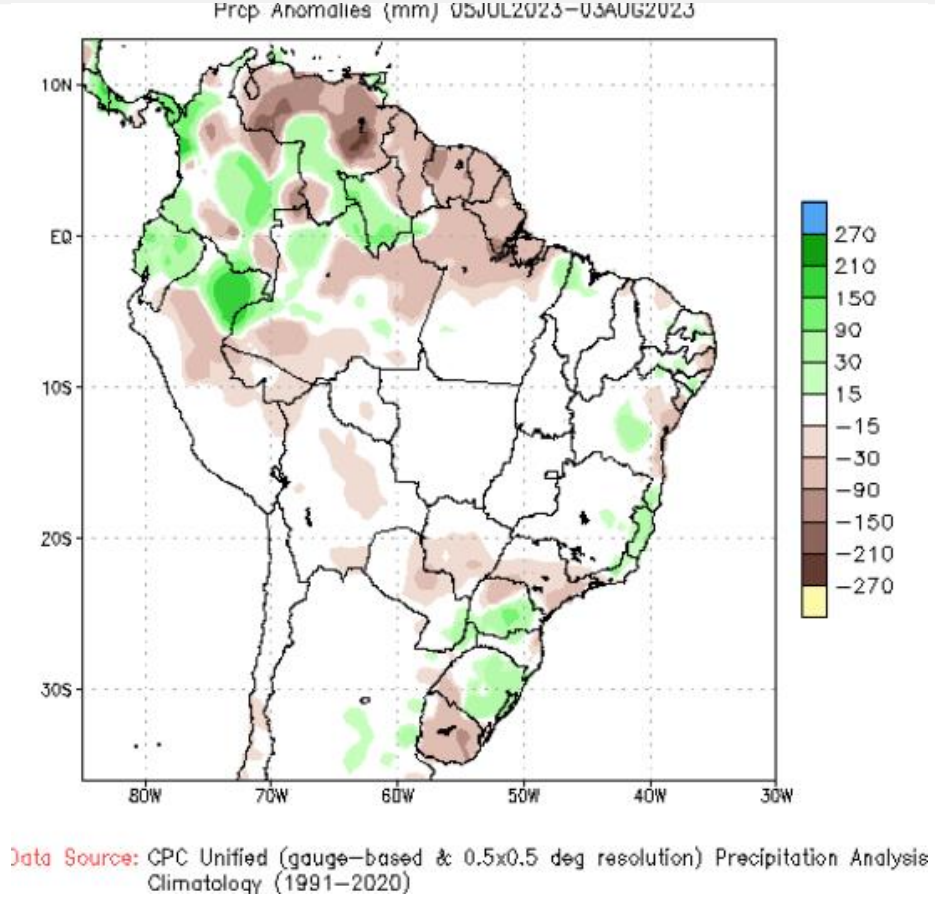


Sources: USDA, Santander.

Agri: A record brazilian grain output

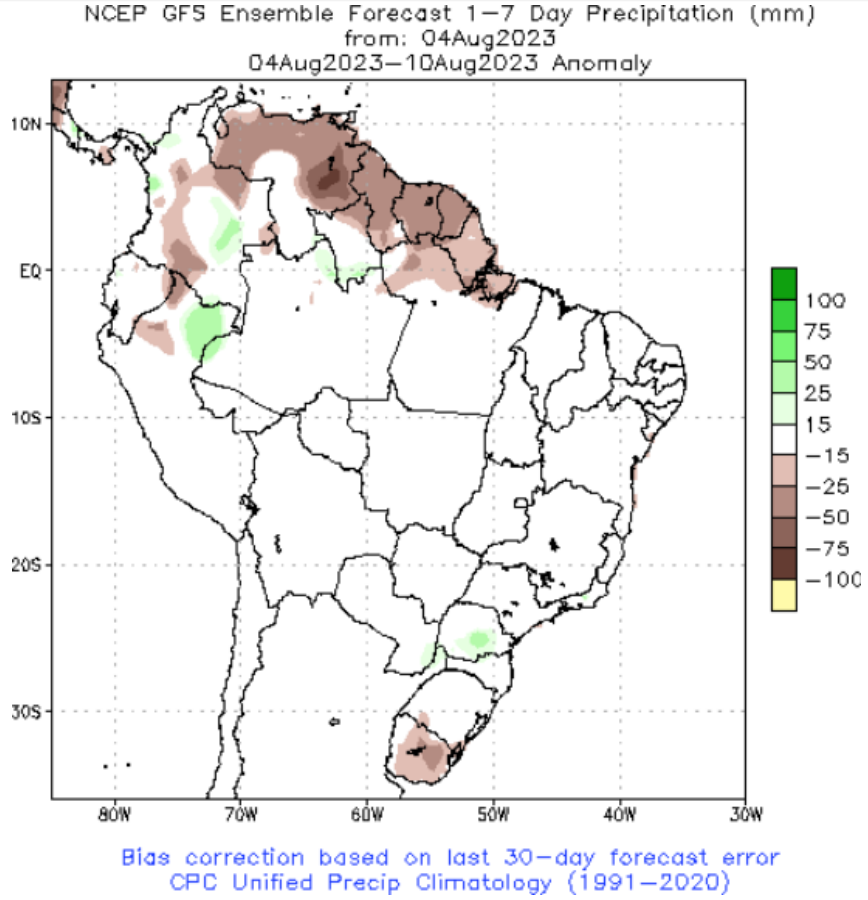
- Precipitation in Brazil has been roughly in line with the historical average for this time of the year, with the south part of the country seeing above average rains. The forecast for the coming days the story is the same.

Precipitation (30-day anomaly)



Sources: NOAA, Santander.

GFS Precipitation Forecasts (7-day anomaly)

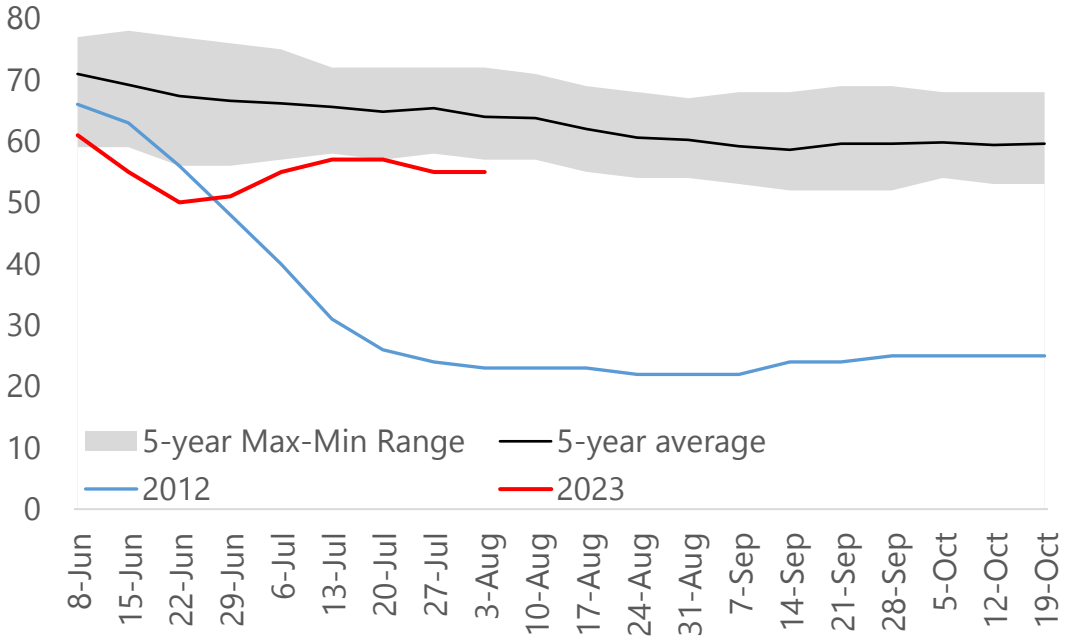


Sources: NOAA, Santander.

Agri: U.S. crop condition improve in July

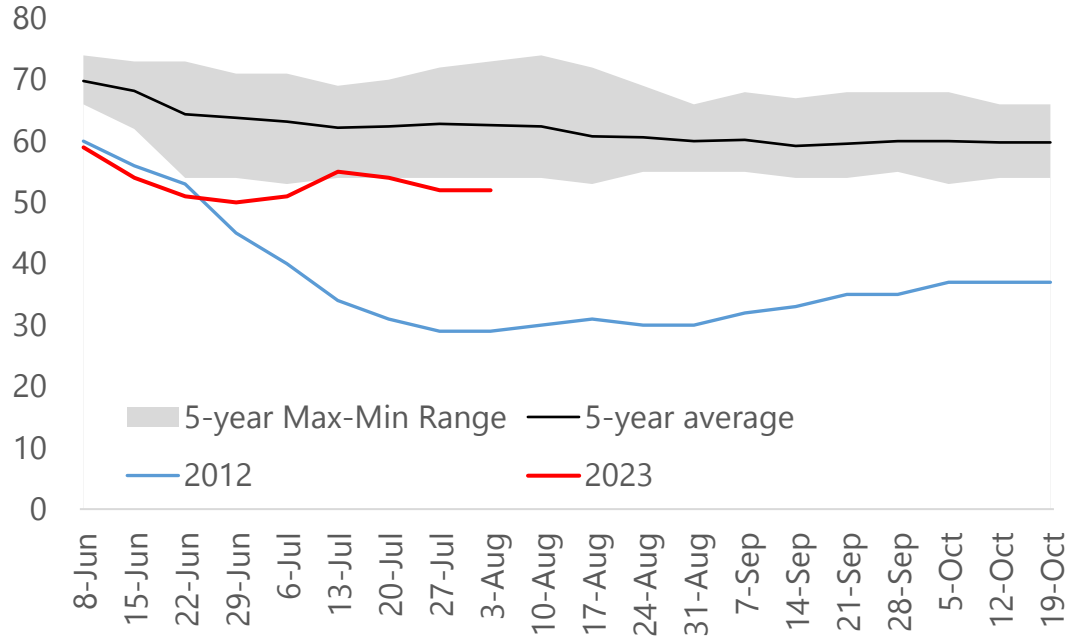
- After initially seeing a sharp decline in U.S. crop rating amid hot and dry weather in parts of the Midwest grain belt (with crop conditions even below 2012 level – a year of severe drought), July brough some respite with widespread rains and cool temperatures.

Corn Crop Condition (% in good/excellent condition)



Sources: USDA, Santander.

Soybean Crop Condition (% in good/excellent condition)



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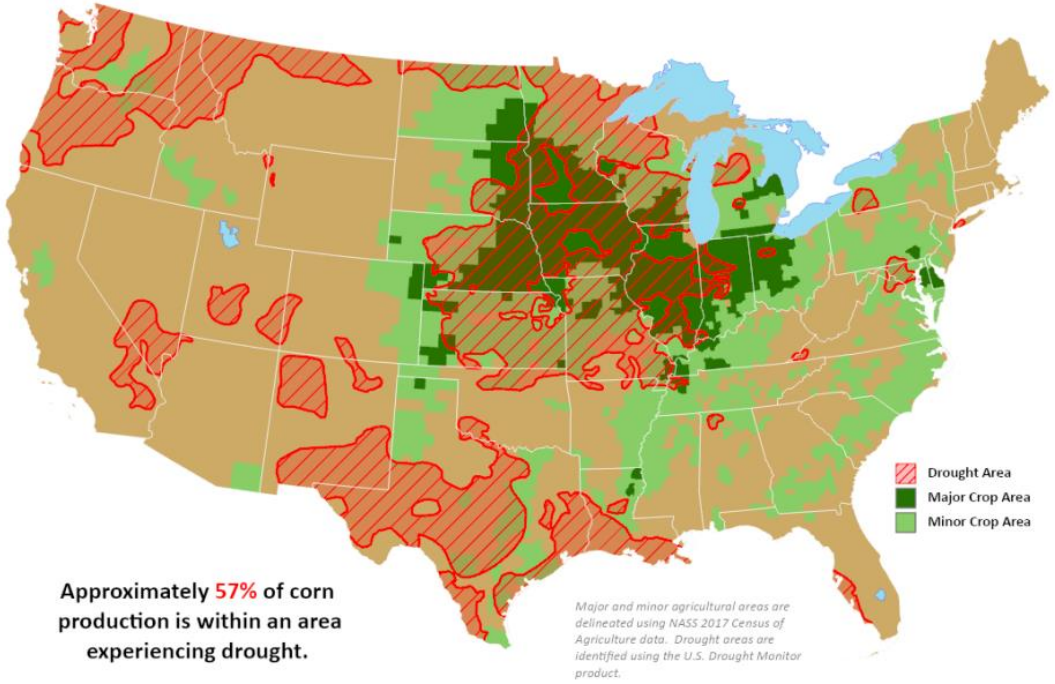
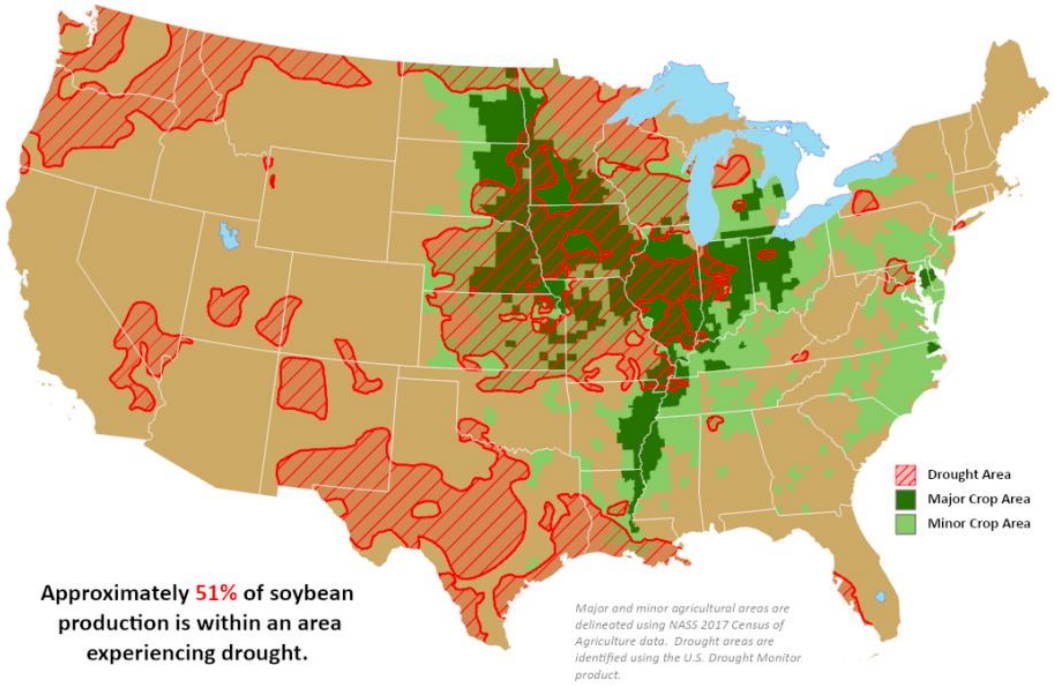
Corn Areas in Drought (as of August 1, 2023)



Sources: USDA, Santander.

Soybean Areas in Drought (as of August 1, 2023)

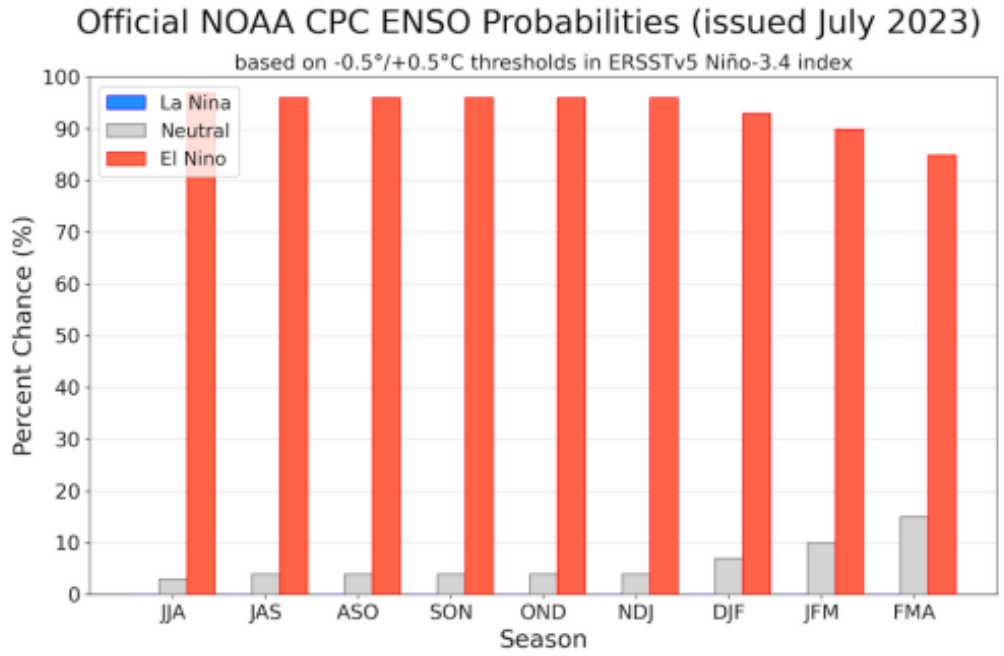


Sources: USDA, Santander.

Agri: The first El Niño in four years is a risk for food and energy inflation

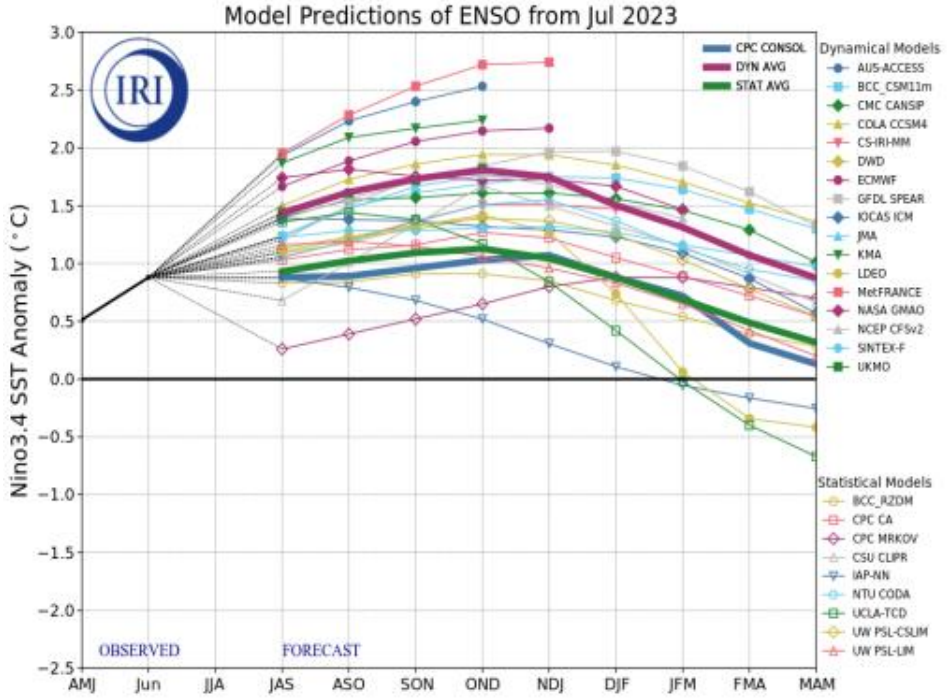
- El Niño is favored through Northern Hemisphere winter 2023-24, with chances exceeding 90% for most of the period.
- Nearly all models indicate El Niño will persist into the Northern Hemisphere winter 2023-24. A strong El Niño (ONI values at or greater than 1.5ºC) is indicated by the dynamical model average through December 2023-February 2024.
- **A strong El Niño is a risk for Brazilian inflation, especially in 4Q23 and 1Q24.**

Official NOAA ENSO Probabilities



Sources: NOAA, Santander.

Model Predictions of ENSO

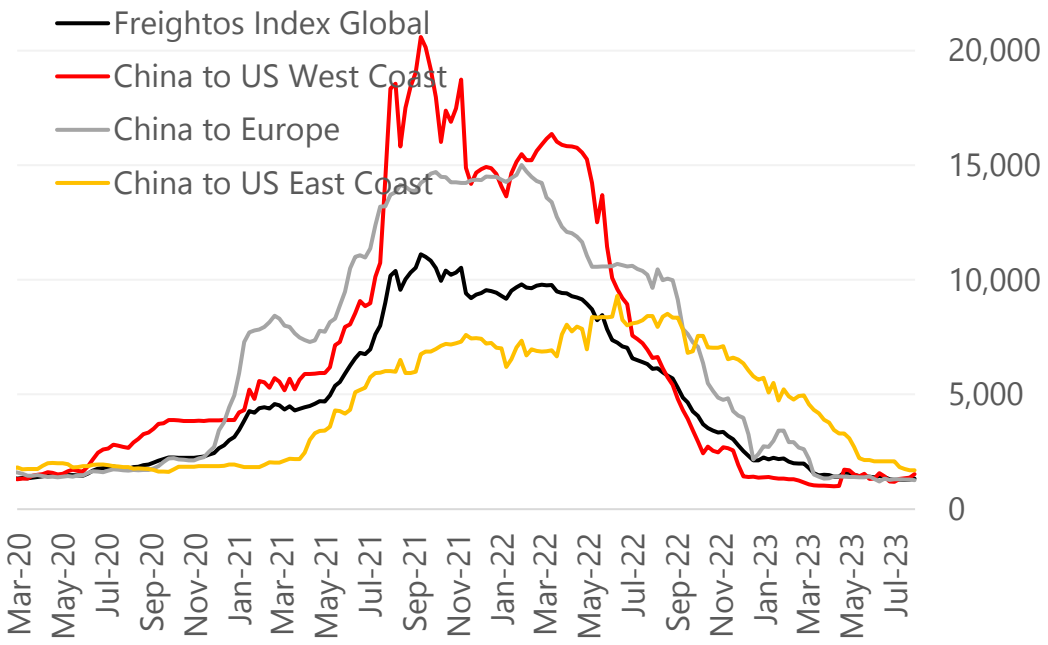


Sources: NOAA, Santander.

Agri: Supply constraints ease back to pre-war levels

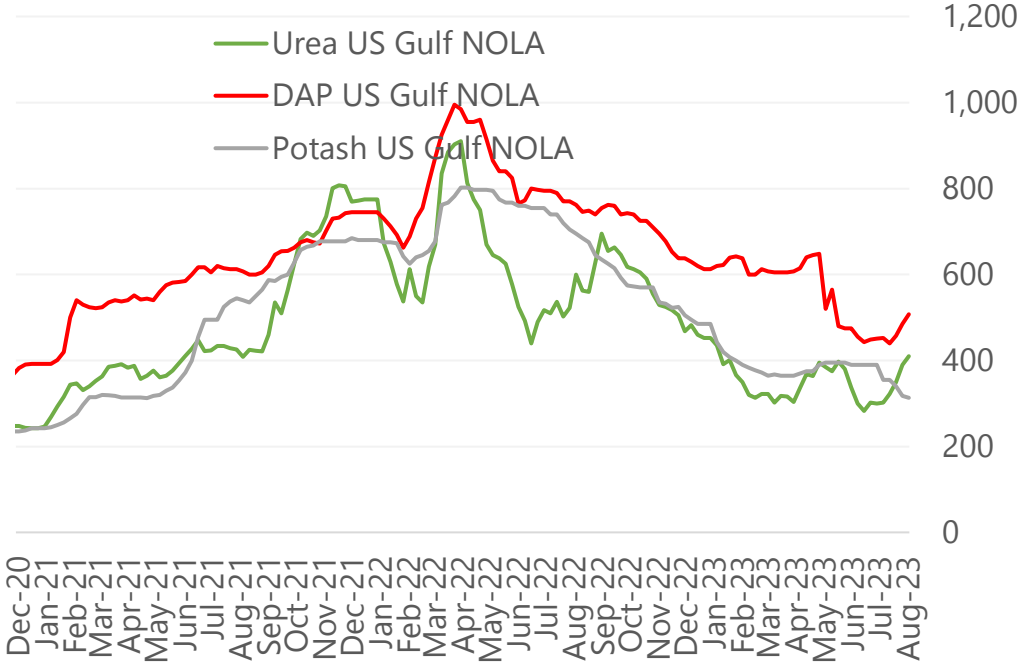
- Freight cost proxies continue to fall at the margin (helping deflation prints), with routes already back to pre-pandemic levels.
- Fertilizers prices are rising at the margin given the geopolitical risk from renewed tension between Russia-Ukraine.

Freight Costs Index



Sources: Bloomberg, Santander.

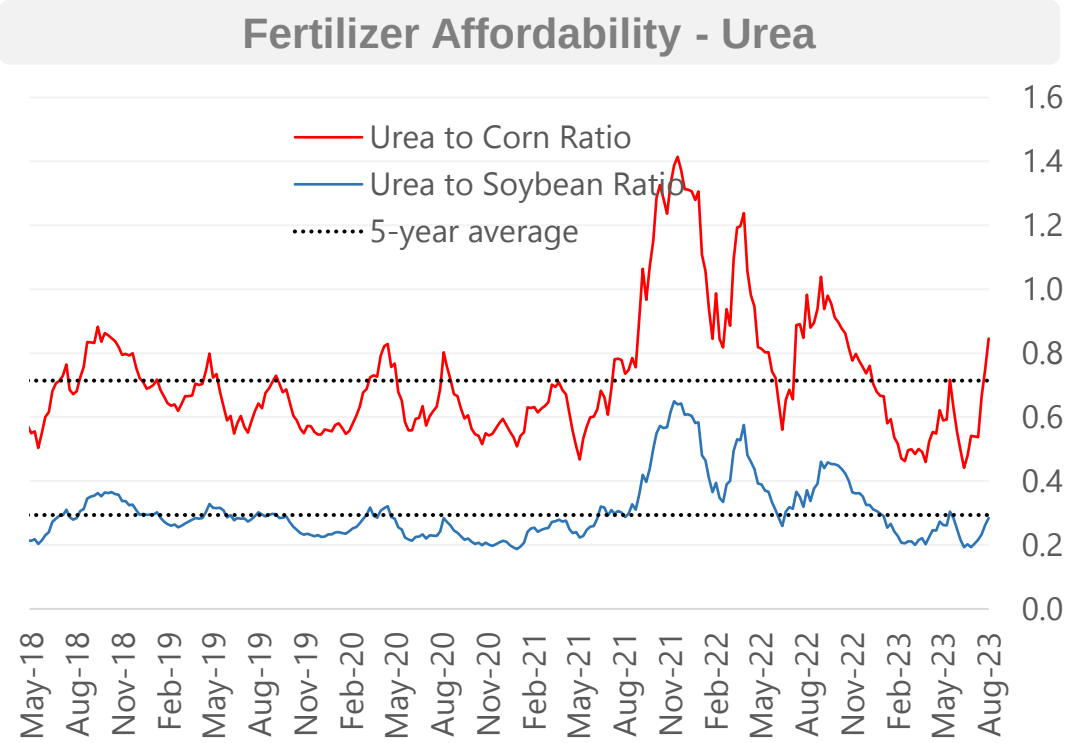
Fertilizers prices (USD/t)



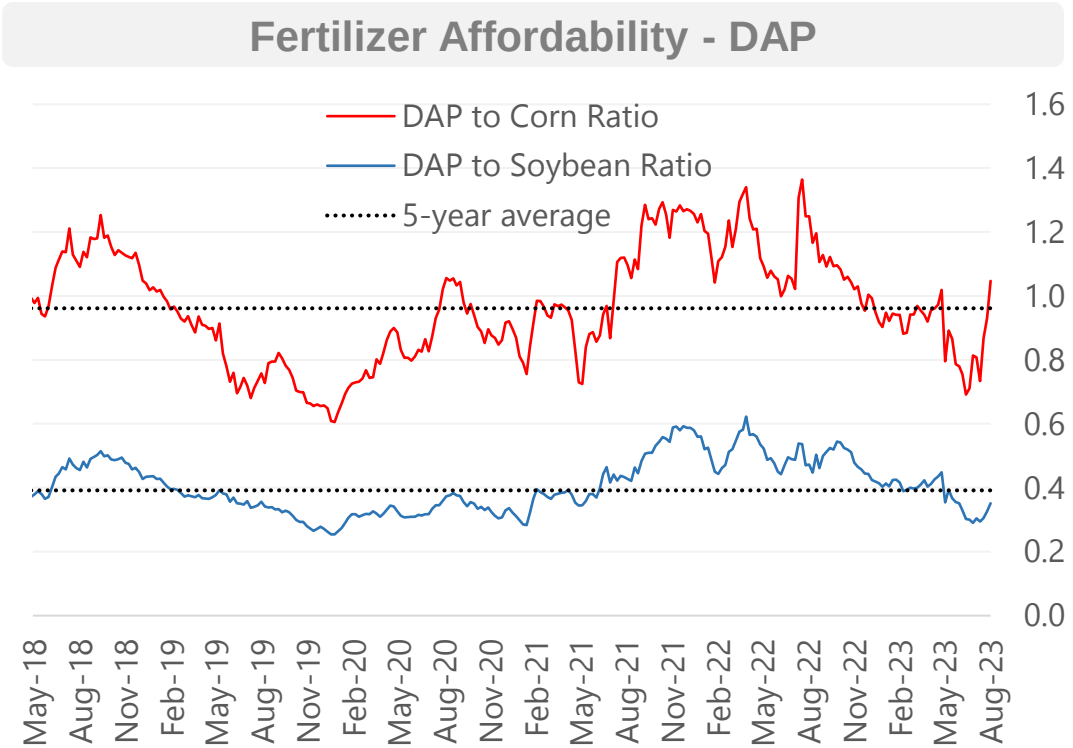
Sources: Bloomberg, Santander.

Agri: Fertilizer affordability climbing to historical average

- The affordability for farmers is returning to historical average, following a period when fertilizer price decline outpaced grain prices decline.
- Still, producers have incentive to both use more fertilizer and increase planted area, hence better prospects for food-inflation.



Sources: Bloomberg, Santander.

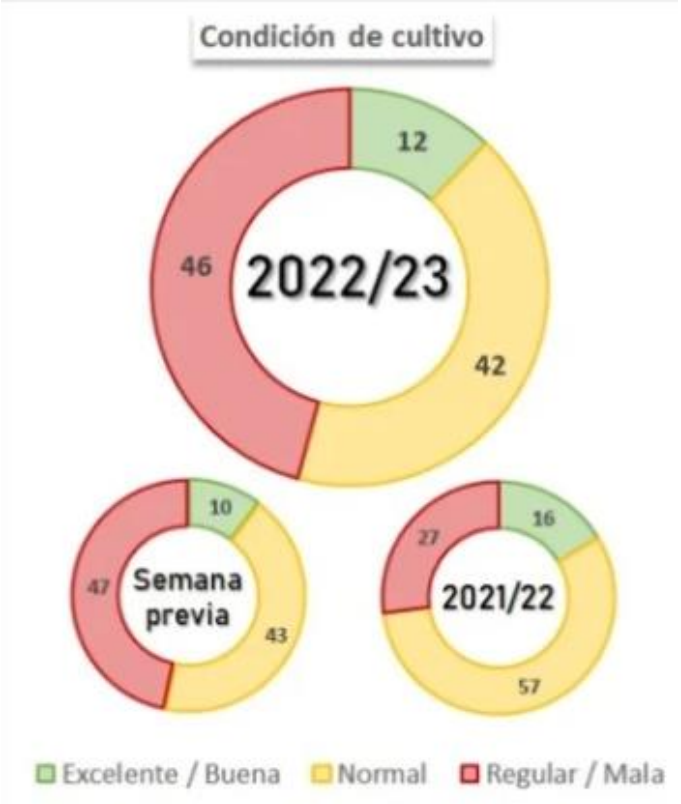


Sources: Bloomberg, Santander.

Agri: High temperature in Argentina help harvest progress

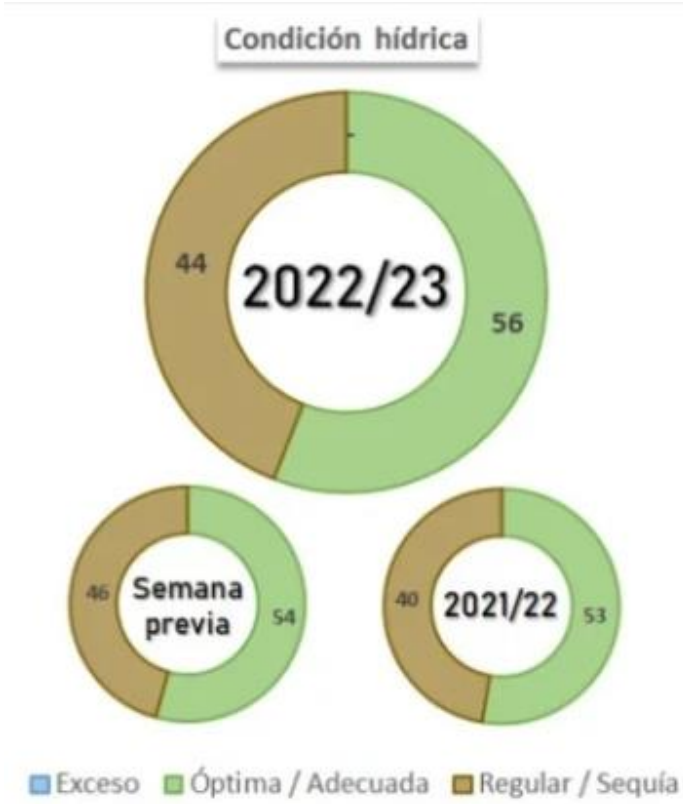
- Professionals from the BCBA (Bolsa de Cereais de Buenos Aires) classify Argentinian corn crops in good or excellent conditions at 12% (up 2 p.p. from last week) in 2022/2023. The condition is below the 16% in 2021/2022. **The estimate for total corn production in Argentina is at 34 million tons, 18 million tons down last year.**

Corn in Argentina - Crop Condition



Sources: BCBA, Santander.

Corn in Argentina – Soil Water Condition

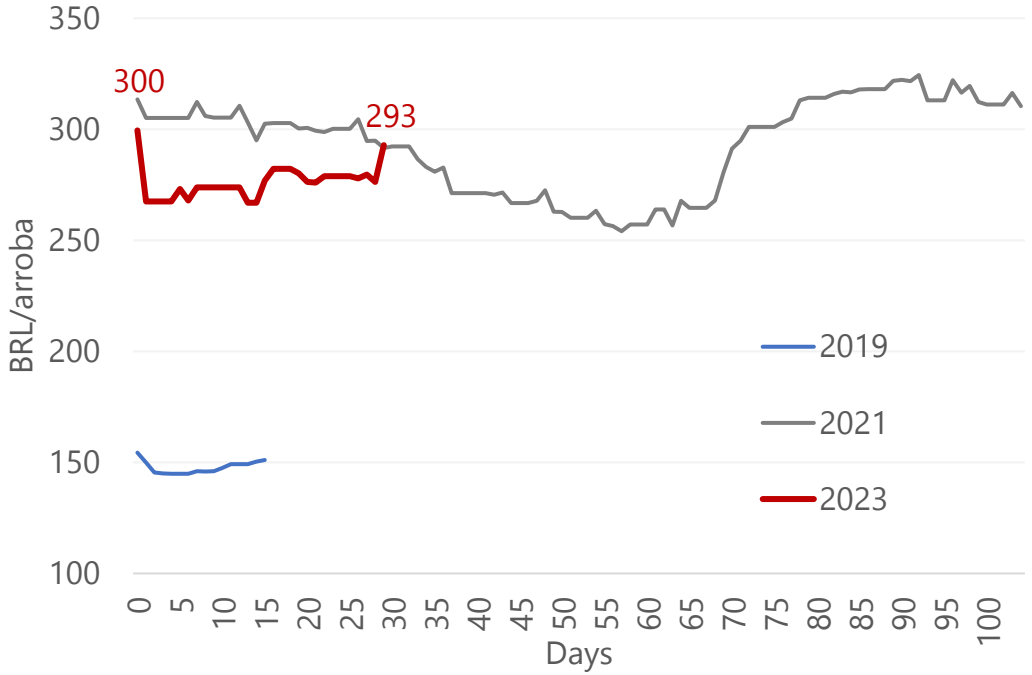


Sources: BCBA, Santander.

Agri: A favorable stage of Brazilian cattle cycle

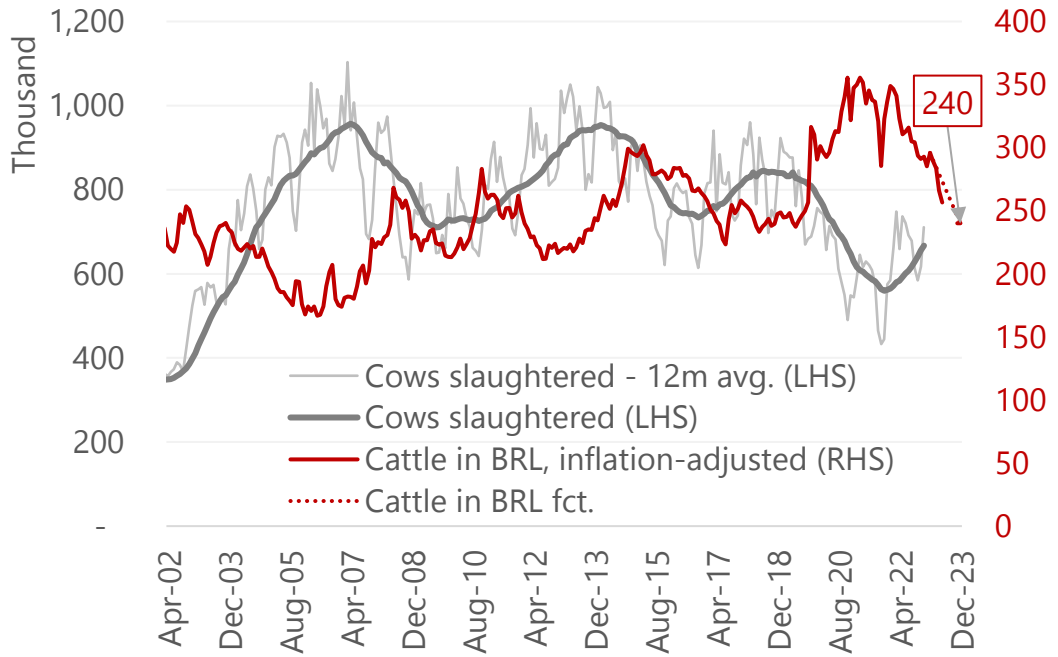
- In Brazil's cattle cycle: a higher percentage of cows is being slaughtered, meaning that more beef is being supplied to the market, helping bring its prices down.
- Taking our estimate of BRL 240/arroba as an input, we forecast that the beef price component of the IPCA (Brazil's official CPI) could see annual deflation of 4% in 2023.

Cattle prices following report of mad cow disease



Sources: Bloomberg, Santander.

Cattle Cycle in Brazil



Sources: IBGE, Bloomberg, Santander.

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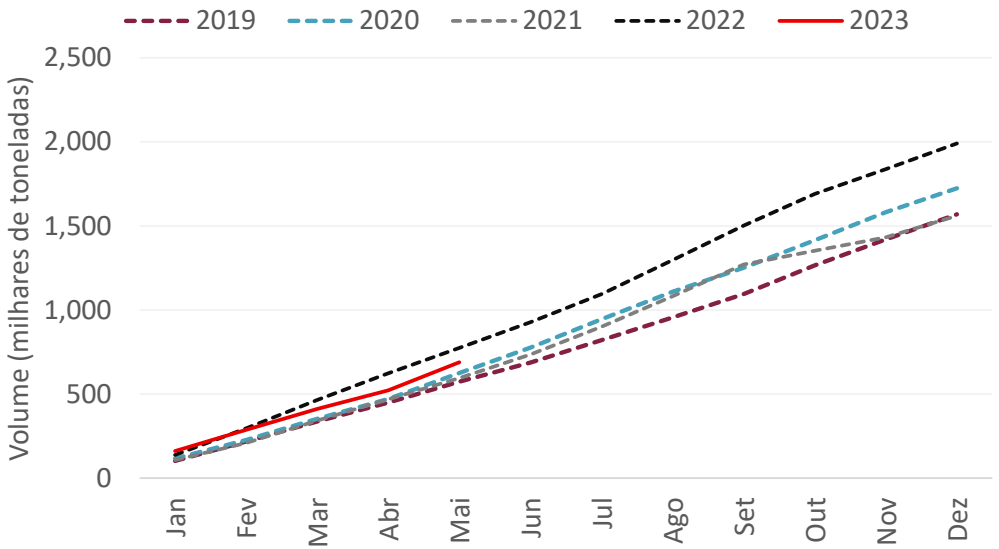
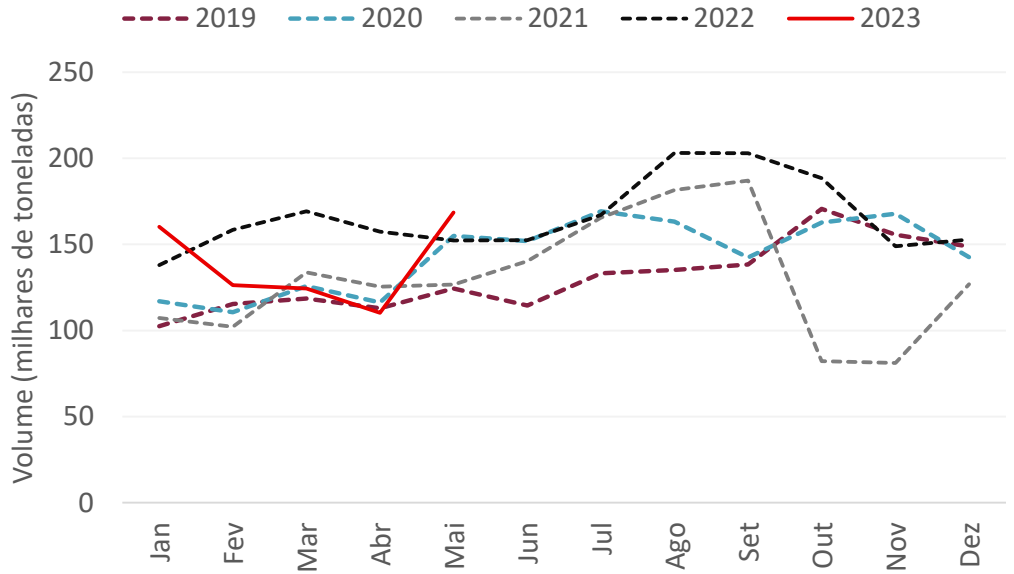
Brazil - Beef export (accumulated)



Sources: SECEX, Santander.

Brazil - Beef export (monthly)



Sources: SECEX, Santander.

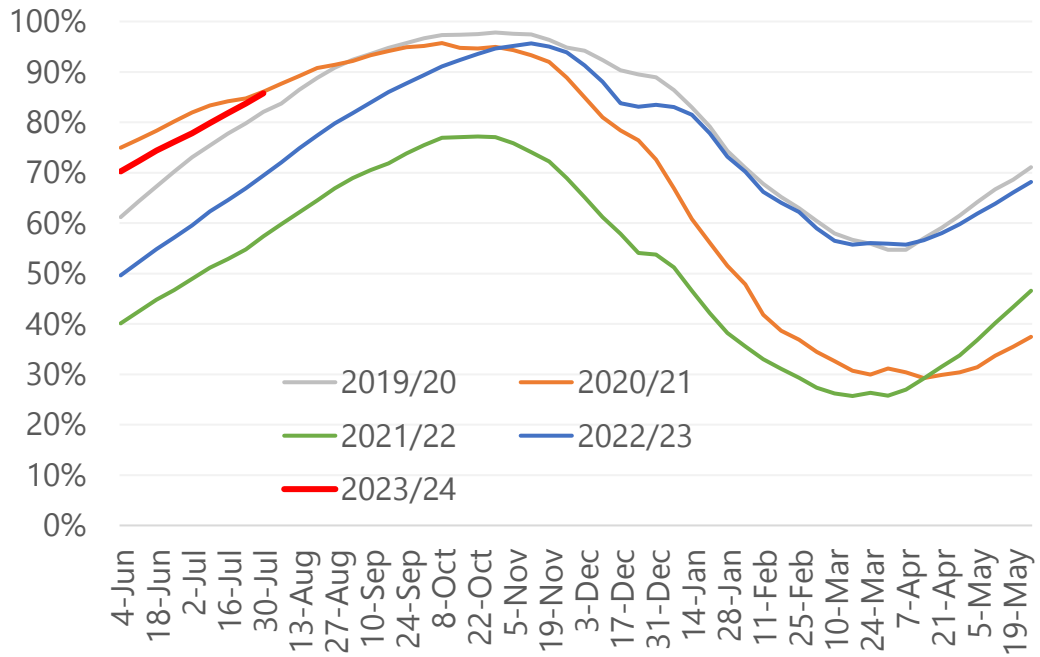
ENERGY

03

Natural gas prices in Europe at comfortable levels given high LNG imports

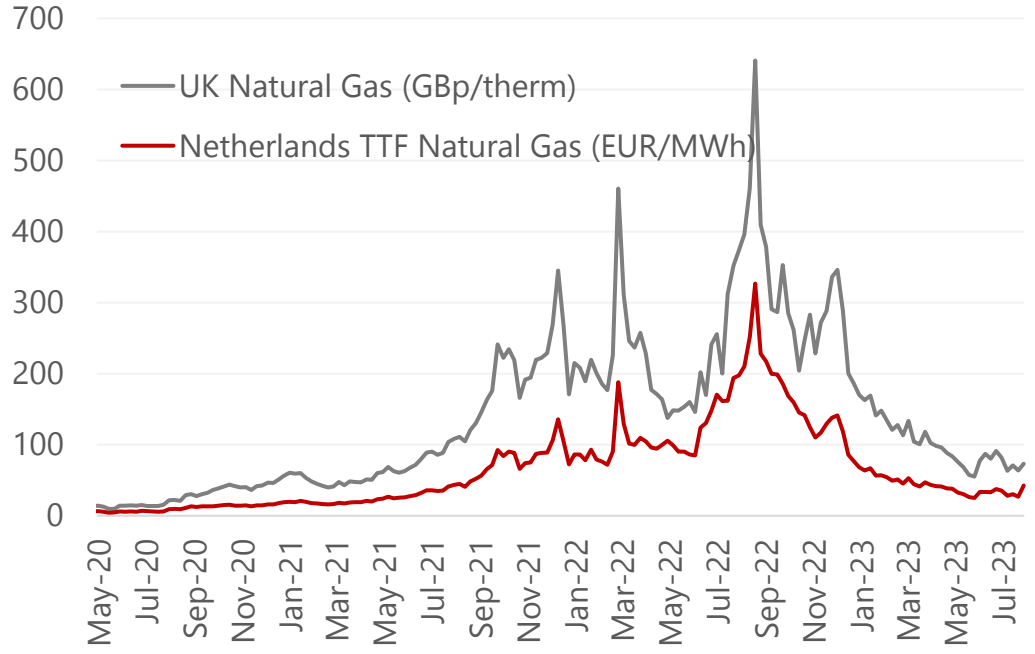
- European gas prices are in 18-month low levels.
- High liquefied natural gas (LNG) imports have contributed to the build of EU gas storage. LNG from the US helped the EU survive last winter (despite warnings of gas shortages, industrial paralysis and compulsory rationing).

European Gas Storage Utilization (%)



Sources: Bloomberg, Santander.

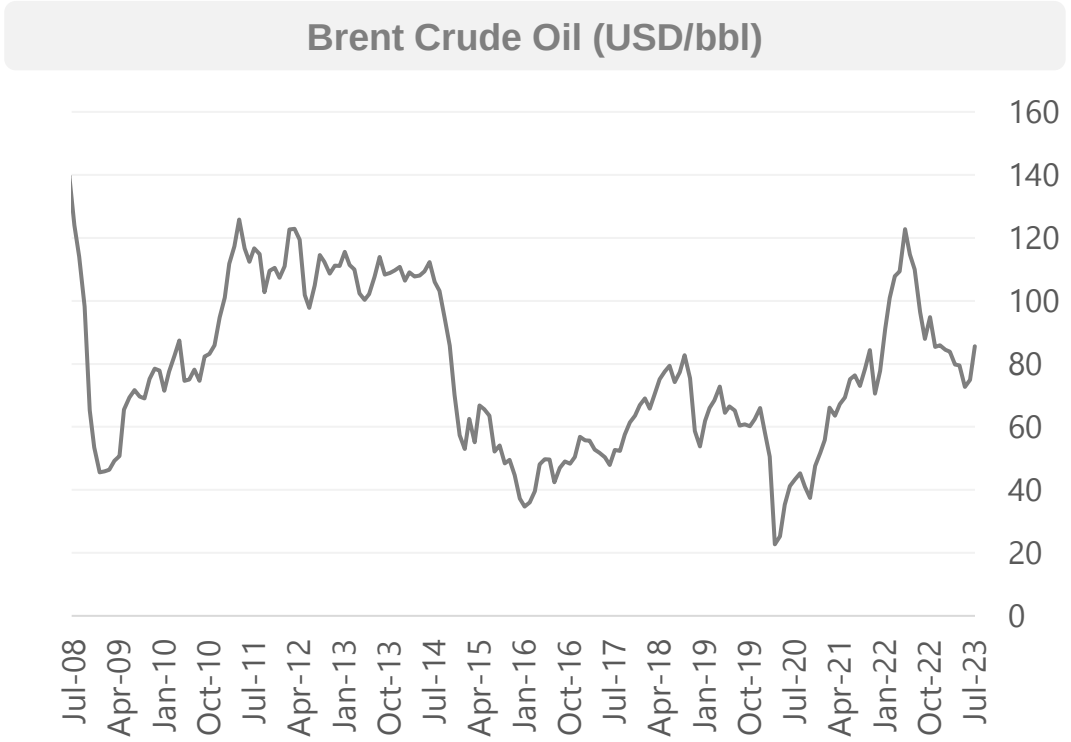
Europe Natural Gas



Sources: Bloomberg, Santander.

Oil: Fundamentals remain bullish, but now with a weak USD tailwind

- In energy, Russian oil flows to Asia surprised market players that expected a tighter global oil balance. At the margin, however, theses flows have been reducing. **Our forecast for Brent oil is at USD 85/bbl for YE2023, and USD 95/bbl for YE2024.**
- Saudi Arabia extended its unilateral 1-million-barrels a day (bpd) oil supply cut into September, while also signaling that deeper reductions could be on the way. In addition, Russia will cut oil exports in September by 300k bpd.



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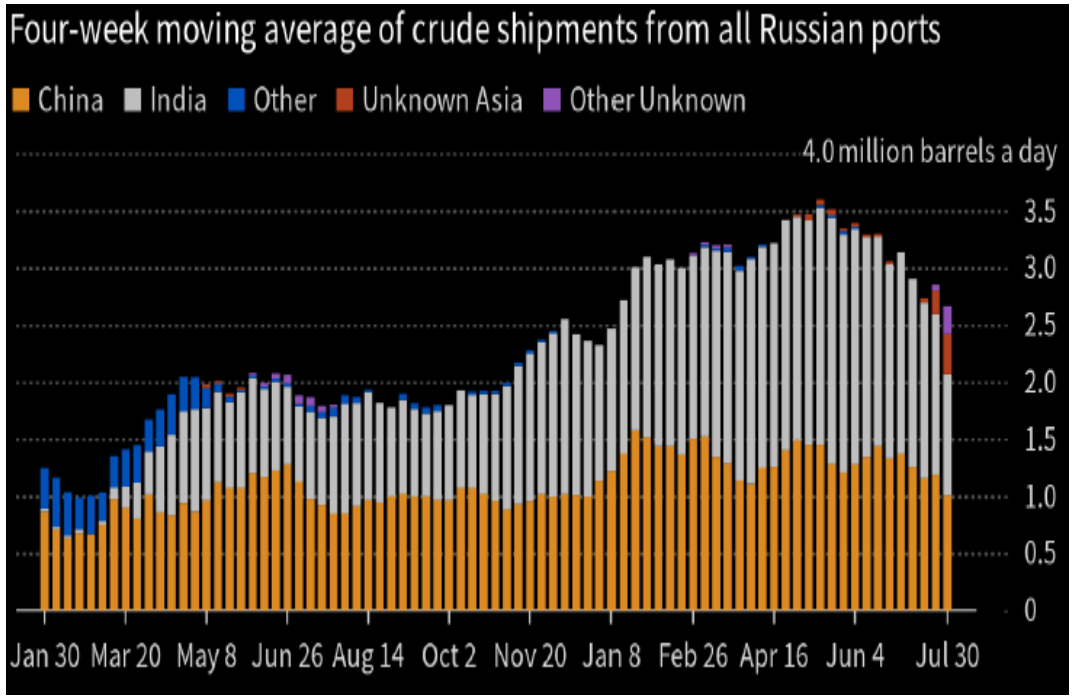
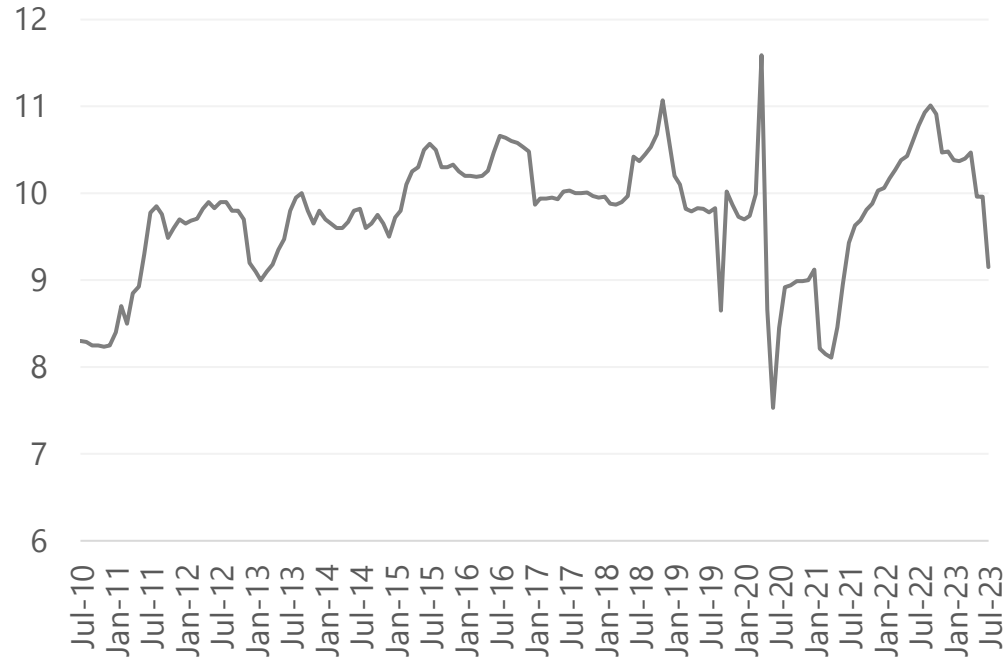
Russia's Asian Customers



Sources: Bloomberg, Santander.

Saudi Arabia Crude Production (million bpd)



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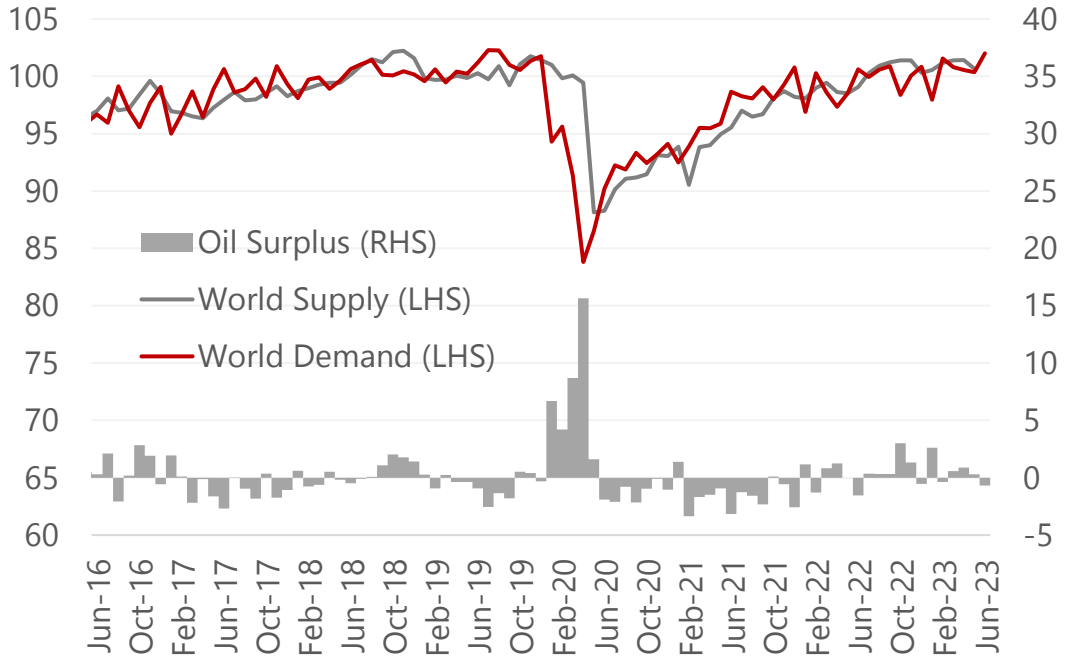
World Oil Supply x Demand (mbd)



Sources: Bloomberg, Santander.

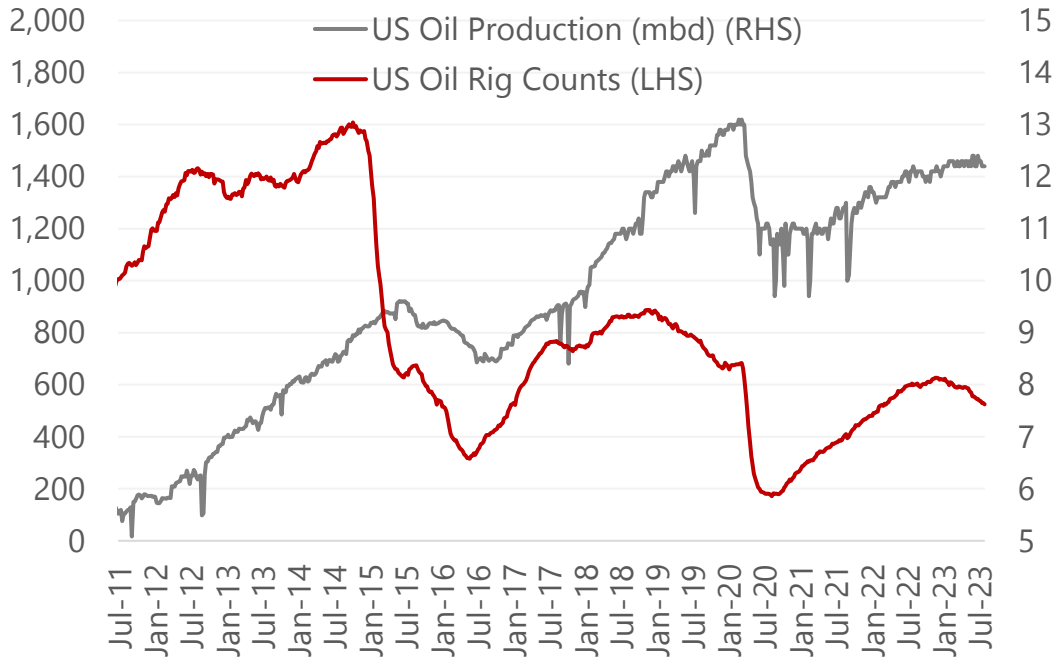
U.S. Total Oil Crude Stocks (million barrels)

Sources: Bloomberg, Santander.

Oil: Fundamentals remain bullish, but now with a weak USD tailwind

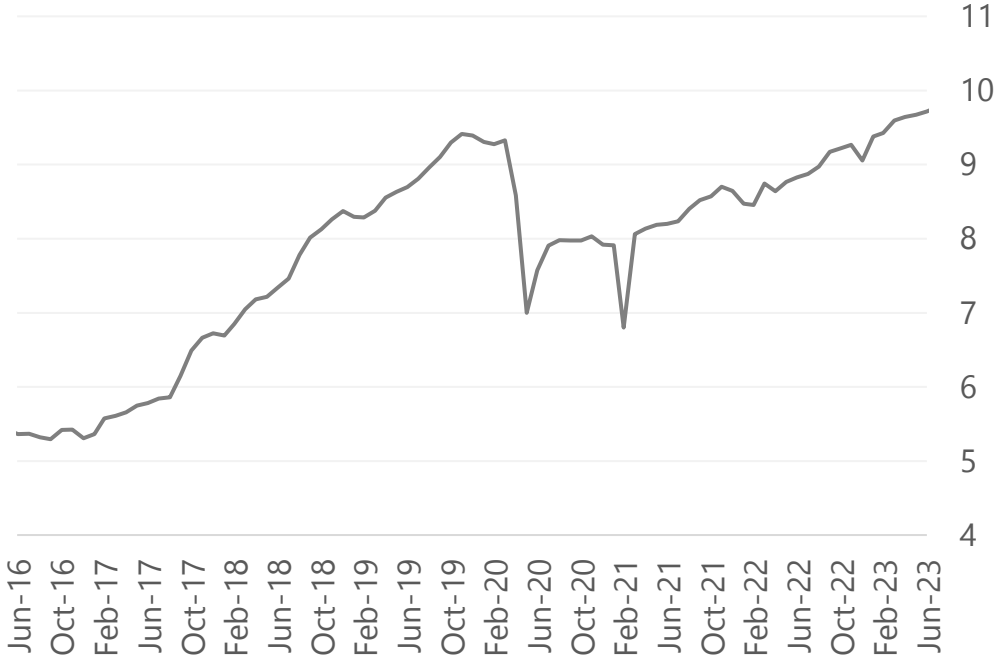
- According to EIA, US shale oil production has likely peaked.
- This should mean more market power for OPEC+.

US Oil Production (Total)



Sources: Bloomberg, Santander.

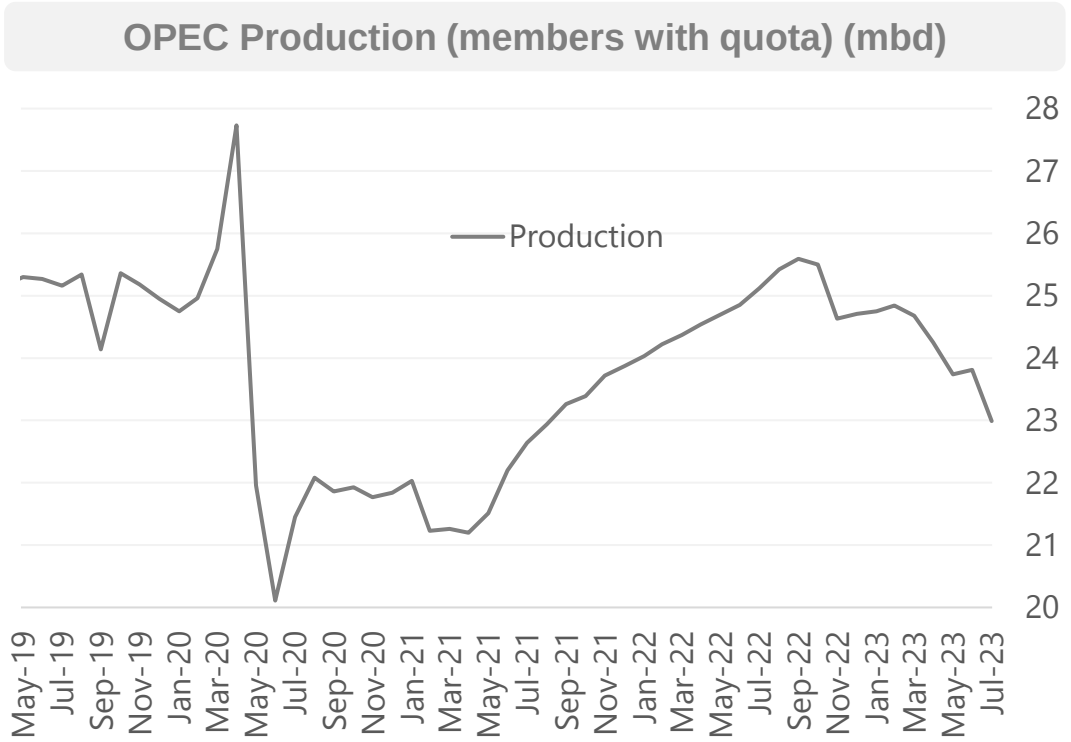
US Shale Production (mbd)



Sources: Bloomberg, Santander.

Oil: Fundamentals remain bullish, but now with a weak USD tailwind

- OPEC+ production in July fell by 900k barrels a day (bpd) to 27.8 million bpd, the largest drop since the organization and its allies cut supplies during the Covid-19 pandemic.
- Following the OPEC+ meeting in early June, Saudi Arabia said it would cut production by another one million barrels per day (bpd), starting in July, and other members of the cartel announced they would extend their oil output voluntary cuts until the end of 2024.

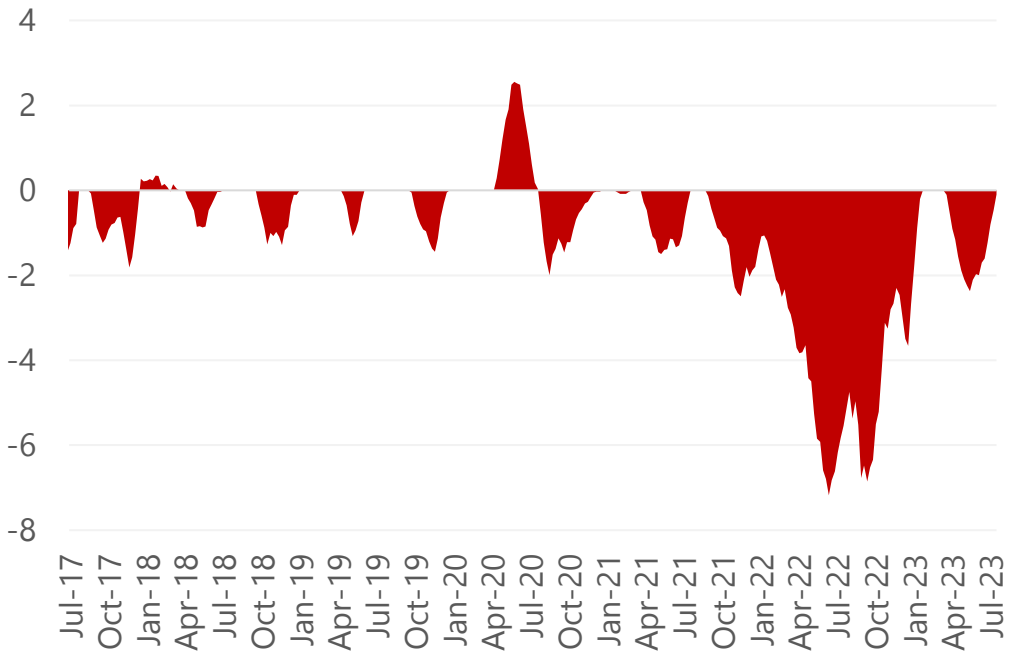


Sources: Bloomberg, Santander.

Oil: U.S. emergency crude stockpiles in the lowest level in 40 years

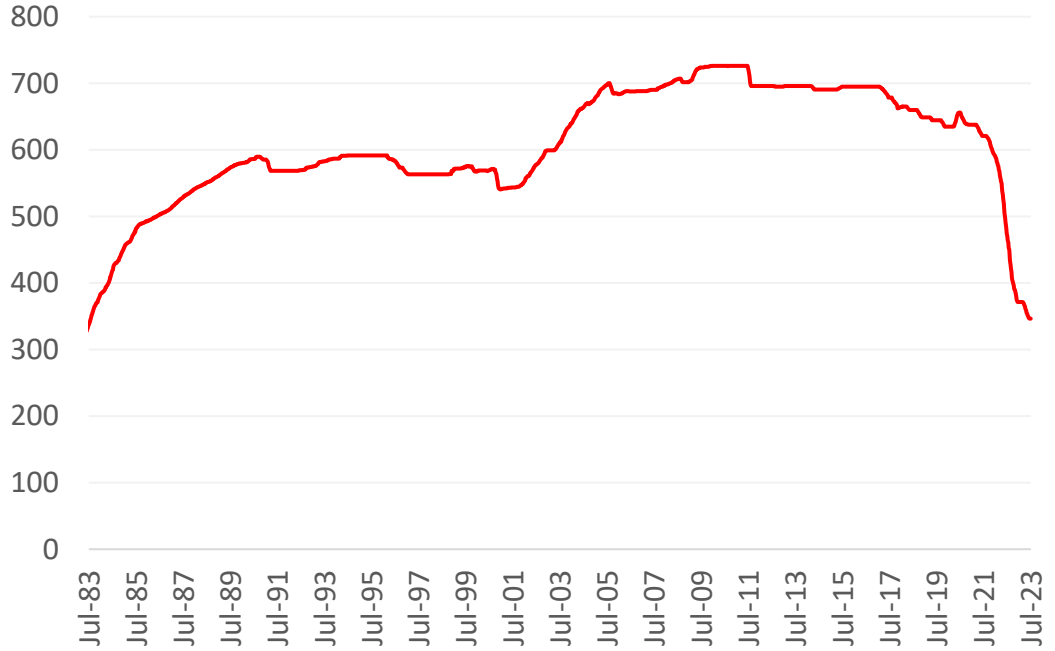
- US is expected to refill its Strategic Petroleum Reserve (SPR) after a historic 180 million-barrel drawdown brought it to about half of its capacity in the aftermath of Russia's invasion of Ukraine.
- The administration has said it wants to buy back oil for the reserve when it costs $67 to $72 per barrel.
- Recently, it pulled back an offer to buy 6 million barrels of oil, a decision made on "market conditions".

Weekly U.S. Change in Crude Oil in SPR (Million Barrels)



Sources: US Department of Energy, Santander.

US Strategic Petroleum Reserves (Million Barrels)

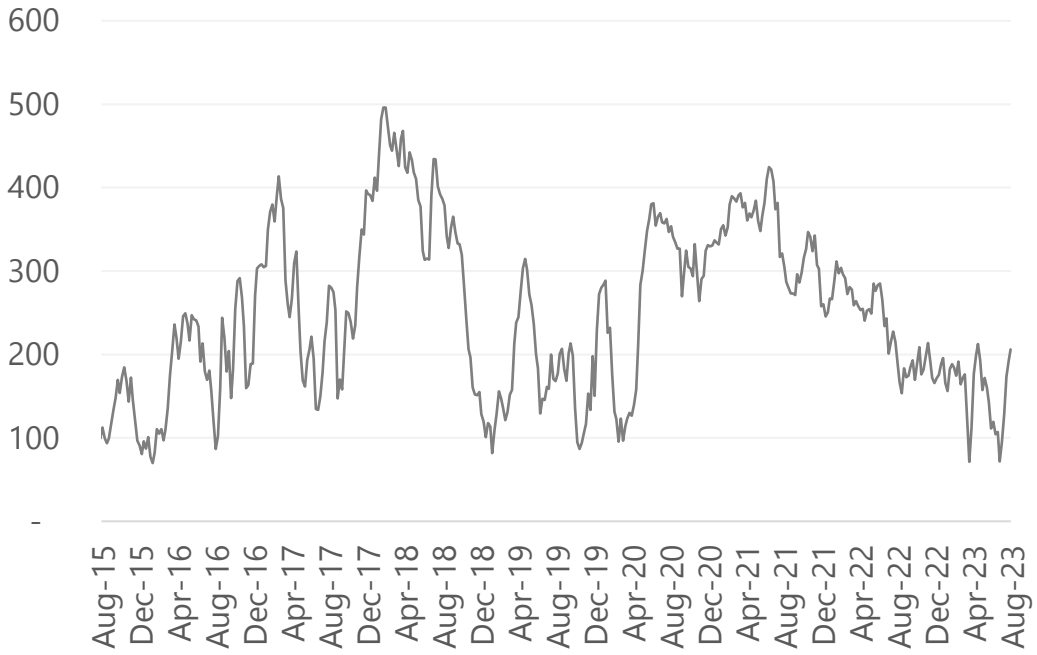


Sources: Bloomberg, Santander.

Oil: Energy agencies outlooks point to a tight market going forward

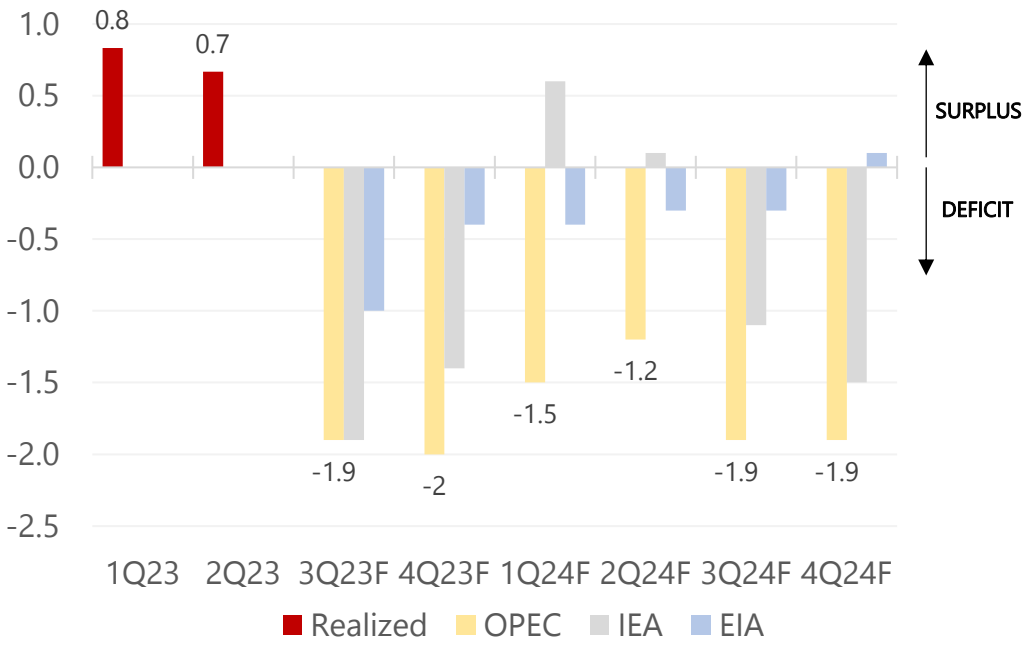
- Speculators raised they net long U.S. crude futures and option positions to the highest level since April 2023.
- Key agency reports forecast a tightening in global oil balance in the coming quarters.

CFTC Crude Oil Managed Money Net Position



Sources: CFTC, Santander.

Global Oil Balance Forecast (million barrels)



Sources: OPEC, IEA, EIA, Santander.

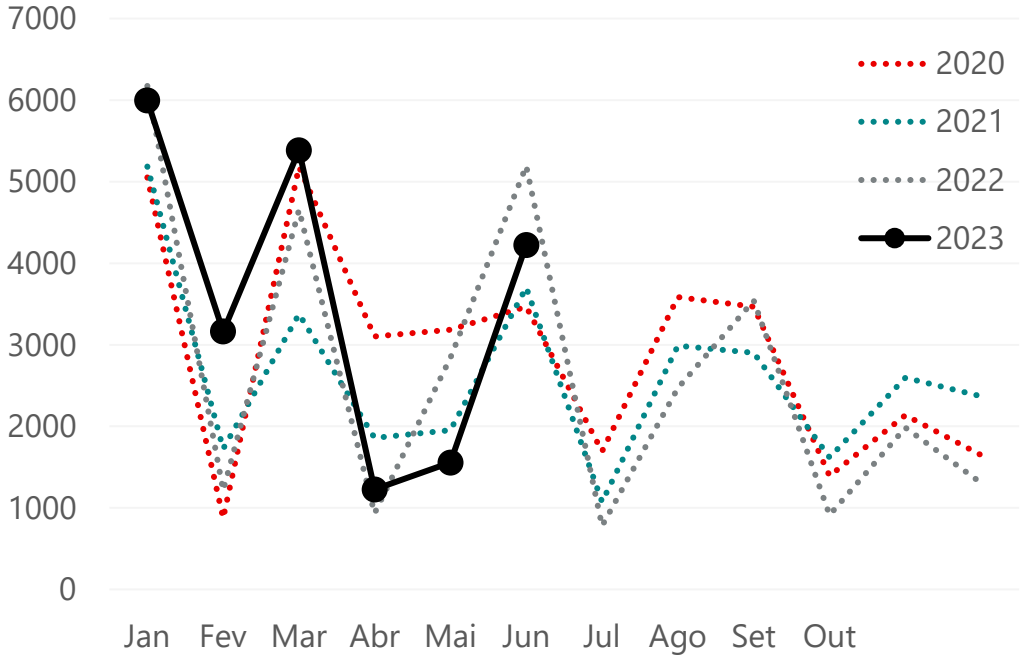
METALS

04

Metals: Chinese recovery disappoints; promises of more stimulus

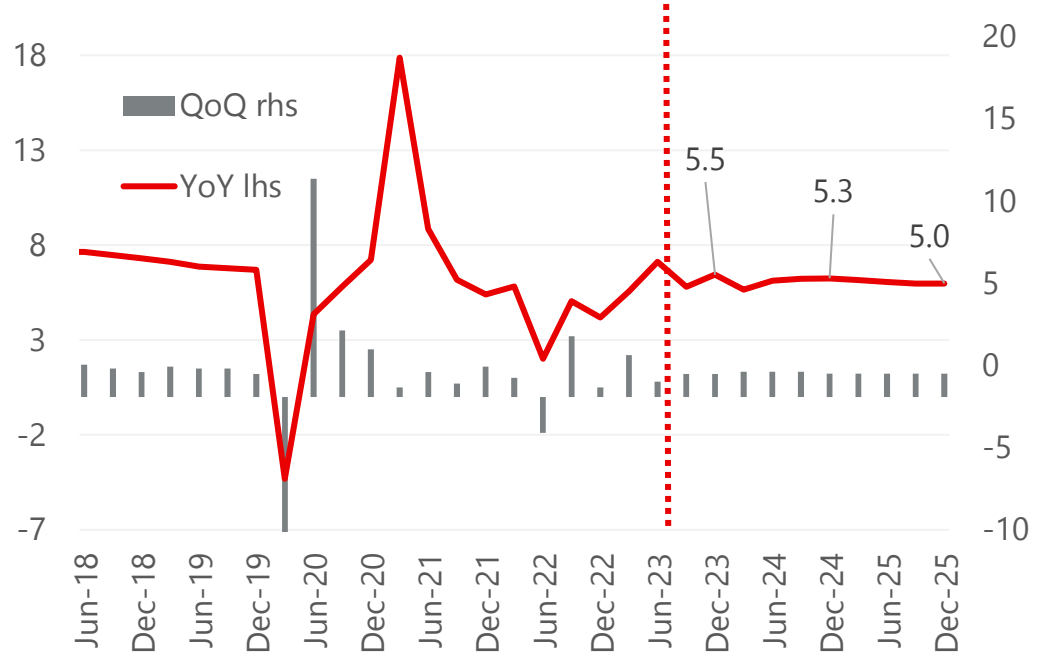
- The reopening had a strong 1Q23, but it lost steam in the 2Q23.
- Target growth (of 5%) will be easily achieved and the government pledges to roll out more measures to spur growth.

Credit expansion surprised on the downside recently



Sources: Bloomberg, Santander.

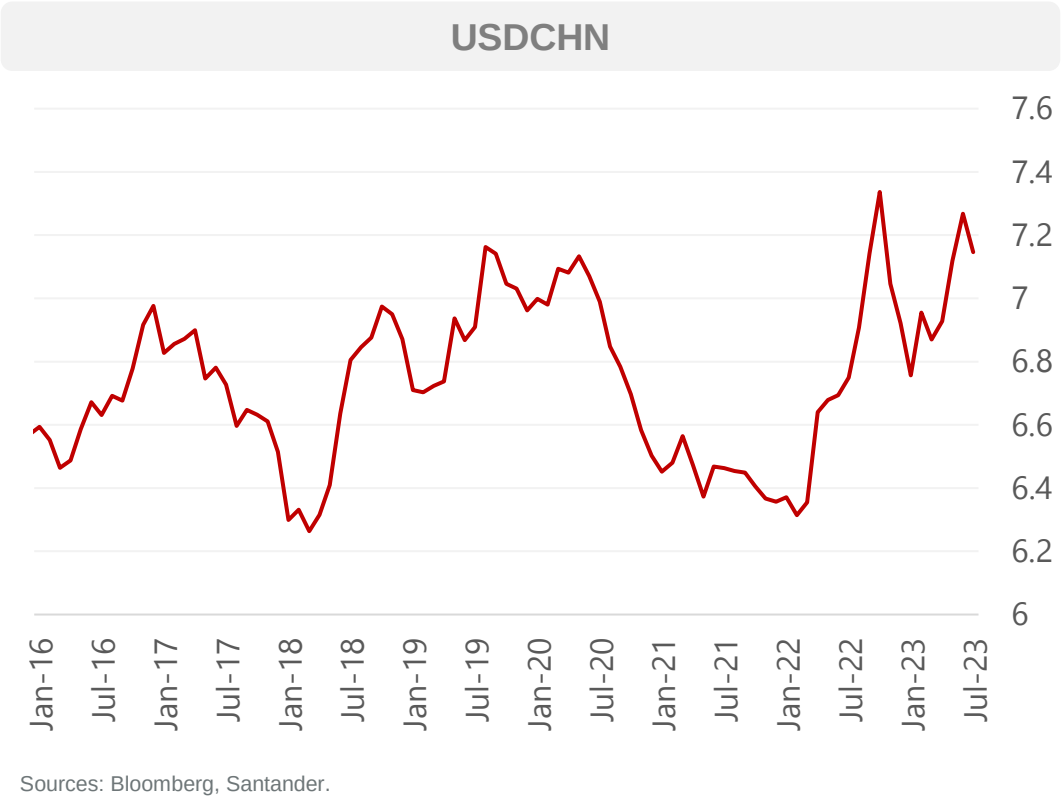
Q2 won't be as strong as previously expected



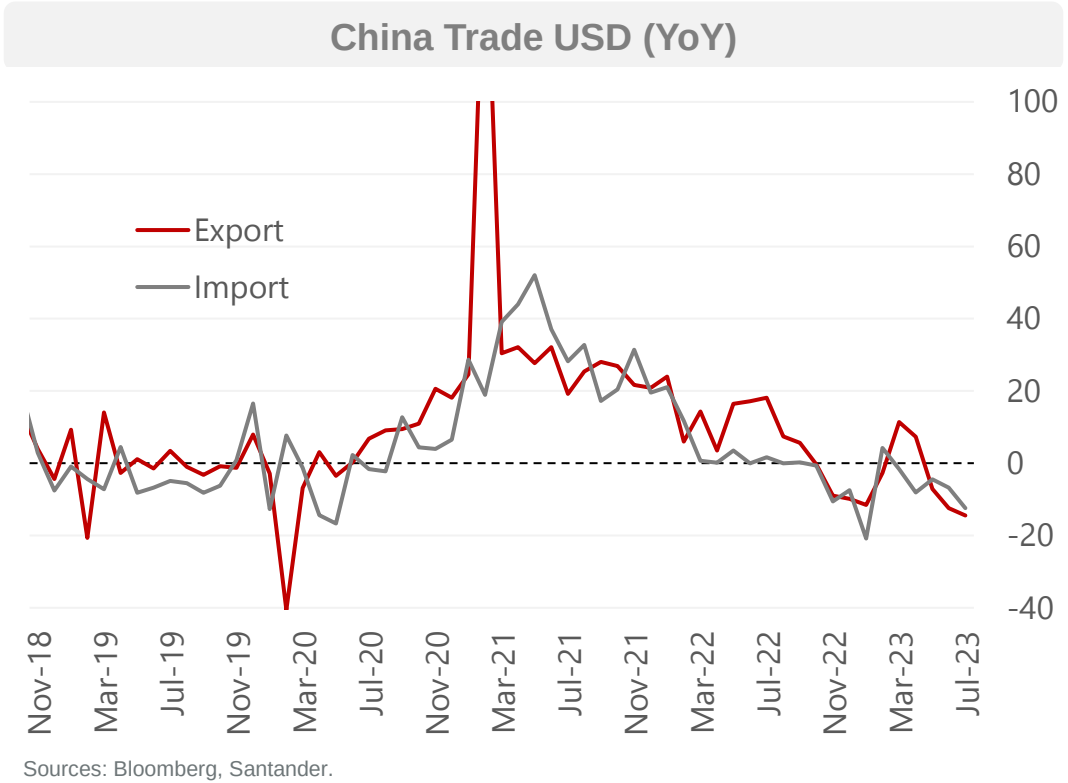
Sources: Bloomberg, Santander.

Metals: Chinese recovery disappoints; promises of more stimulus

- China's imports and exports fell faster than expected in July as weaker demand threatens recovery prospects. The trade numbers reinforce expectations that economic activity could slow further in the third quarter.
- **China’s exports decline was the largest since February 2020 and its imports tumble was the biggest since January 2023.**



Sources: Bloomberg, Santander.

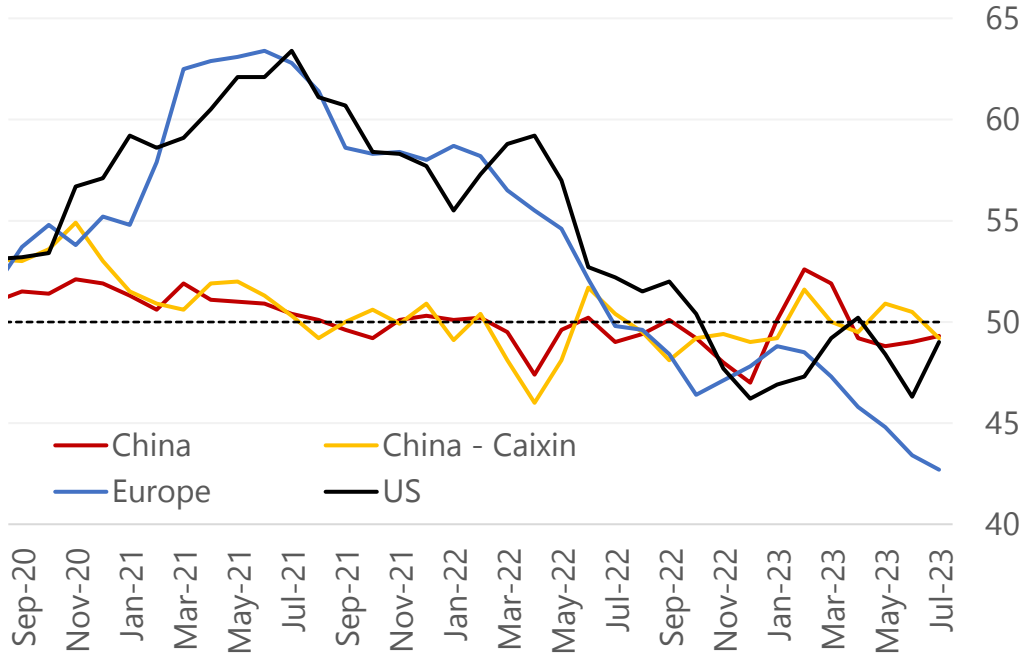


Sources: Bloomberg, Santander.

Metals: Weak Chinese economic data pulls metals prices down

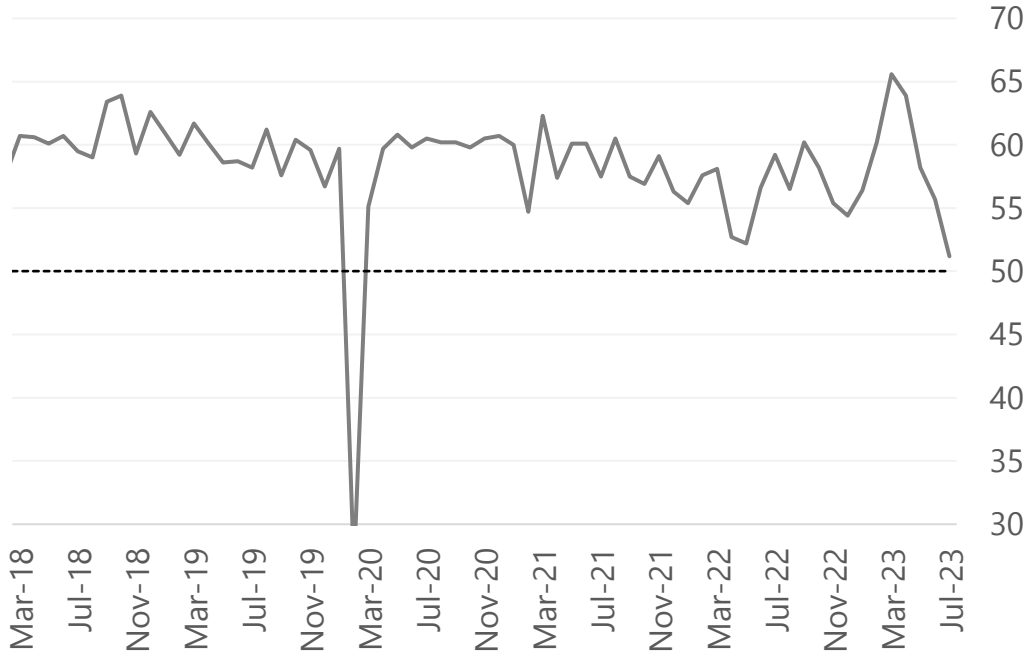
- China's manufacturing activity dropped for a fourth consecutive month in July.
- The sub-index for the key construction sector is down sharply from a high in March.

PMIs Manufacturing



Sources: Bloomberg, Santander.

China - Construction Business Activities Index

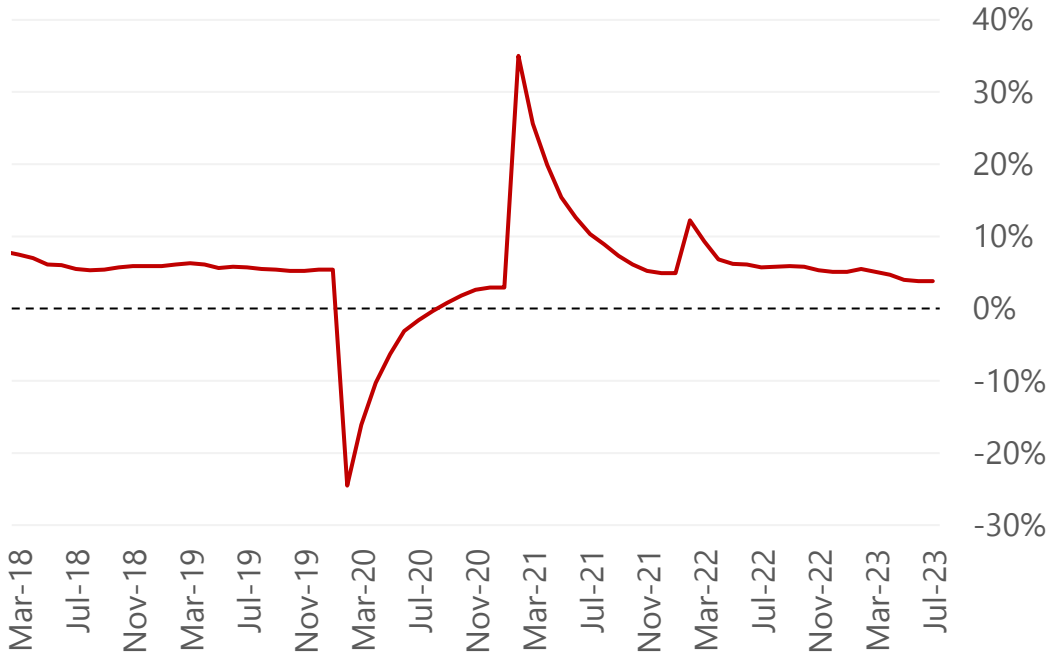


Sources: Bloomberg, Santander.

Metals: Weak Chinese economic data pulls metals prices down

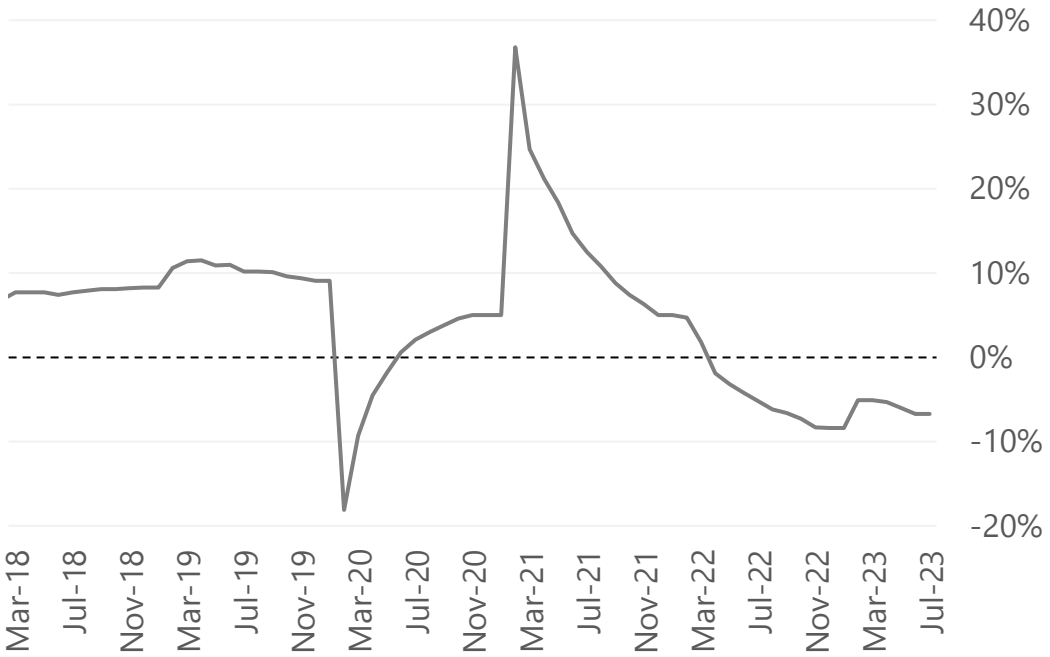
- China's sluggish economic data has been spurring demand concerns. Activity slowed down in Q23 in the absence of relevant stimuli announcements.
- Even with more Chinese government stimuli on the way, especially for the property sector, we believe these will not be enough to sustain a strong recovery in China. **As a result, we expect that the current recovery in metals prices will be short-lived.**

China Fixed Assets Investments (FAI) YoY



Sources: Bloomberg, Santander.

China FAI - Real Estate YoY



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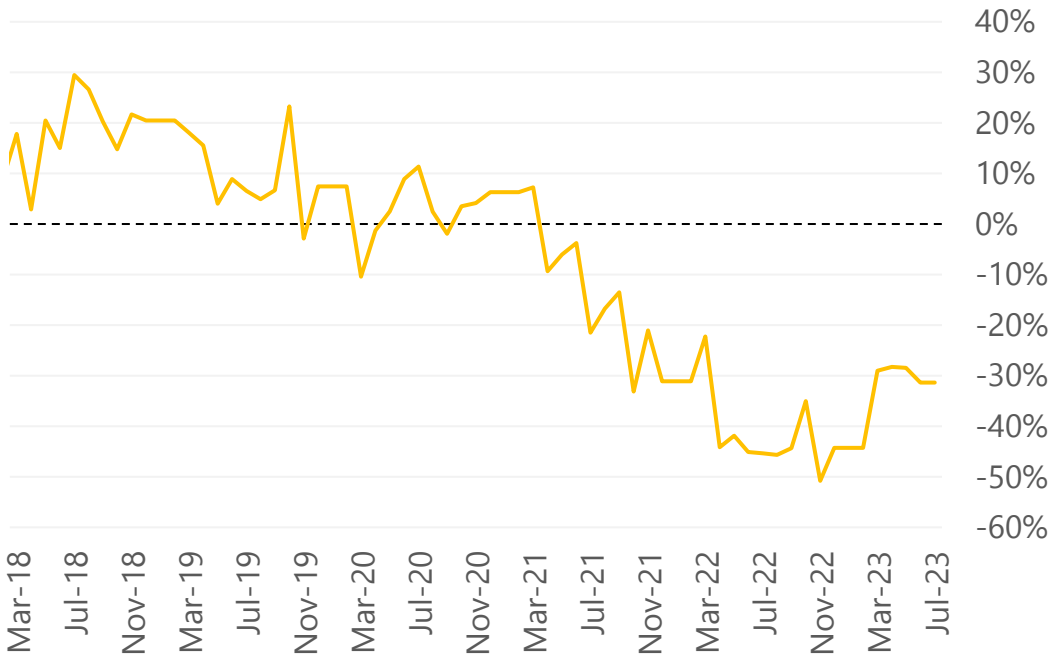
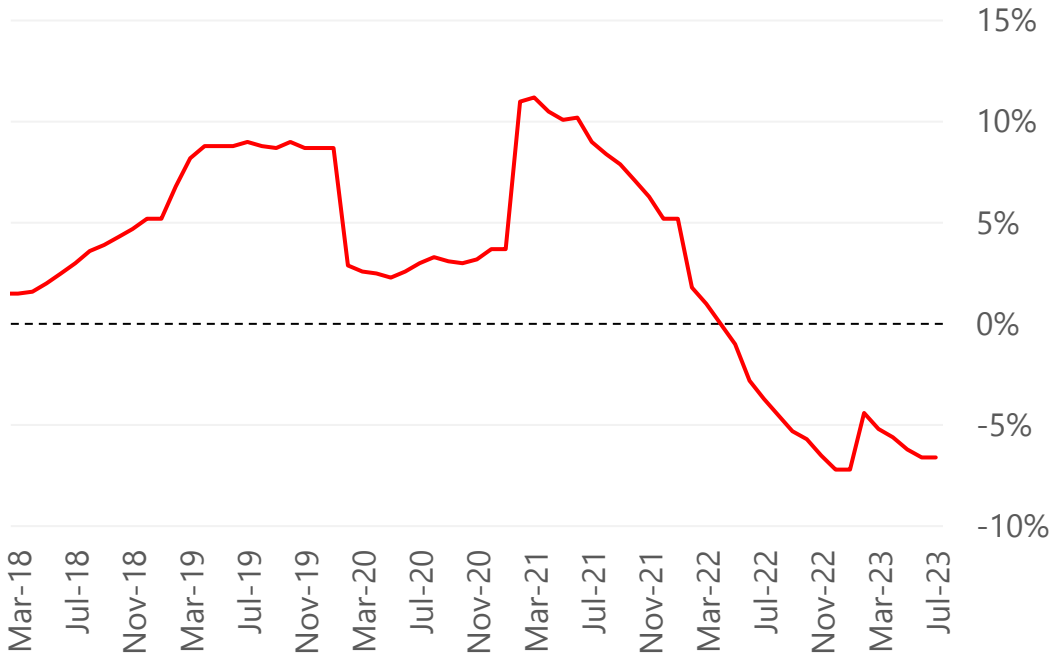
China Property - Floor Space of Houses Newly Started YoY



Sources: Bloomberg, Santander.

China Property -Floor Space of Buildings Under Construction YoY

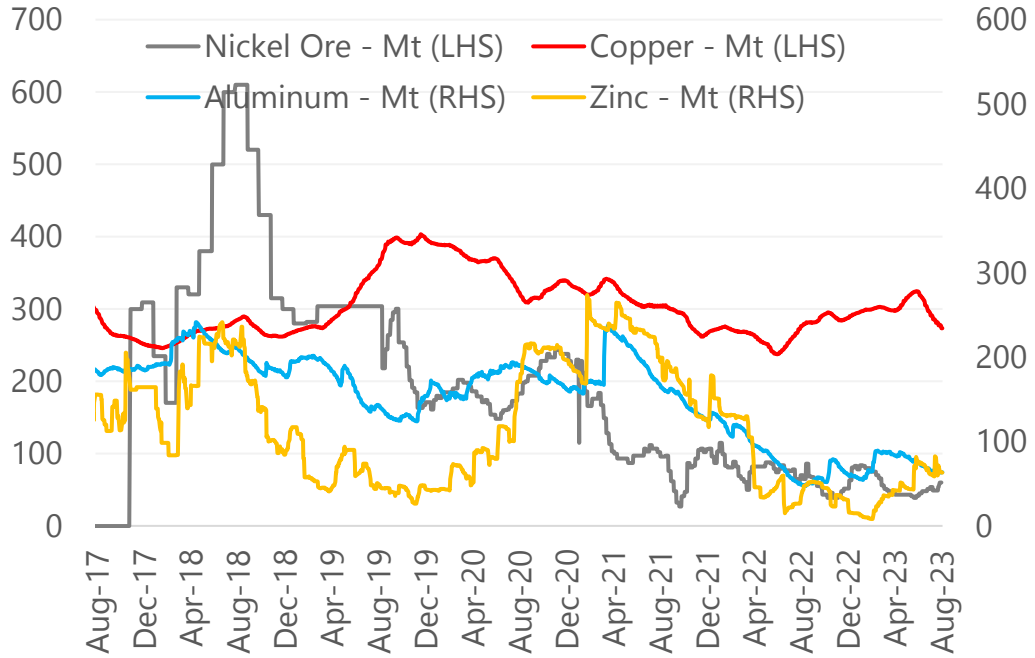


Sources: Bloomberg, Santander.

Metals: Weak Chinese economic data pulls metals prices down

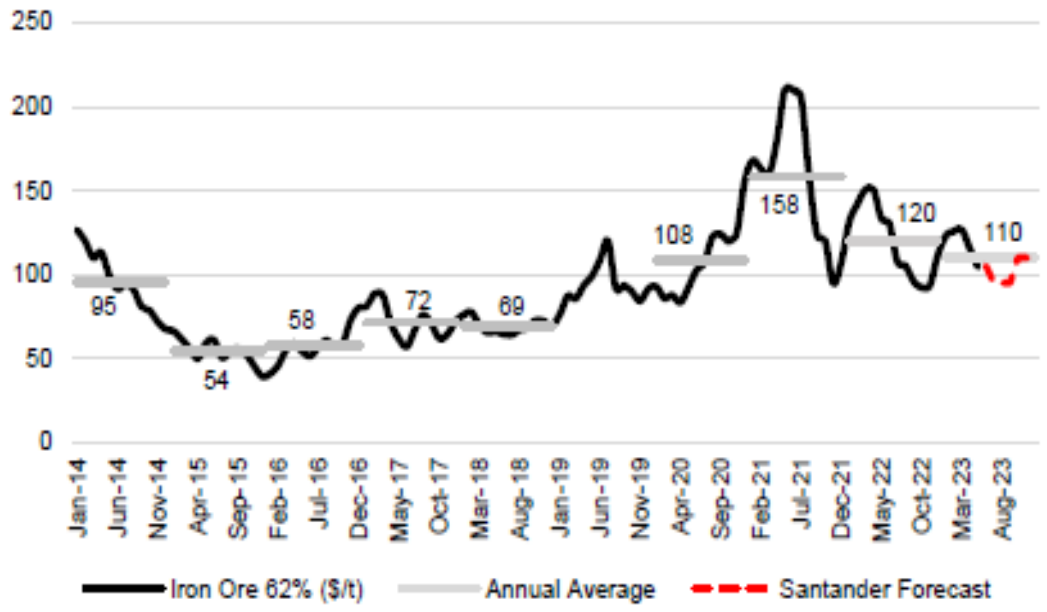
- Metals inventories remain near-record levels, but the weak demand of China is prevailing in the outlook for metals.
- As for iron ore, with exports from key producing countries (Brazil and Australia) flowing at a decent pace, we see little room for further gains in iron prices.

Base Metals Inventories



Sources: Bloomberg, Santander.

Iron Ore Price Forecast



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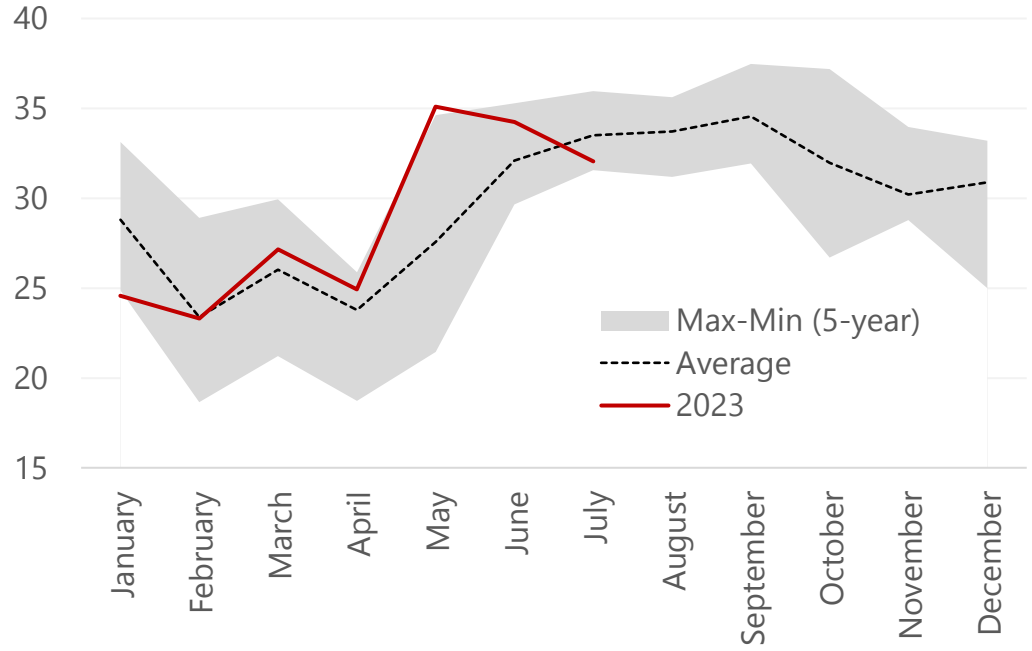
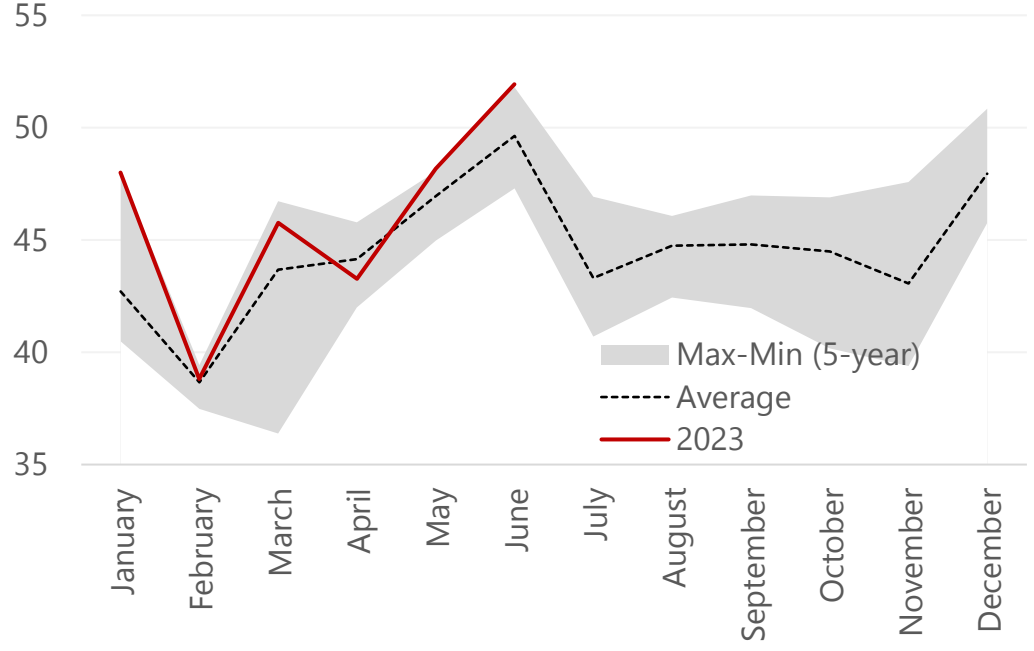
Brazil Iron Ore Monthly Exports (ton)



Sources: Bloomberg, Santander.

Australia Iron Ore Monthly Exports (ton)



Sources: Bloomberg, Santander.

Thank you.

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Our culture is based on believing that everything we do should be:

Simple Personal Fair

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