Brazil Macro | March 2022

Commodities

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SUMMARY

- **The ongoing geopolitical shock adds to already tight markets for key commodities: low inventories for most raw materials coupled with idiosyncratic factors (adverse weather, underinvestment, and high cost of production) have been feeding the commodity rally early in 2022. On average our forecasts have been revised upward for all indexes (2022E and 2023E): CRB +5%; Food +5%; Energy +7%; Metal +2%. We still see a downward trajectory for most commodity prices, but the reversal from the pandemic-led spike in 2021 may take longer to occur. Our scenario considers that the downward trajectory will begin from 2Q22 onward.**

- For farm commodities, hot and dry weather slashed the production outlook in South America following a favorable start to 2022. As a result, demand (especially from China) is shifting to U.S. grains, as U.S. soybean exports are rising at a time of year when Brazilian shipments typically dominate. Importantly, the short-term weather outlook is still mostly dry for South Brazil and Argentina, and once again, the winter corn harvest will be under close scrutiny.

- In energy, oil prices have recovered strongly following signs of less economic impact from the Omicron variant of COVID-19 compared to previous variants. We still see output shortages in the oil market, as global inventories are low, and producers (ranging from OPEC+ members to independent U.S. shale companies) struggle to boost supply following the underinvestment in recent years. Bottom line, we revised our Brent forecast to US$115 from US$95 for 2022 eop.

- In metals, inventories are worryingly low. From aluminum (prices at a 13-year high) to nickel (prices at an 11-year high), stocks are low throughout the entire supply chain. Moreover, smelters in Europe and China have been cutting production capacity owing to the financial strain caused by high energy costs. As for iron ore, prices for the commodity have strongly rebounded on expectations that consumption will pick up this year due to Chinese government.

OVERVIEW

01

Geopolitical shock adds volatility to an already tight commodities market

- The Russia-Ukraine war led to a commodities shock across the board. As a result, we revised all our index forecasts up on average (2022e, 2023e): **CRB** +**5%**; **Food** +**5%**; **Energy** +**7%**; **Metal** +**2%**.
- Idiosyncratic factors (adverse weather) as well as low inventories and rising costs of production have been feeding the commodity rally early in 2022. We still see a downward trajectory for most commodities prices, but the payback from the pandemic-led spike might take longer with this new geopolitical shock. Our scenario counts on a U-turn in such a rising trend from 3Q22 onwards.

Our Forecasts for CRB Index – End of Period

YE	2019	2020	2021	2022e	2023e
CRB Food	331	355	483	503 ⬆	425 ⬆
CRB Energy	1647	1161	1521	1750 ⬆	1710 ⬆
CRB Metal	749	887	1259	1213 ⬆	1083 ⬆
CRB	401	444	571	574 ⬆	514 ⬆

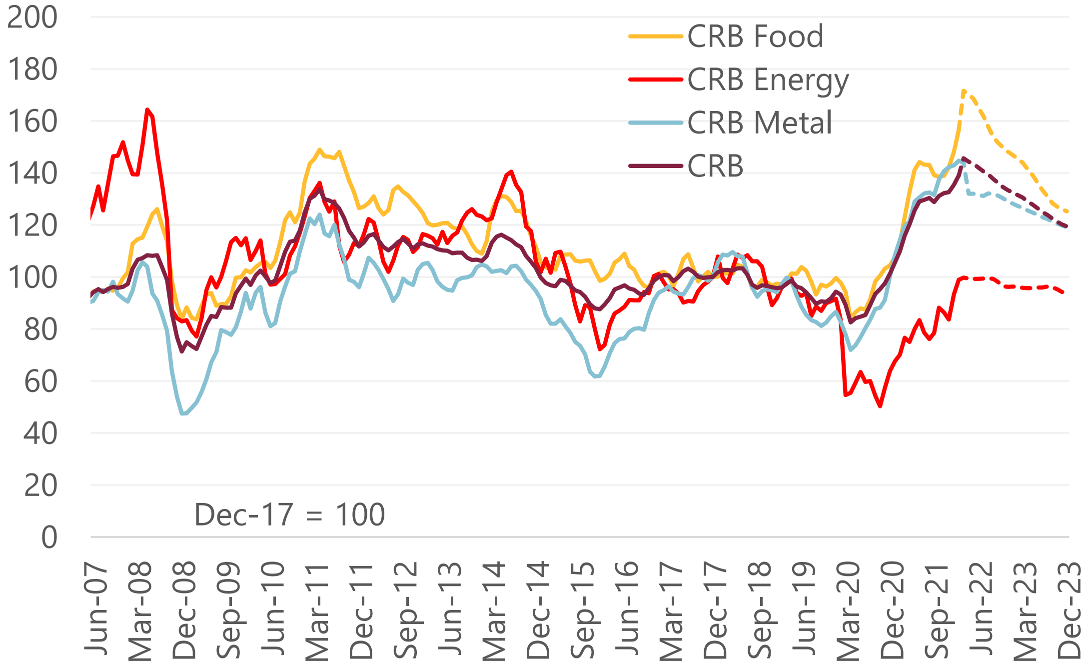
YE YoY	2019	2020	2021	2022e	2023e
CRB Food	1%	7%	36%	4%	-15%
CRB Energy	2%	-30%	31%	15%	-2%
CRB Metal	-11%	18%	42%	-4%	-11%
CRB	-3%	11%	29%	0%	-10%

	Iron Ore	Soybean	Corn	Brent
YTD* %	15%	21%	18%	29%

*Mar 15, 2022.

Sources: Bloomberg, Santander.

Our Forecasts for CRB Index – Monthly Averages



Sources: Bloomberg, Santander.

Comments on Brazil's trade relations with Russia and Ukraine

Trade with Russia (2019)	
Share of exports and imports	Russia represents 4.2% of total Brazilian exports and 6.6% of Brazilian imports.
Main exported goods	Farm products are the main export agenda Russia, with soybeans (+20.4%) and frozen bovine meat (+12.3%) as the highlights.
Main imported goods	Fertilizers and other chemical products accounts for more than 60% of the import agenda with Russia, while refined petroleum and coal briquetes account together for more than 10%.
Trade with Ukraine (2019)	
Share of exports and imports	Ukraine represents 0.27% of total Brazilian exports and 0.23% of Brazilian imports.
Main exported goods	Food and tobacco products are the main products in the export agenda with Ukraine, with raw tobacco (+19.9%) and coffee and tea extracts (+19.9%) as the highlights.
Main imported goods	Packaged medicaments accounts fore more than 30% of the main imports agenda from Ukraine, while metallic products like hot-rolled iron and cold-rolled iron accounts for almost 20%.
Agribusiness	
Exported and imported goods	Both Russia and Ukraine import food items from Brazil, but the trade volume with these countries is small.
Fertilizers	The dependency of Brazil on fertilizers from Russia and Belarus is relevant. Almost 50% of potassic fertilizers come from Russia and Belarus, while almost 30% of nitrogenous fertilizers come Russia. Other important sources are Canada, Germany and China.

Source: OEC, Santander

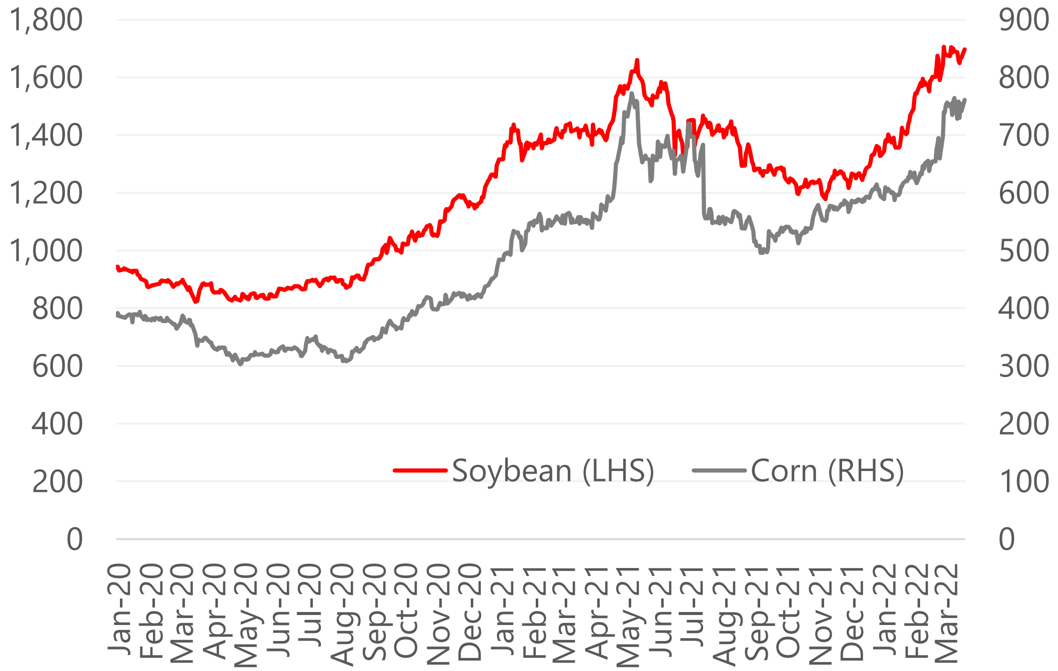
AGRICULTURE

02

Low stocks amid weather and geopolitical shock

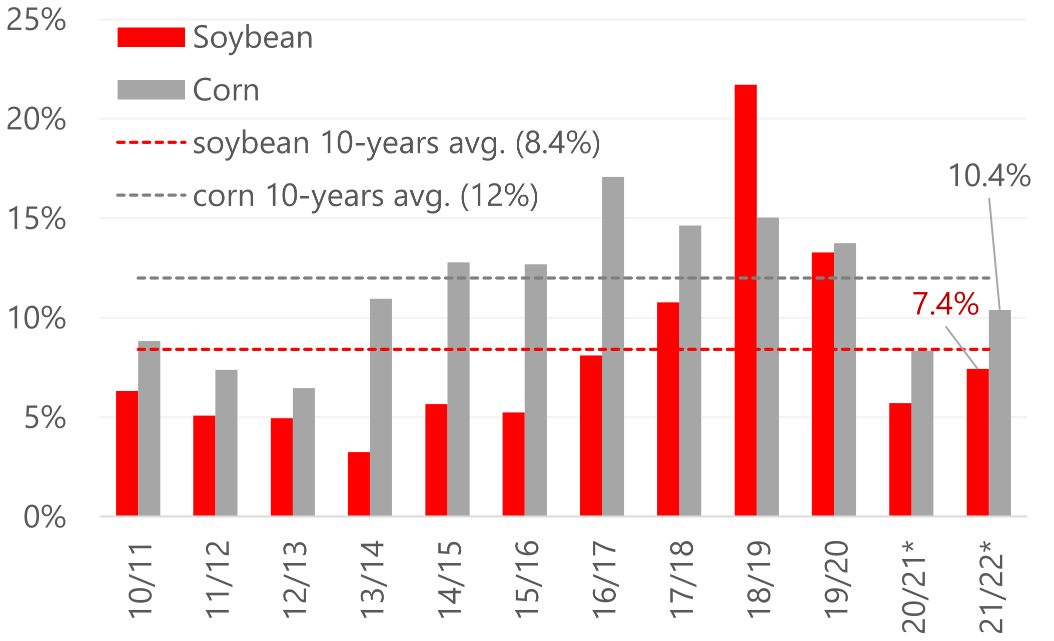
- Low stock-to-use ratio of grains in the US point to a tight market.
- The recent conflict between Russia and Ukraine has been pressuring the grain market even further, as both countries are key exporters: taken together, they account for 30% and 18% of wheat and corn global trade, respectively.

Chicago Board of Trade - Grains (USD cents)



Sources: Bloomberg, Santander.

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



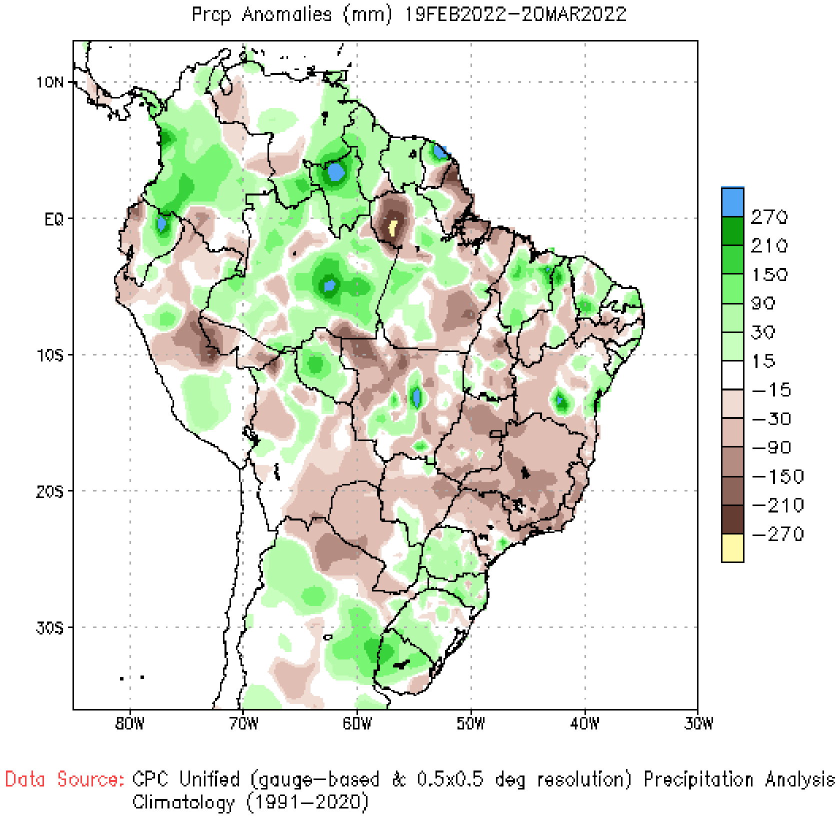
*February 2022 WASDE Report

Sources: USDA, Santander.

Low stocks amid weather and geopolitical shock

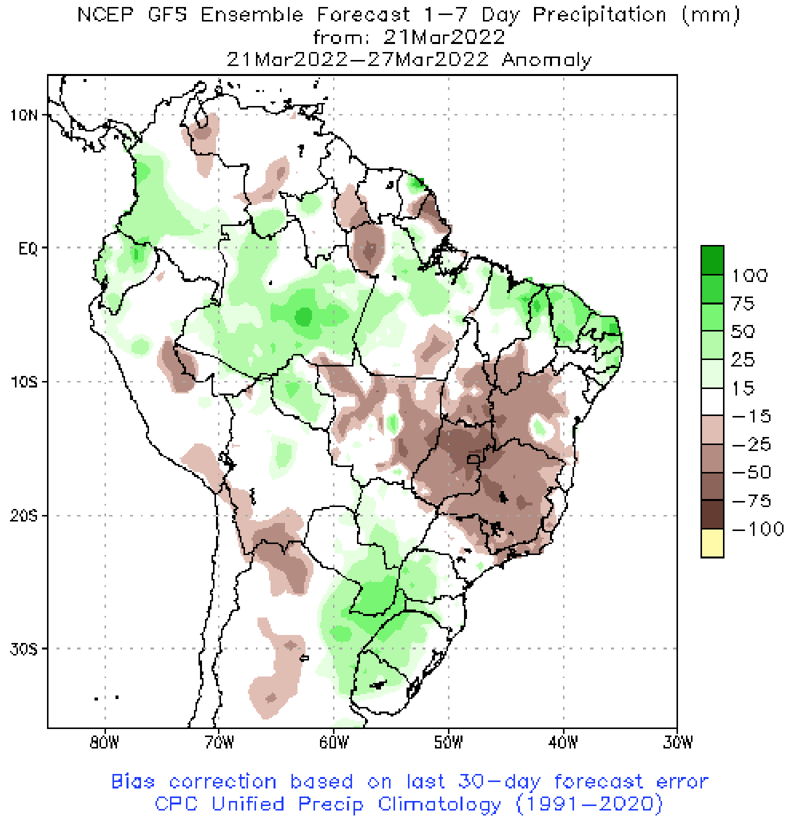
- Rains are expected to continue in the south part of Brazil, while the Mid-West and Southeast should see fewer rains.

Precipitation (30-day anomaly)



Sources: NOAA, Santander.

GFS Precipitation Forecasts (7-day anomaly)

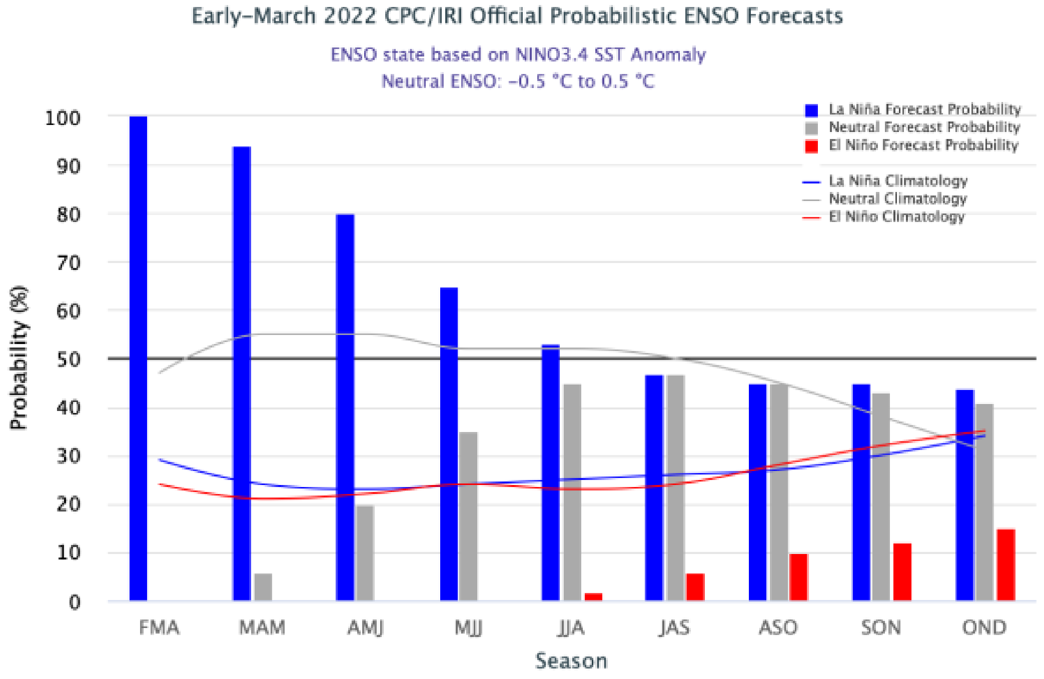


Sources: NOAA, Santander.

Low stocks amid weather and geopolitical shock

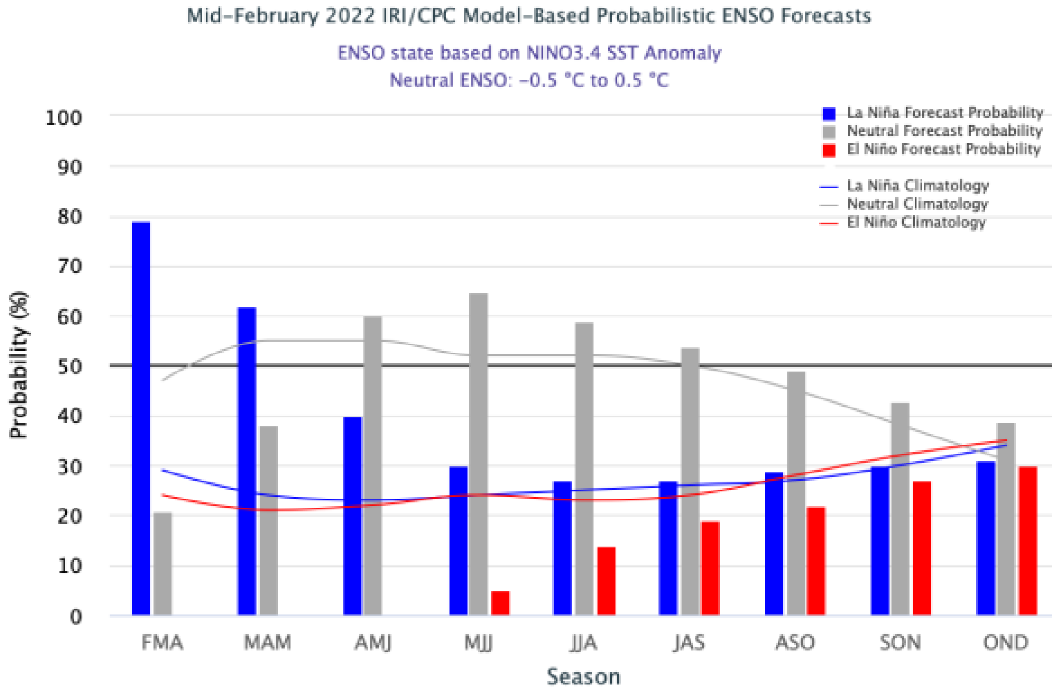
- According to NOAA forecast, La Niña could extend itself in the coming months, a risk for the south part of South America that could suffer from drought conditions once again.

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



Sources: NOAA, Santander.

La Niña Outlook – CPC/IRI PROBABILISTIC
Second half of February



Sources: NOAA, Santander.

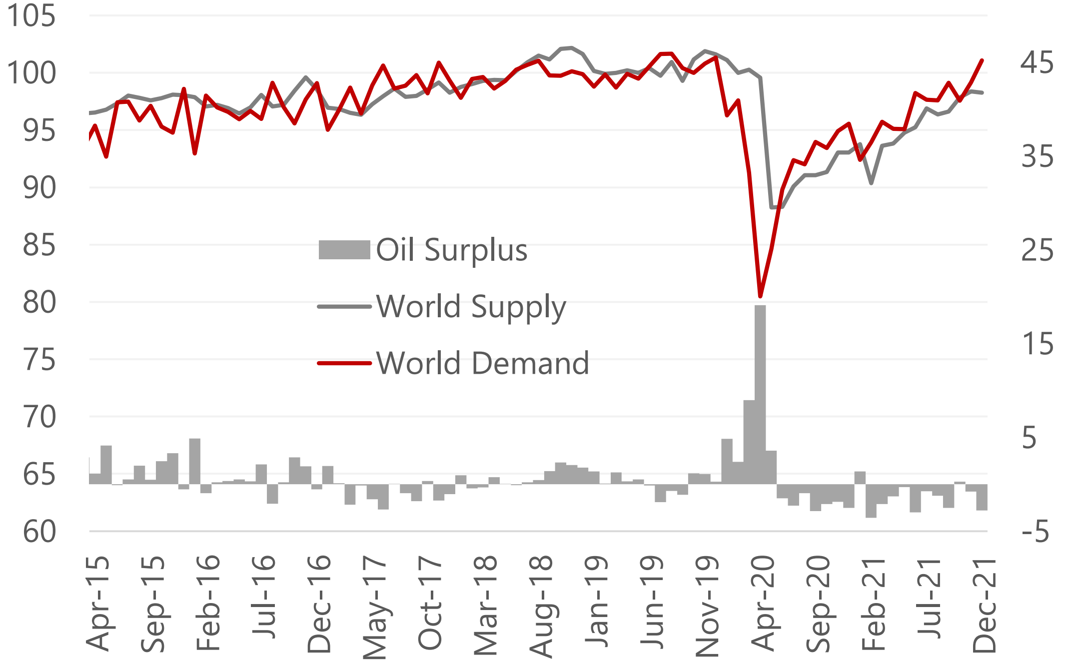
ENERGY

03

Geopolitical shock adds volatility to an already tight commodities market

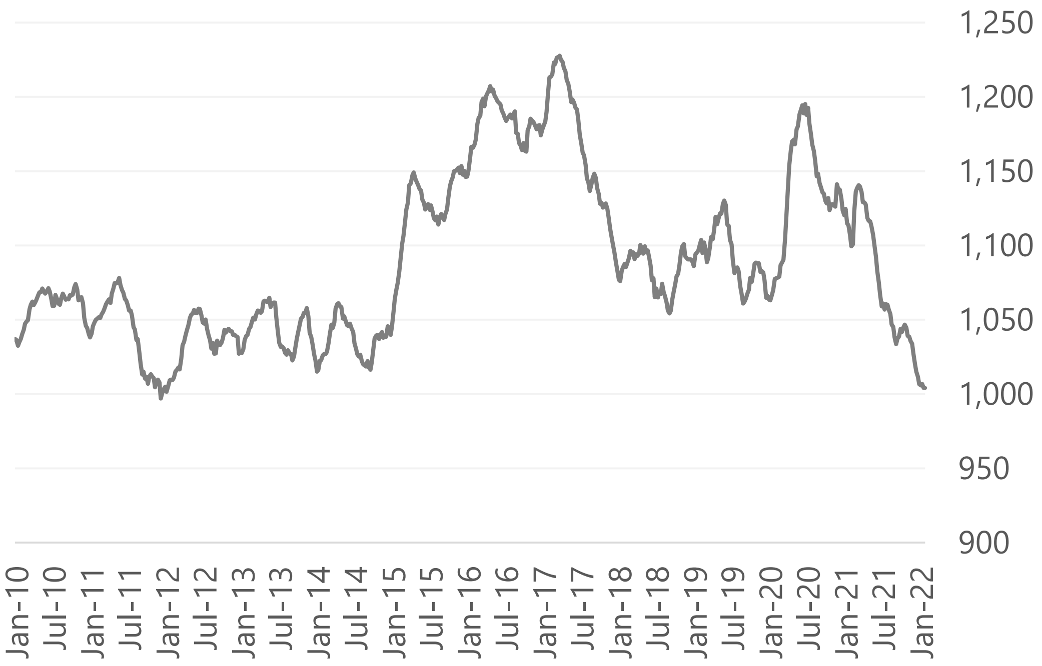
- Global market deficit. As the economy recovers from the coronavirus pandemic and majors oil producers fall short of output, the global oil balance of supply and demand has been consistently running on deficit.
- As a result, global inventories are the tightest in at least 7 years: US crude inventories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

World Oil Supply x Demand (mbd)



Sources: Bloomberg, Santander.

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

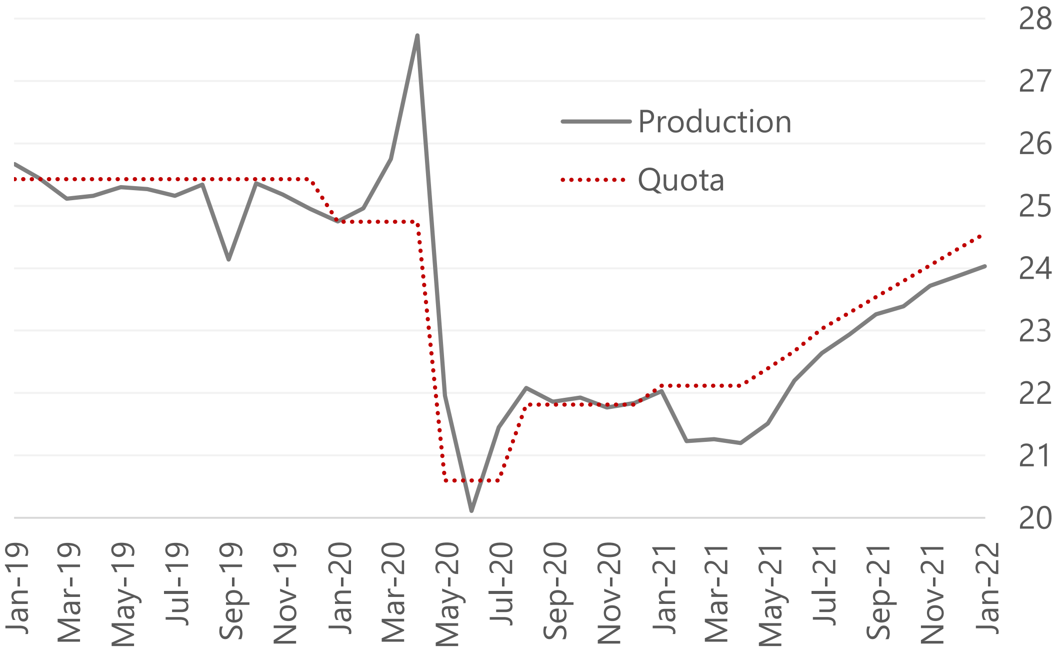


Sources: Bloomberg, Santander.

Geopolitical shock adds volatility to an already tight commodities market

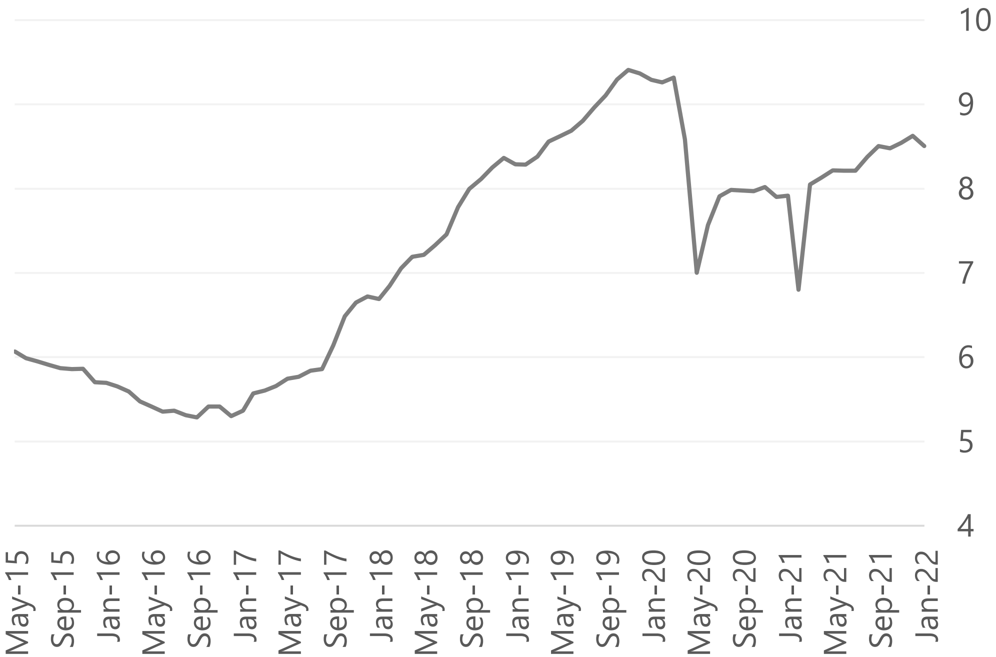
- Underinvestment in OPEC+. The organization has been gradually increasing its production quota on a monthly basis. However, it has been failing to meet its target due to production shortfalls in several members, owing to low investments before and during the pandemic.
- Underinvestment in shale producers. US oil production is currently at 11.6 million barrels, still 11% 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.

OPEC Production (members with quota) (mbd)



Sources: Bloomberg, Santander.

US Shale Production (mbd)

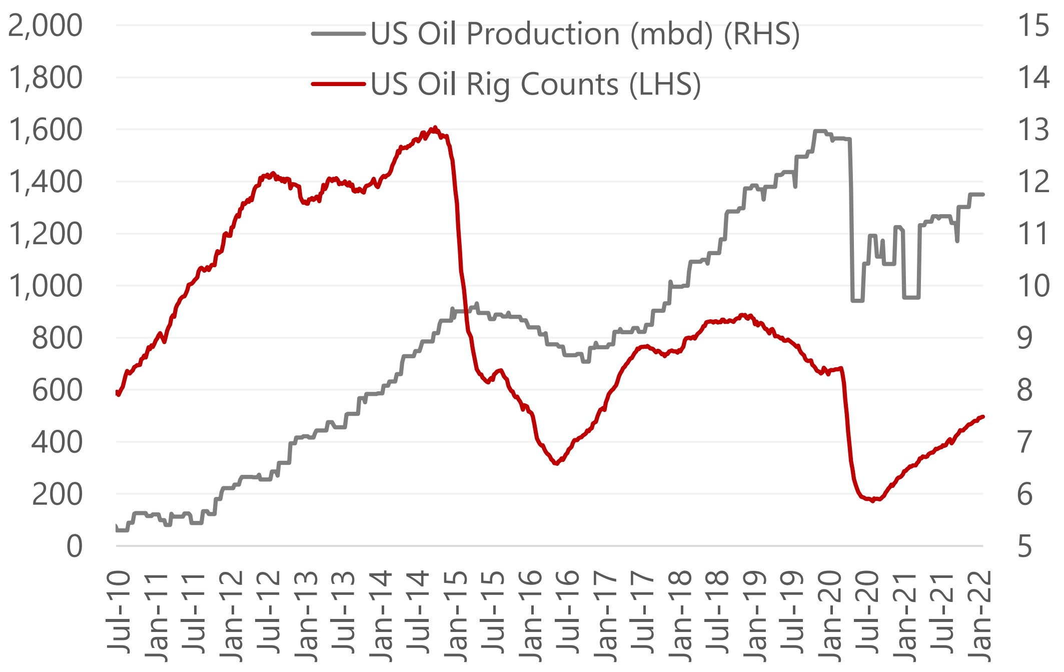


Sources: Bloomberg, Santander.

Geopolitical shock adds volatility to an already tight commodities market

- 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.

US Oil Production



Sources: Bloomberg, Santander.

Brent Crude Oil (USD/bbl)

Sources: Bloomberg, Santander.

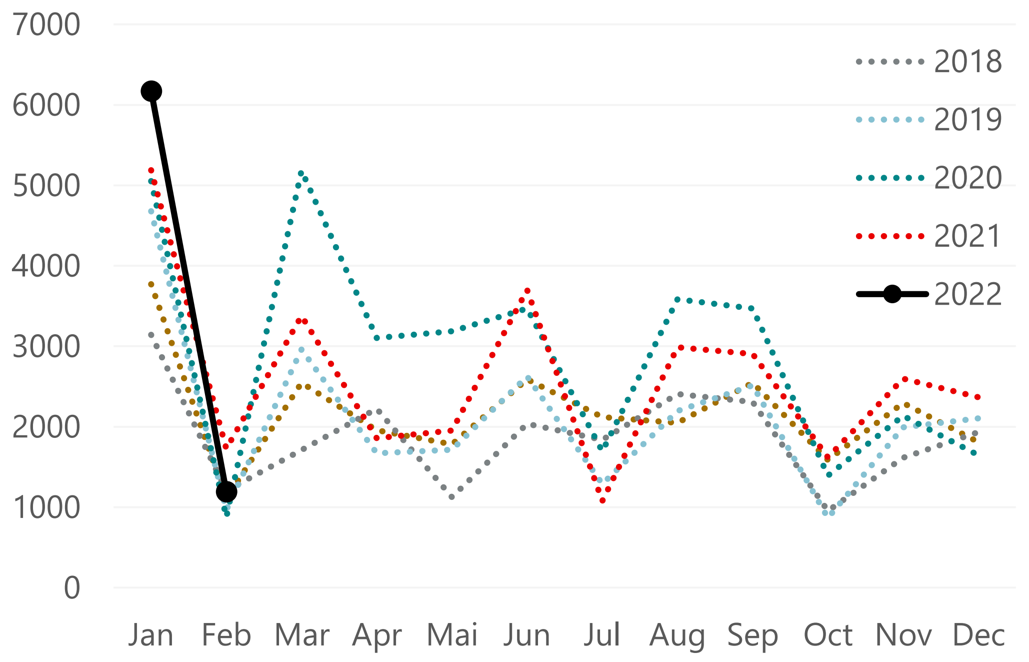
METALS

04

China Will Keep Adding Stimulus To Support Growth

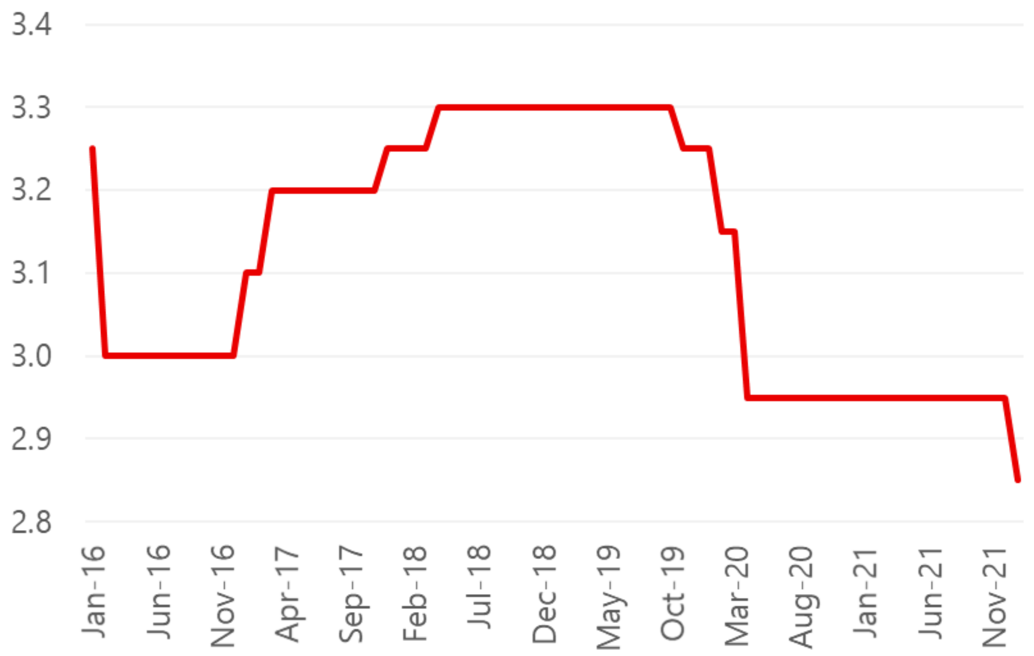
- Government is concerned with the activity slowdown and is already acting to support growth. The traditional instruments are being used (monetary, credit and fiscal tools). We expect 2022 to be a year of “stability”, with growth just below 5.5%.
- Stimulus in China means a tailwind for industrial metals.

Aggregate Financing (CNY Billions)



Sources: PBOC, Santander

1 Year Medium Term Lending Facility (%)

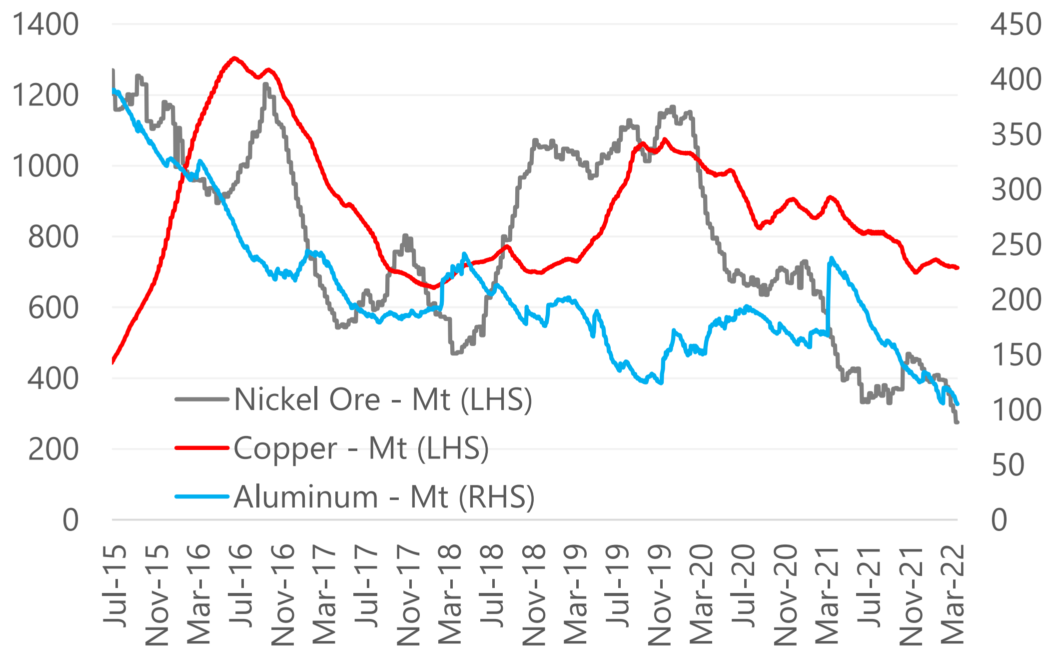


Sources: Bloomberg, Santander

Several metals facing low stocks and higher production costs

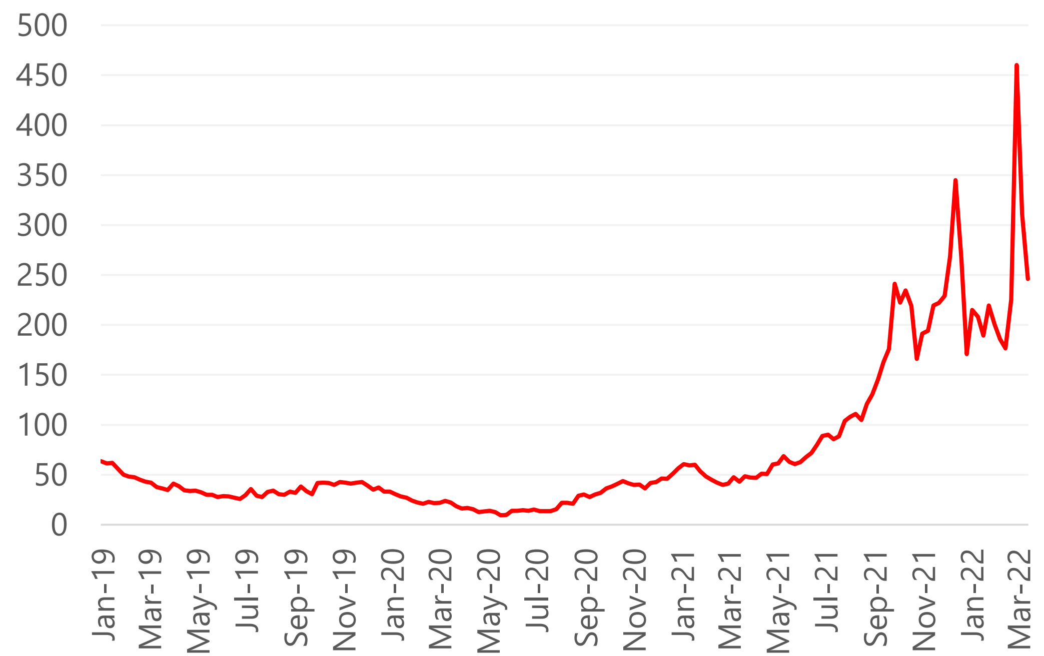
- From London to Shanghai warehouses, some metals have inventory levels at multi-year lows.
- The power crunch in China and Europe send prices up, raising concerns about supply shortage in industrial metals. The geopolitical shock adds to this already tight scenario.

Metals Inventories



Sources: Bloomberg, Santander.

UK Natural Gas (GBp/therm)



Sources: PBOC, Santander.

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