



Brazil Macro | June 2022

Commodities

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SUMMARY

- **Low inventories for most raw materials, coupled with idiosyncratic factors (e.g., adverse weather, past underinvestment, high cost of production) have been contributing to extend the commodity rally into 2022. Yet global macro headwinds (higher interest rate, slowing economic activity) could hinder demand for raw materials. Since our last revision, we slightly downgraded our forecast based on the demand elements but we still envision a slow “normalization” in commodity prices, meaning an extended cycle.**
- For farm commodities, hot and dry weather slashed the grain production outlook in South America following a favorable start to 2022. Still, it is headed for a better output than last year. Importantly, La Niña is likely to continue this year (for a third year running), imparting risks for the upcoming season. Adverse weather has also been hindering crop yield in other parts of the world, triggering several cases of protectionisms. All in all, the recent evidence suggests that food inflation could take (even) longer to cool down.
- In energy, oil prices remain at a high level as stockpiles across the globe continue to dwindle, as some key economies tap their emergency reserves. Geopolitical themes continue to impact the oil market, and the latest concern regarding a global shortage of oil refined products (diesel, gasoline, jet fuel) could further deepen the energy crisis globally. Bottom line, we kept our Brent forecast of USD 115 bbl for YE2022 and USD 95 bbl for YE2023, with risks clearly skewed to the upside.
- In metals, inventories remain worryingly low, but the entire complex took a hit from renewed lockdowns in China and a weaker global demand outlook. As for iron ore, prices for the commodity receded considerably since our last revision, but consumption will likely pick up this year as the Chinese government adds stimulus (as expressed recently with Chinese banks cutting interest rate for mortgages by a record amount) and COVID restrictions being eased.

OVERVIEW

01

Macro Headwinds Amid Still Tight Supply-Demand Balances

- The ongoing geopolitical shock coming from Eastern Europe adds to the global supply disruptions and the economic sanctions imposed against Russia further aggravates the supply-demand imbalances for key commodities (e.g., grains, fuels, fertilizers).
- Since our last revision, we slightly downgraded our forecast based on the demand elements but we still envision a slow “normalization” in commodity prices, meaning an extended cycle.

Our Forecasts for CRB Index – End of Period

| YE | 2019 | 2020 | 2021 | 2022e | 2023e |
|------------|------|------|------|-------|-------|
| CRB Food | 331 | 355 | 483 | 542 | 488 |
| CRB Energy | 1647 | 1161 | 1521 | 1850 | 1809 |
| CRB Metal | 749 | 887 | 1259 | 1294 | 1165 |
| CRB | 401 | 444 | 571 | 596 | 561 |

| YE YoY | 2019 | 2020 | 2021 | 2022e | 2023e |
|------------|------|------|------|-------|-------|
| CRB Food | 1% | 7% | 36% | 12% | -10% |
| CRB Energy | 2% | -30% | 31% | 22% | -2% |
| CRB Metal | -11% | 18% | 42% | 3% | -10% |
| CRB | -3% | 11% | 29% | 4% | -6% |

Our Forecasts for CRB Index – Monthly Averages



Sources: Bloomberg, Santander.

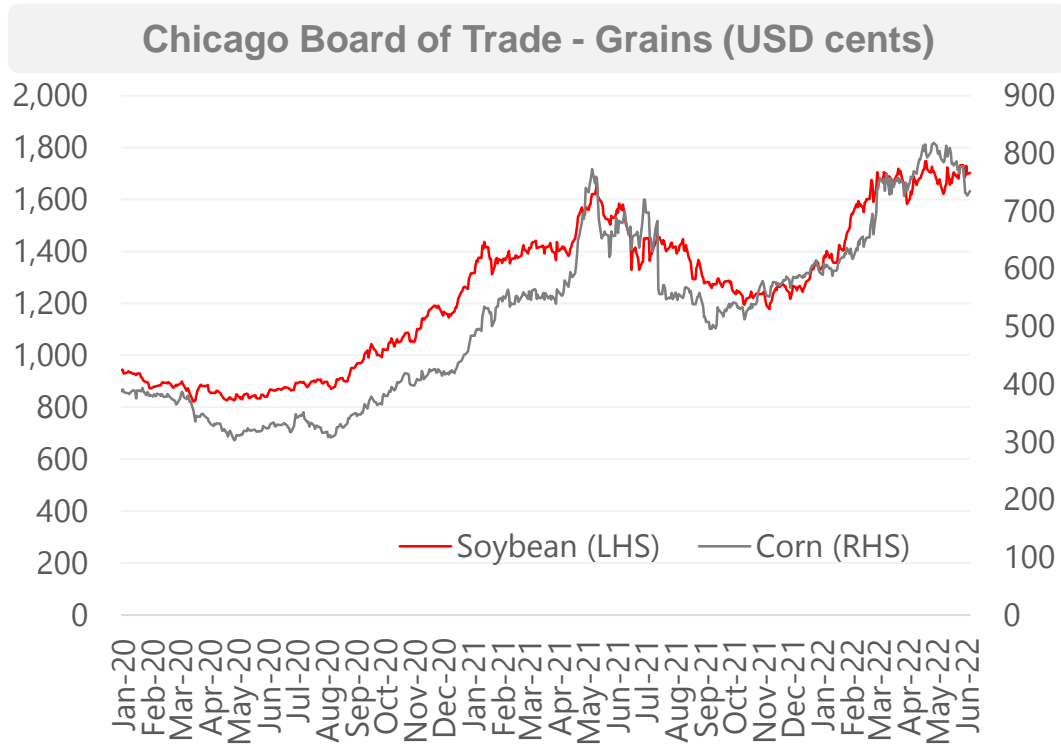
Sources: Bloomberg, Santander.

AGRICULTURE

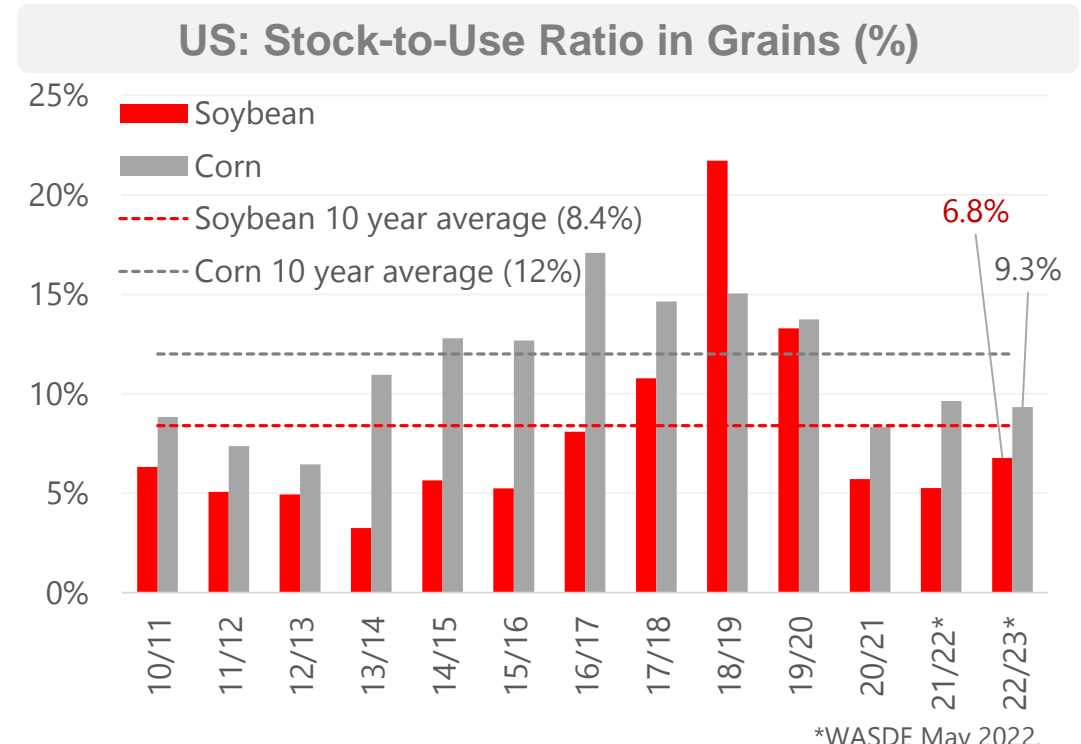
02

Low Stocks Fueled By Weather And Geopolitical Shock

- Low stock-to-use ratio of grains in the US point to a tight market. Both corn and soybean are close all-time high prices.
- Adverse weather has also been hindering crop yield in other parts of the world, triggering several cases of protectionisms (e.g. the episodes of palm oil in Indonesia, wheat and sugar in India).



Sources: Bloomberg, Santander.



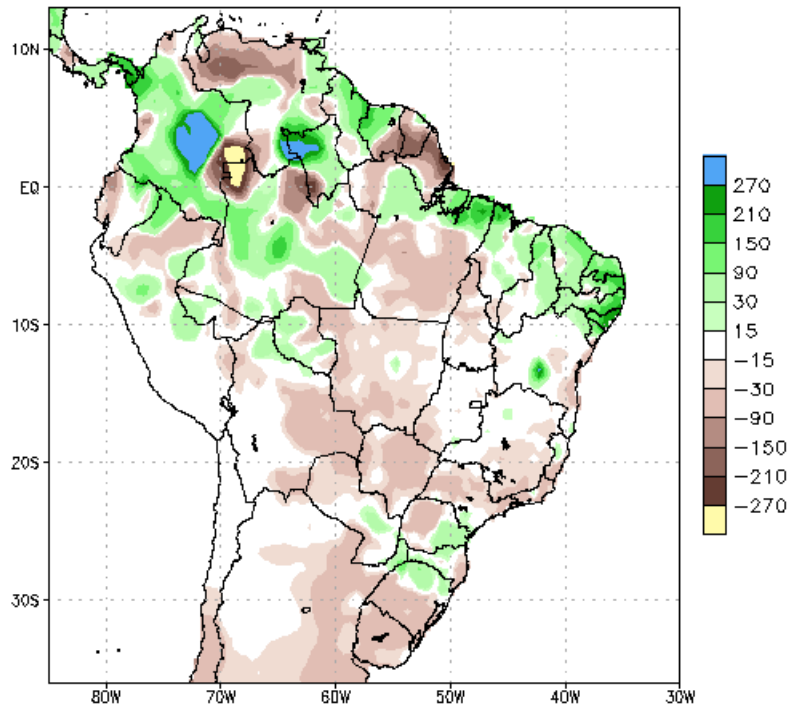
Sources: USDA, Santander.

Low Stocks Fueled By Weather And Geopolitical Shock

- Harvest of “safrinha” corn has started, with estimates hovering around 87 mmt (+40% last years output).
- Frosts that took place in the second half of May did not caused major setbacks in corn crops.

Precipitation (30-day anomaly)

Prp Anomalies (mm) 07MAY2022–05JUN2022

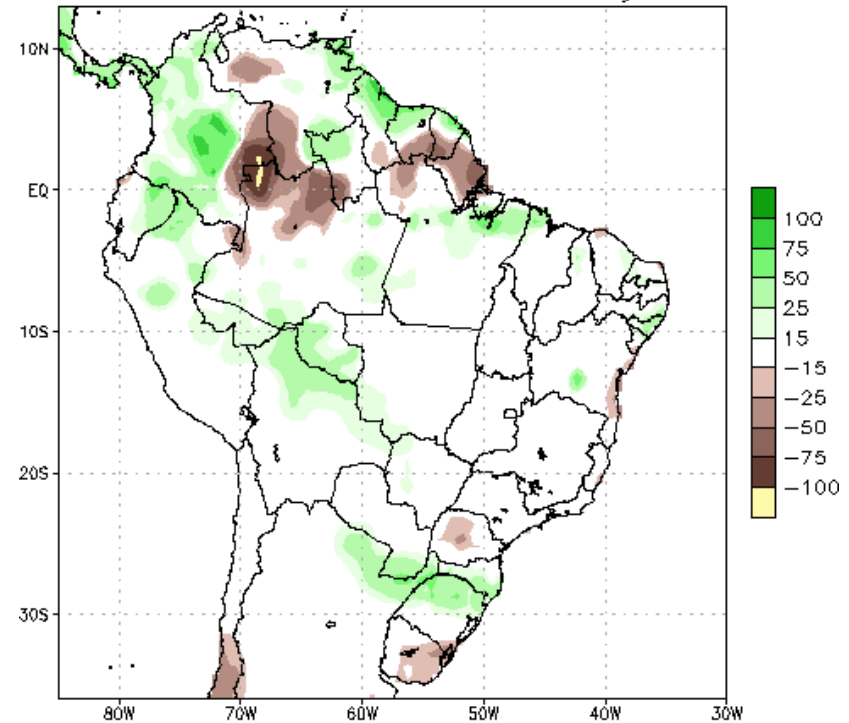


Data Source: CPC Unified (gauge-based & 0.5x0.5 deg resolution) Precipitation Analysis Climatology (1991–2020)

Sources: NOAA, Santander.

GFS Precipitation Forecasts (7-day anomaly)

05Jun2022–11Jun2022 Anomaly



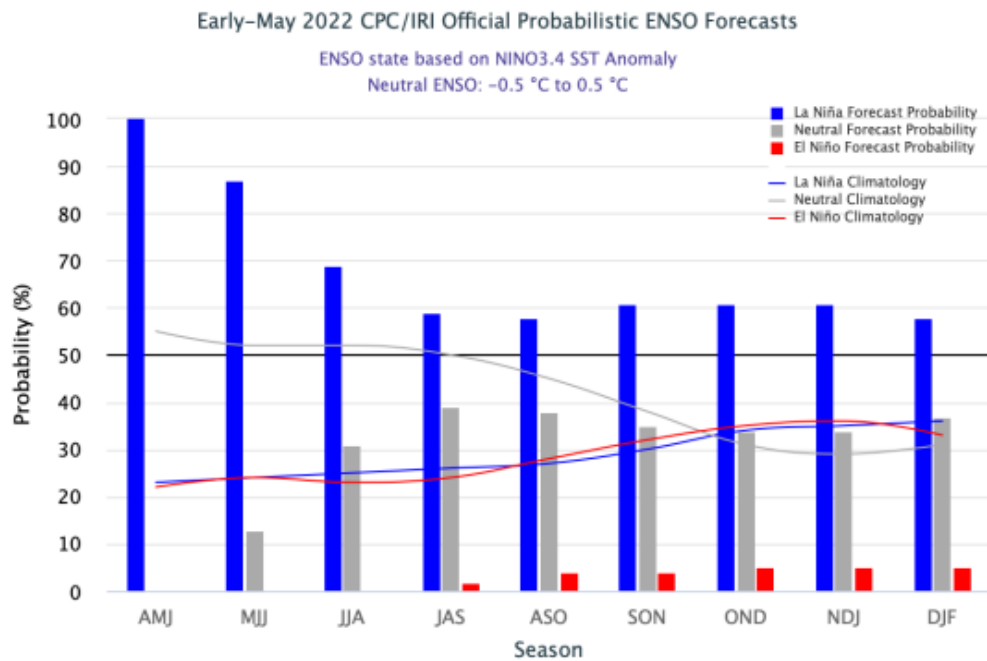
Bias correction based on last 30-day forecast error
CPC Unified Precip Climatology (1991–2020)

Sources: NOAA, Santander.

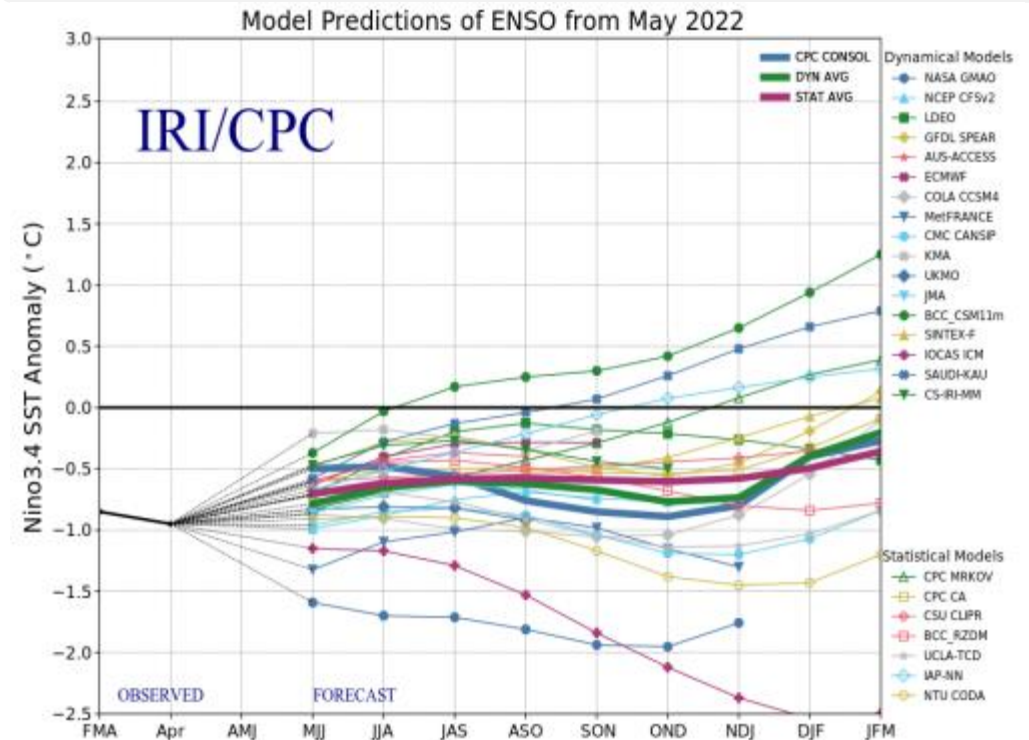
Low Stocks Fueled By Weather And Geopolitical Shock

- According to NOAA forecast, La Niña is expected to weaken, but persist through the Northern Hemisphere summer and into early winter 2022-23. **It will be the third year running, imparting risks for the upcoming season.**

La Niña Outlook – CPC/IRI PROBABILISTIC First half of May

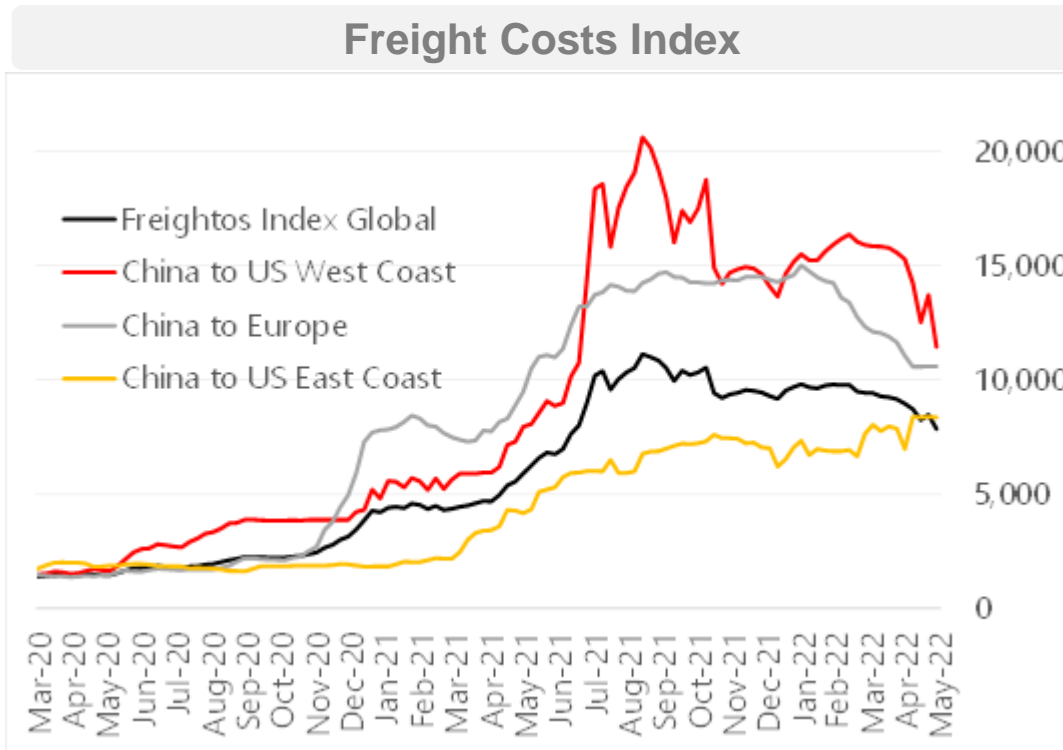


La Niña – Model Prediction

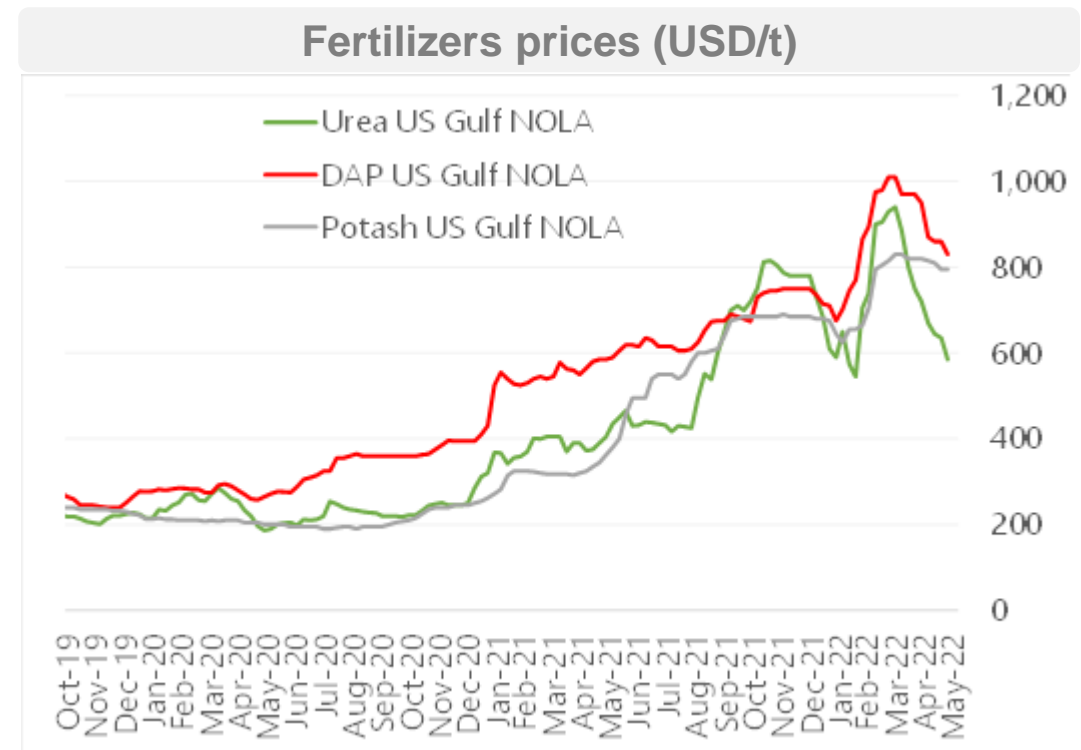


Low Stocks Fueled By Weather And Geopolitical Shock

- Prices of material inputs (ammonia, nitrogen, nitrates, phosphates and potash) for the fertilizer market rose significantly since 2020. **However, in YoY terms freight costs continue to slowly trend down.**
- The Russia-Ukraine conflict added to this tight market, as Russia (and ally Belarus) are significant producer of fertilizer ingredients. **As with freight costs, we see a downward trend at the margin.**



Sources: Bloomberg, Santander.

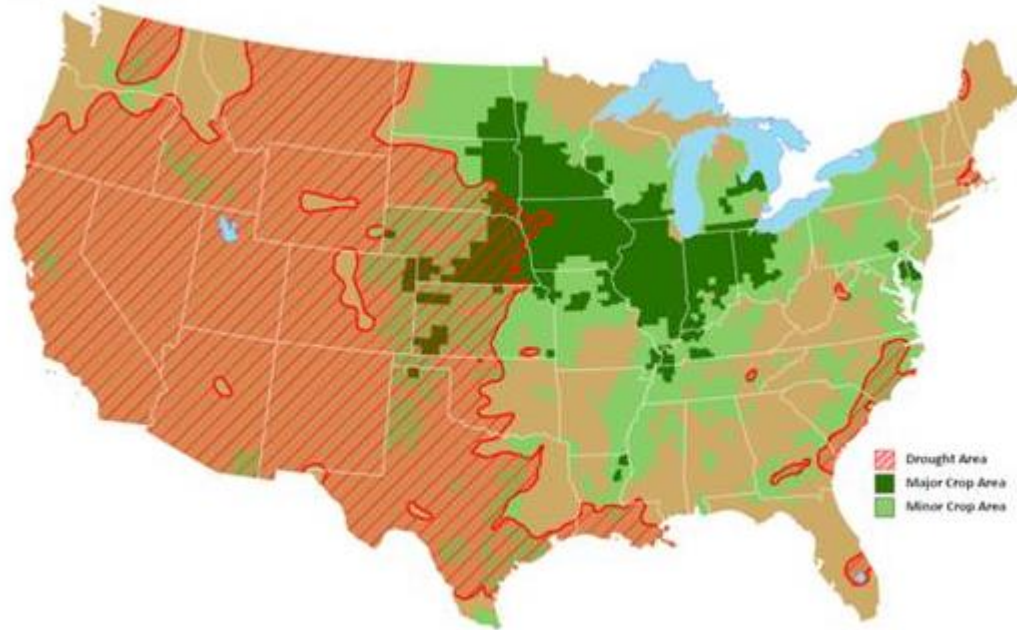


Sources: Bloomberg, Santander.

Low Stocks Fueled By Weather And Geopolitical Shock

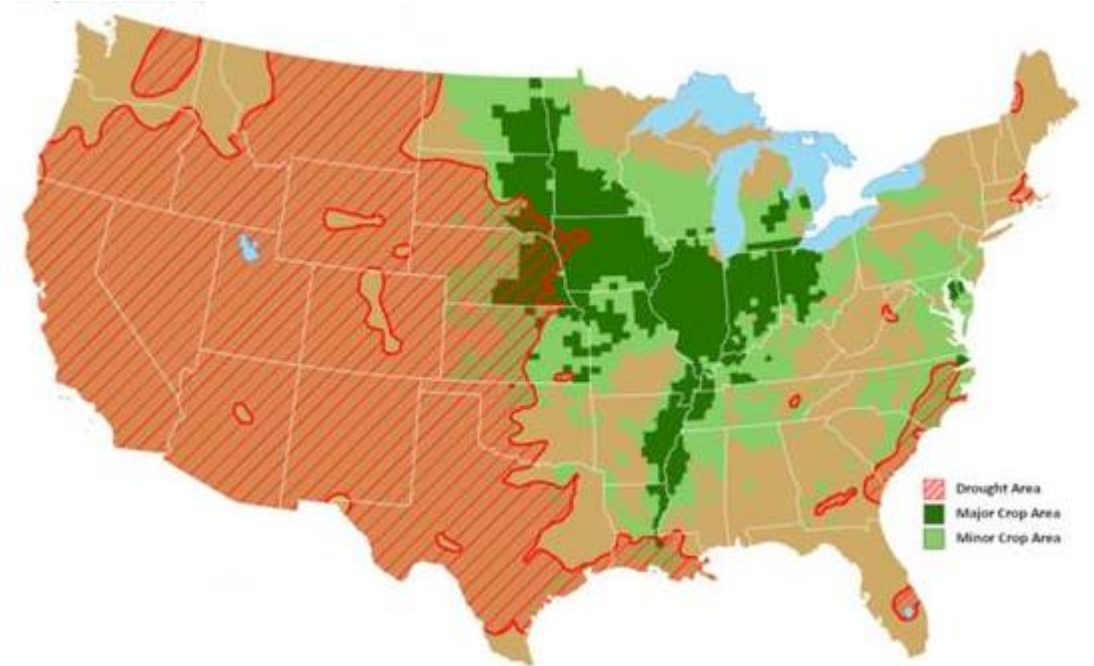
- U.S. corn planting is 86% complete by May 27 as better weather allowed for a rapid plating following a slow start.
- Approximately 20% of corn production is within an area experiencing drought; for soybean, 12%.

U.S. Corn Areas in Drought
May 24, 2022



Sources: USDA, Santander.

U.S. Soybean Areas in Drought
May 24, 2022



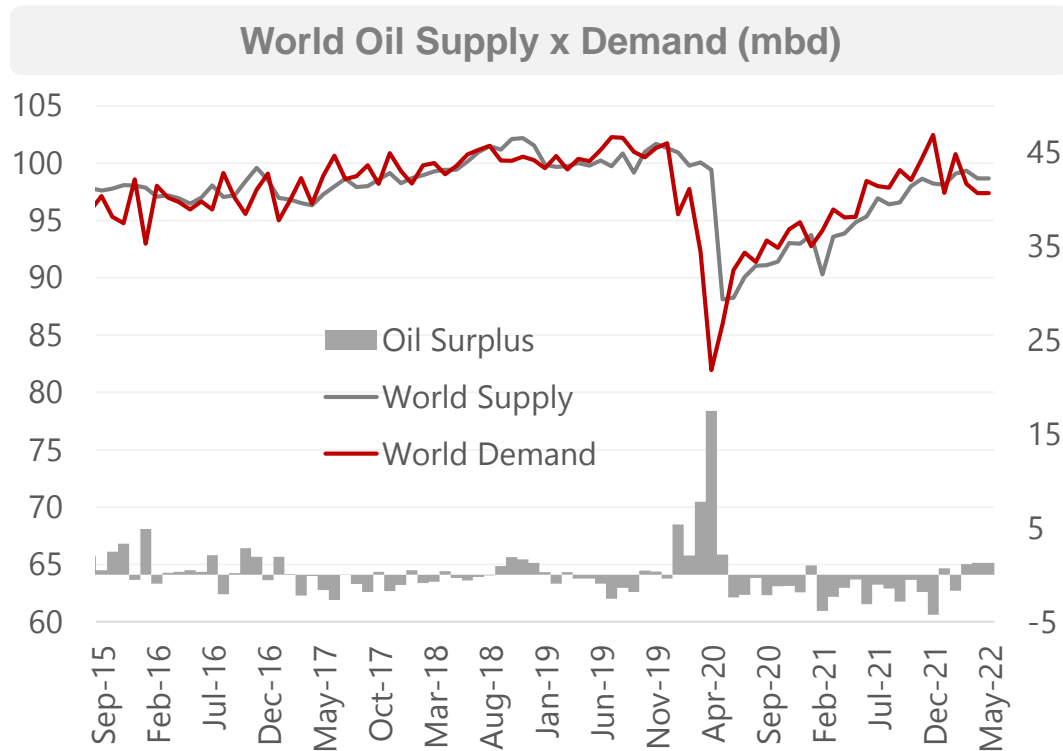
Sources: USDA, Santander.

ENERGY

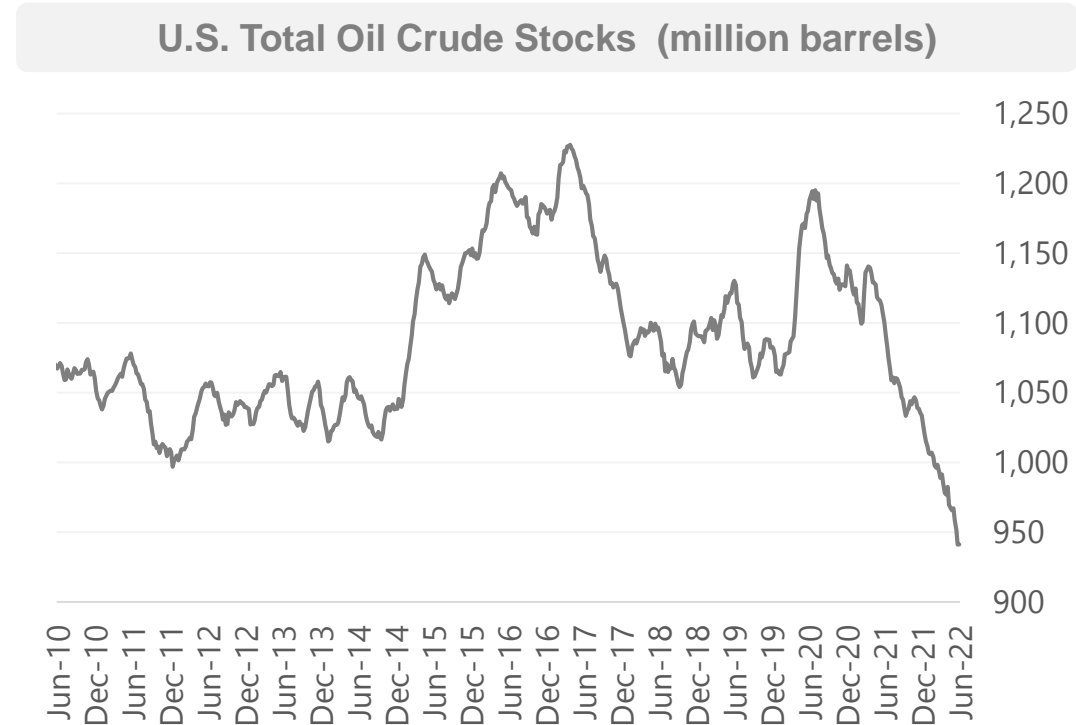
03

Geopolitical Shock Adds Volatility to a Constrained Supply

- As the economy recovers from the coronavirus pandemic and majors oil producers fall short of output, the global oil balance of supply and demand has been consistently running on deficit.
- As a result, global inventories are the tightest in at least 7 years: US crude inventories is already below 2011-2015 levels when Brent crude oil stayed above \$100/bbl.



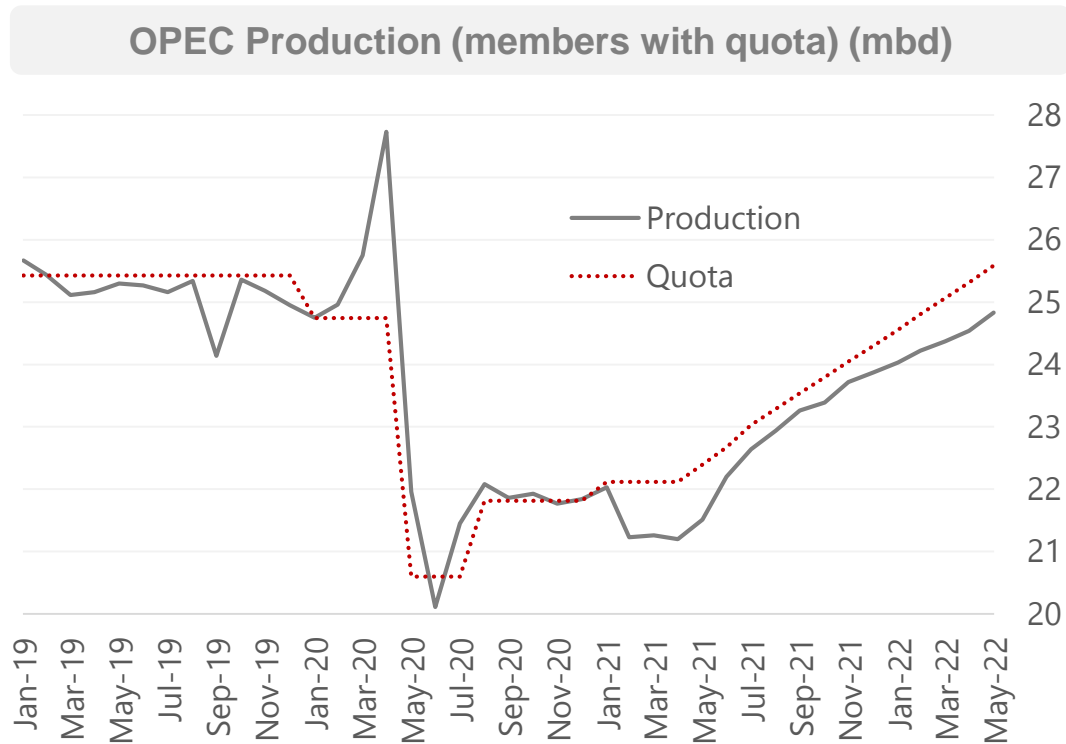
Sources: Bloomberg, Santander.



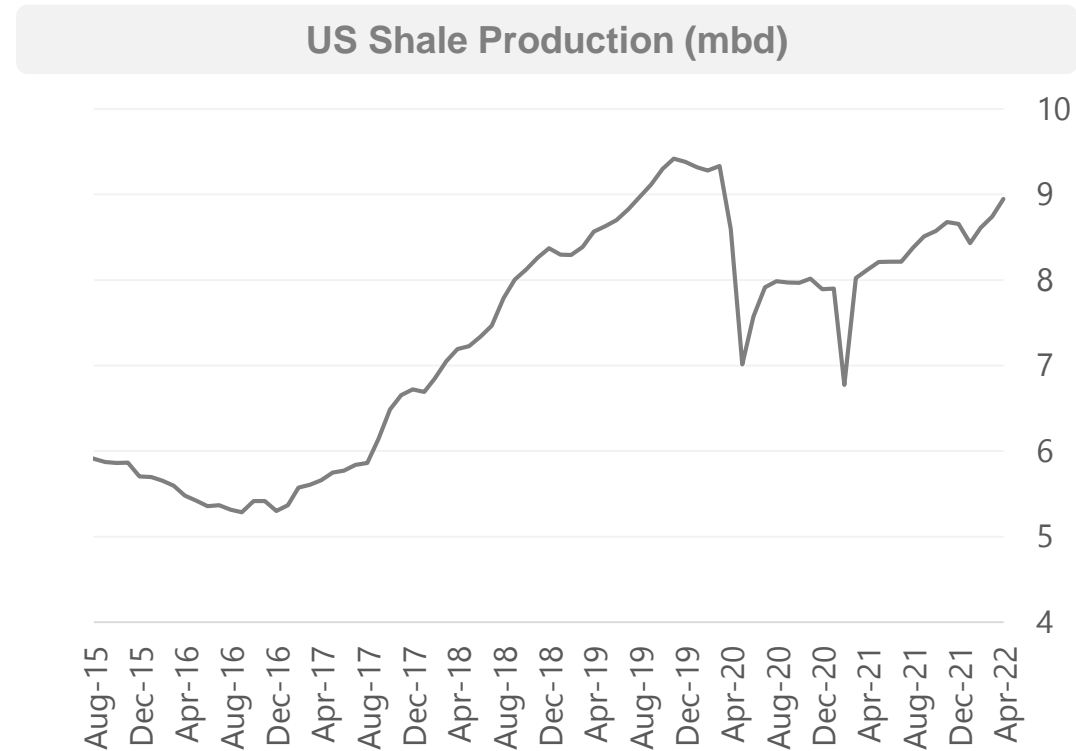
Sources: Bloomberg, Santander.

Geopolitical Shock Adds Volatility to a Constrained Supply

- The organization has been gradually increasing its production quota on a monthly basis. However, it has been failing to meet its target due to production shortfalls in several members, owing to low investments before and during the pandemic.
- US oil production is currently at 11.9 million barrels, still 9% down the pre-pandemic level. This discipline – to prioritize investor’s return rather than output growth - has so far proved resilient to higher oil prices.



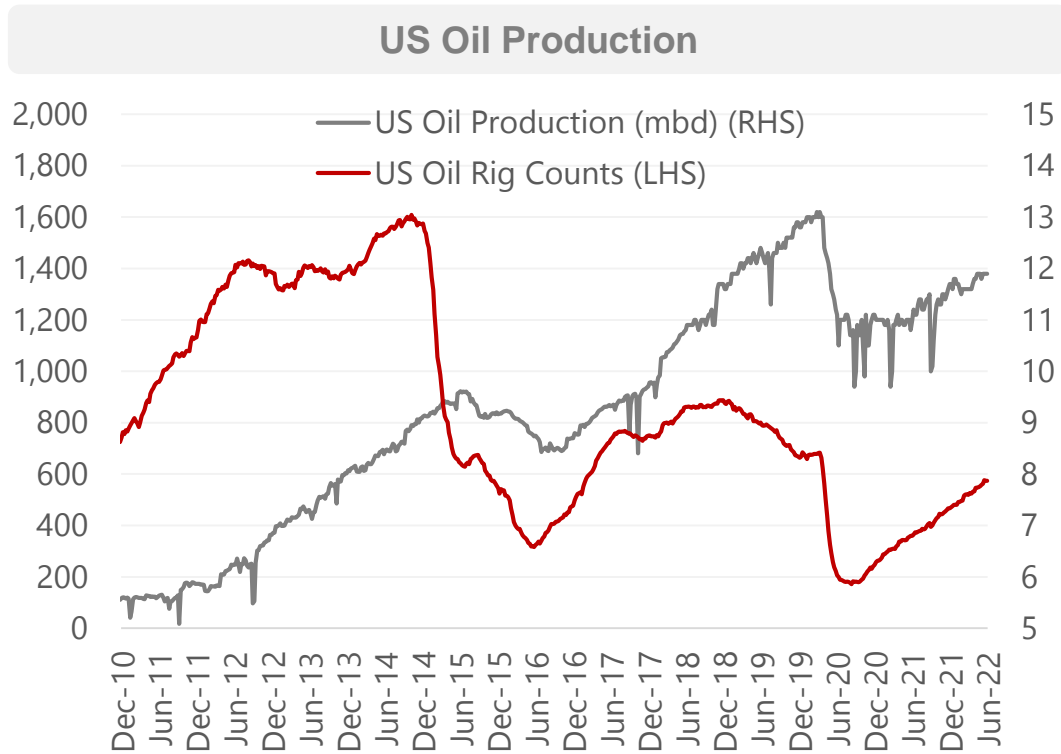
Sources: Bloomberg, Santander.



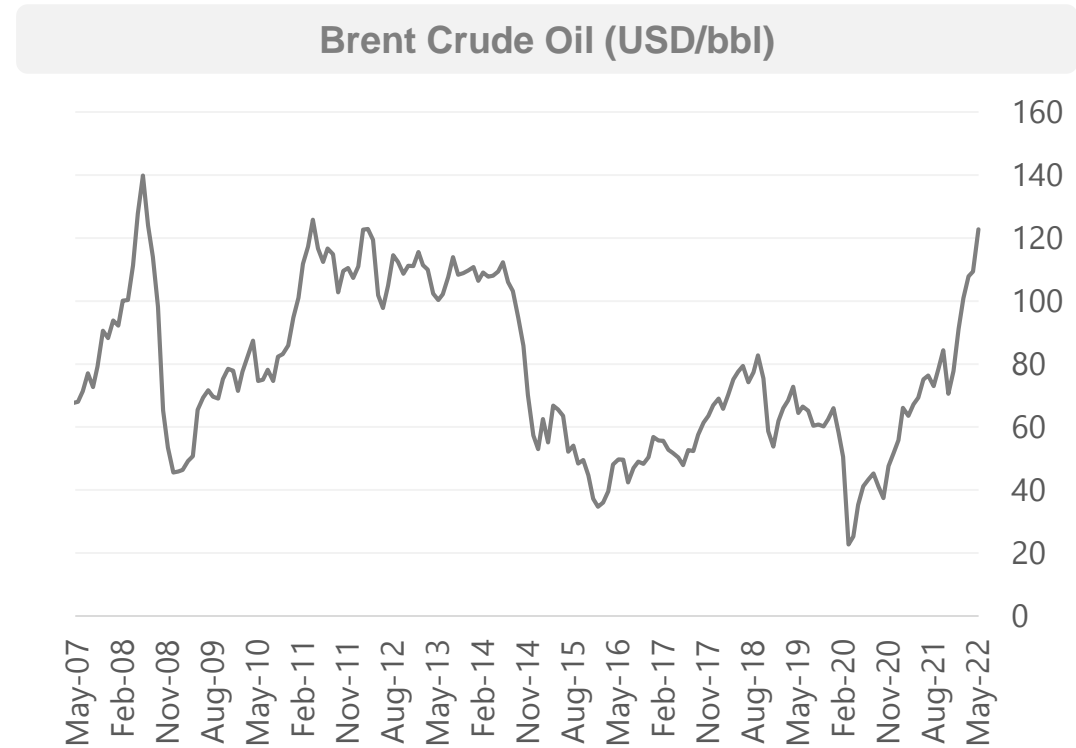
Sources: Bloomberg, Santander.

Geopolitical Shock Adds Volatility to a Constrained Supply

- Rig counts in the US are increasing, but are still below pre-pandemic levels.
- Following the Russian invasion of Ukraine, Brent oil reached \$130/bbl, and it is now within the \$115-\$120 range. Risks are skewed to the upside, in our view.



Sources: Bloomberg, Santander.

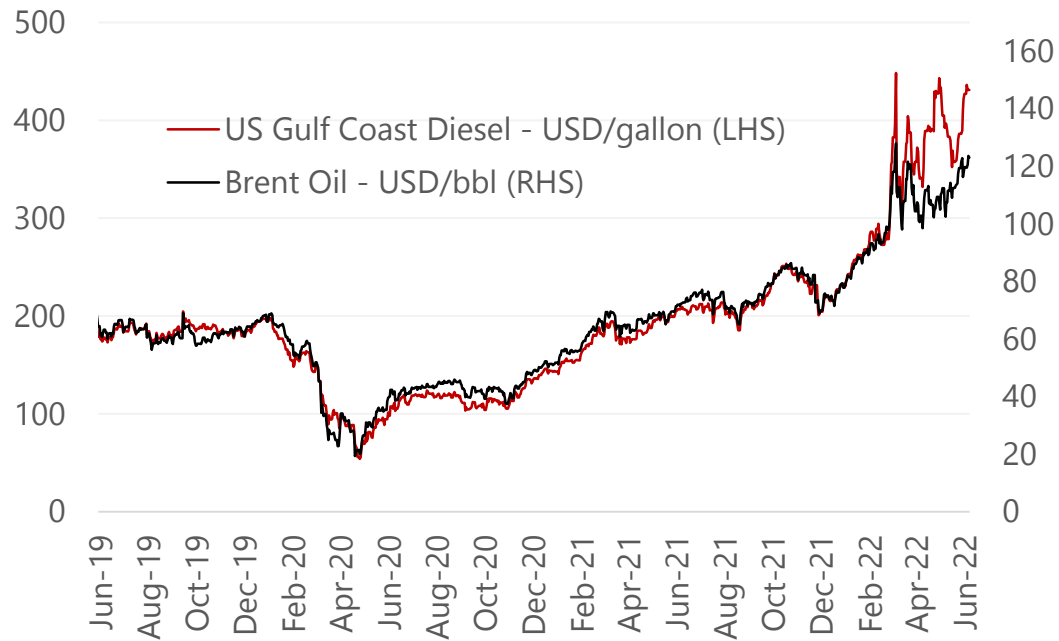


Sources: Bloomberg, Santander.

Diesel Shortage Looms Over Brazil

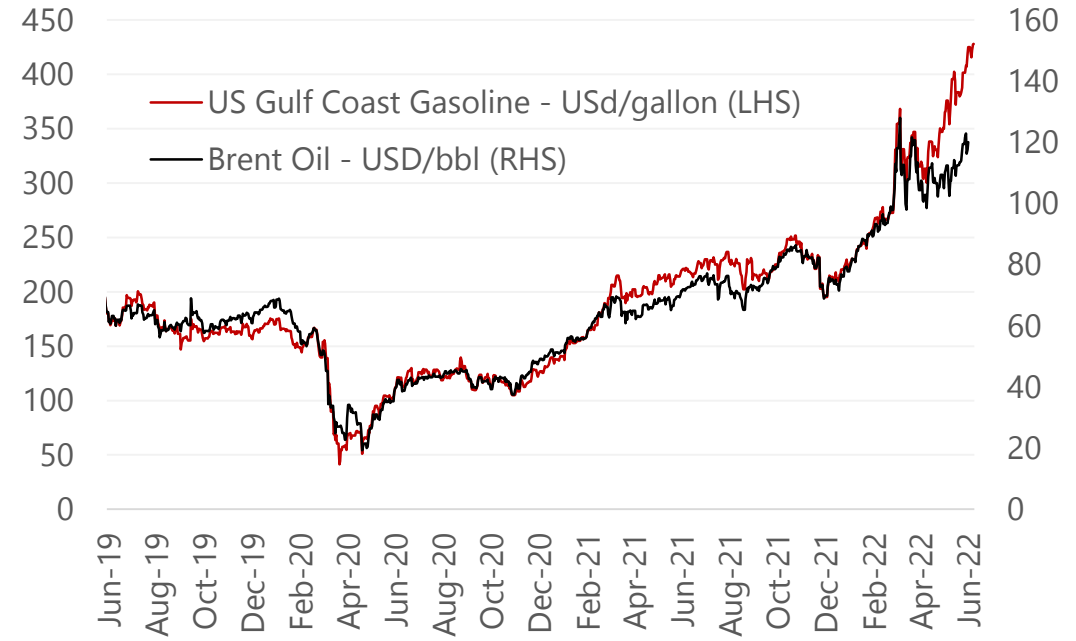
- Brazil imports nearly 30% of its domestic demand for diesel, of which 80% comes from the U.S. Gulf Coast.
- A hypothetical shortage of fuel could quickly exacerbate domestic inflation pressures and dent economic activity.

Oil and Refined Products Price Gap - Diesel



Sources: Bloomberg, Santander.

Oil and Refined Products Price Gap - Gasoline



Sources: Bloomberg, Santander.

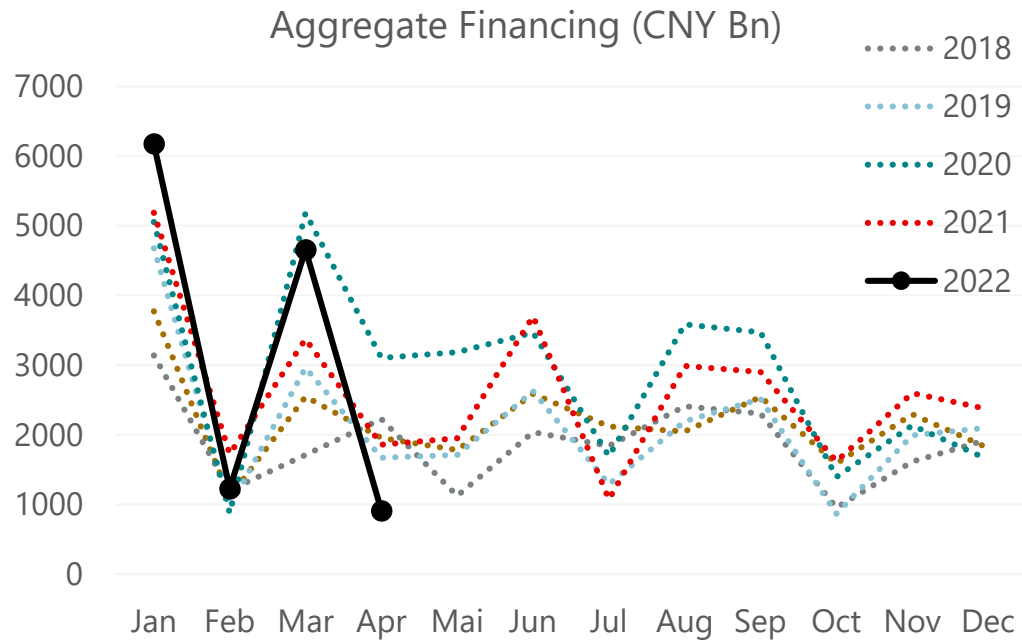
METALS

04

China Will Keep Adding Stimulus To Support Growth

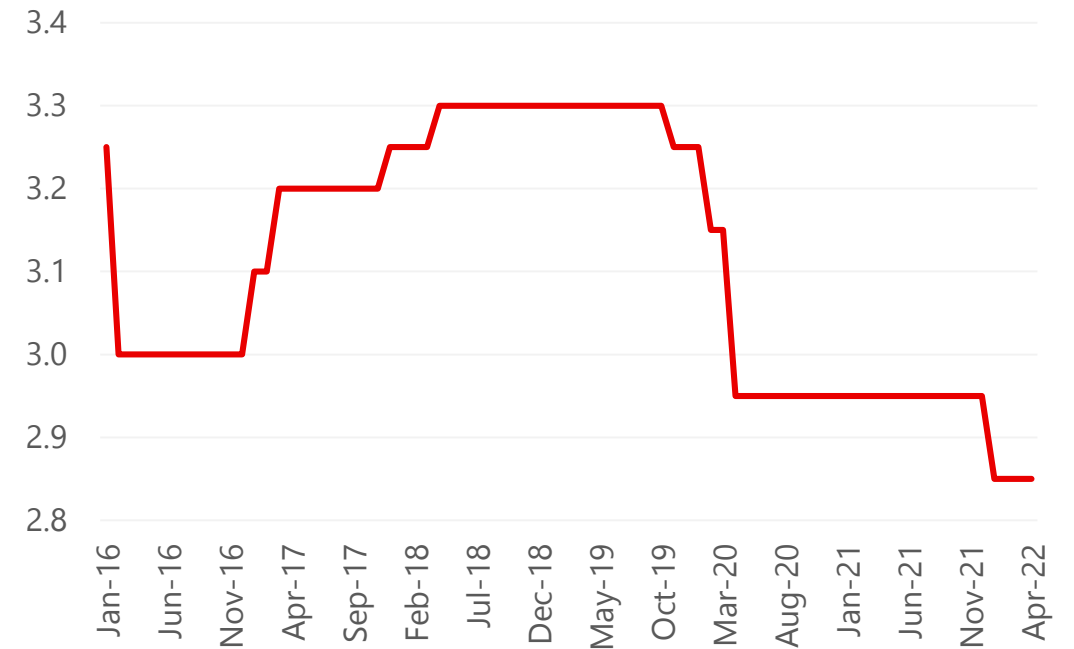
- Assuming that the economy reopens in June, and that there are not new lockdowns in the months ahead, the economy should benefit from strong momentum once the government add stimuli, a tailwind for industrial metals.

Aggregate Financing (CNY Billions)



Sources: PBOC, Santander

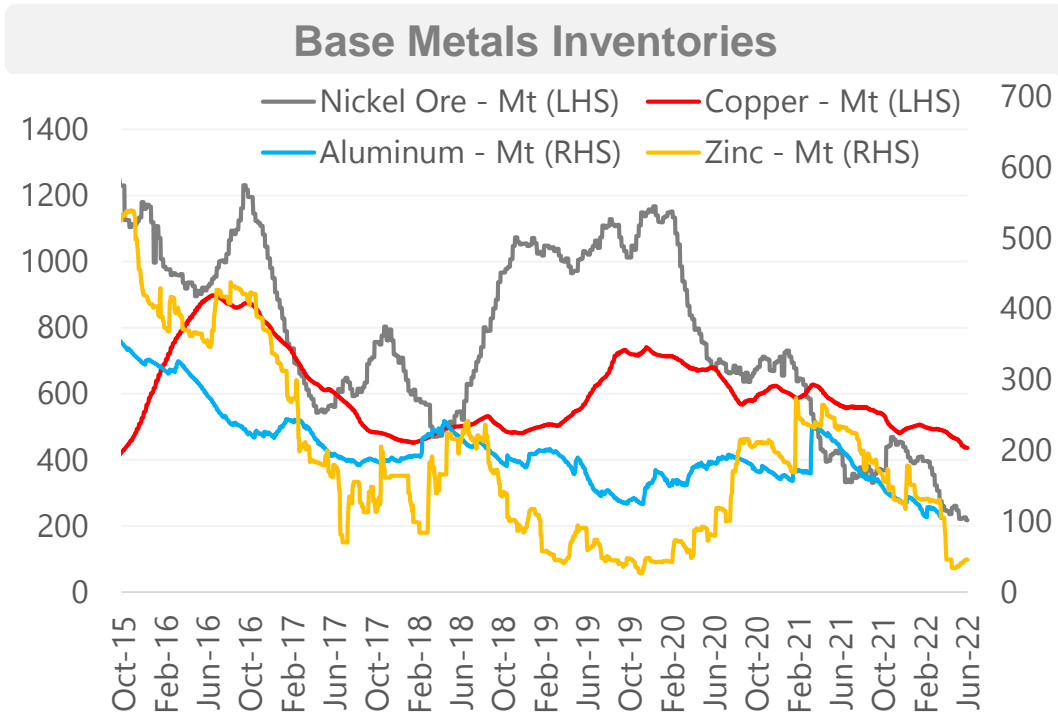
1 Year Medium Term Lending Facility (%)



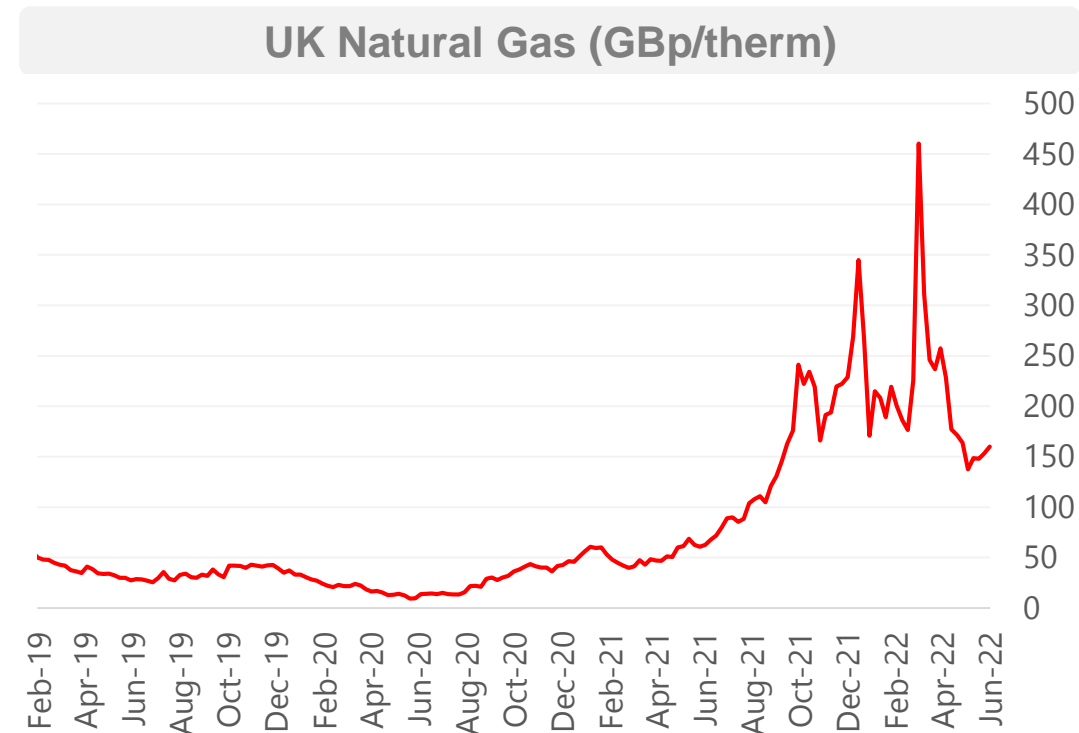
Sources: Bloomberg, Santander

Several Metals Facing Low Stocks and High Production Costs

- From London to Shanghai warehouses, some metals have inventory levels at multi-year lows.
- The power crunch in China and Europe send prices up, raising concerns about supply shortage in industrial metals. The geopolitical shock adds to this already tight scenario.



Sources: Bloomberg, Santander.



Sources: Bloomberg, Santander.

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