Brazil Macro | March 2023

Commodities

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SUMMARY

Commodity markets have recently been affected by the international banking crisis, spurring increased volatility, particularly in oil markets, with crude prices tumbling on fears of a potential recession and slowdown in consumption, even with a little support from further output cuts by OPEC+. Fundamentally, supply issues remain in place and continue to support prices at high levels (the CRB index is still 30% above pre-pandemic levels), but the monetary tightening promoted by key central banks is expected to spark a deceleration in global activity, a headwind for commodities demand. We have slightly downgraded our aggregate commodity price indexes forecast for YE2023, on the back of an improved outlook for agricultural output. We still forecast 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 Global Slowdown Amid Macro Woes

- With a slowdown in global economic growth in a backdrop of rising global interest rates, we expect a worse demand for raw materials. The current banking crisis adds uncertainty to the outlook.
- We slightly downgraded our 2023e forecast, driven by agri commodities. We still expect **a slow downward path** for the headline CRB Index and its key components, **suggesting an extended commodity cycle**.

Our Forecasts for CRB Index – End of Period

YE	2019	2020	2021	2022	2023e	2024e	2025e
CRB Food	331	355	483	539	431 ↓	395 →	371 →
CRB Energy	1647	1161	1521	2078	1863 →	1724 →	1619 →
CRB Metal	749	887	1259	1010	1060 →	977 →	918 →
CRB	401	444	571	558	514 ↓	474 →	445 →

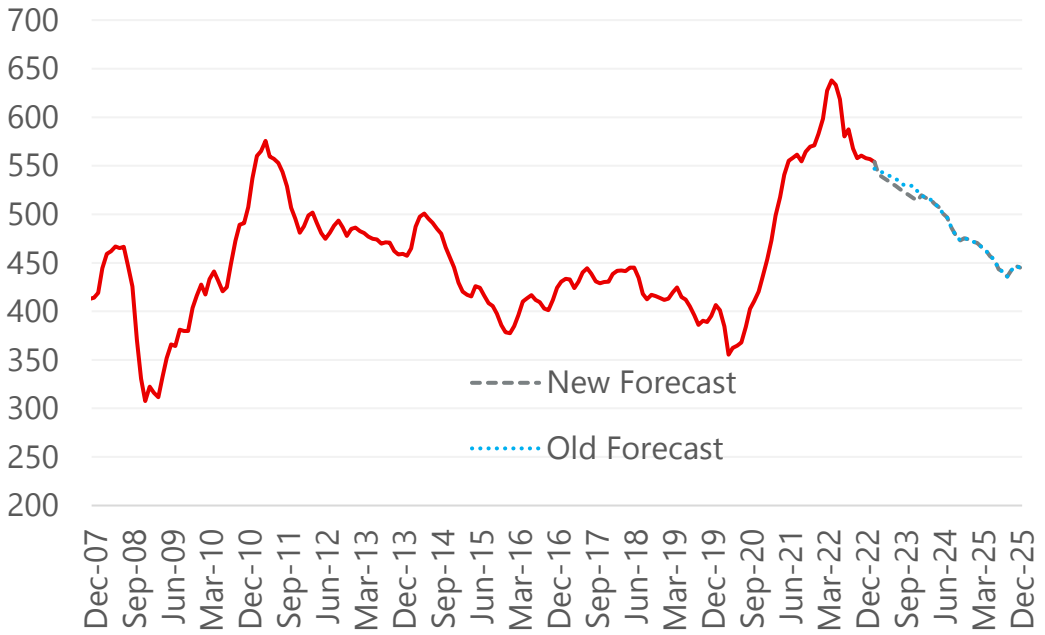
YE YoY	2019	2020	2021	2022	2023e	2024e	2025e
CRB Food	1%	7%	36%	12%	-20%	-8%	-6%
CRB Energy	2%	-30%	31%	37%	-10%	-7%	-6%
CRB Metal	-11%	18%	42%	-20%	5%	-8%	-6%
CRB	-3%	11%	29%	-2%	-8%	-8%	-6%

	Iron Ore	Soybean	Corn	Brent
2023 change*	6%	-5%	-7%	-7%

* March 29, 2023.

Sources: Santander.

Our Forecasts for CRB Index – Monthly Averages



Sources: Bloomberg, Santander.

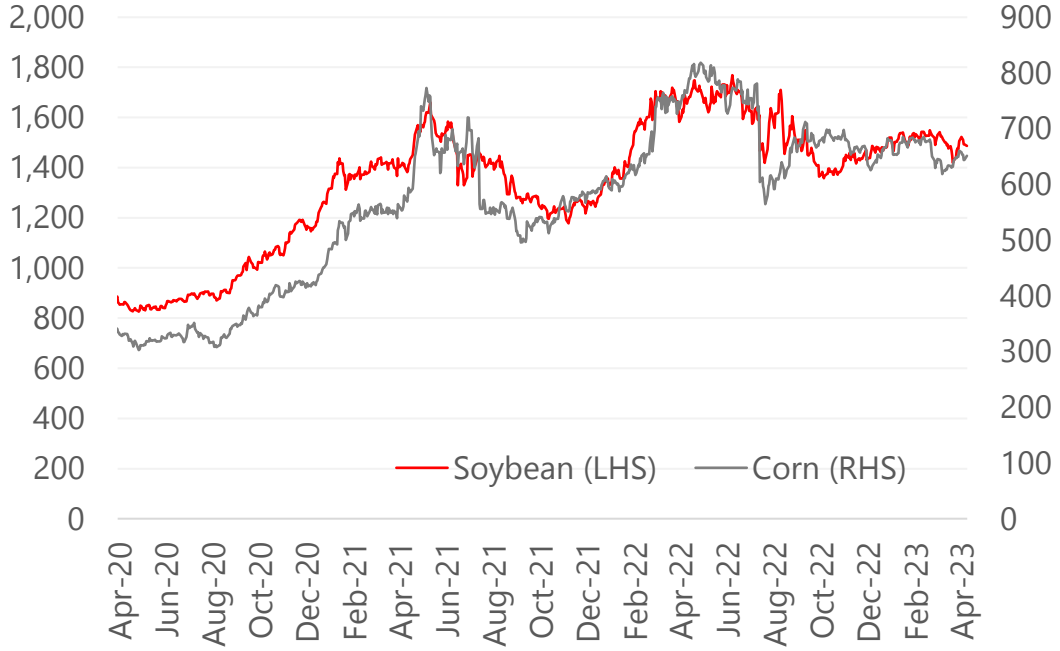
AGRICULTURE

02

Agri: A transition to El Niño

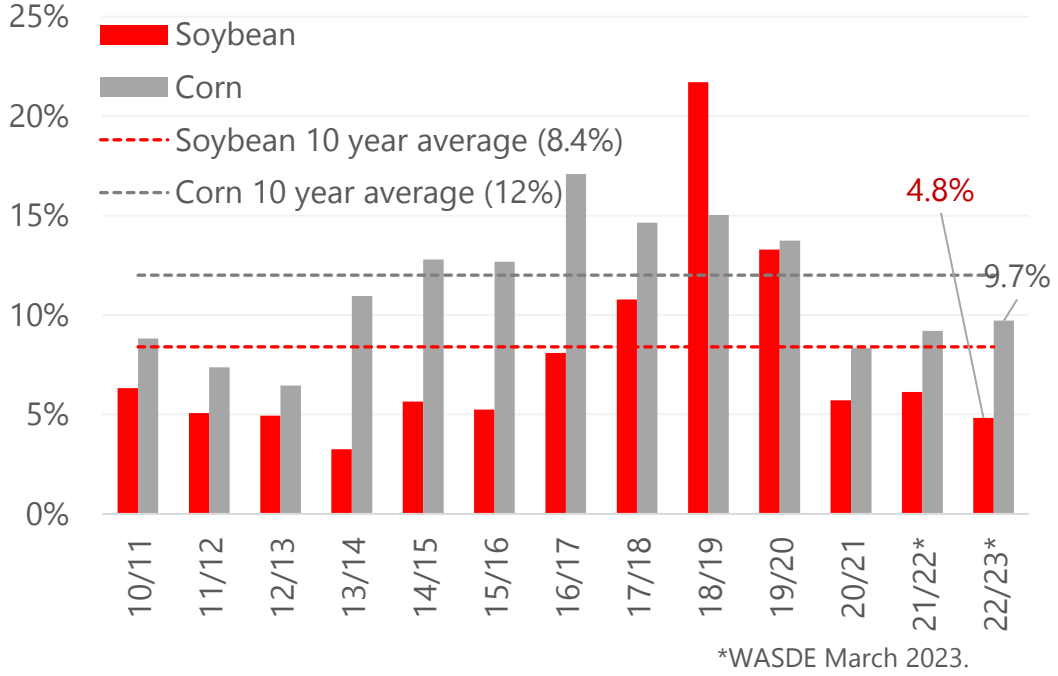
- For agricultural commodities, following three consecutive years of La Niña, crops in South America (notable Brazil and Argentina) will finally see some relief as a transition to El Niño is favored by the 3Q23.
- In Europe, Ukraine said the agreement with Russia to allow grain exports from Ukrainian ports through a corridor in the Black Sea has been extended for at least 60 days (the countries involved still disagree over how the length of the extension).

Chicago Board of Trade - Grains (USD cents)



Sources: Bloomberg, Santander.

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



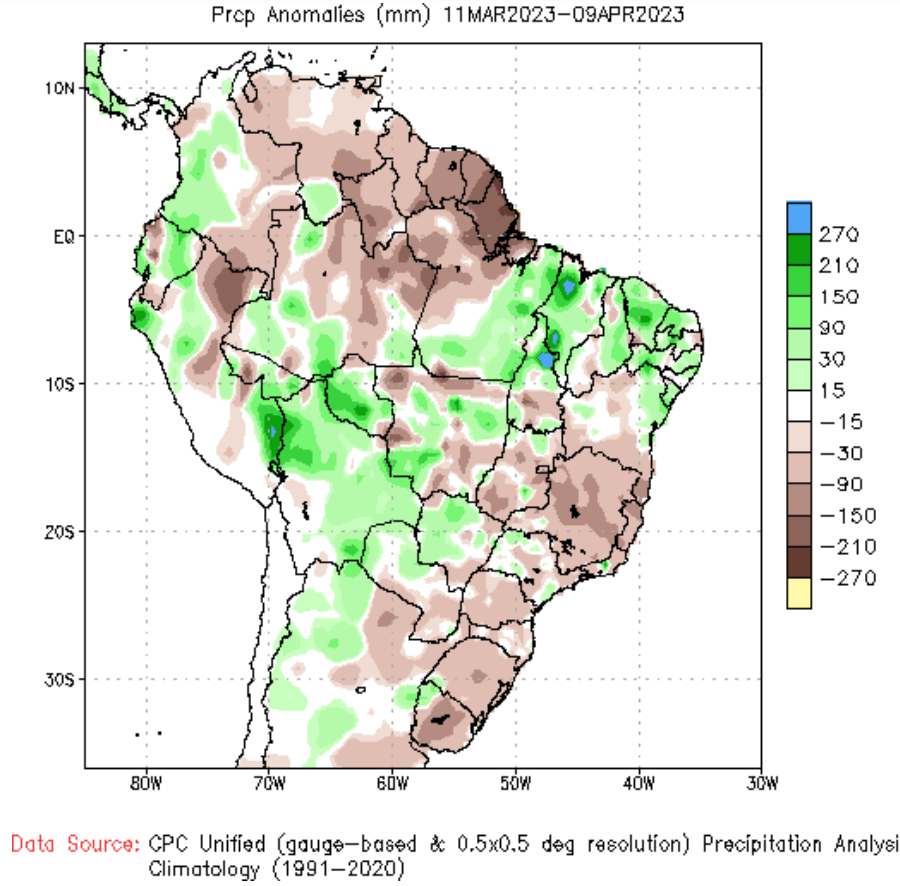
*WASDE March 2023.

Sources: USDA, Santander.

Agri: A transition to El Niño

- 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.

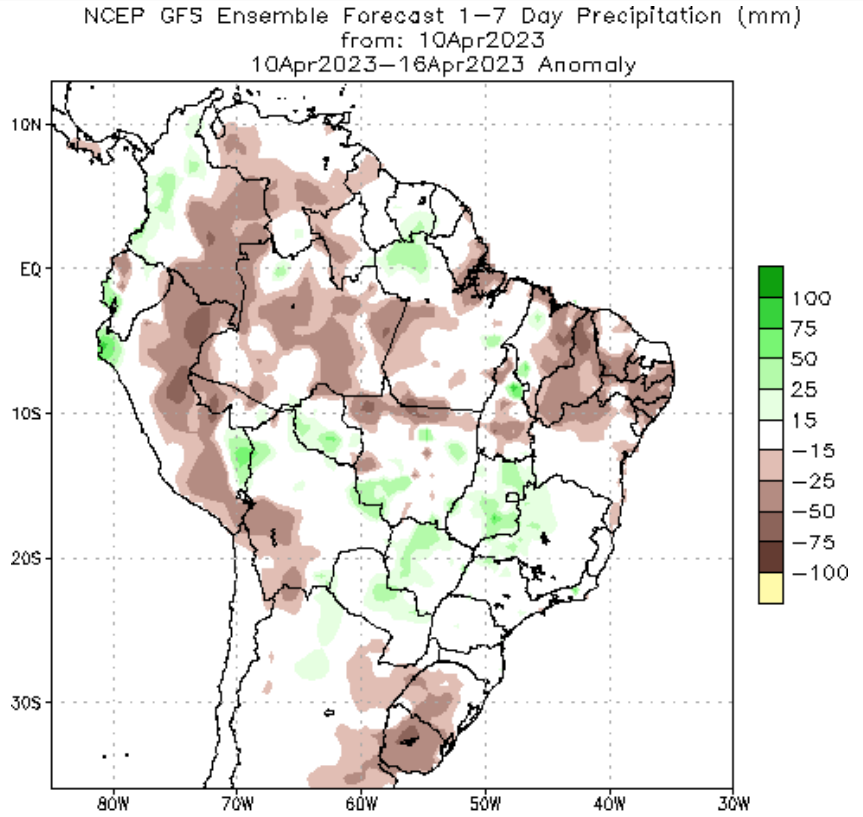
Precipitation (30-day anomaly)



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)



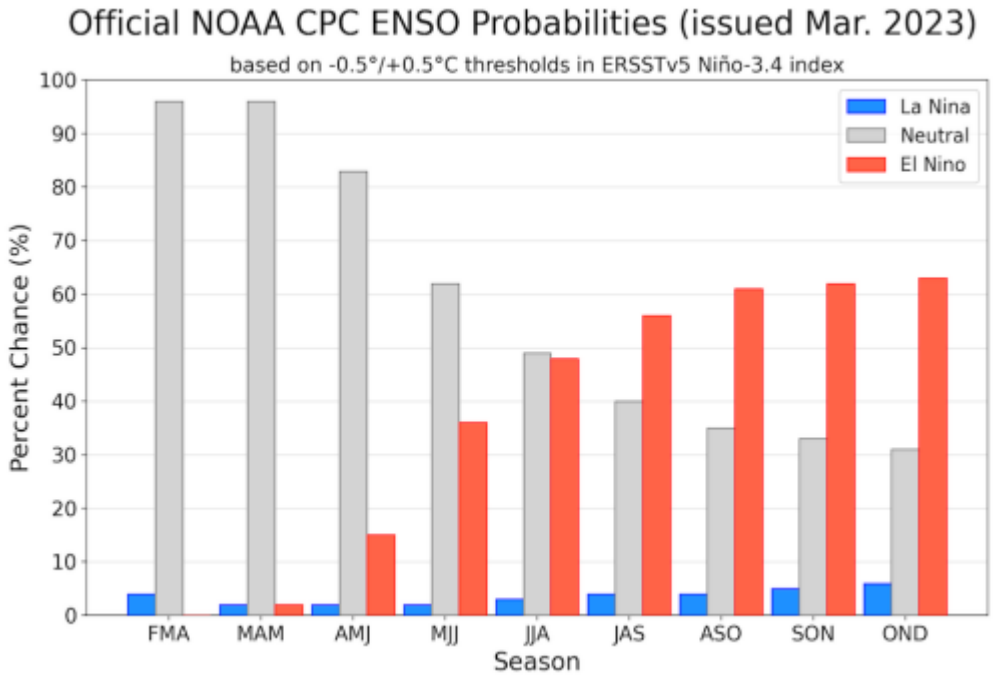
Bias correction based on last 30-day forecast error
CPC Unified Precip Climatology (1991-2020)

Sources: NOAA, Santander.

Agri: A transition to El Niño

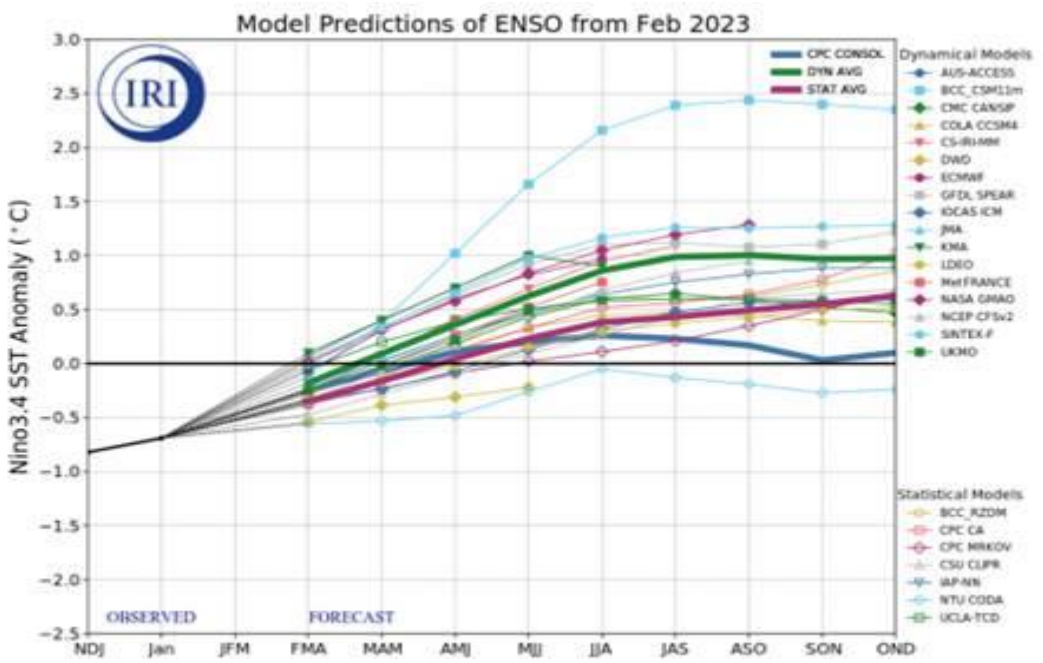
- ENSO-neutral is expected to persist through the Northern Hemisphere early summer 2023. A transition to El Niño is favored by July-September 2023, with chances of El Niño increasing through the fall.
- By May-July 2023, the dynamical models suggest a potential return to El Niño, while the statistical models indicate the continuation of ENSO-neutral into the Northern Hemisphere summer, before warming up to borderline El Niño conditions in the late summer/fall 2023.

Official NOAA ENSO Probabilities



Sources: NOAA, Santander.

Model Predictions of ENSO

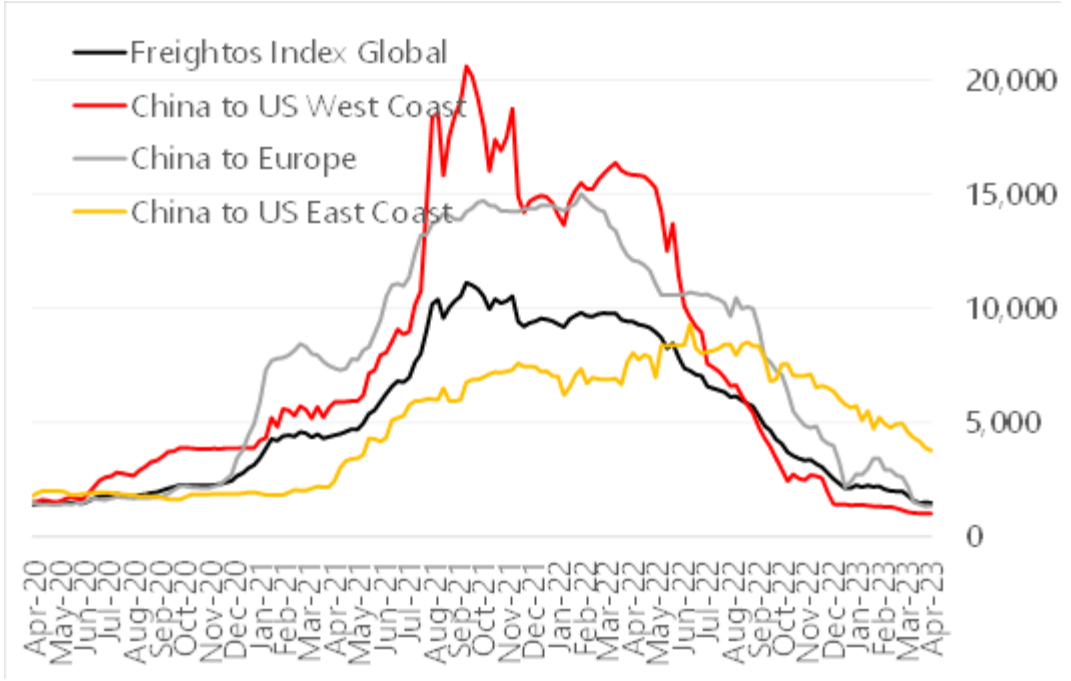


Sources: NOAA, Santander.

Agri: A transition to El Niño

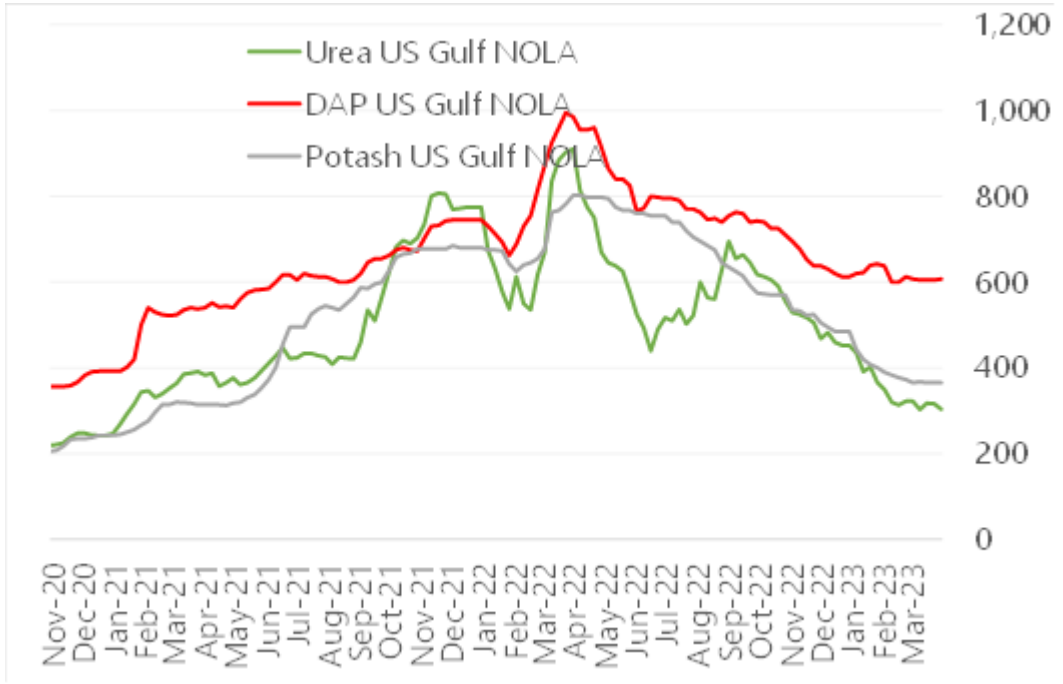
- Most freight cost proxies continue to fall at the margin (helping deflation prints), with some routes already back to pre-pandemic levels. This suggests that the supply chain problems triggered by the pandemic continue to ease.
- Fertilizers prices are also seeing a relief at the margin (although still in high level). This generates better prospects for food-inflation.

Freight Costs Index



Sources: Bloomberg, Santander.

Fertilizers prices (USD/t)

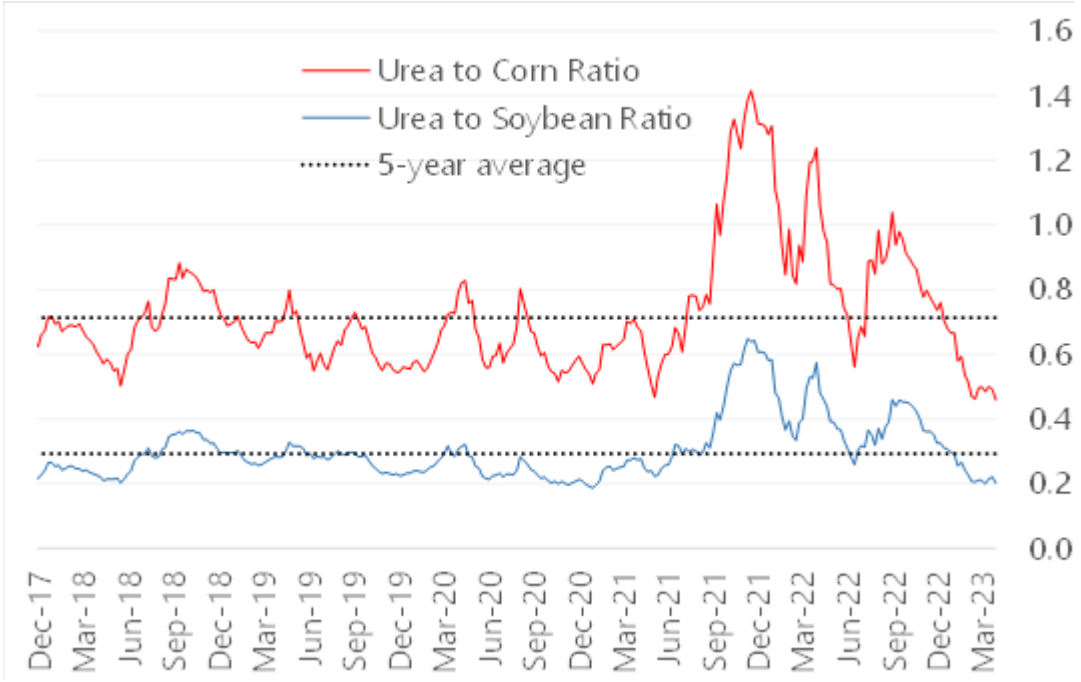


Sources: Bloomberg, Santander.

Agri: A transition to El Niño

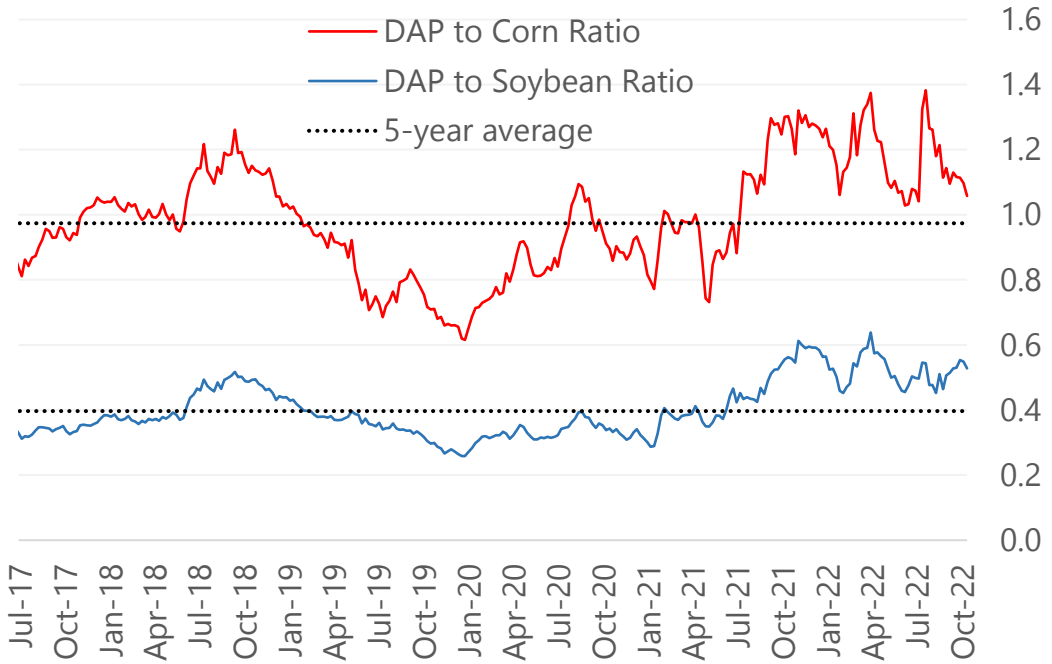
- Fertilizer-to-grain price ratios for urea, an important affordability metric, are below the 5-year average for corn and soybean.
- Fertilizer-to-grain price ratios for DAP is close to the 5-year average. With a good affordability, producers have incentive to both use more fertilizer and increase planted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

Fertilizer Affordability - Urea



Sources: Bloomberg, Santander.

Fertilizer Affordability - DAP

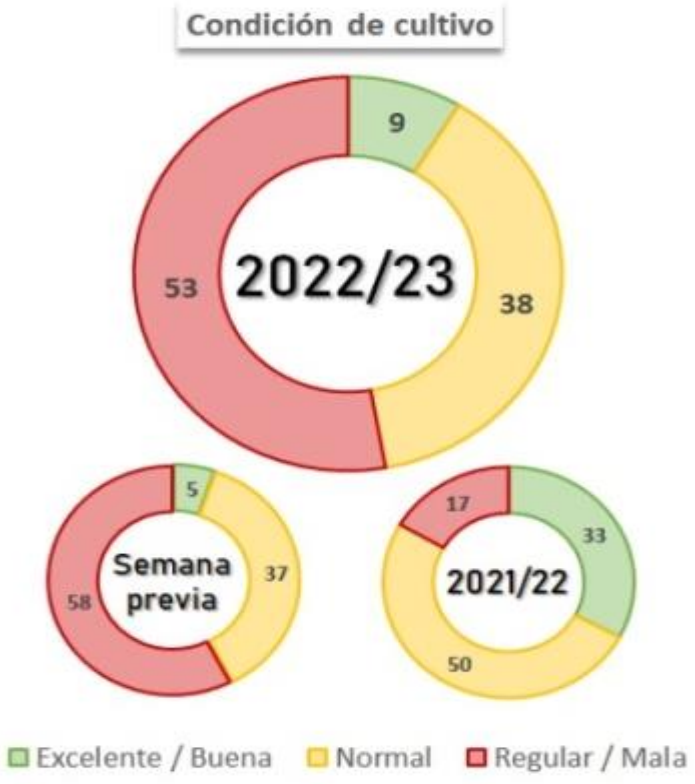


Sources: Bloomberg, Santander.

Agri: A transition to El Niño

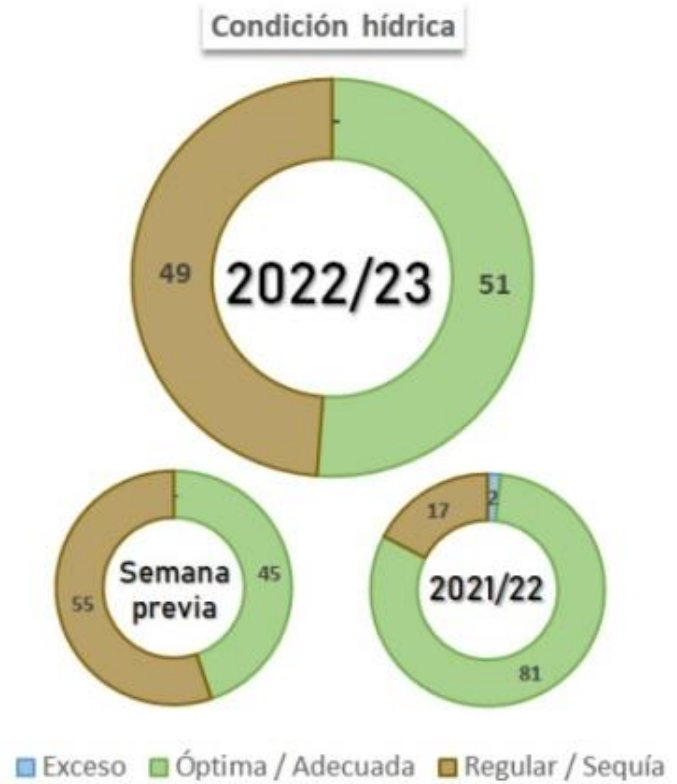
- Professionals from the BCBA (Bolsa de Cereais de Buenos Aires) classify Argentinian corn crops in good or excellent conditions at 9% (up from 5% last week) in 2022/2023. The condition is below the 33% in 2021/2022.

Corn in Argentina - Crop Condition



Sources: BCBA, Santander.

Corn in Argentina – Soil Water Condition

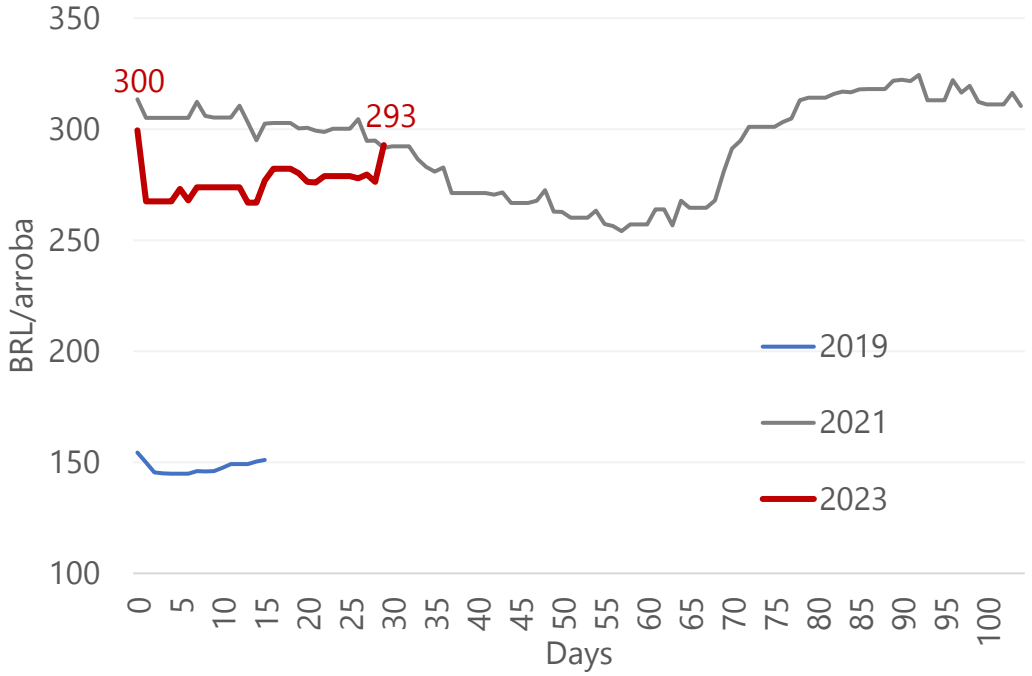


Sources: BCBA, Santander.

Agri: China resumes Brazilian beef imports

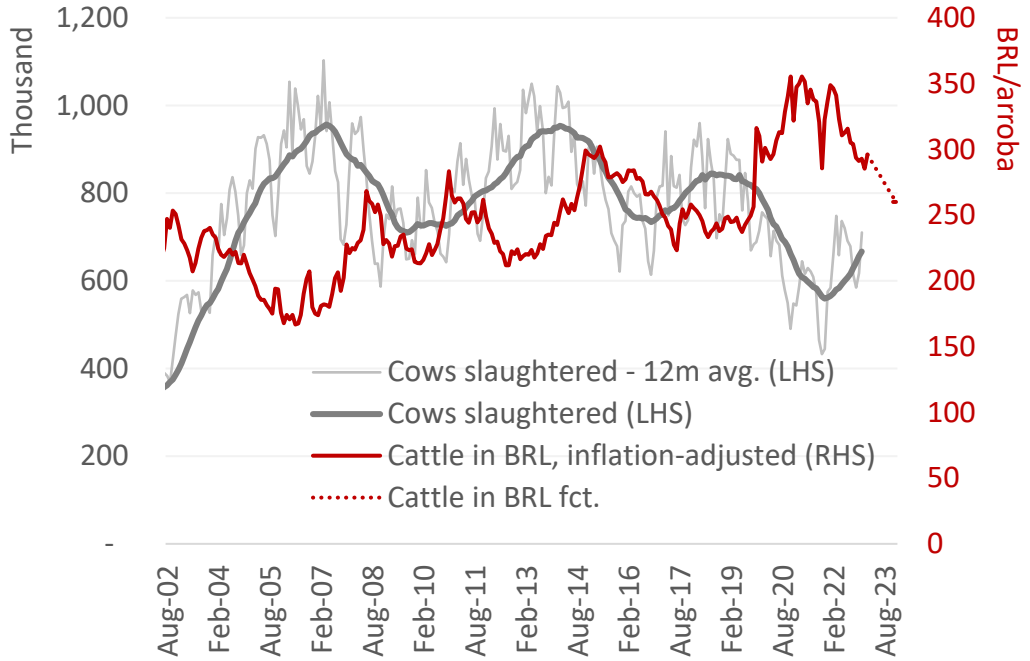
- On March 23, China has agreed to resume import of Brazilian beef following an atypical case of mad cow disease in Brazil (the embargo lasted for 30 days).

Cattle prices following report of mad cow disease



Sources: Bloomberg, Santander.

Cattle Cycle in Brazil



Sources: IBGE, Bloomberg, Santander.

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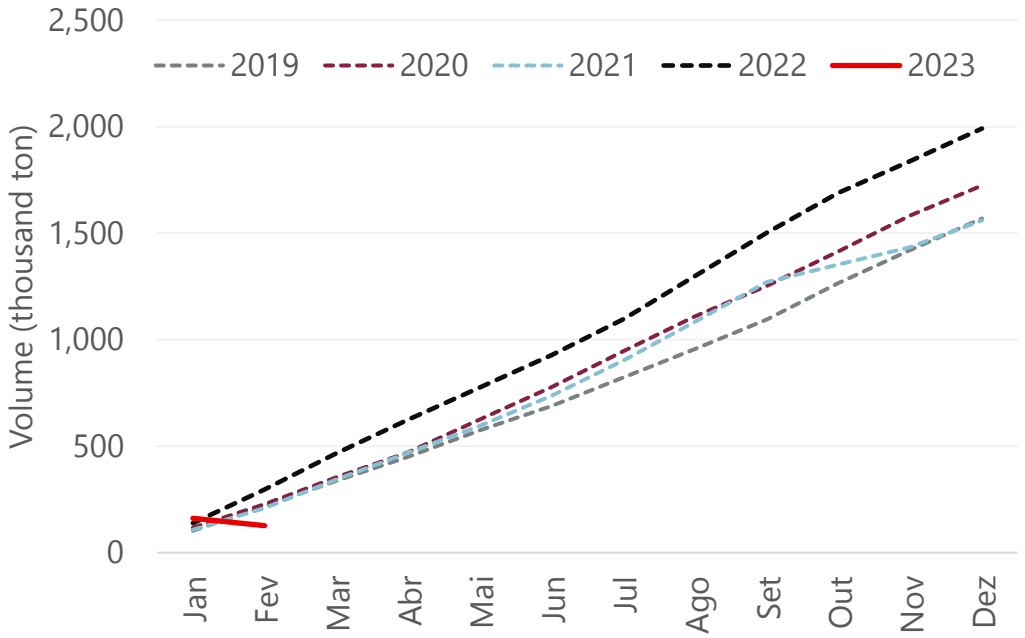
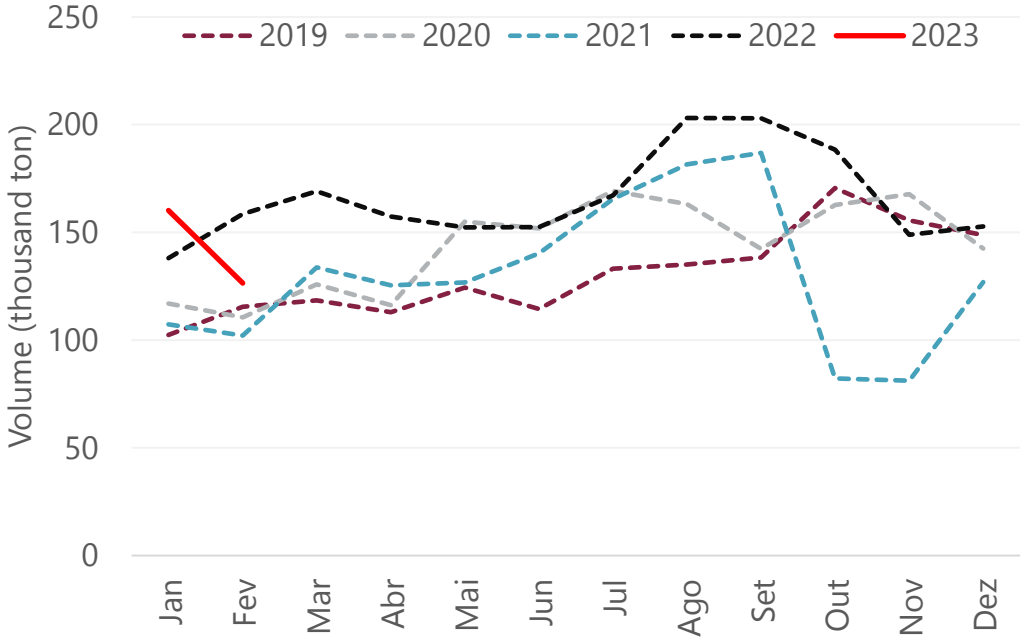
Brazil - Beef export (accumulated)



Sources: SECEX, Santander.

Brazil - Beef export (monthly)



Sources: SECEX, Santander.

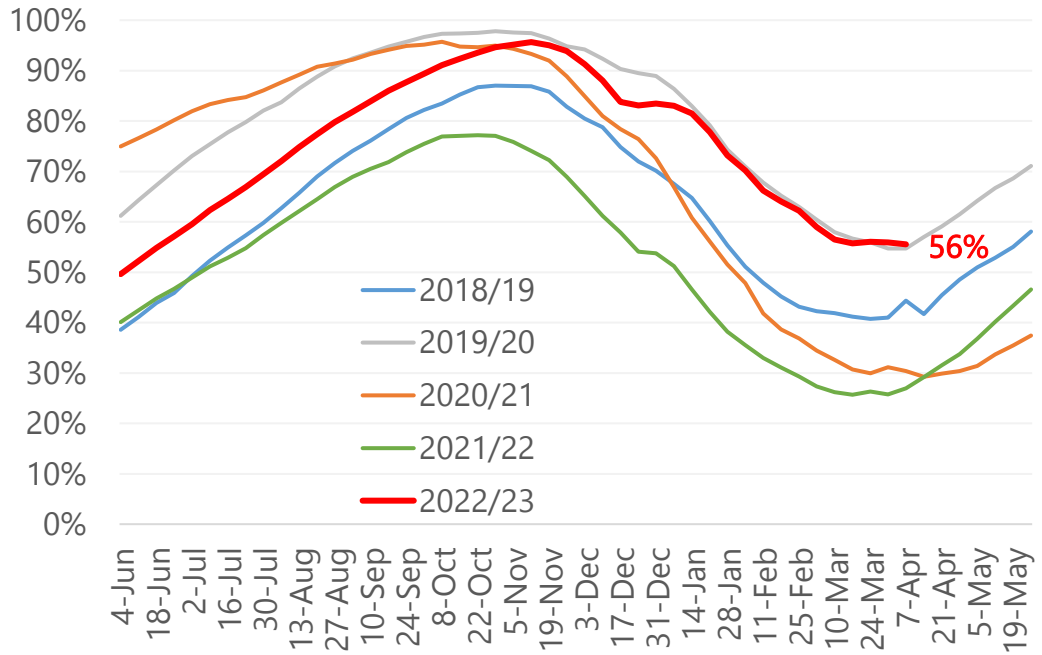
ENERGY

03

Natural Gas in Europe Recedes Following Demand Destruction and LNG Imports

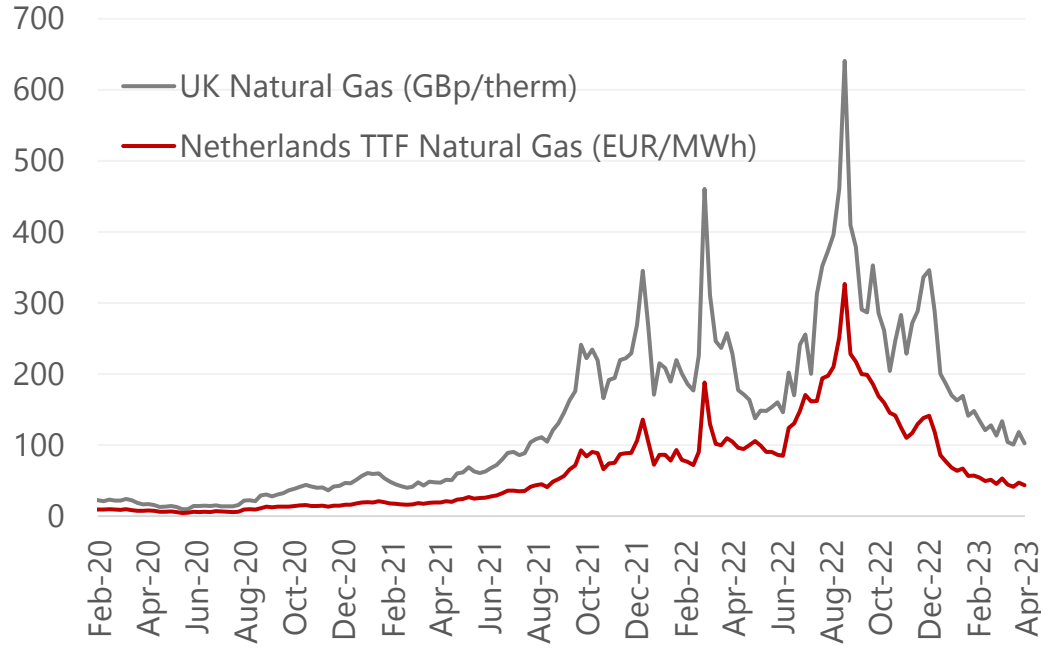
- European gas prices are in 18-month low levels.
- High liquefied natural gas (LNG) imports have contributed to the build of EU gas storage, now at 56%. LNG from the US helped the EU survive last winter (despite warnings of gas shortages, industrial paralysis and compulsory rationing), and more is promised for this year.

European Gas Storage Utilization (%)



Sources: Bloomberg, Santander.

Europe Natural Gas

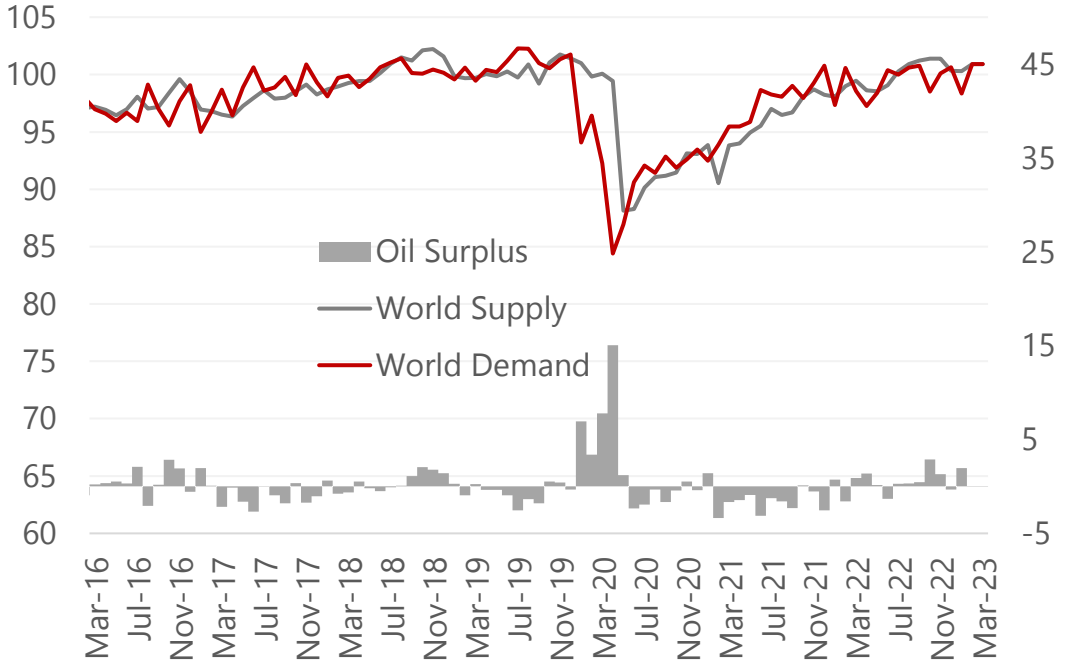


Sources: Bloomberg, Santander.

Oil: China's reopening still on track, though overshadowed by macro risk-off

- Oil prices tumbled on fears about contagion from crises involving some international banks triggered a broad risk-off sentiment in the market. Nevertheless, we still see oil fundamentals as bullish: (i) China's ongoing reopening should drive global oil demand growth; (ii) the Strategic Petroleum Reserve (SPR) and oil commercial stocks in the U.S. – the largest consumer of oil in the world – are at historically low levels; and (iii) investors preference for capital discipline has placed a cap on U.S. shale oil production growth.

World Oil Supply x Demand (mbd)



Sources: Bloomberg, Santander.

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

Sources: Bloomberg, Santander.

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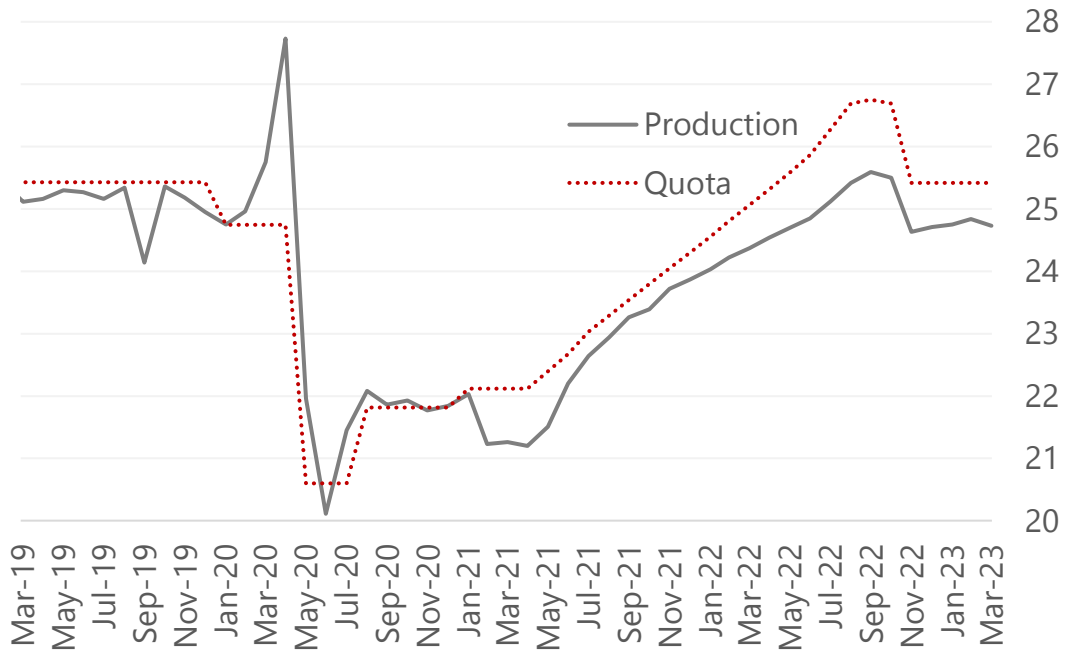
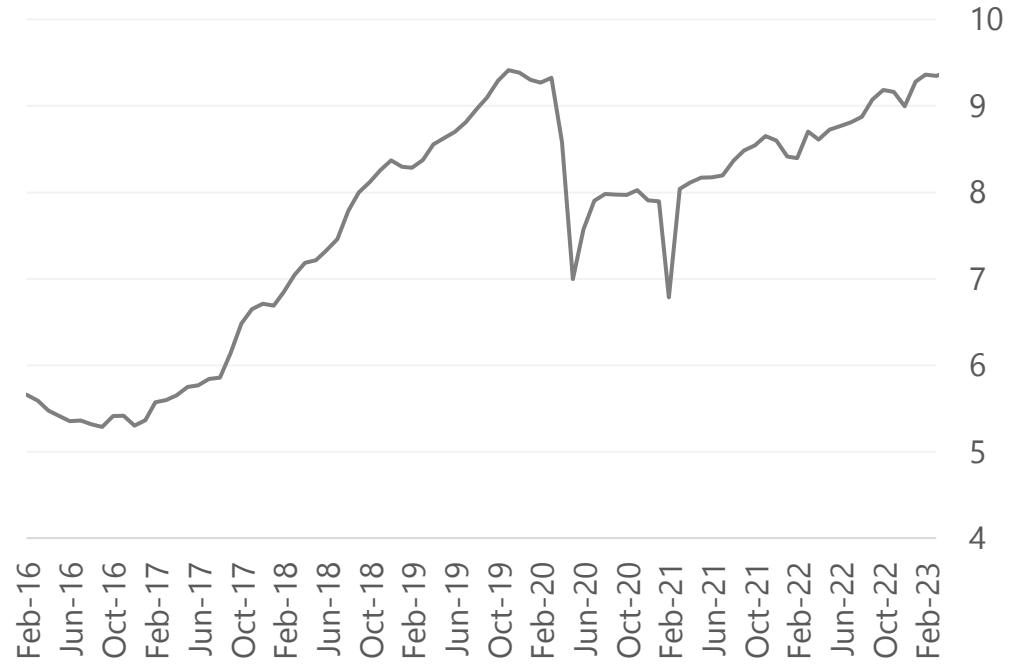
OPEC Production (members with quota) (mbd)



Sources: Bloomberg, Santander.

US Shale Production (mbd)

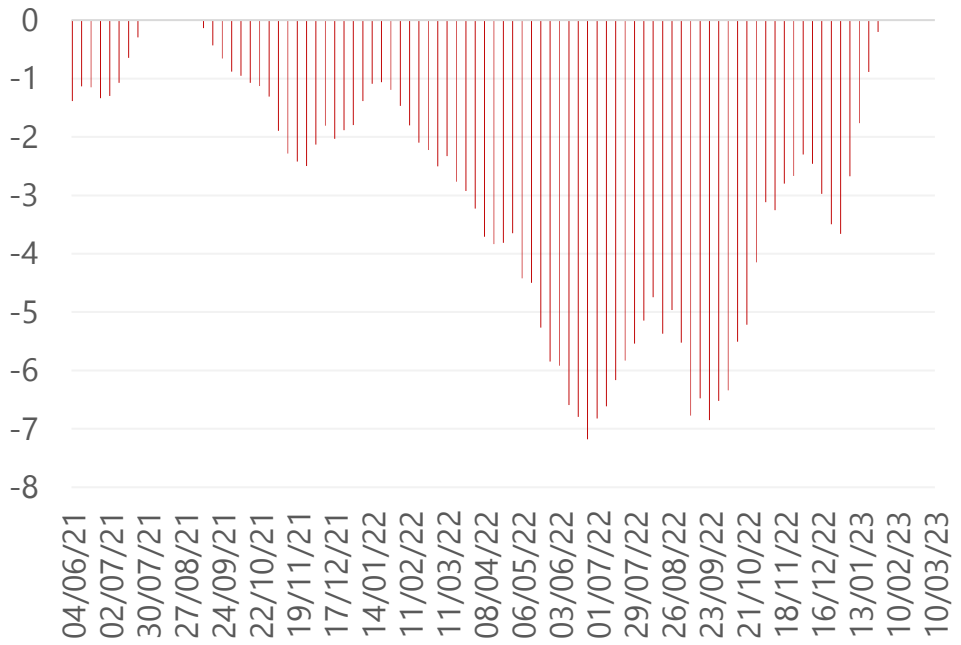


Sources: Bloomberg, Santander.

Oil: China's reopening still on track, though overshadowed by macro risk-off

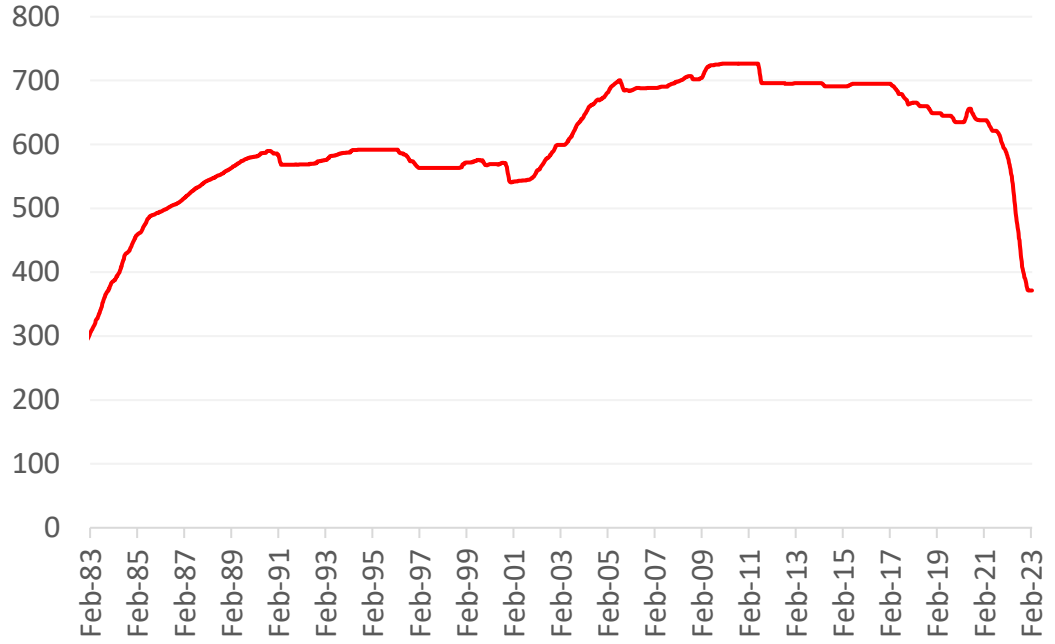
- Saudi Arabia and other OPEC+ members announced surprise oil production cuts of more than 1 million bpd, while Russia said it would extend its existing production cut until the end of the year. We believe supply constraints will start to drive price formation gradually in the coming months. With lower 2Q23 and 3Q23 prices, **we now see our Brent forecast (year-average) at USD90/bbl for 2023 (from USD95/bbl previously), but we are keeping our year-end forecast unchanged at USD95/bbl for 2023.**

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



Sources: US Department of Energy, Santander.

US Strategic Petroleum Reserves (Million Barrels)



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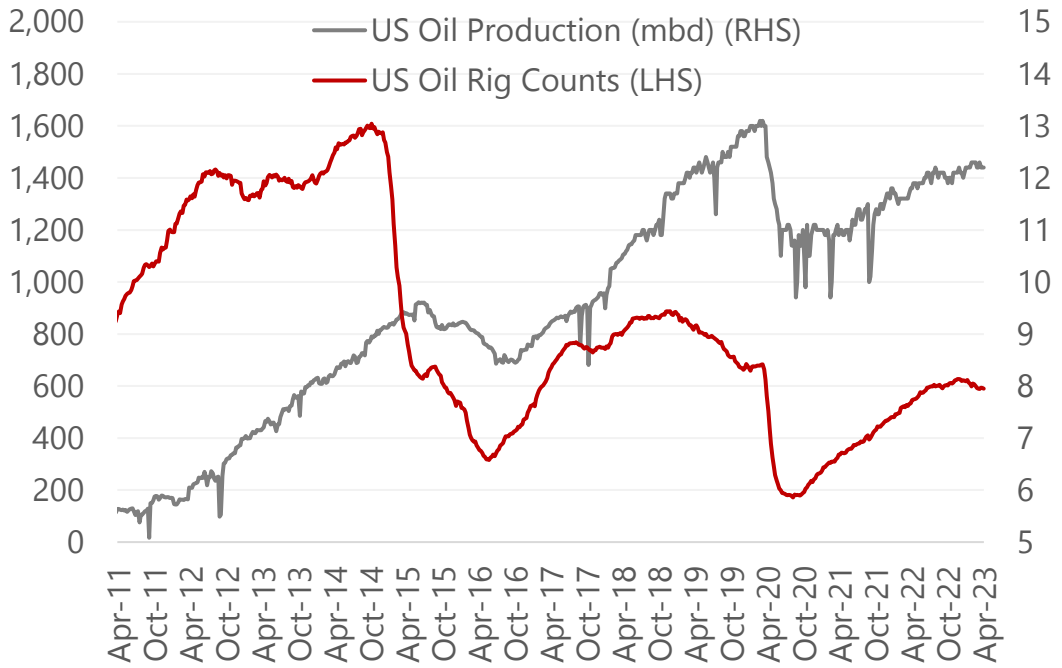
US Oil Production



Sources: Bloomberg, Santander.

Brent Crude Oil (USD/bbl)

Sources: Bloomberg, Santander.

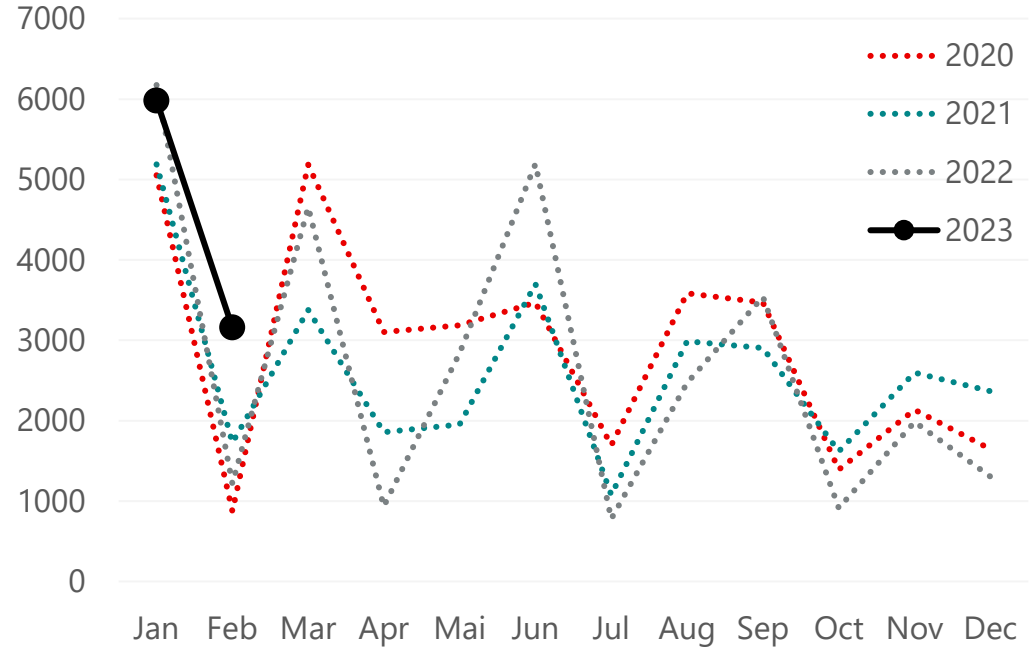
METALS

04

Metals: Rebound in China's activity is already starting in Q1

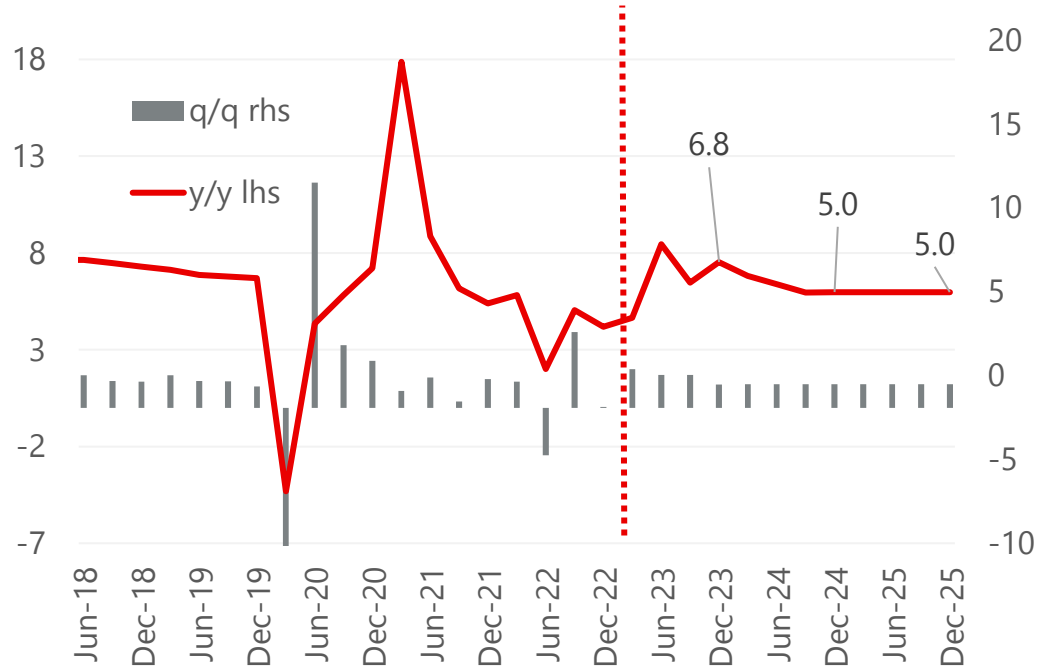
- Reopening started earlier and was more intense than previously expected.
- Government has been adding stimuli to the economy, and credit has been an important driver.

Credit is expanding in a faster pace



Sources: Bloomberg, Santander.

Reopening is anticipating economic recovery

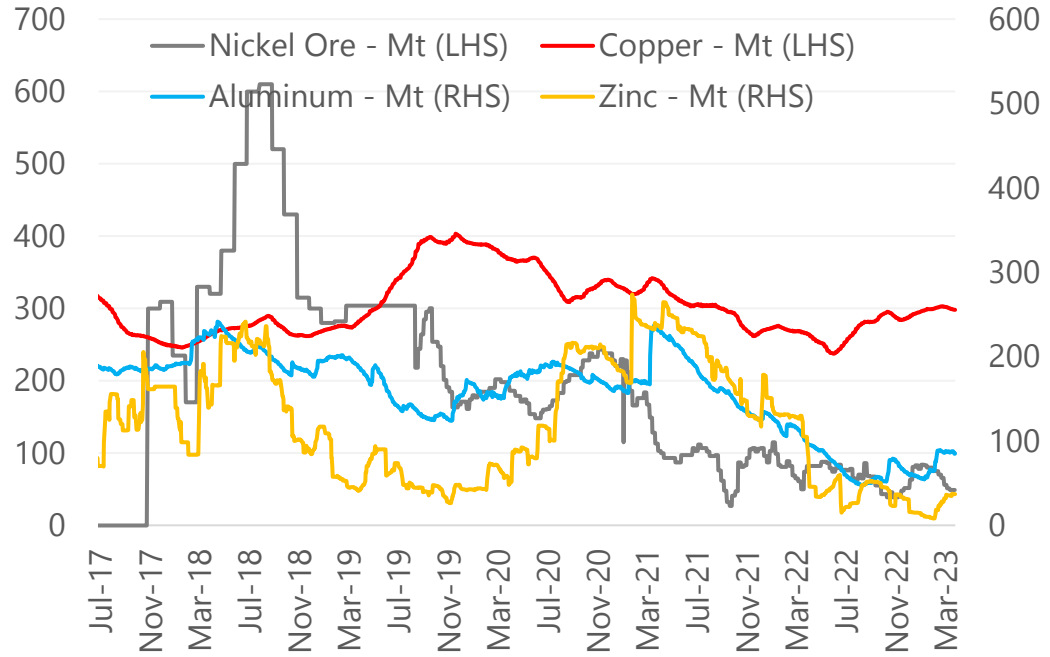


Sources: Bloomberg, Santander.

Metals: However, China's real estate crisis isn't over yet

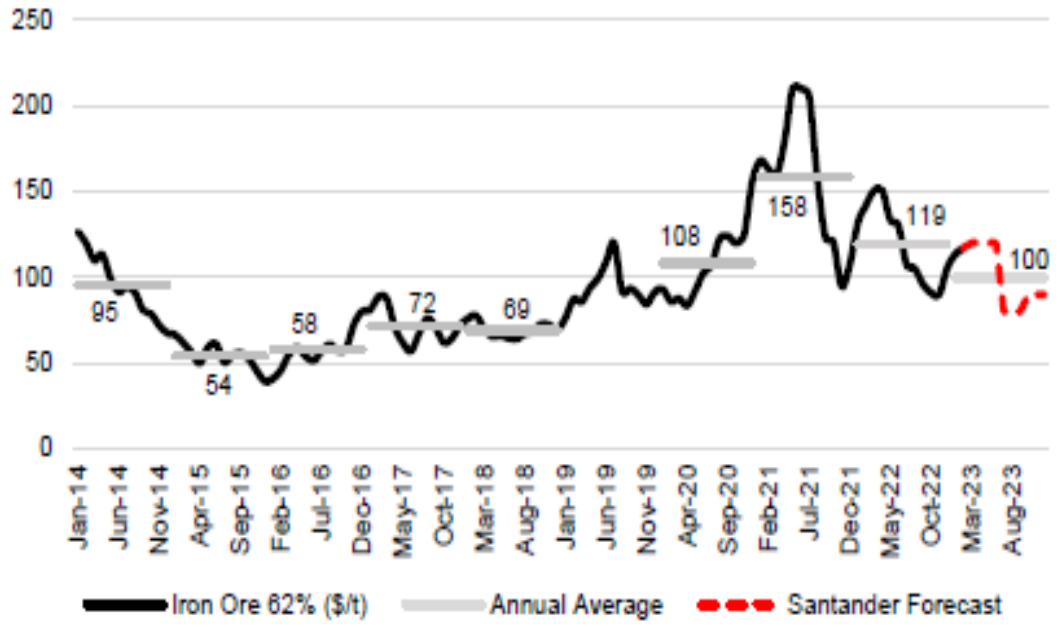
- Inventories remain worryingly low, but we maintain a more cautious medium-term view as Chinese demand is expected to weaken in the second half the year. The Chinese government will again cut annual crude steel production in 2023 (for the third year running) to cut back carbon emission from the sector. It will also ban new steelmaking capacity.
- Another risk is that China's economic recovery might be more focused on boosting consumer spending rather than rebuilding the residential property sector — so still not out of the woods.

Base Metals Inventories



Sources: Bloomberg, Santander.

Iron Ore Price Forecast



Sources: Santander.

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

Simple Personal Fair

Santander

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