Brazil Macro | July 2023

Commodities

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SUMMARY

While the macro backdrop for commodities remains unchanged, idiosyncratic factors are helping commodities cool down. Fears of a potential global recession linger — as the monetary tightening promoted by the main central banks is expected to cause a deceleration in global activity — but two specific factors have been driving down raw material prices of late. They are: (i) record grain output in key producing countries; and (ii) unexpected consolidation of the global oil map, with Russian oil flowing to Asia. Given that the expected imbalance in oil markets following the Western sanctions seems less likely now, we lowered our forecast for Brent oil to USD 85/bbl (from USD 95/bbl) for YE2023. As a result, we have downgraded our aggregate commodity index for the same period. In general, however, supply issues persist for many materials, with the CRB Index still running ~30% above pre-pandemic levels. We expect a gradual decline in material costs in the coming years, as global demand softens and aggregate supply gradually catches up.

OVERVIEW

01

Materials: Idiosyncratic Factors Playing Out in Cooling Commodity Prices

- While the macro backdrop for commodities remains the same, idiosyncratic factors are helping commodities cool down.
- As a result, we have downgraded our aggregate commodity index for the same period. In general, however, supply issues persist for many materials, with the CRB Index still running 28% above pre-pandemic levels.

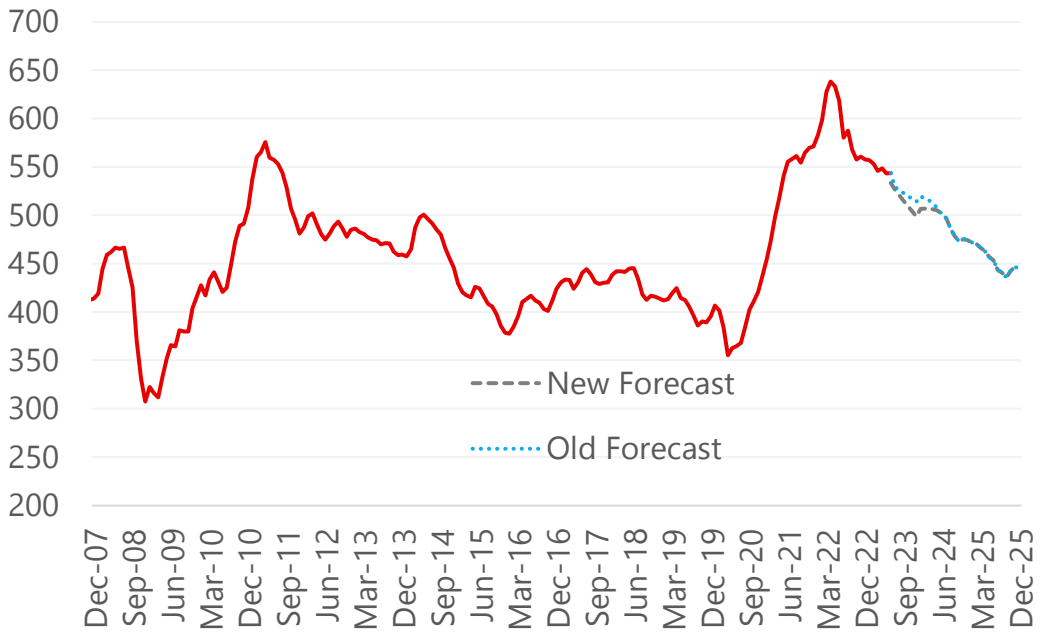
Our Forecasts for CRB Index – End of Period

YE	2021	2022	2023e	2024e	2025e
CRB Food	483	539	431 ➡	395 ➡	371 ➡
CRB Energy	1521	2078	1677 ⬇	1724 ➡	1619 ➡
CRB Metal	1259	1010	1060 ➡	977 ➡	918 ➡
CRB	571	558	498 ⬇	474 ➡	445 ➡

YE YoY	2021	2022	2023e	2024e	2025e
CRB Food	36%	12%	-20%	-8%	-6%
CRB Energy	31%	37%	-19%	3%	-6%
CRB Metal	42%	-20%	5%	-8%	-6%
CRB	29%	-2%	-11%	-5%	-6%

Sources: Santander.

Our Forecasts for CRB Index – Monthly Averages



Sources: Bloomberg, Santander.

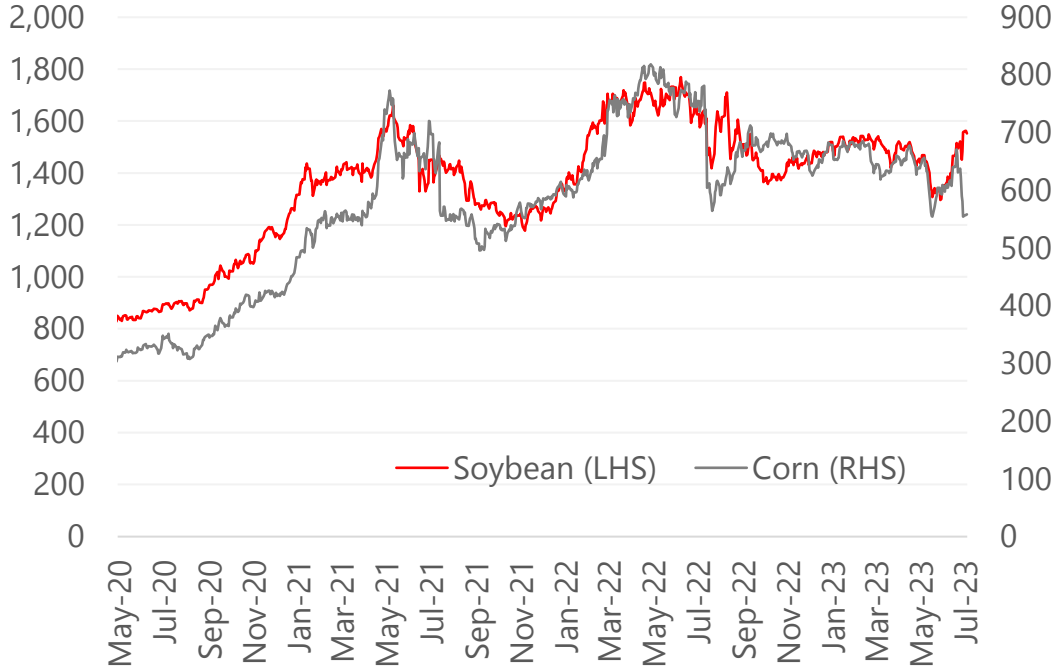
AGRICULTURE

02

Agri: A transition to El Niño Amid a Record Brazilian Grain Output

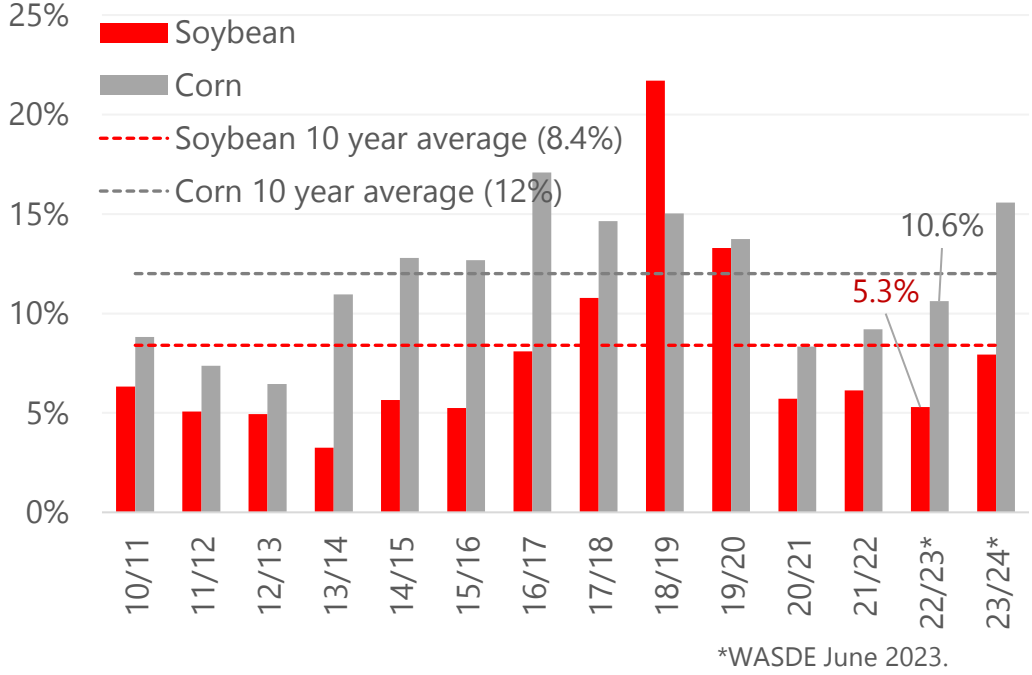
- For agricultural commodities, Brazil is set for record soybean and corn output as a result of favorable growing conditions across most of the country. In the U.S., despite planting ahead of schedule, this growing season is just getting started as a drought expands across the Corn Belt — the eastern part of the region has just experienced one of the driest Mays on record.
- In Europe, on May 17 the grain corridor in the Black Sea was extended for another 60 days, and these extra supplies from Ukraine are expected to continue help global food balances.

Chicago Board of Trade - Grains (USD cents)



Sources: Bloomberg, Santander.

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

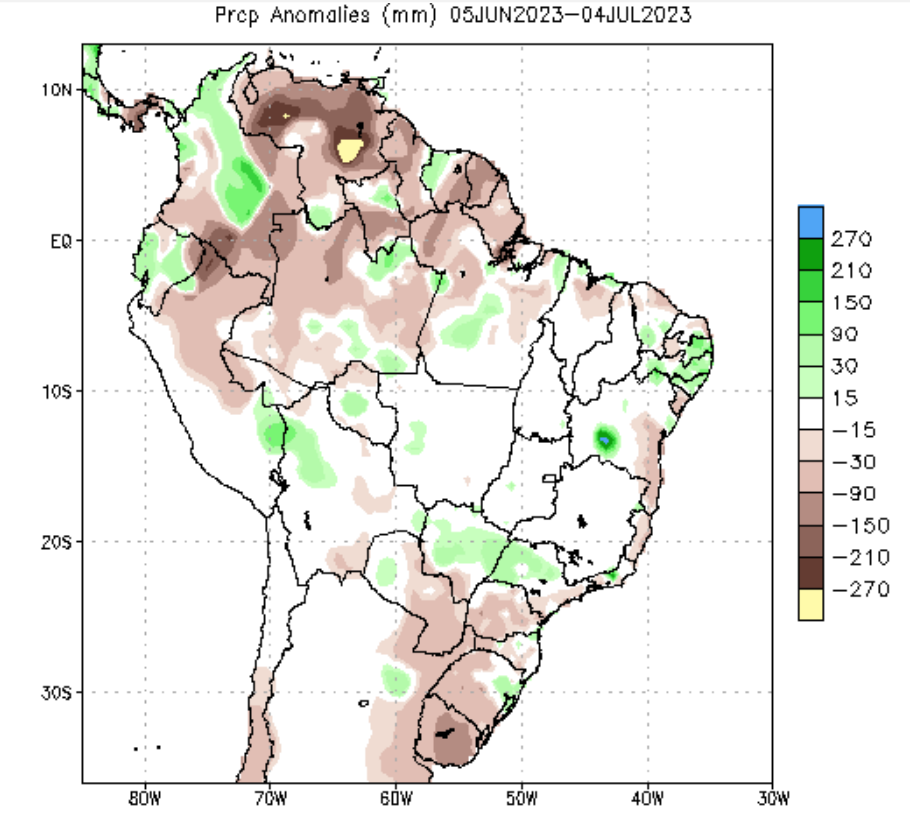


Sources: USDA, Santander.

Agri: A transition to El Niño Amid a Record Brazilian Grain Output

- While crop productivity has been low in Argentina on the back of a severe drought hitting the country, Brazil is set for a record soybean and corn output in several states.

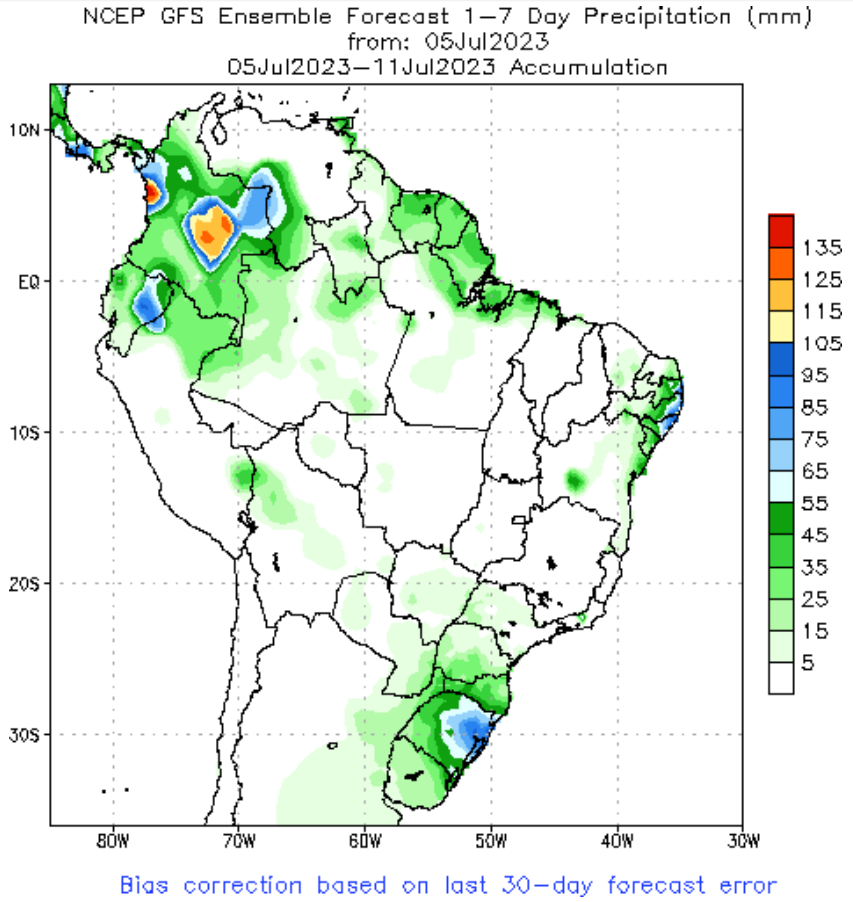
Precipitation (30-day anomaly)



Data Source: CPC Unified (gauge–based & 0.5x0.5 deg resolution) Precipitation Analysis Climatology (1991–2020)

Sources: NOAA, Santander.

GFS Precipitation Forecasts (7-day anomaly)

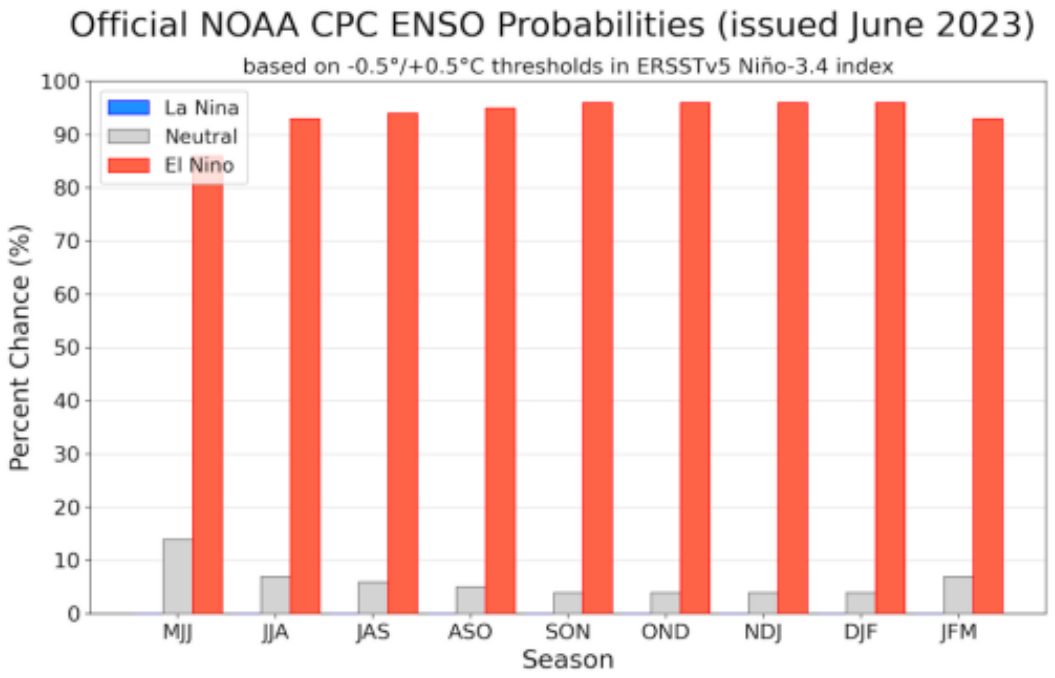


Sources: NOAA, Santander.

Agri: A transition to El Niño Amid a Record Brazilian Grain Output

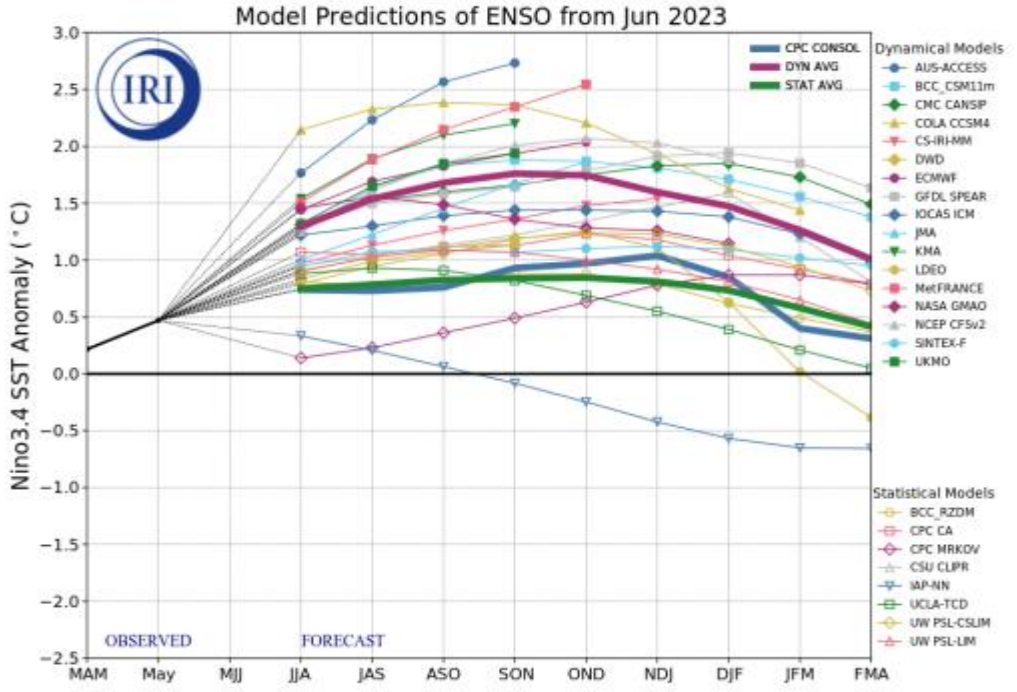
- El Niño is favored through Northern Hemisphere winter 2023-24, with chances exceeding 90% for most of the period.
- Nearly all models indicate El Niño will persist into the Northern Hemisphere winter 2023-24. A strong El Niño (ONI values at or greater than 1.5ºC) is indicated by the dynamical model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

Official NOAA ENSO Probabilities



Sources: NOAA, Santander.

Model Predictions of ENSO

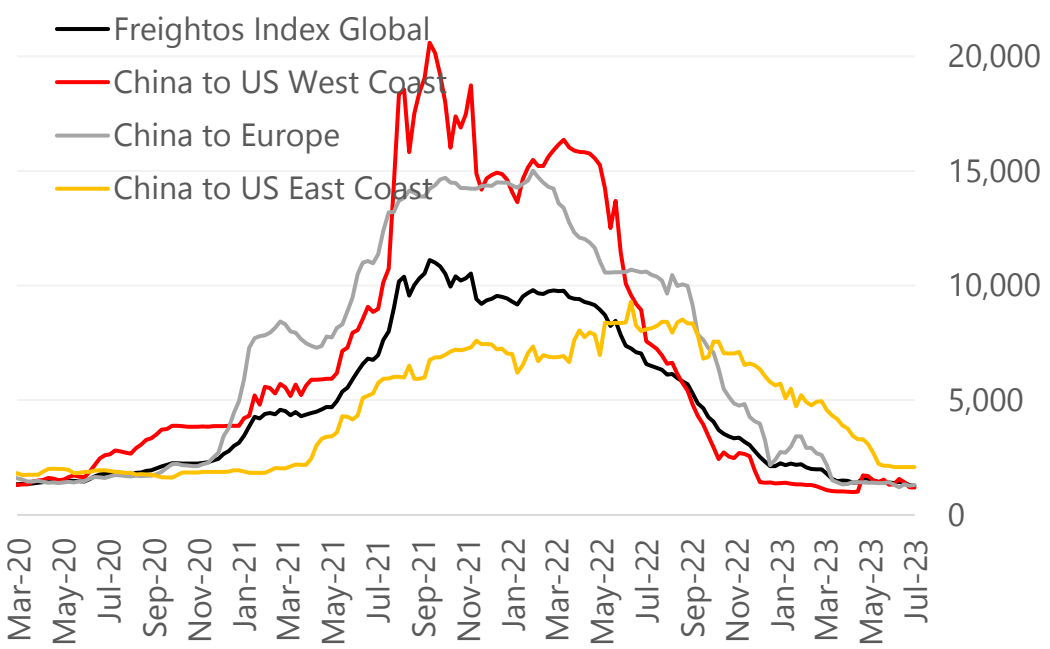


Sources: NOAA, Santander.

Agri: A transition to El Niño Amid a Record Brazilian Grain Output

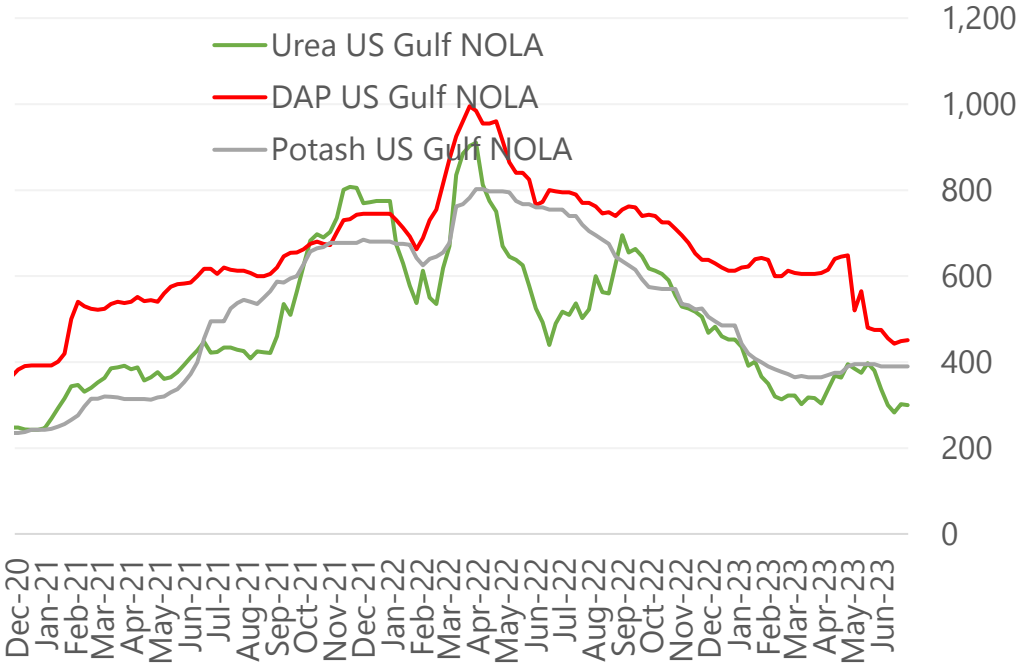
- Freight cost proxies continue to fall at the margin (helping deflation prints), with routes already back to pre-pandemic levels. This suggests that the supply chain problems triggered by the pandemic continue to ease.
- Fertilizers prices were rising, but DAP recently plunged at the margin.

Freight Costs Index



Sources: Bloomberg, Santander.

Fertilizers prices (USD/t)



Sources: Bloomberg, Santander.

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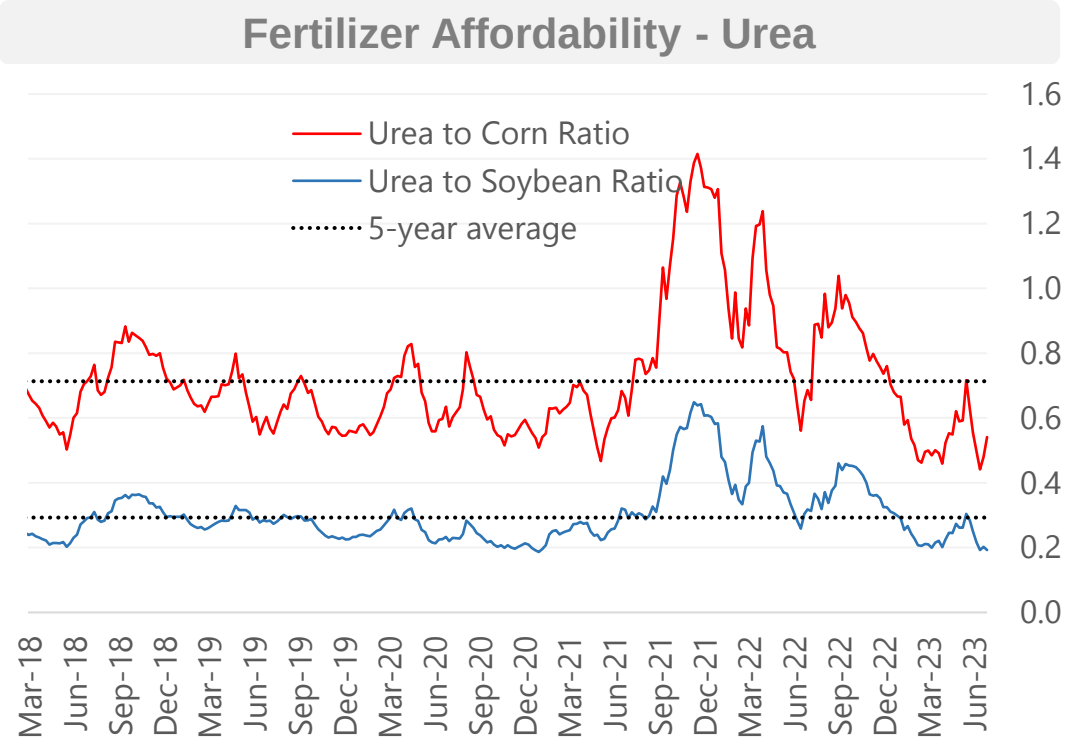
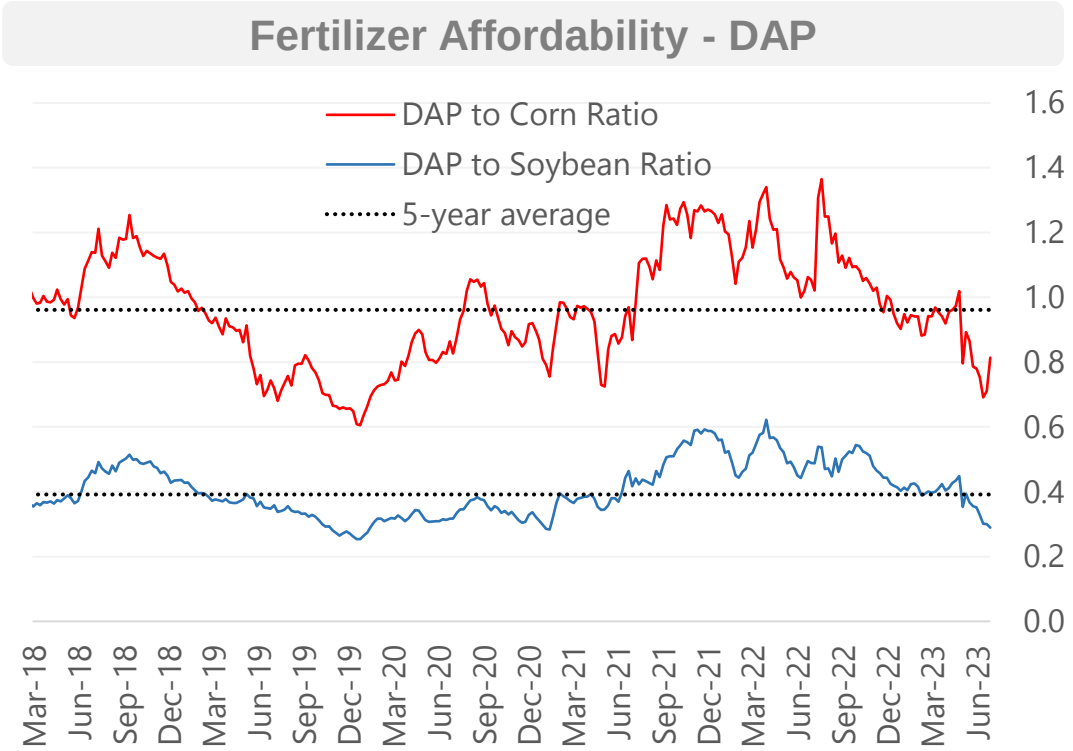
- Fertilizer-to-grain price ratios for urea, an important affordability metric, are below the 5-year average for corn and soybean.
- Fertilizer-to-grain price ratios for DAP was close to the 5-year average, but with DAP prices plunging, the ratio also plunged. With a good affordability, producers have incentive to both use more fertilizer and increase planted area, hence better prospects for food-inflation.



Sources: Bloomberg, Santander.

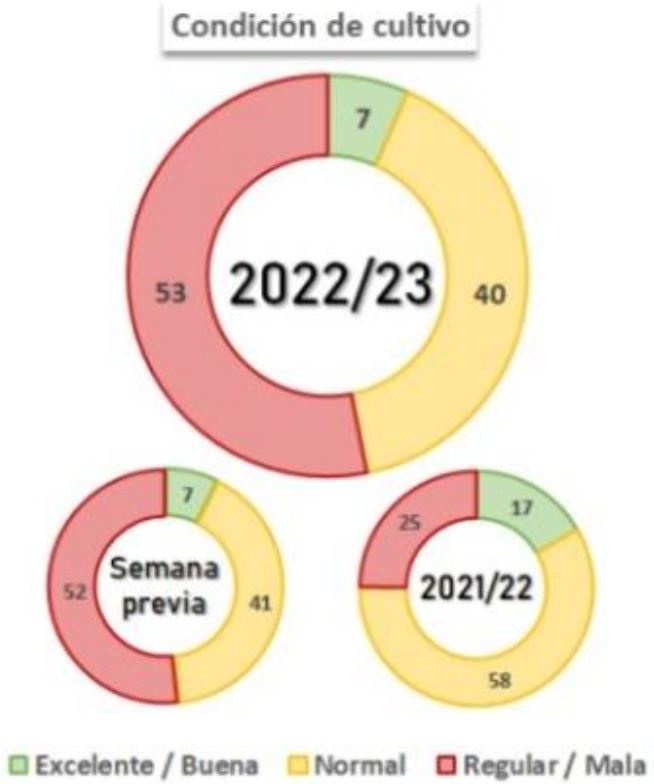


Sources: Bloomberg, Santander.

Agri: A transition to El Niño Amid a Record Brazilian Grain Output

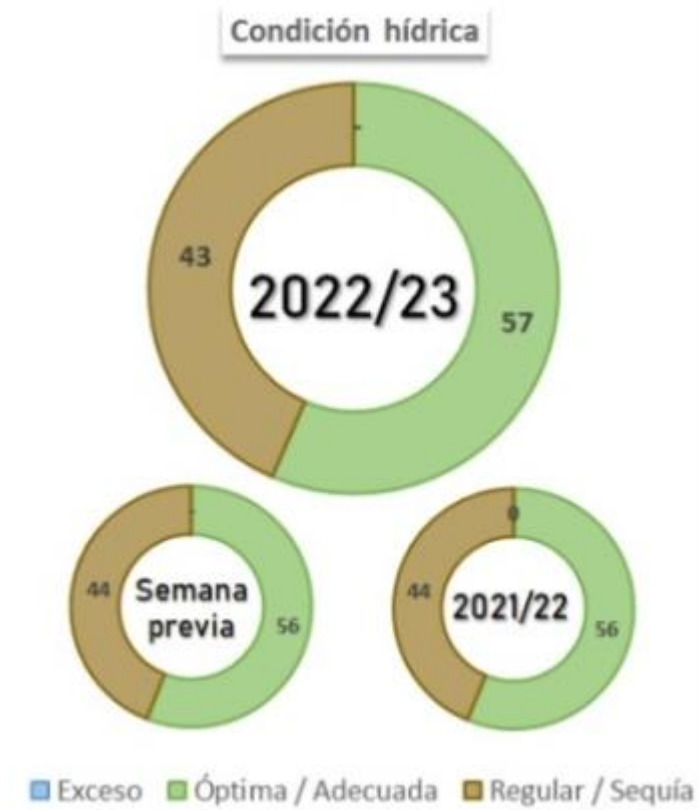
- Professionals from the BCBA (Bolsa de Cereais de Buenos Aires) classify corn crops in good or excellent conditions at 7% (unchanged from last week) in 2022/2023. The condition is below the 17% in 2021/2022.

Corn in Argentina - Crop Condition



Sources: BCBA, Santander.

Corn in Argentina – Soil Water Condition

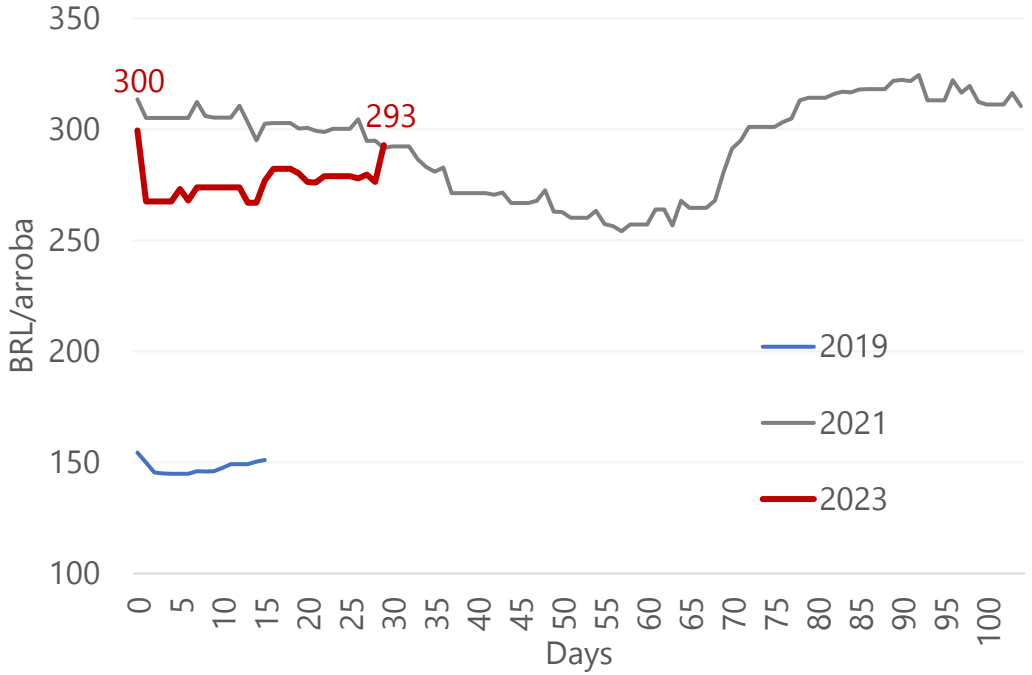


Sources: BCBA, Santander.

Agri: A favorable stage of Brazilian cattle cycle

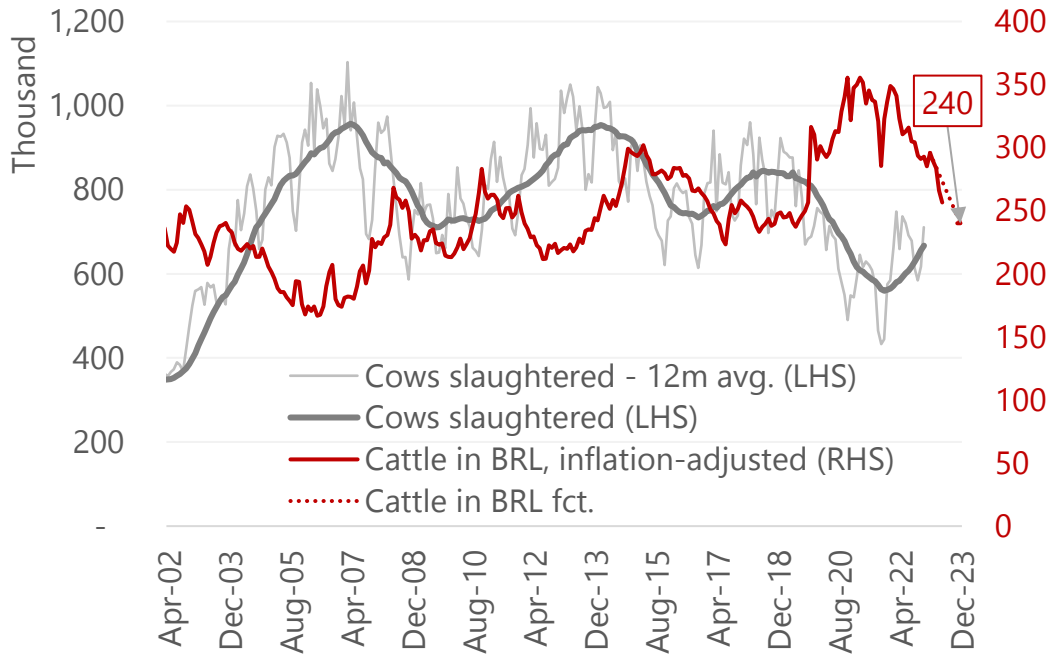
- In Brazil's cattle cycle: a higher percentage of cows is being slaughtered, meaning that more beef is being supplied to the market, helping bring its prices down.
- Taking our estimate of BRL 240/arroba as an input, we forecast that the beef price component of the IPCA (Brazil's official CPI) could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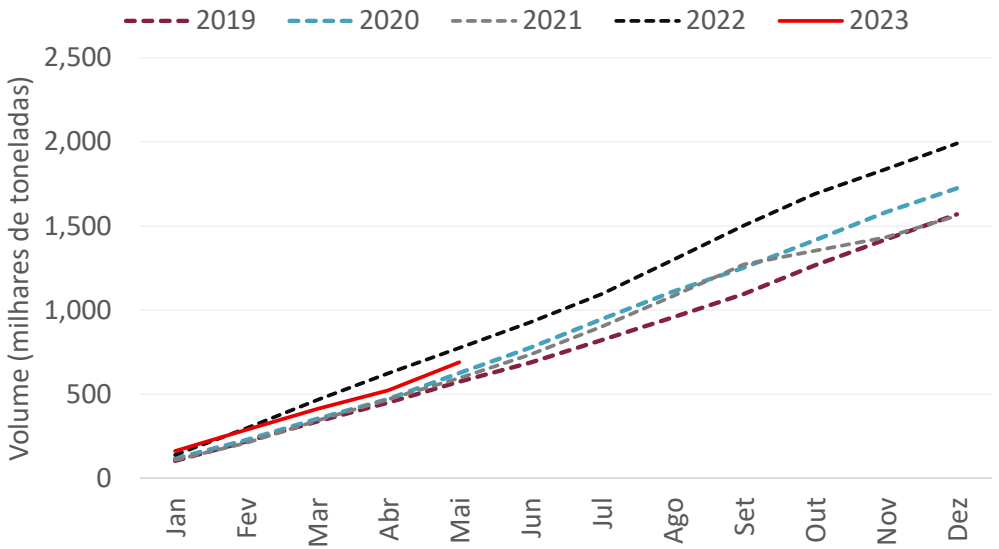
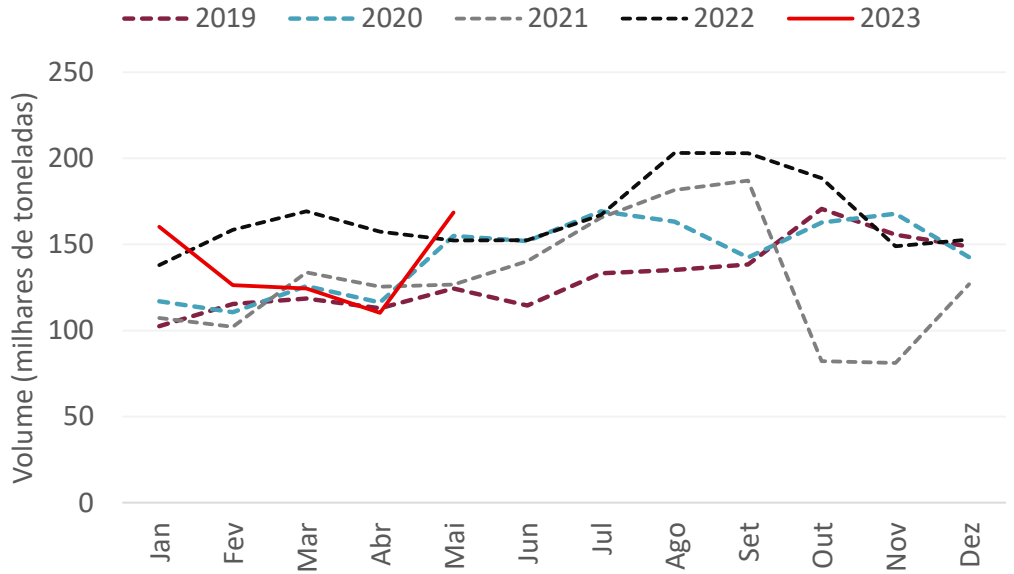
Brazil - Beef export (accumulated)



Sources: SECEX, Santander.

Brazil - Beef export (monthly)



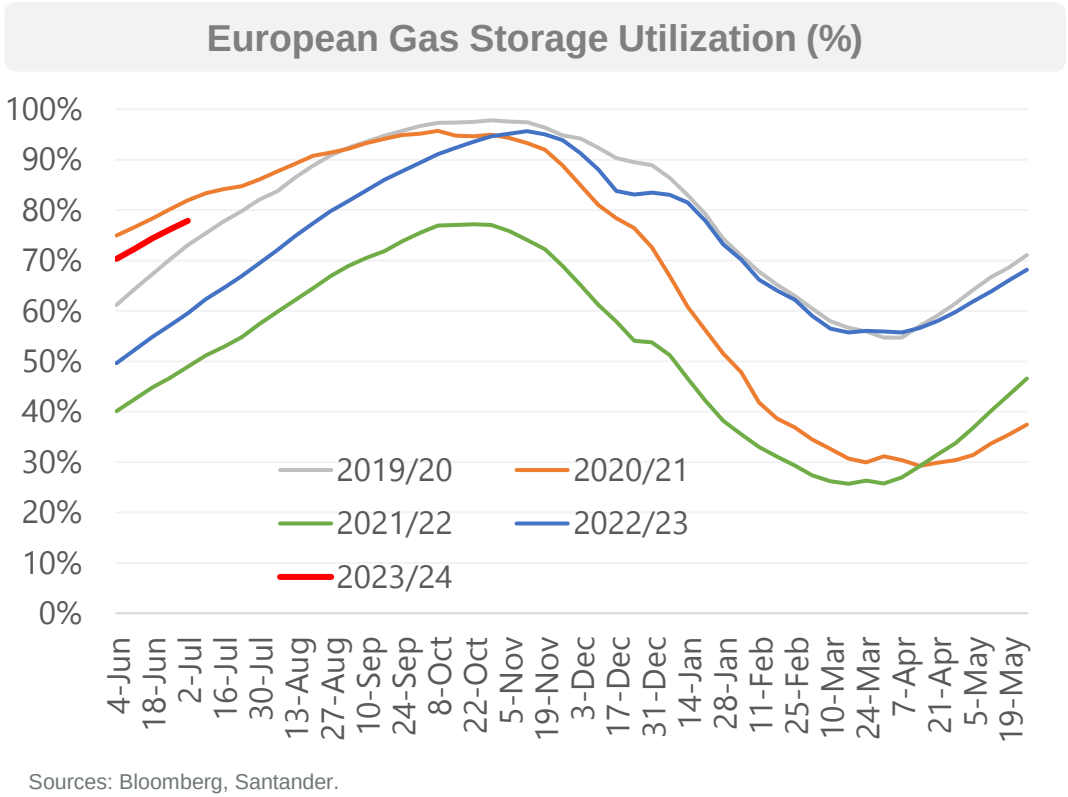
Sources: SECEX, Santander.

ENERGY

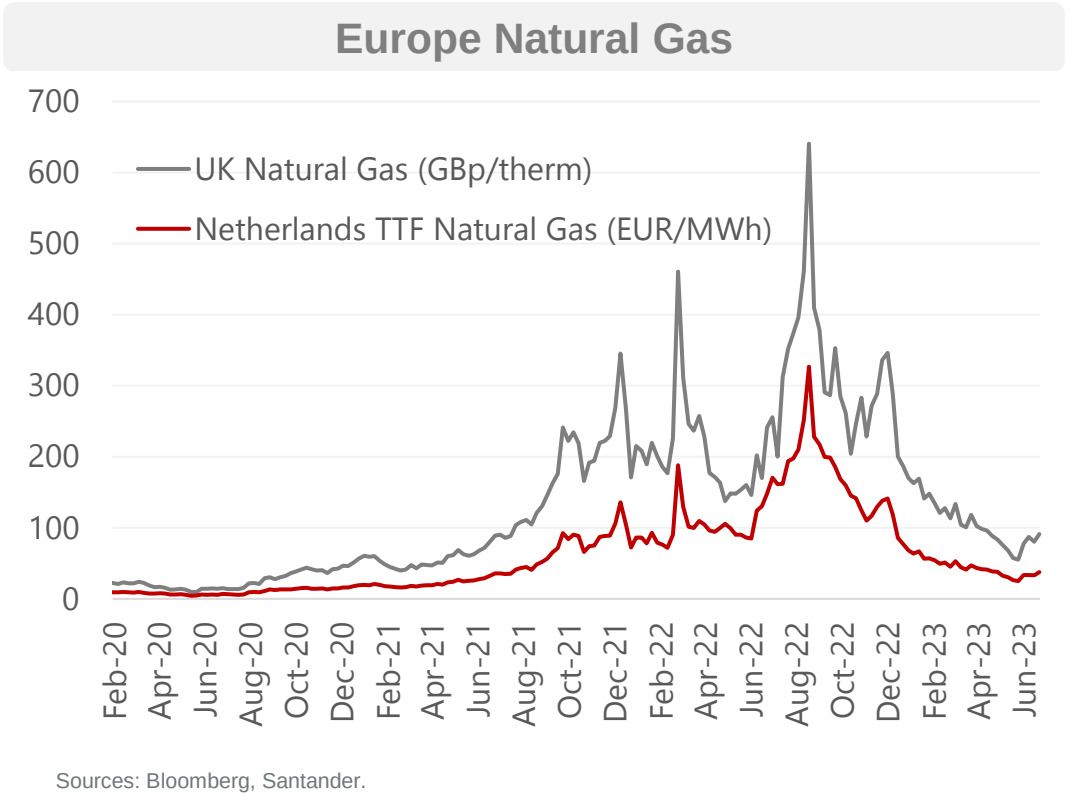
03

Natural gas prices 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).



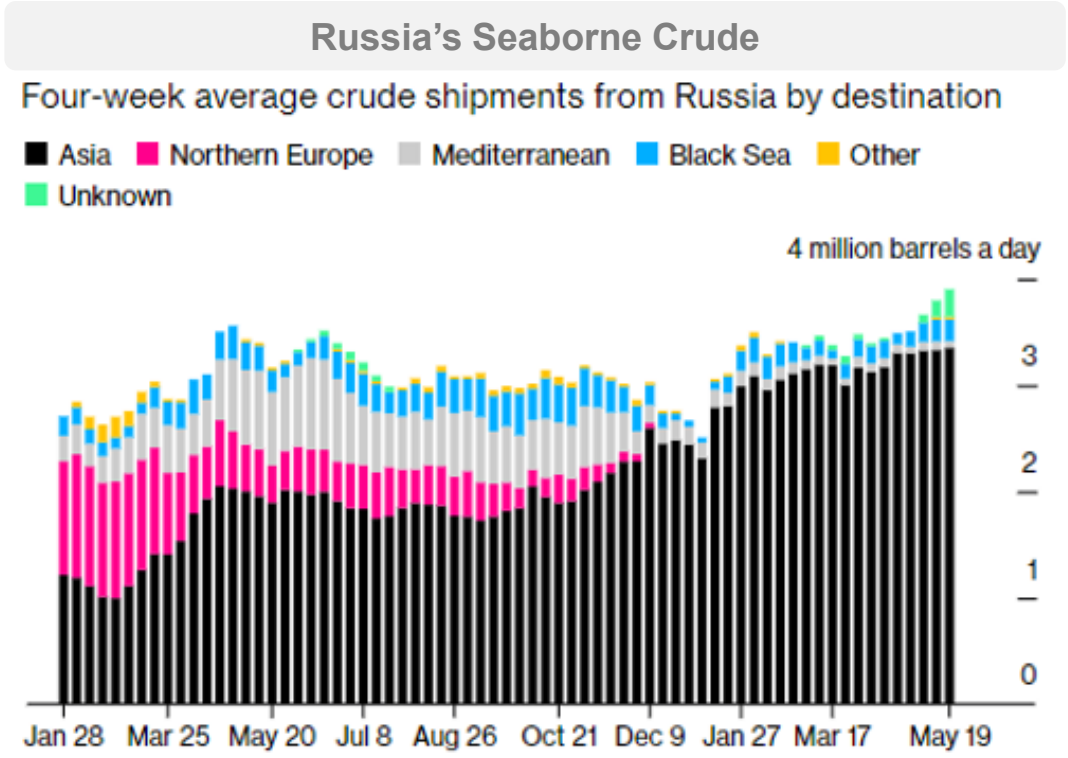
Sources: Bloomberg, Santander.



Sources: Bloomberg, Santander.

Oil: Oversupply and weak demand disappoint oil bulls

- In energy, consistent and increasing Russian oil flows to Asia mean that the expected imbalance in oil markets resulting from the Western sanctions seems less likely now. Along with disappointing reopening data from China, this has prompted us to lower our forecast for Brent oil to USD 85/bbl (from USD 95/bbl) for YE2023.
- In our view, OPEC+ will manage production to seek to keep prices above USD80 per barrel.



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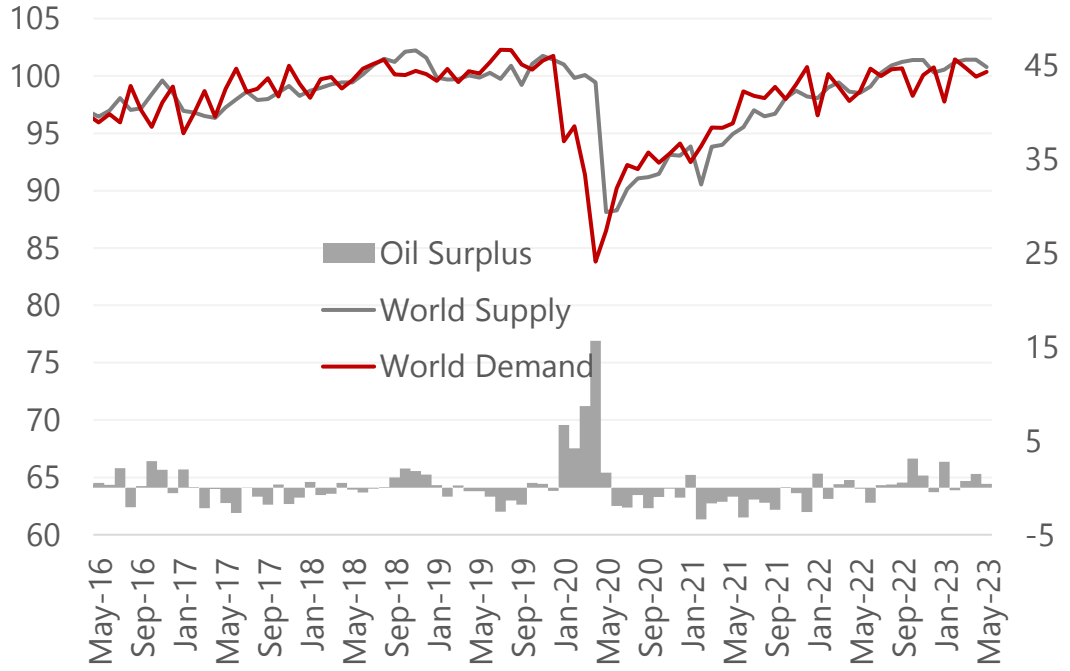
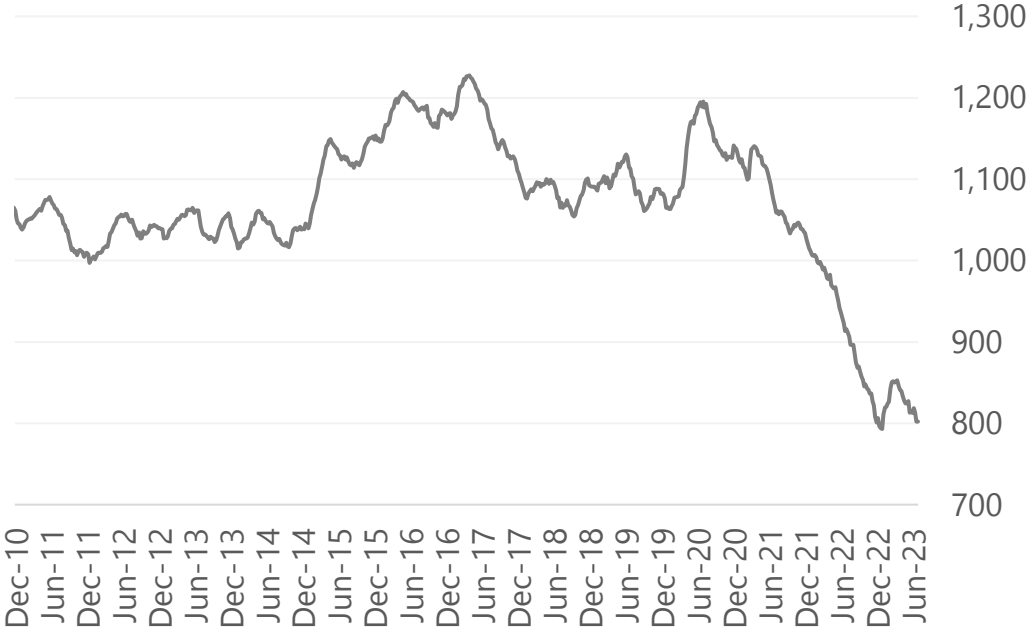
World Oil Supply x Demand (mbd)



Sources: Bloomberg, Santander.

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



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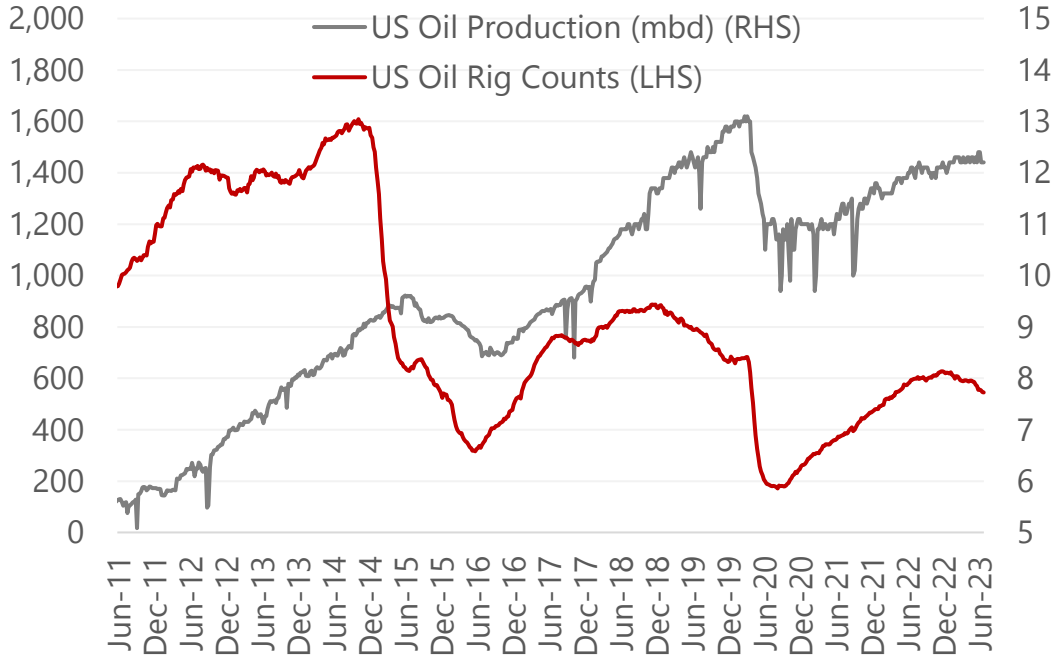
US Oil Production



Sources: Bloomberg, Santander.

Brent Crude Oil (USD/bbl)

Sources: Bloomberg, Santander.

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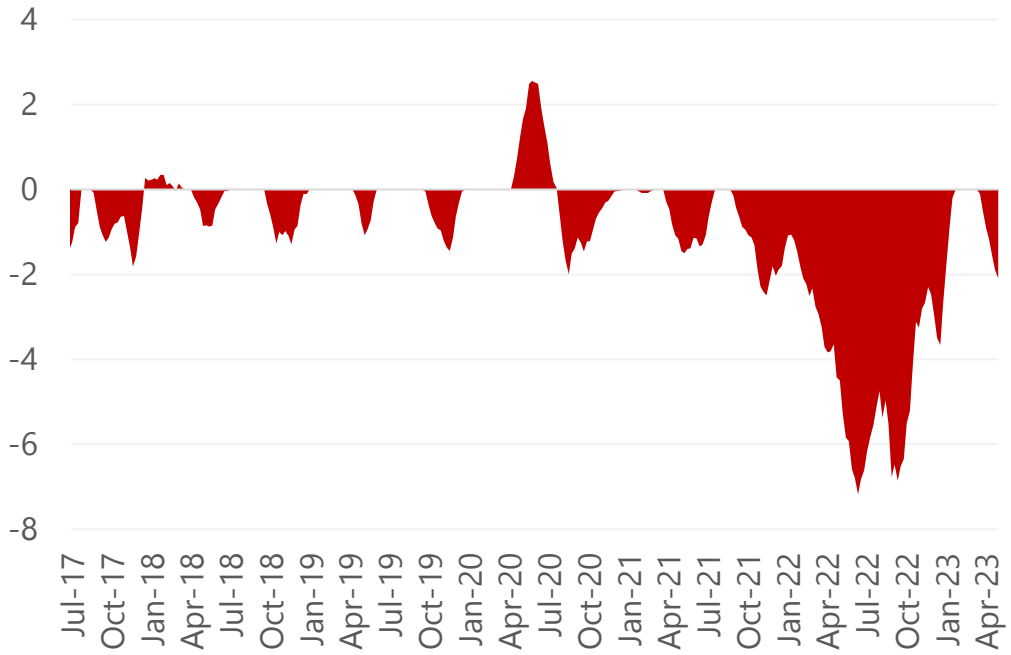
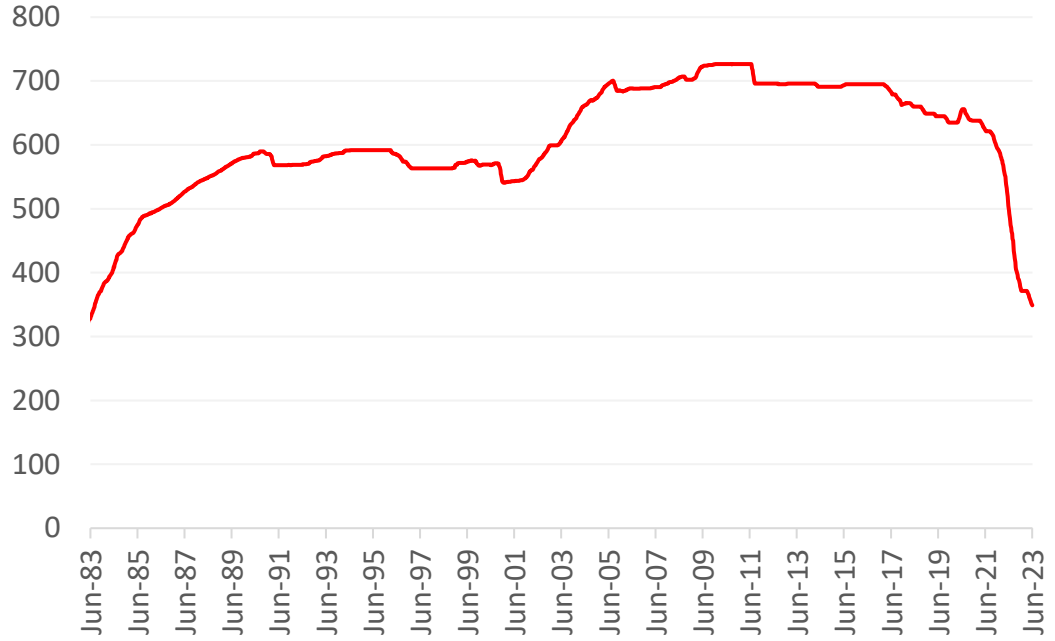
Weekly U.S. Change in Crude Oil in SPR (Million Barrels)



Sources: US Department of Energy, Santander.

US Strategic Petroleum Reserves (Million Barrels)

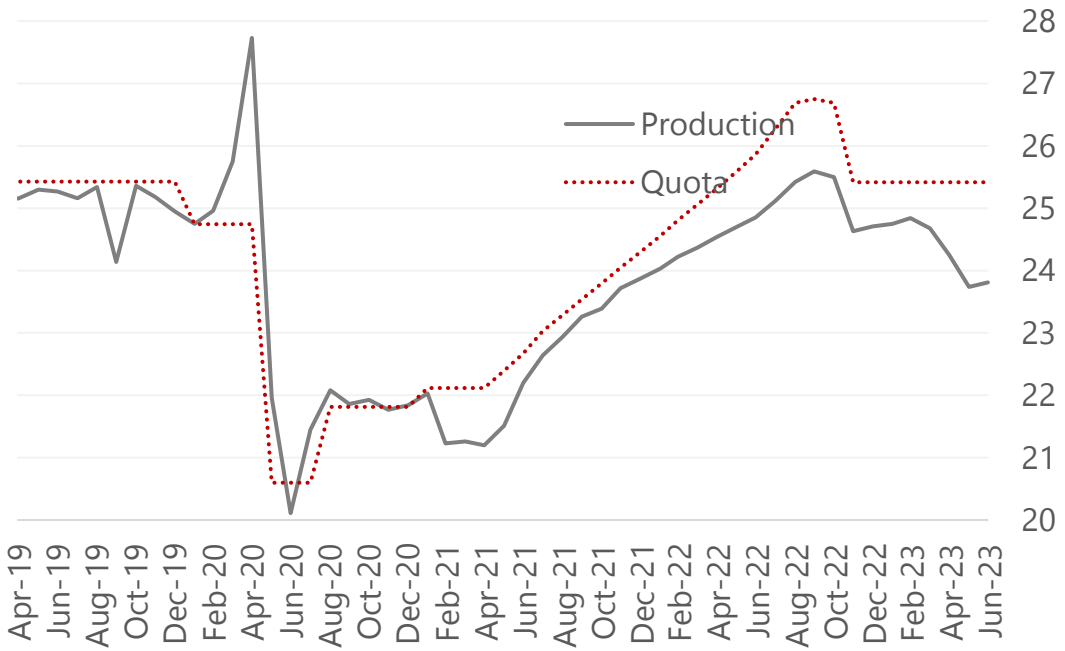


Sources: Bloomberg, Santander.

Oil: Oversupply and weak demand disappoint oil bulls

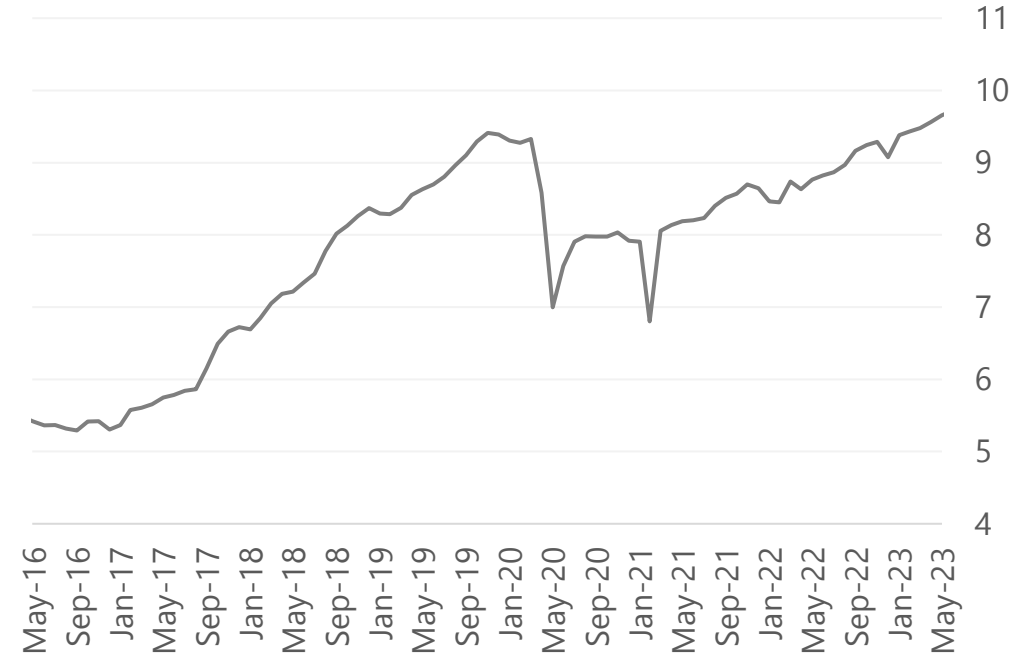
- Following the OPEC+ meeting in early June, Saudi Arabia said it would cut production by another one million barrels per day (bpd), starting in July, and other members of the cartel announced they would extend their oil output voluntary cuts until the end of 2024.

OPEC Production (members with quota) (mbd)



Sources: Bloomberg, Santander.

US Shale Production (mbd)



Sources: Bloomberg, Santander.

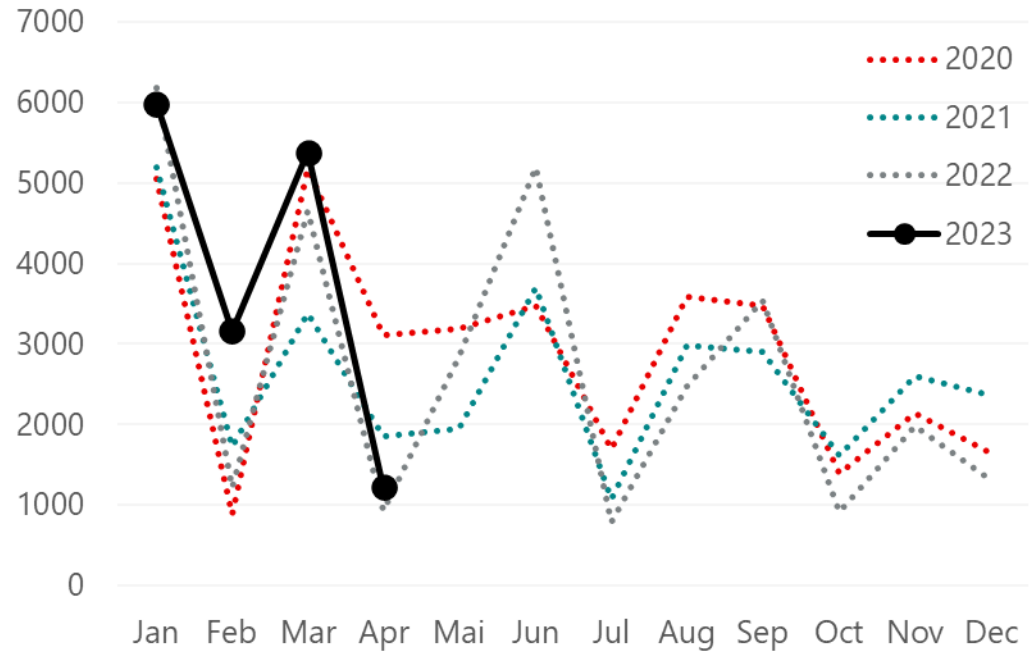
METALS

04

Metals: Chinese data has been weak of late

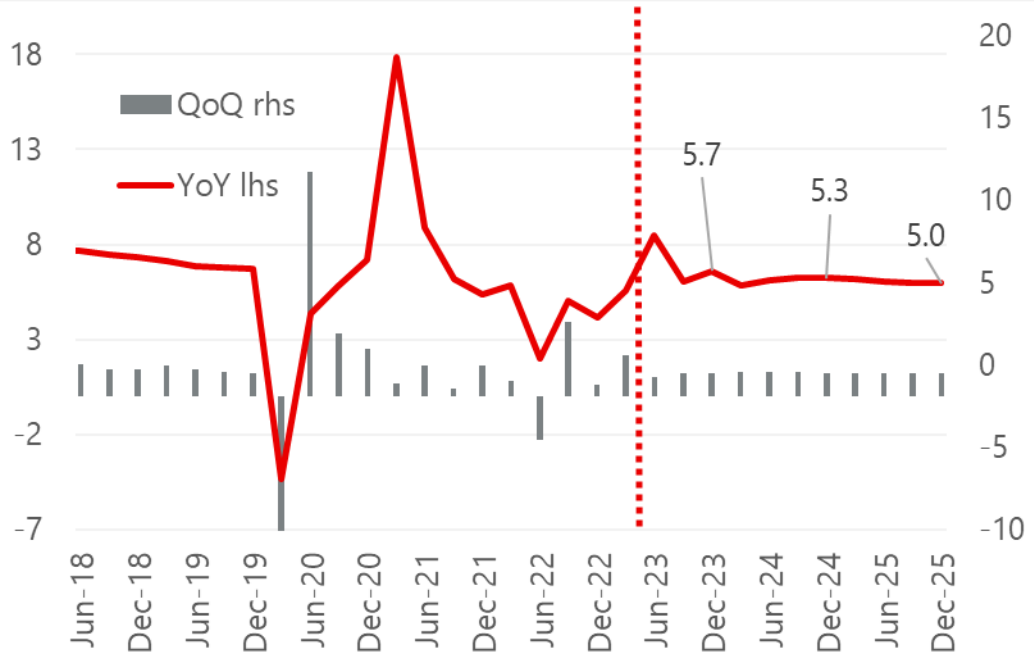
- In our view, the slowdown following a decent start of the year is probably due mostly to a fading of the pent-up demand that boosted sales following the lockdowns in 2022.
- Property sales and new construction are decelerating, with funding going toward completing existing projects.
- Even with more 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, meaning less support for metal prices ahead.

Credit expansion surprised on the downside recently



Sources: Bloomberg, Santander.

Q2 won't be as strong as previously expected



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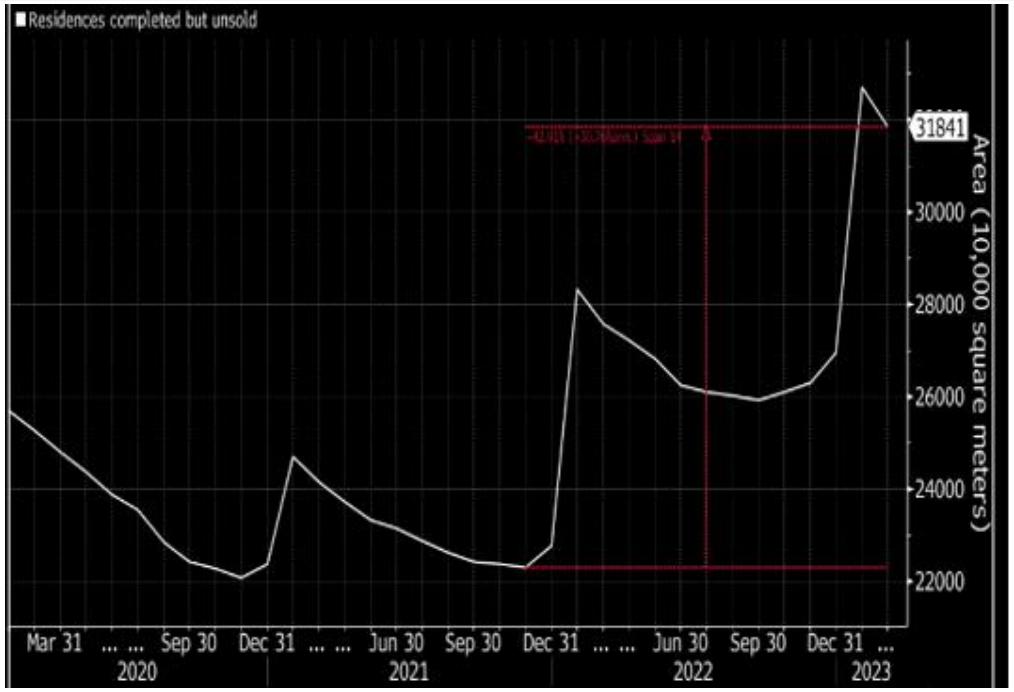
China's housing inventory remains elevated



Sources: Bloomberg, Santander.

China's mortgage slide in sign of weak buyers sentiment

Sources: Bloomberg, Santander.

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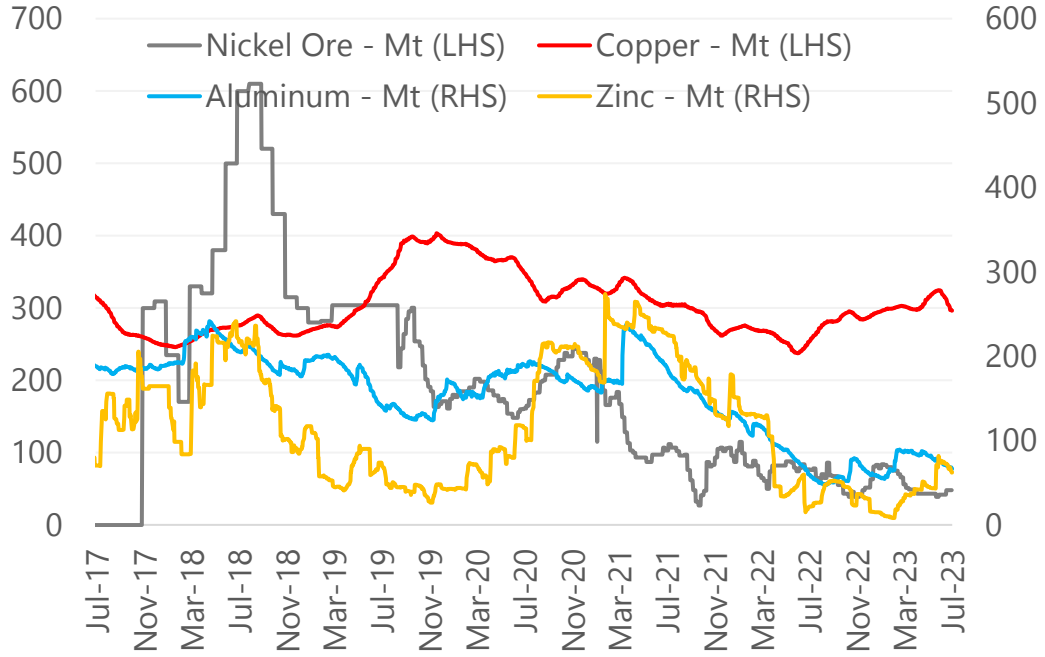
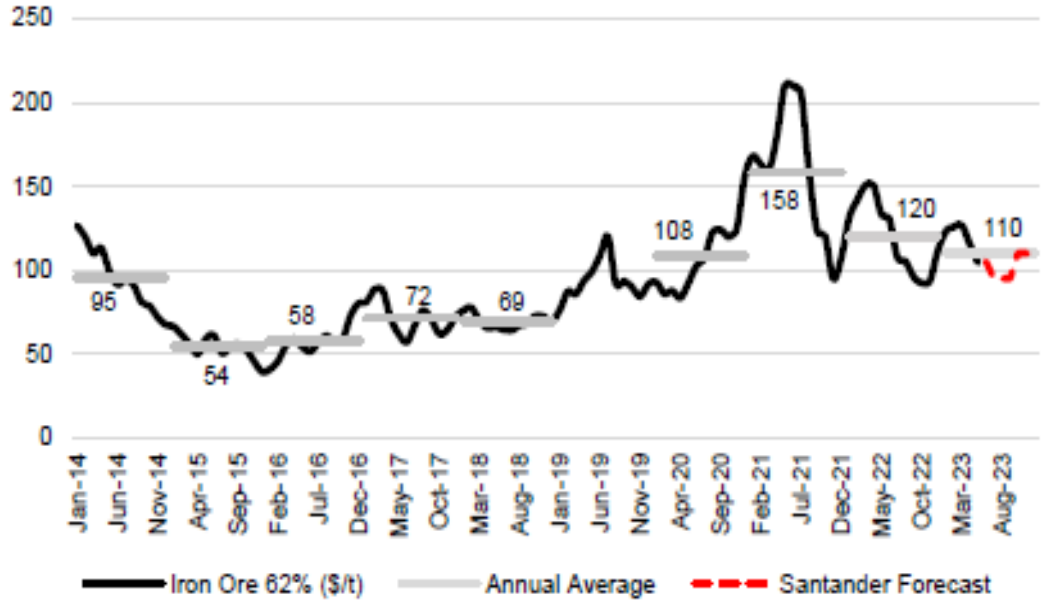
Base Metals Inventories



Sources: Bloomberg, Santander.

Iron Ore Price Forecast



Sources: Santander.

Thank you.

Our purpose is to help people and businesses prosper.

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

Simple Personal Fair

Santander

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IMPORTANT DISCLOSURES

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