Brazil Macro | September 2023

Commodities

Felipe Kotinda
felipe.kotinda@santander.com.br

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SUMMARY

Notwithstanding mounting concerns over China's faltering growth—portrayed in the property market crisis, deflation, and a weak yuan—commodities prices are holding up well. Also, 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). However, monetary tightening promoted by the main central banks is still expected to cause a deceleration in global activity, and fundamentals continue to point to a gradual drop in global material costs in the coming years, as aggregate supply gradually catches up. We still see: (i) a record grain output in key producing countries; (ii) Brent oil prices at USD 85/bbl for YE2023 and USD 95/bbl for YE2024; and (iii) fiscal and monetary stimulus from the Chinese government having a short-lived impact on metal prices. As a result, we are maintaining our aggregate commodity index forecast for YE2023 and for YE2024.

OVERVIEW

01

Despite the recent rebound, prices should continue trending lower

- We are maintaining our aggregate commodity index forecast for YE2023 and for YE2024.
- 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	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 ➡

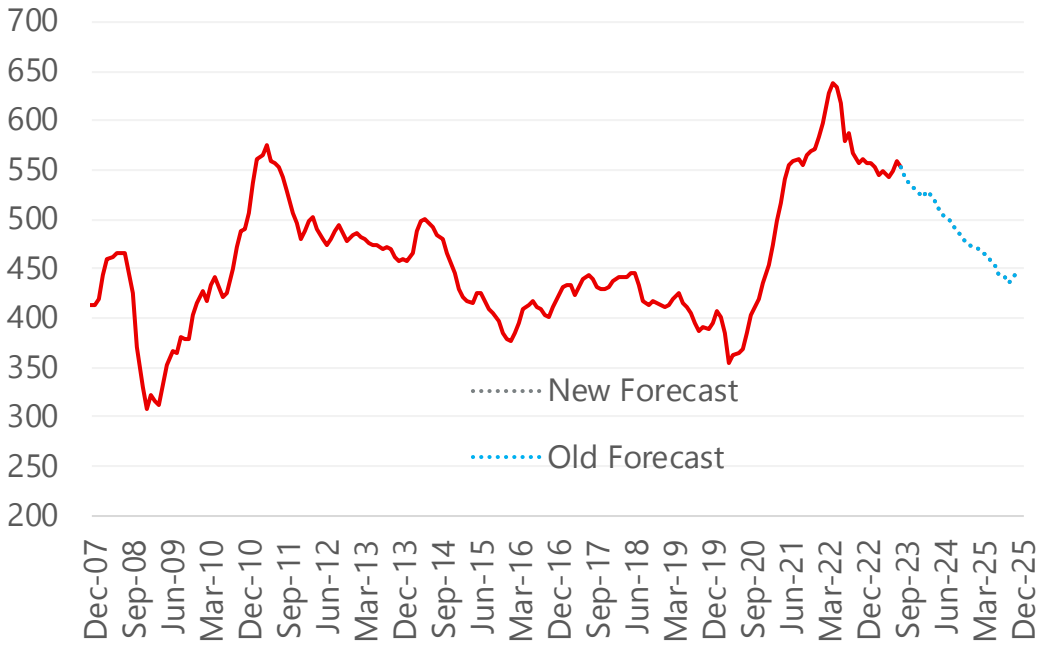
YE YoY	2021	2022	2023e	2024e	2025e
CRB Food	36%	12%	-16%	-13%	-6%
CRB Energy	31%	37%	-15%	-2%	-6%
CRB Metal	42%	-20%	10%	-12%	-6%
CRB	29%	-2%	-5%	-10%	-6%

	Iron Ore (ton)	Soybean (bu)	Corn (bu)	Brent (bbl)
2023 change*	-3%	-9%	-29%	7%
Current price (USD)	114	13.8	4.8	87.7

* September 1st, 2023.

Sources: Santander.

Our Forecasts for CRB Index – Monthly Averages



Sources: Bloomberg, Santander.

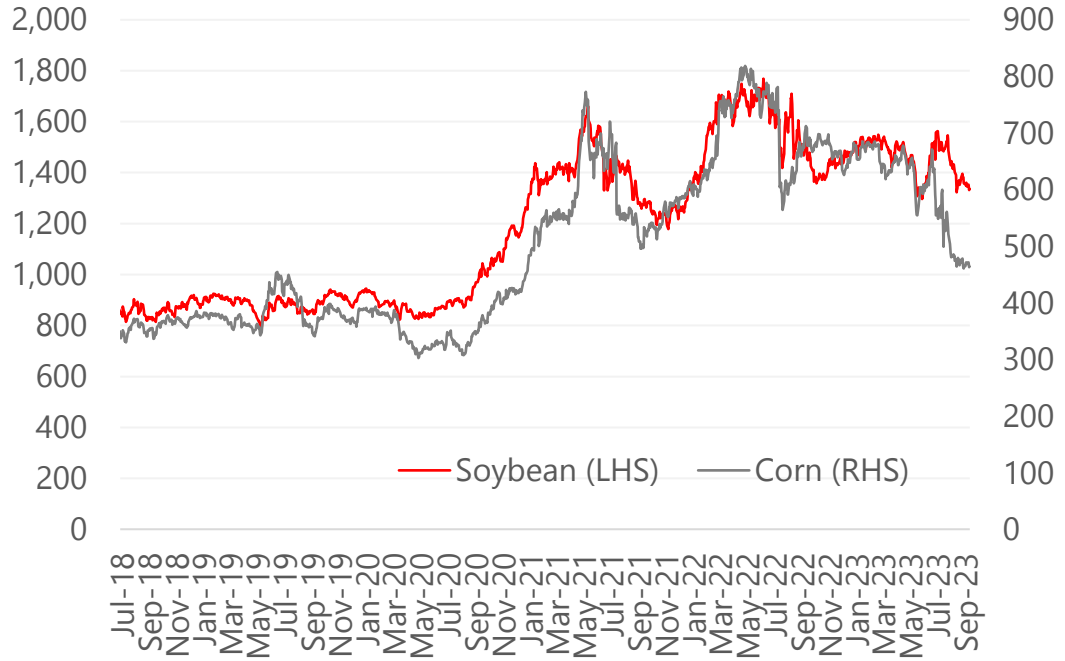
AGRICULTURE

02

Agri: A record brazilian grain output, and good prospects for 2023/24

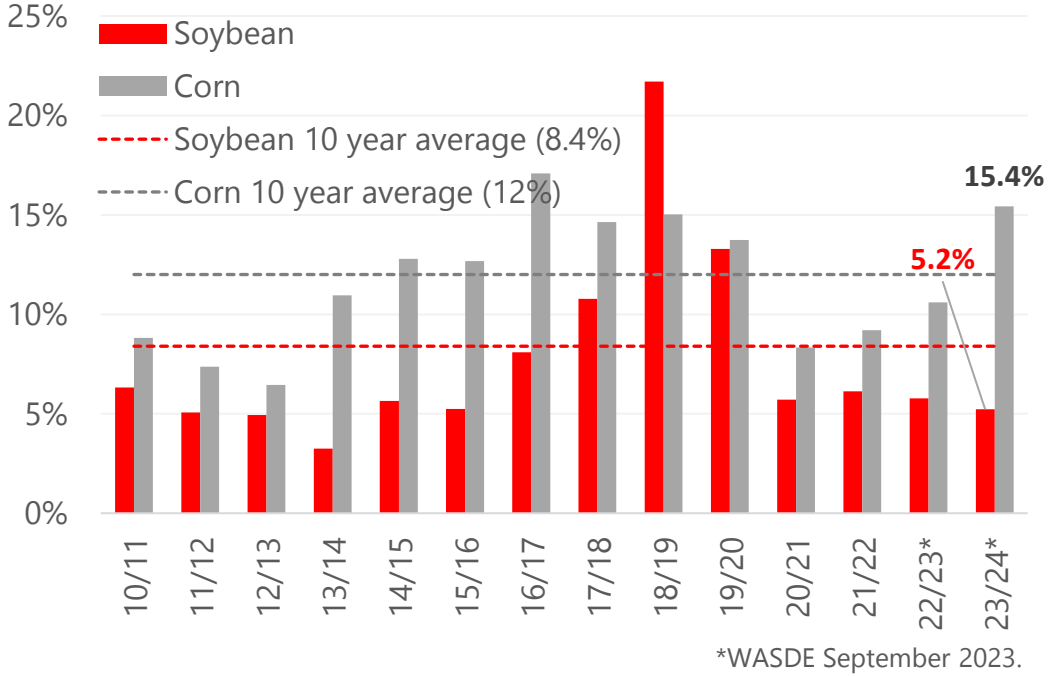
- Brazil harvested a record soybean (154 million ton) and corn (132 million ton) crops as a result of favorable growing conditions across most of the country. **We expect this to be a key factor dampening food inflation over time.**
- In Europe, Ukraine is discussing a proposal with Turkey to reopen the grain corridor in the Black Sea without Russia participation, which could help global food balances.

Chicago Board of Trade - Grains (USD cents)



Sources: Bloomberg, Santander.

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



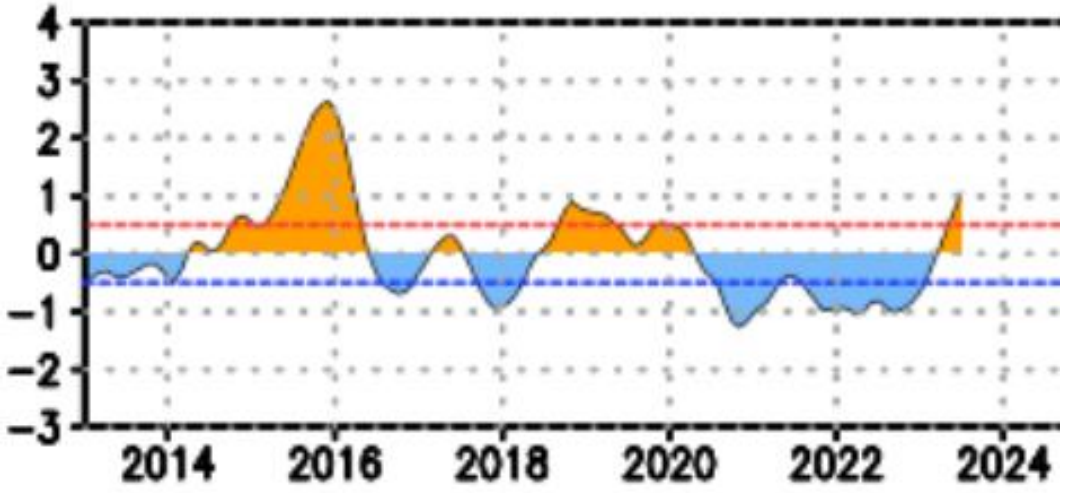
*WASDE September 2023.

Sources: USDA, Santander.

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

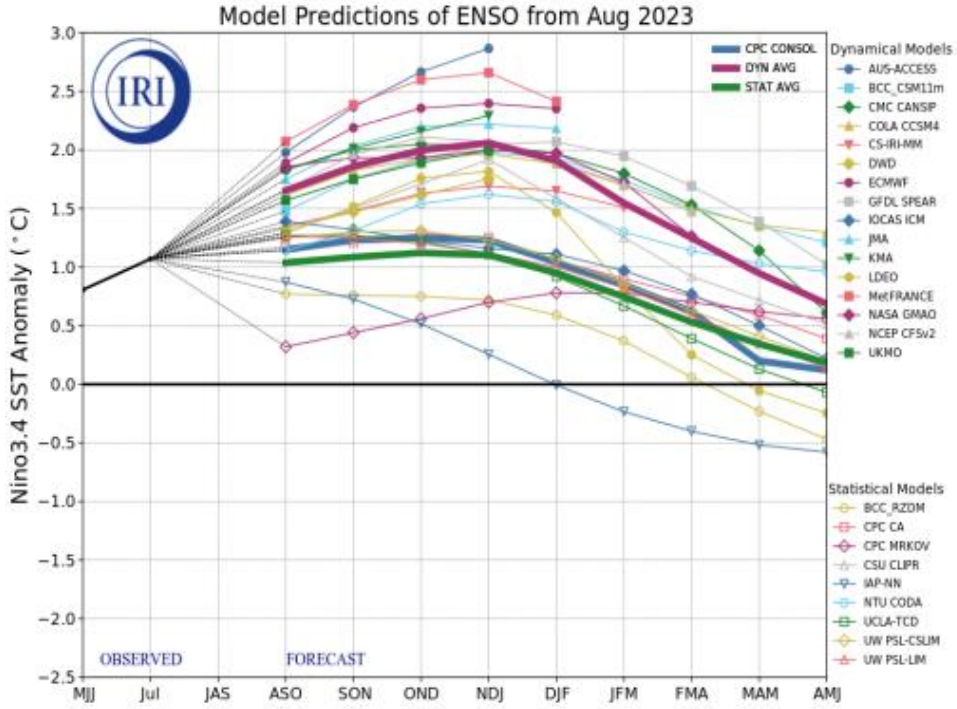
- For the upcoming season, a strong El Niño will take place. The phenomenon is usually associated with decent crop yield in South America. **For Brazilian inflation, we see some risks especially in 4Q23 and 1Q24.**
- Nearly all models indicate El Niño will persist into the Northern Hemisphere winter 2023-24. A strong El Niño (ONI values at or greater than 1.5ºC) is indicated by the dynamical model average.

ONI (°C) Evolution



Sources: NOAA, Santander.

Model Predictions of ENSO

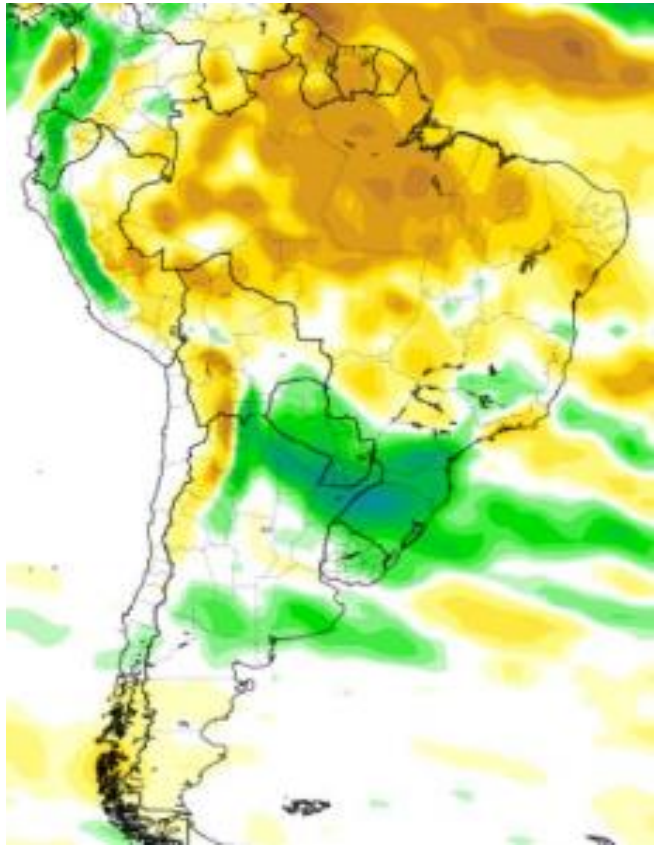


Sources: NOAA, Santander.

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

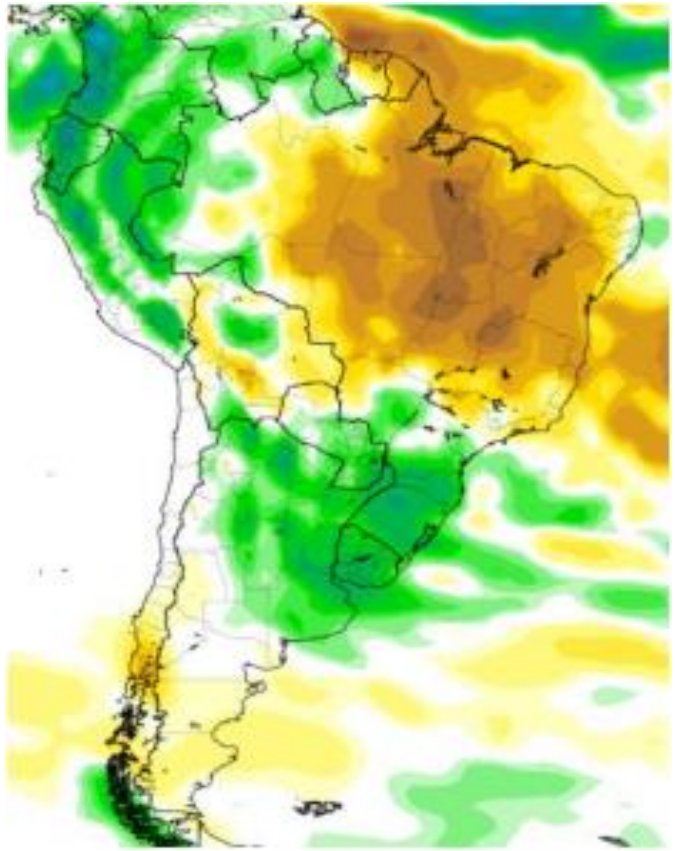
- We see some risk that the drought in the northeast part of the country spreads out to the mid-west, hitting key producing states.
- For now, given the volatile nature of such models, our base case is that grain crop yield will no be significantly affected.

Anomaly for November - Forecast CFS (as of 28 Aug)



Sources: NOAA, Santander.

Anomaly for December - Forecast CFS (as of 28 Aug)

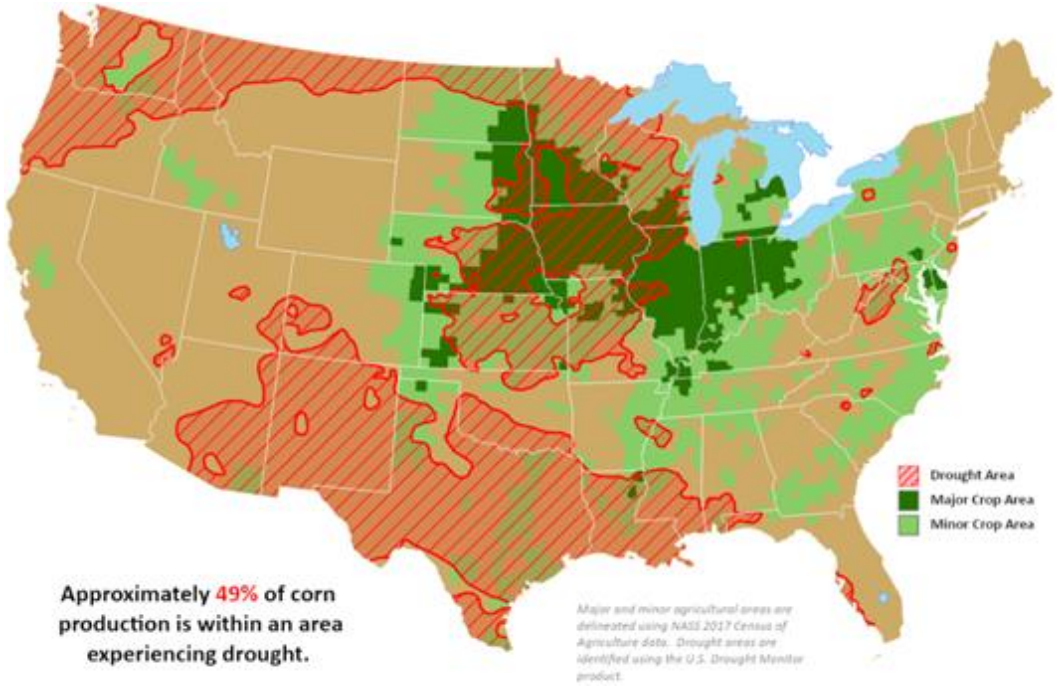


Sources: NOAA, Santander.

Agri: Hottest July and August on record in the U.S.

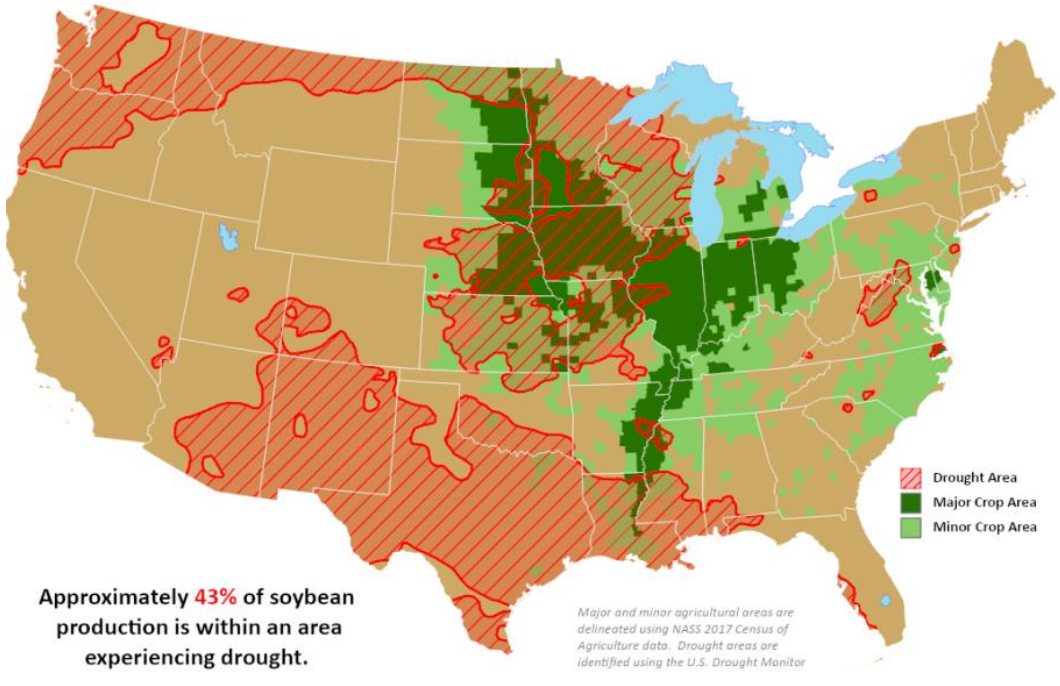
- Key growing regions in the Midwest have been suffering from high temperatures recently, a risk for corn and soybean crops.
- According to USDA, 49% of corn and 43% of soybean production is within areas experiencing drought.

Corn Areas in Drought (as of September 5, 2023)



Sources: USDA, Santander.

Soybean Areas in Drought (as of September 5, 2023)

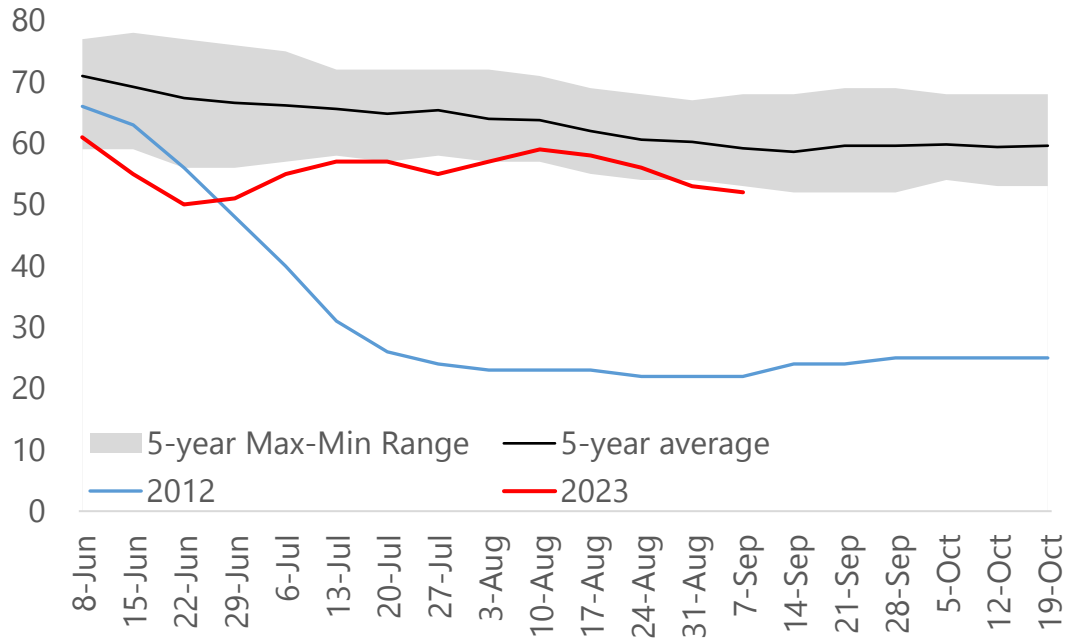


Sources: USDA, Santander.

Agri: U.S. crop condition a bit below average

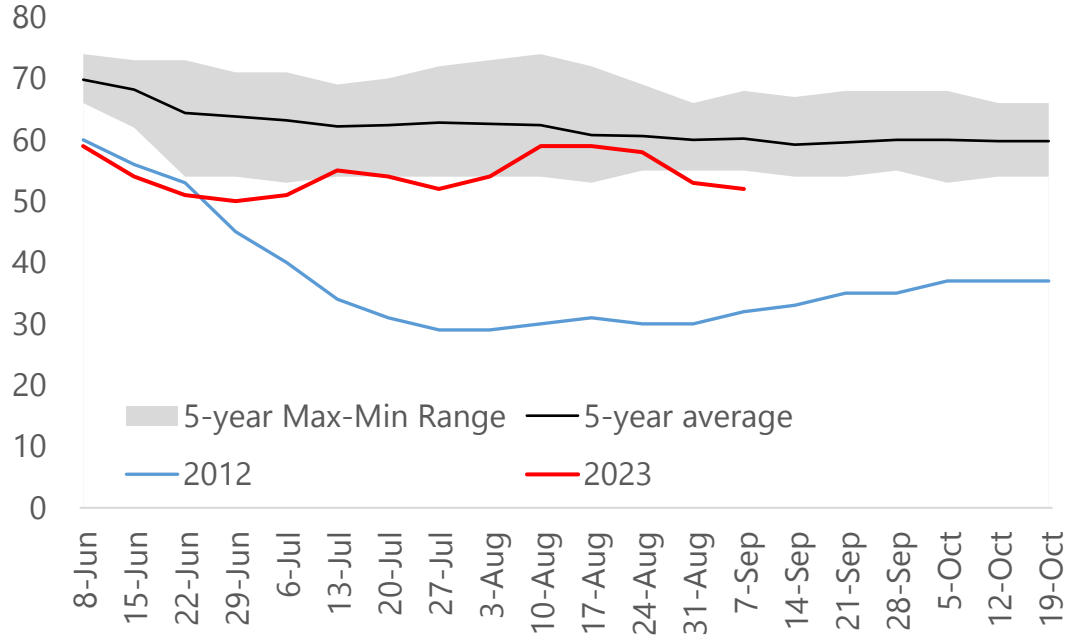
- After initially seeing a sharp decline in U.S. crop rating amid hot and dry weather in parts of the Midwest grain belt (with crop conditions even below 2012 level – a year of severe drought), conditions are now a bit below 5-year average.

Corn Crop Condition (% in good/excellent condition)



Sources: USDA, Santander.

Soybean Crop Condition (% in good/excellent condition)

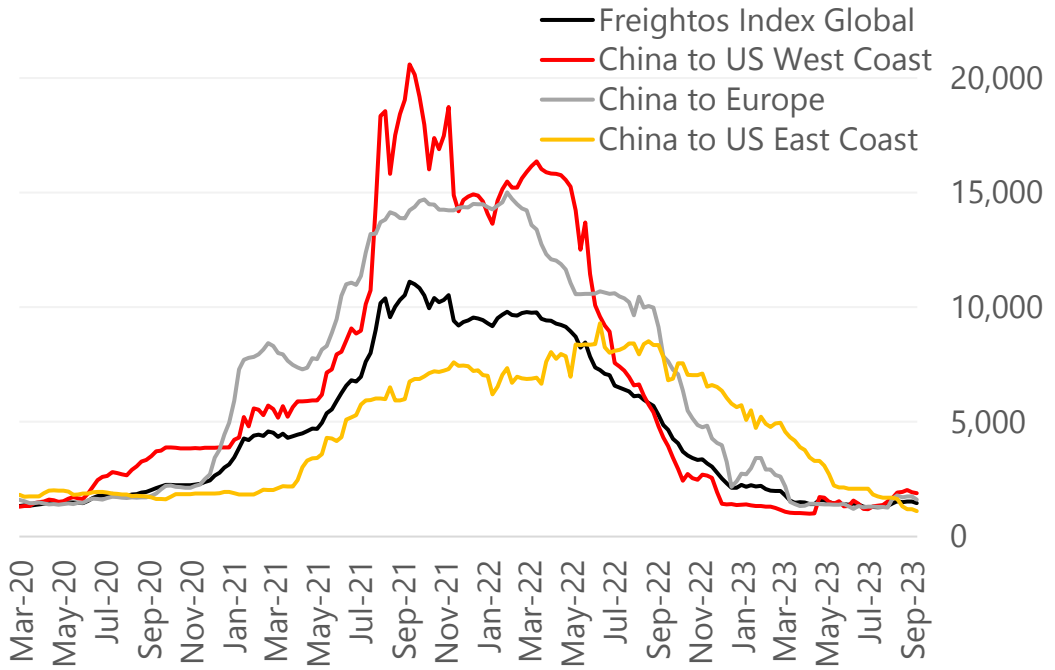


Sources: USDA, Santander.

Agri: Supply constraints ease back to pre-war levels

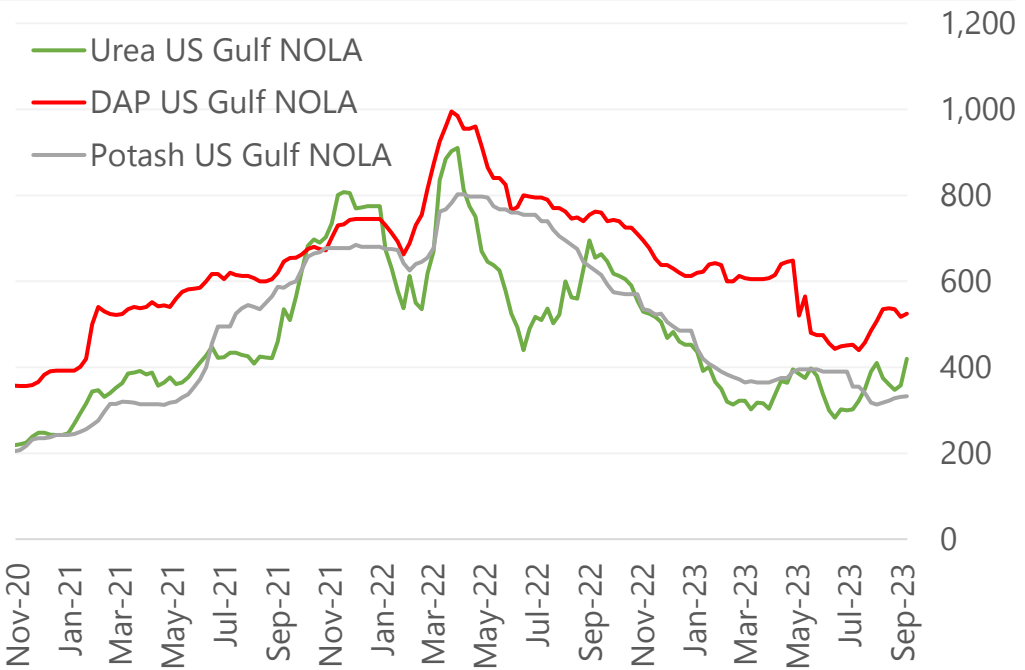
- Freight cost proxies are at low levels (helping deflation prints), with routes back to pre-pandemic levels.
- Fertilizers prices are relatively flat since March, and much lower than last year peak when the war in Ukraine started.

Freight Costs Index



Sources: Bloomberg, Santander.

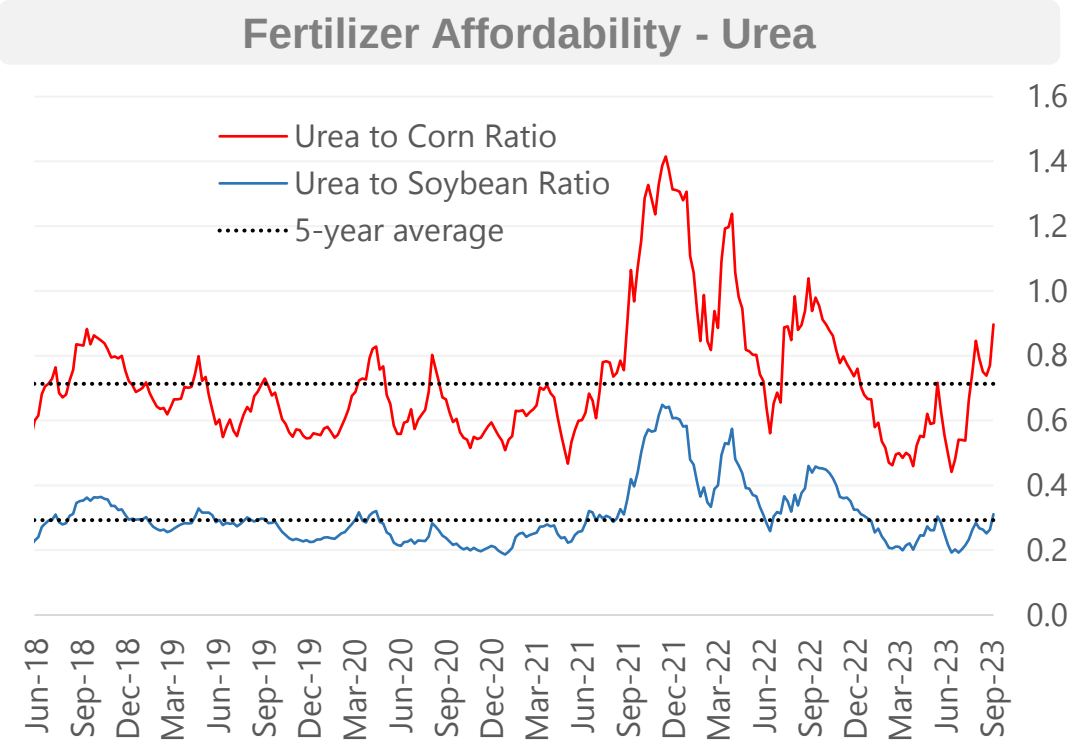
Fertilizers prices (USD/t)



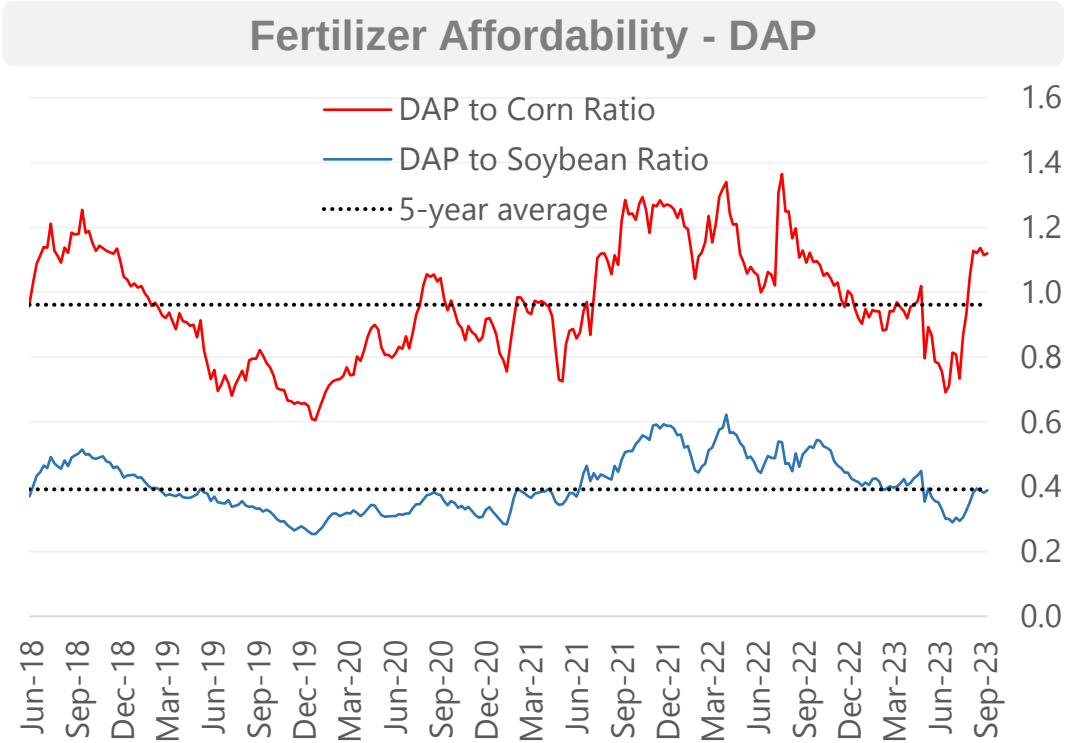
Sources: Bloomberg, Santander.

Agri: Fertilizer affordability above historical average for corn

- The affordability for corn is above historical average, given that corn prices decline outpaced fertilizer prices decline.
- Still, producers have incentive to use more fertilizer and increase planted area, hence better prospects for food-inflation.



Sources: Bloomberg, Santander.

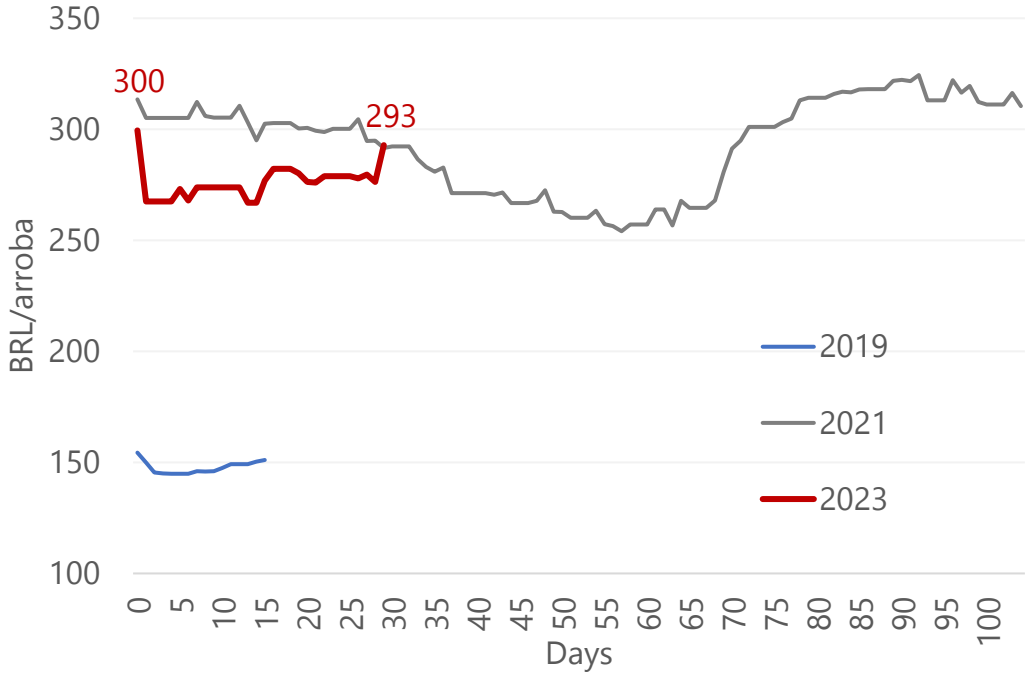


Sources: Bloomberg, Santander.

Agri: A favorable stage of Brazilian cattle cycle

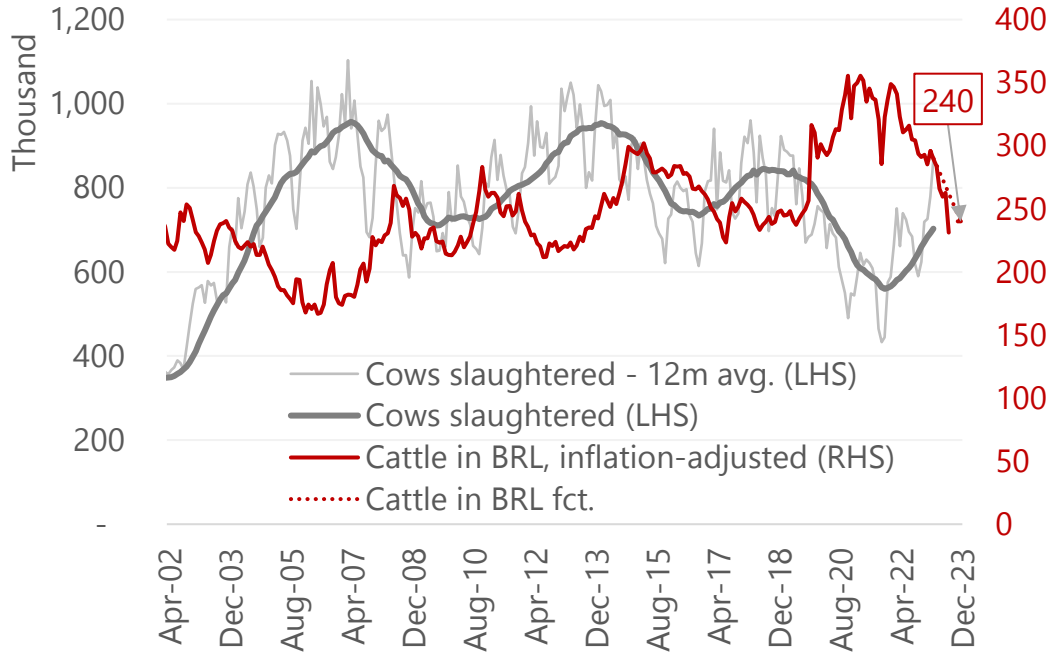
- Cattle prices on B3 continued to plunge, reaching below BRL200/arroba, the lowest level since May 2020.
- **In our special report (It's Barbecue Time*), we argued that beef prices would fall on the back of ample domestic supplies of cattle, given the current favorable moment in Brazil's cattle cycle.**

Cattle prices following report of mad cow disease



Sources: Bloomberg, Santander.

Cattle Cycle in Brazil

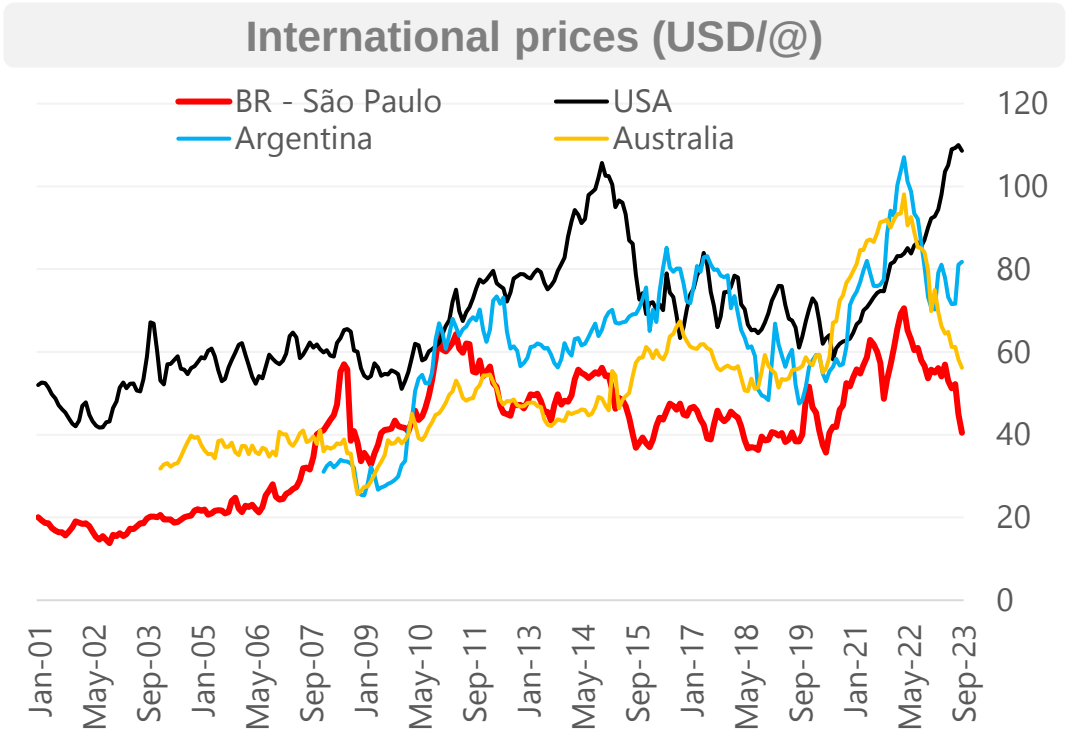


Sources: IBGE, Bloomberg, Santander.

***Santander Brazil Special Report: "It's Barbecue Time" – May 19, 2023 – Available on: https://bit.ly/Std-special-051923**

Agri: Brazilian beef is the cheapest among the main exporting countries

- Ample domestic supplies coupled with the BRL appreciation pushed Brazilian beef prices even lower when compared to its peers.

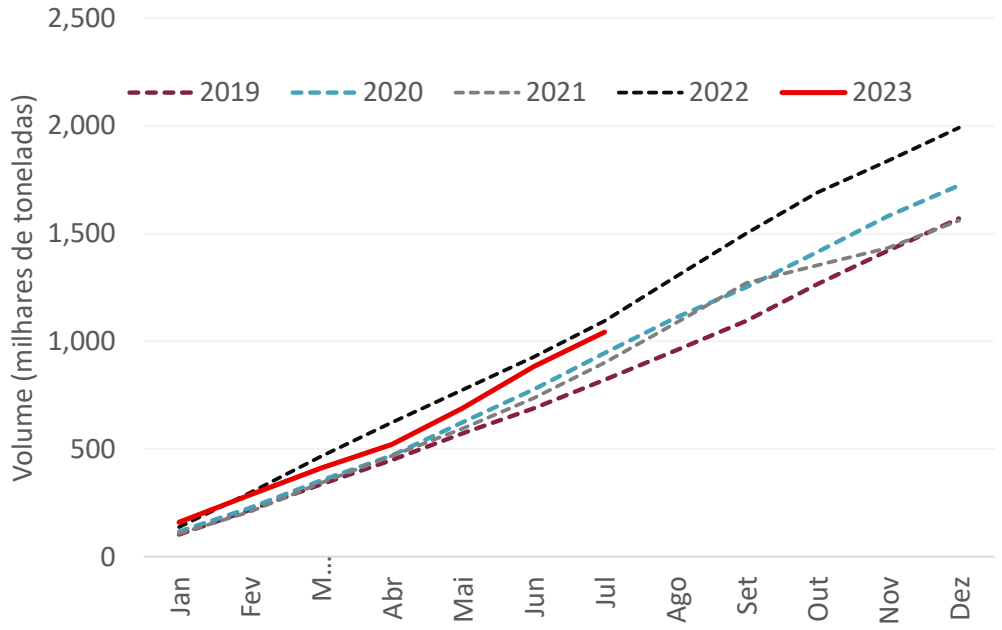


Sources: Athenagro, Santander.

Agri: A favorable stage of Brazilian cattle cycle

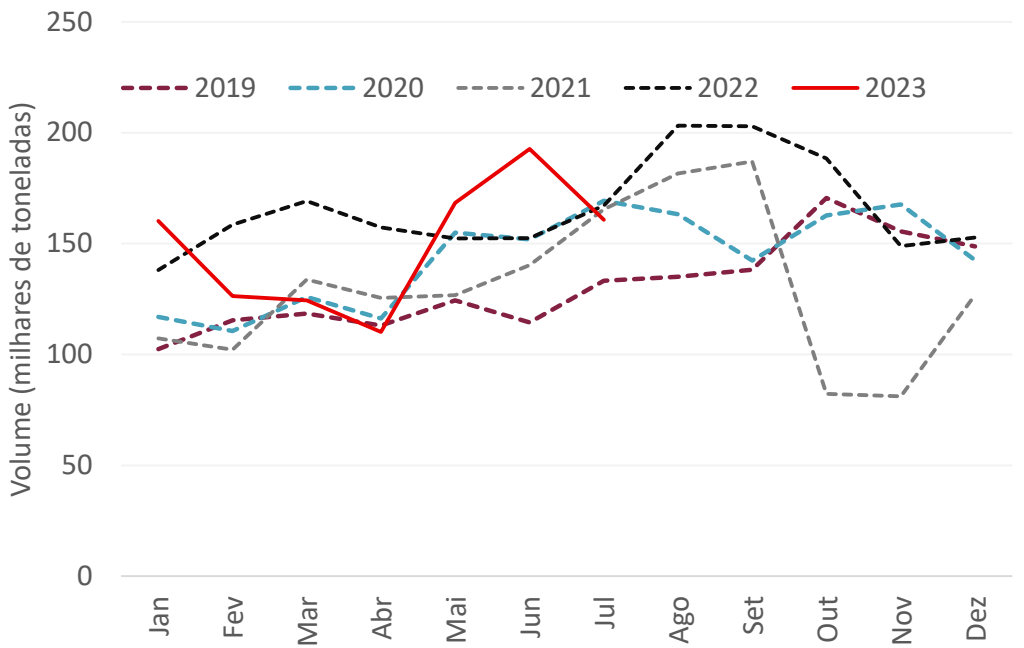
- With a competitive price, Brazilian beef exports continue at a good pace. Accumulated beef exports in 2023 YTD are close to the record performance in 2022.
- China remains the main importer (~50% of total).

Brazil - Beef export (accumulated)



Sources: SECEX, Santander.

Brazil - Beef export (monthly)



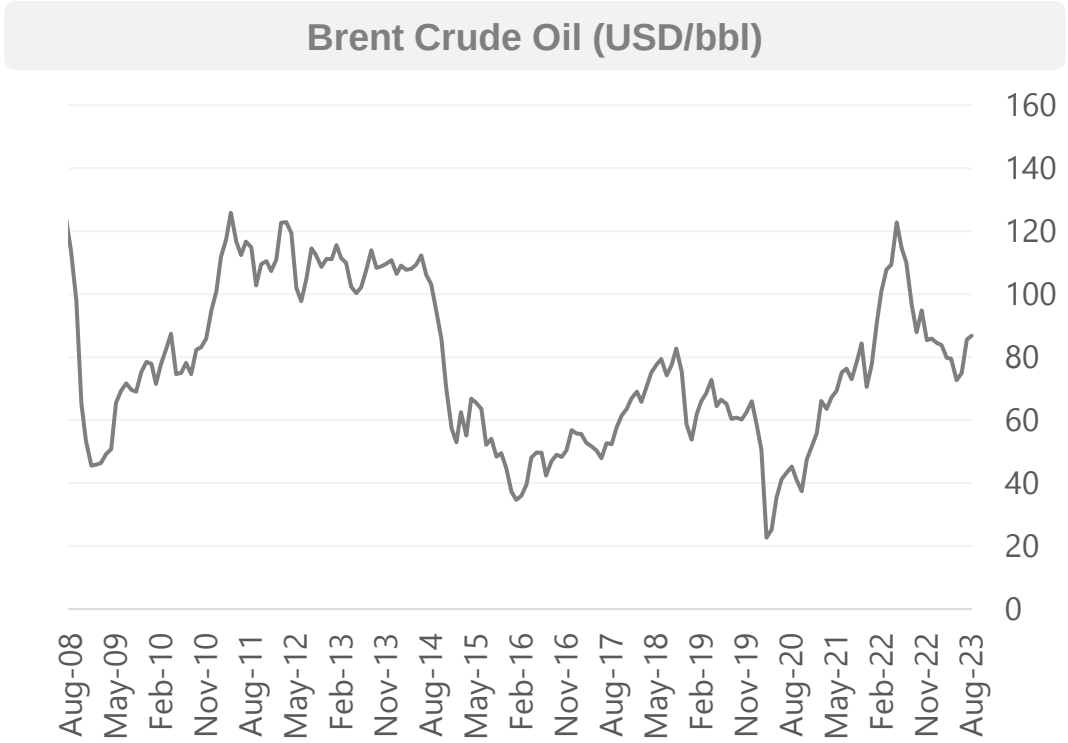
Sources: SECEX, Santander.

ENERGY

03

Oil: Fundamentals “put a floor” on prices

- **Our forecast for Brent oil is at USD 85/bbl for YE2023 and USD 95/bbl for YE2024.** Our call hinges on factors that would effectively “put a floor” under oil prices: (i) supply cuts from key producing countries; (ii) China’s demand; (iii) and the U.S. replenishing stockpiles by buying oil price dips.

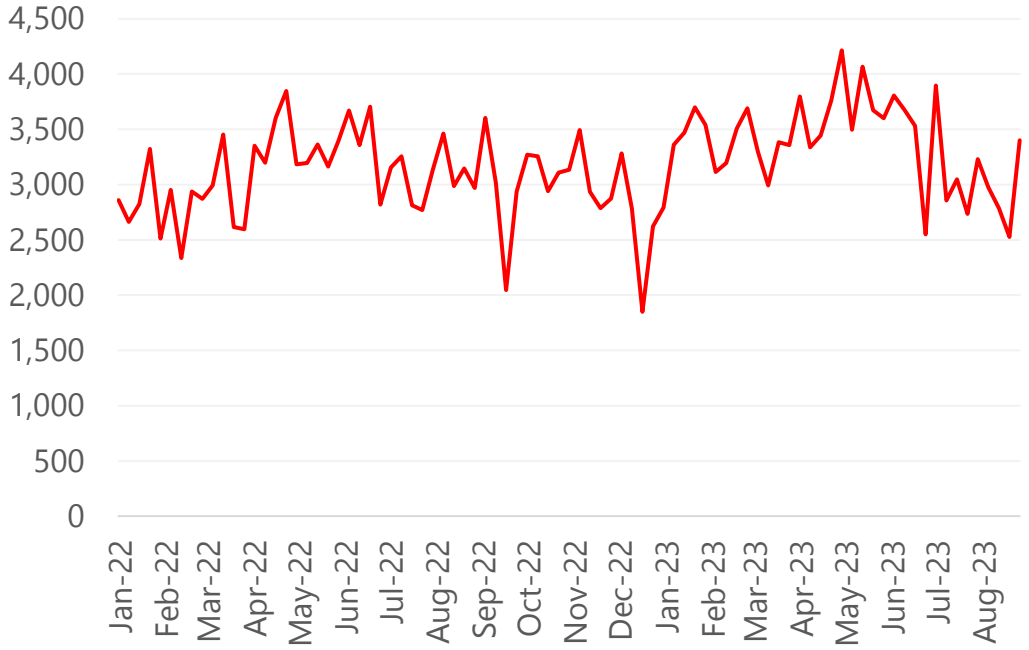


Sources: Bloomberg, Santander.

Oil: Supply cuts from Saudi Arabia and Russia

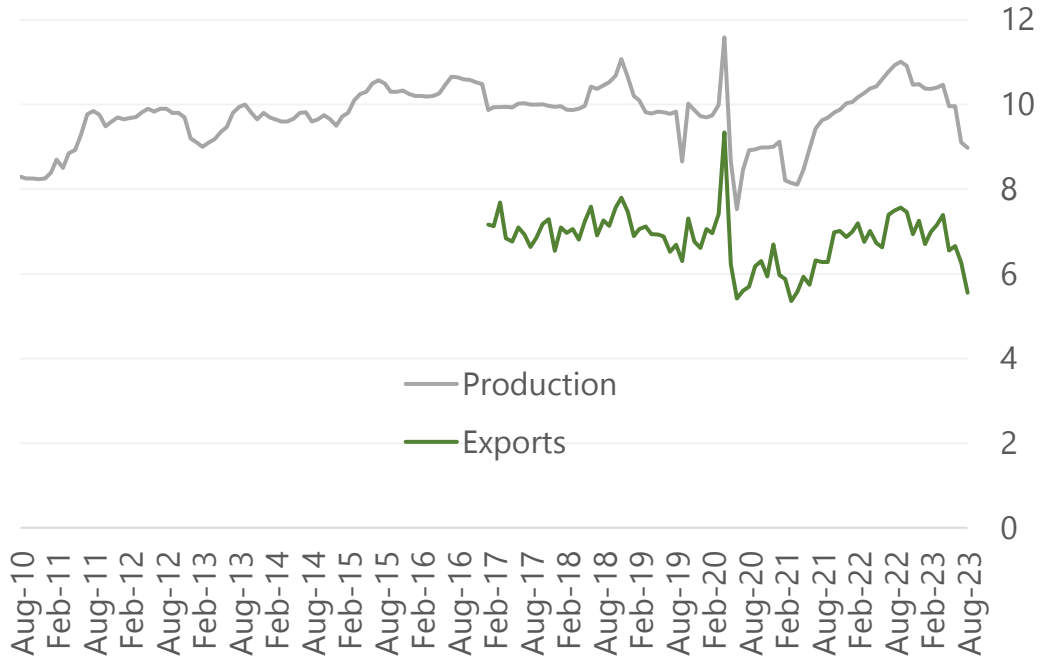
- Saudi Arabia (1 million bpd) and Russia (0.3 million bpd) said they would extend voluntary oil cuts to the end of 2023.
- These cuts are on top of the April cut agreed by several OPEC+ producers, which extends to the end of 2024.
- On the other hand, Iran plans to keep raising oil production, partially countering the OPEC+ efforts to tight the market.

Russia Oil Seaborne Exports (k bpd)



Sources: Bloomberg, Santander.

Saudi Arabia Oil (mm bpd)



Sources: Bloomberg, Santander.

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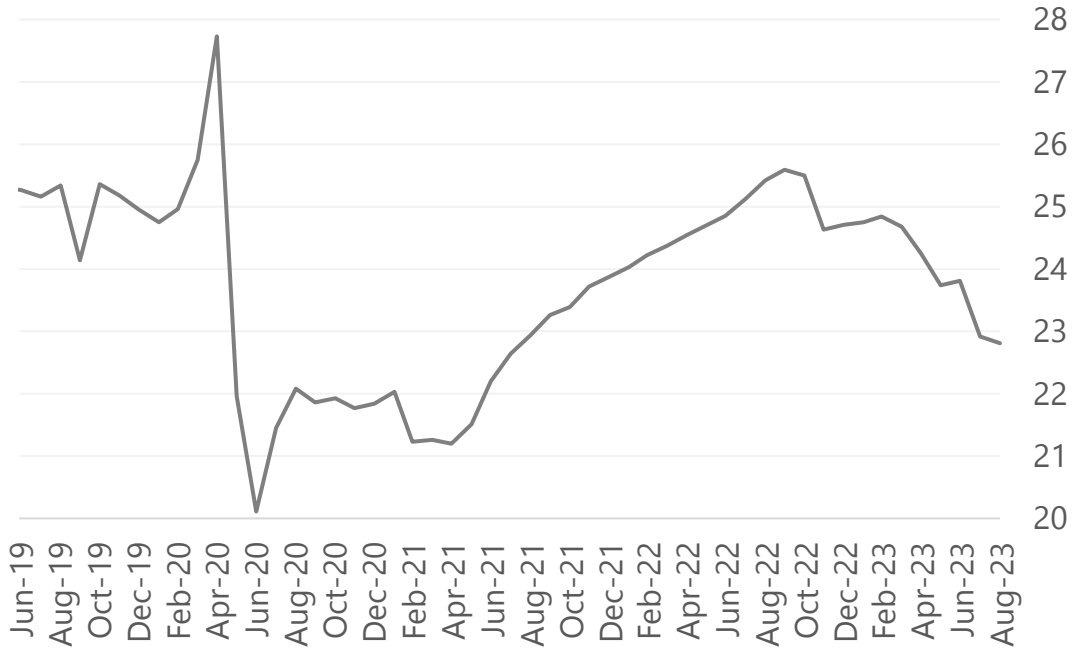
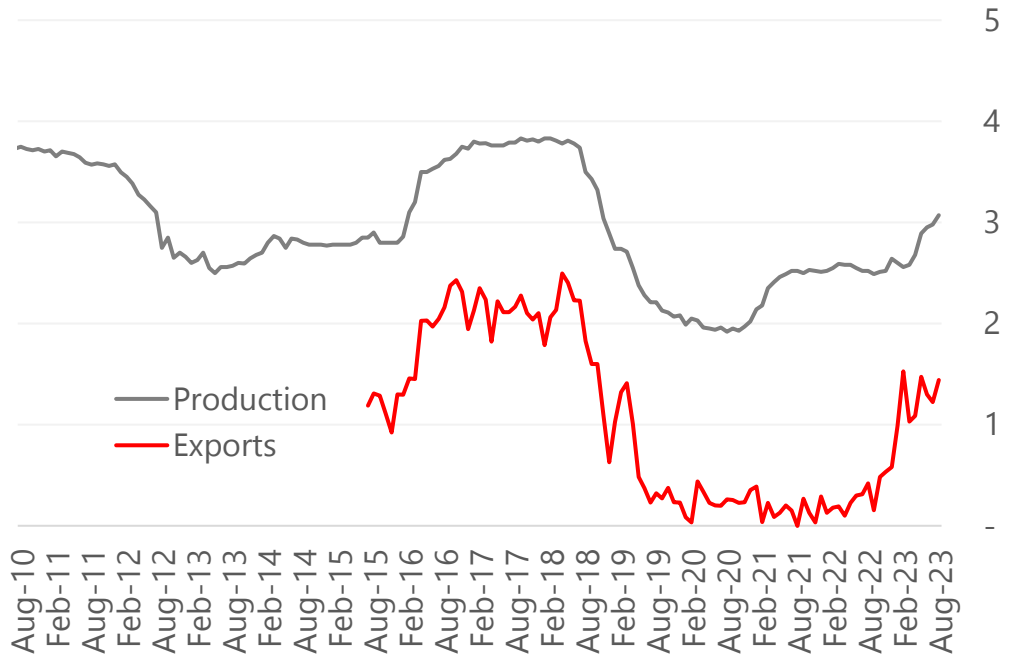
OPEC Production (members with quota) (mm bpd)



Sources: Bloomberg, Santander.

Iran Oil (mm bpd)

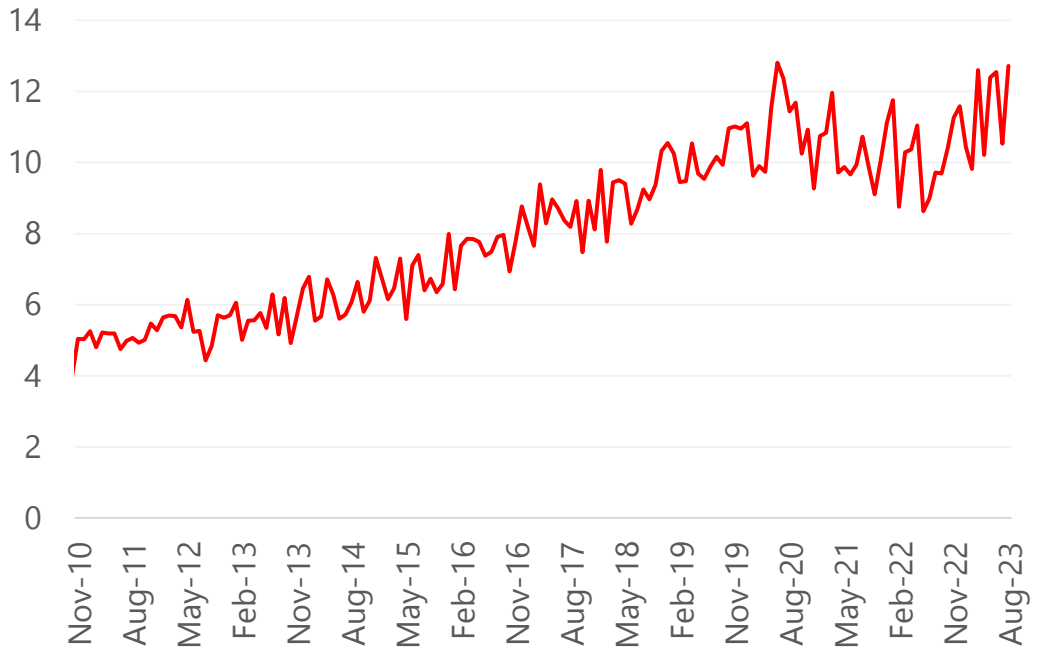


Sources: Bloomberg, Santander.

Oil: China imports running high

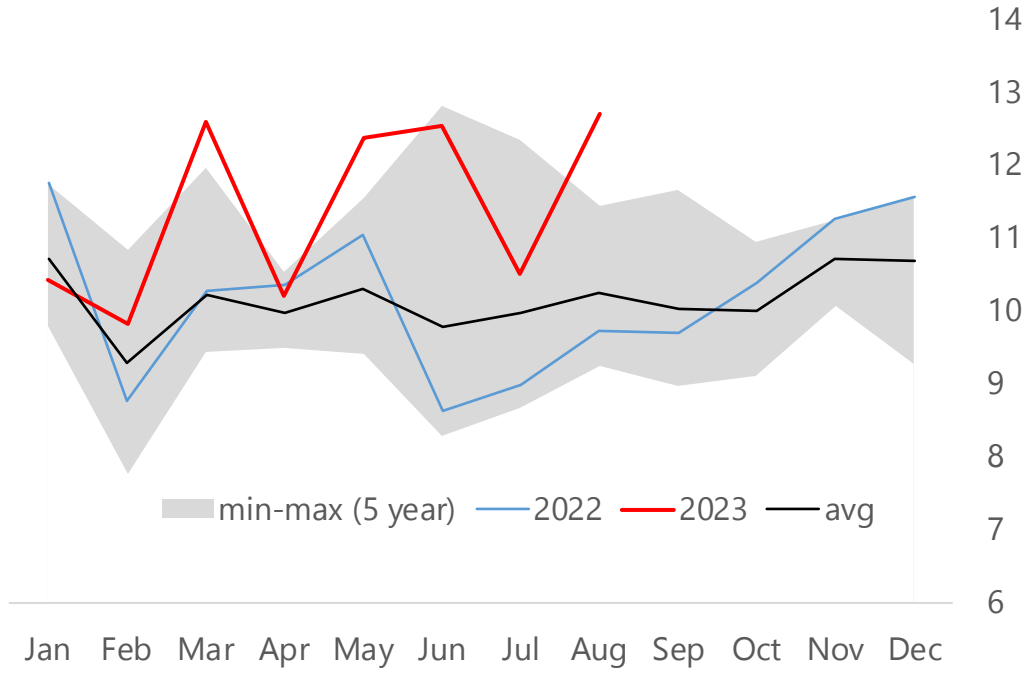
- China is the world's single biggest oil importer. Its imports are running above previous year's, given strong demand. In August, it remained at near record levels.
- Yet it is unclear how much of these imports were actually consumed, and how much went into inventories.

China Oil Import (mm bpd)



Sources: Bloomberg, Santander.

China Oil Import (mm bpd) - seasonal

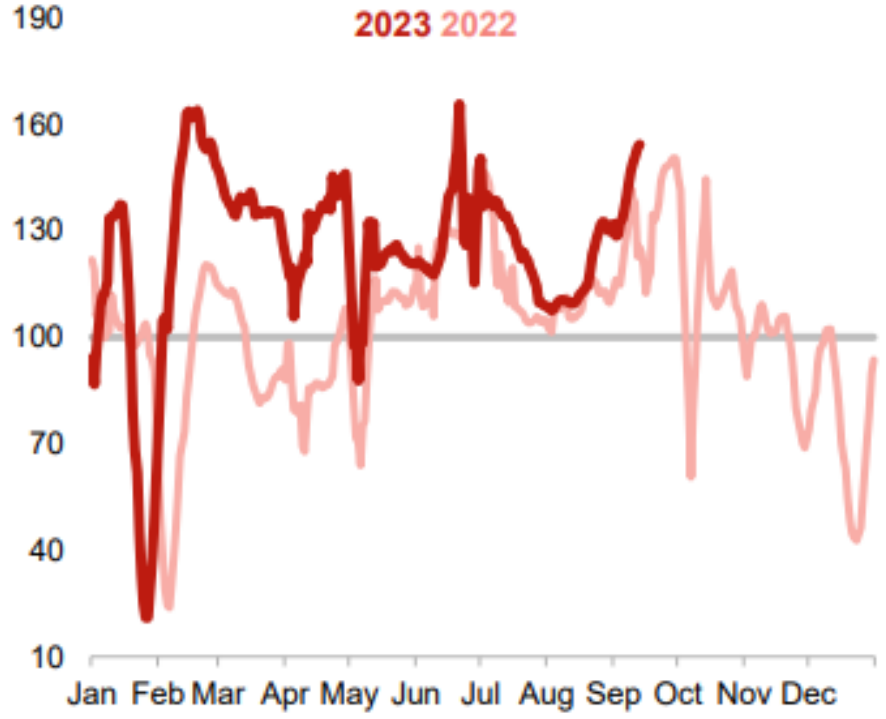


Sources: Bloomberg, Santander.

Oil: Global road congestion is up in the North Hemisphere

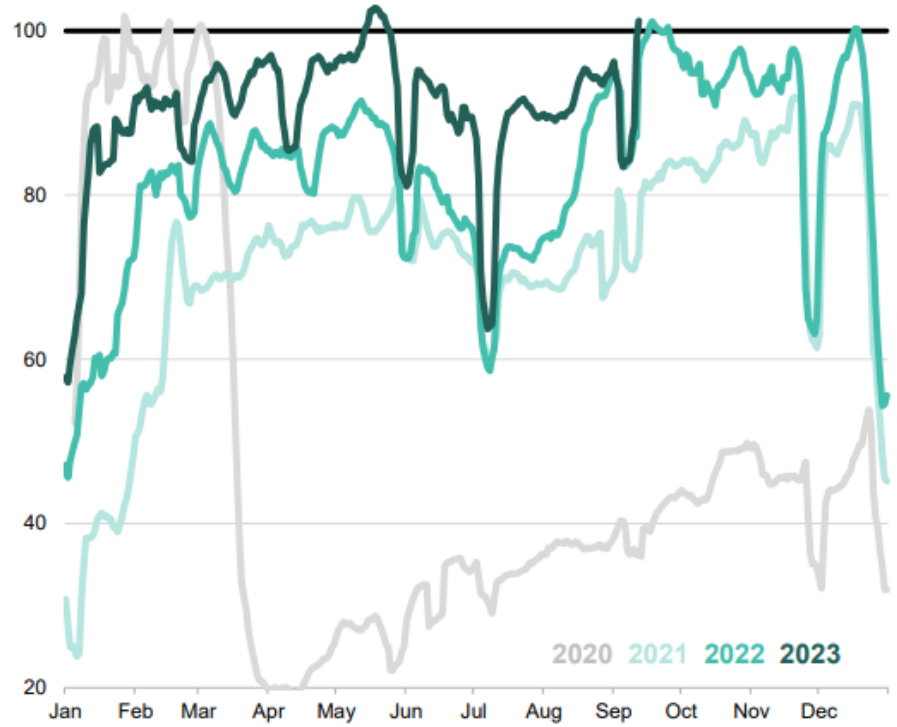
- China's congestion in the end of summer rises above last year's level.
- In the U.S., traffic is also up at the margin.

China Congestion Index (Jan-21 = 100)
15 cities with the highest number of vehicle registrations



Sources: Bloomberg, Baidu, Santander.

U.S. Congestion Index (2019 = 100)

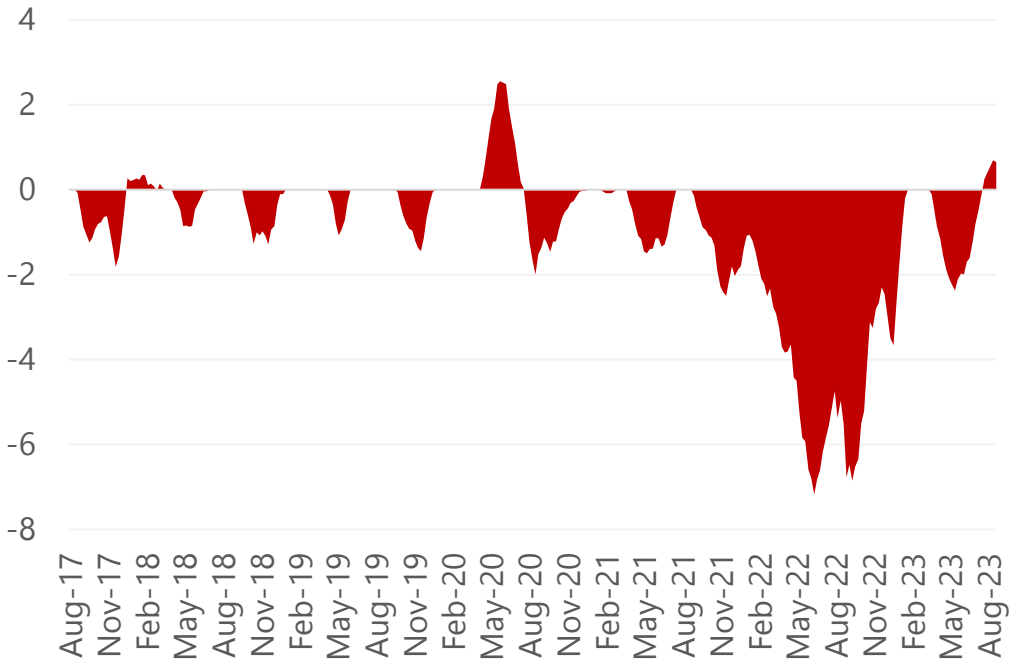


Sources: Bloomberg, TomTom, Santander.

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

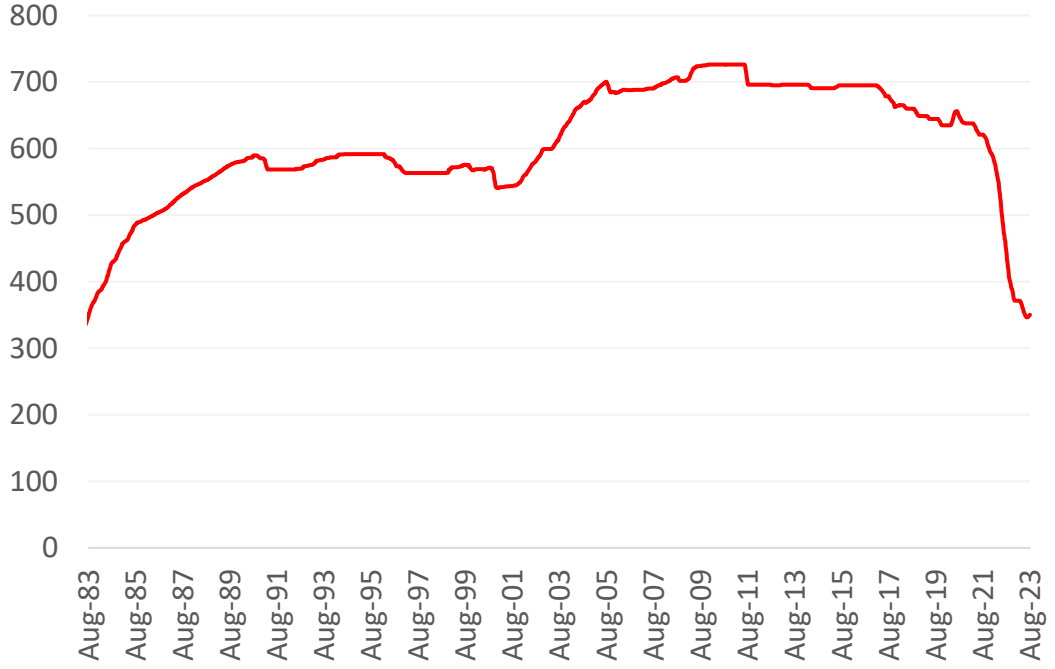
- US is expected to refill its Strategic Petroleum Reserve (SPR) after a historic 180 million-barrel drawdown brought it to about half of its capacity in the aftermath of Russia's invasion of Ukraine.
- The administration has said it wants to buy back oil for the reserve when it costs $67 to $72 per barrel.

Weekly U.S. Change in Crude Oil in SPR (million barrels)



Sources: US Department of Energy, Santander.

US Strategic Petroleum Reserves (million barrels)

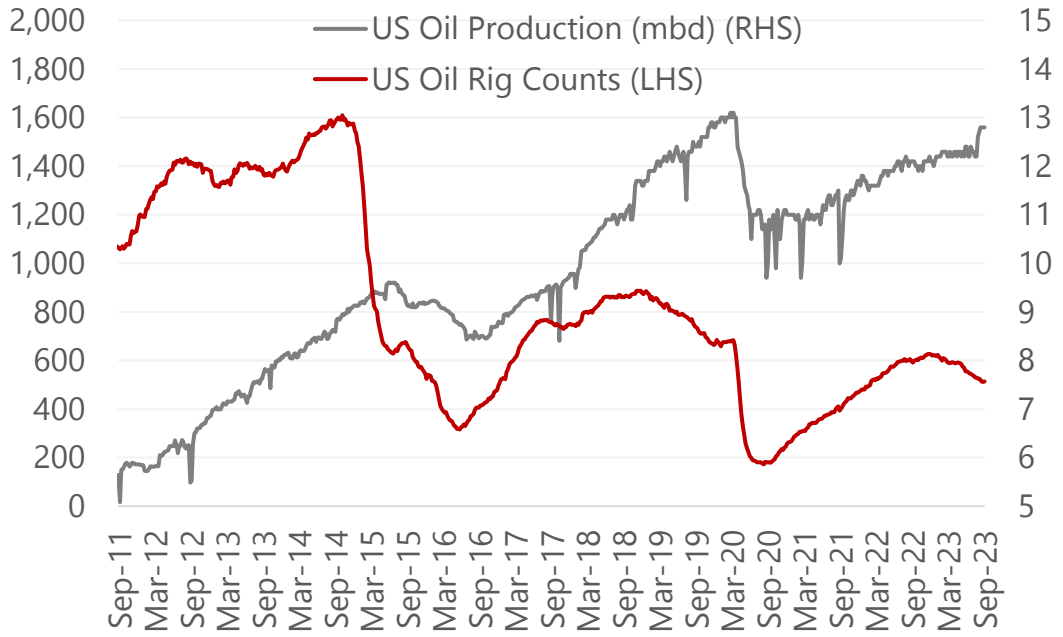


Sources: Bloomberg, Santander.

Oil: U.S. production nears the record high, but the pace of growth is slowing

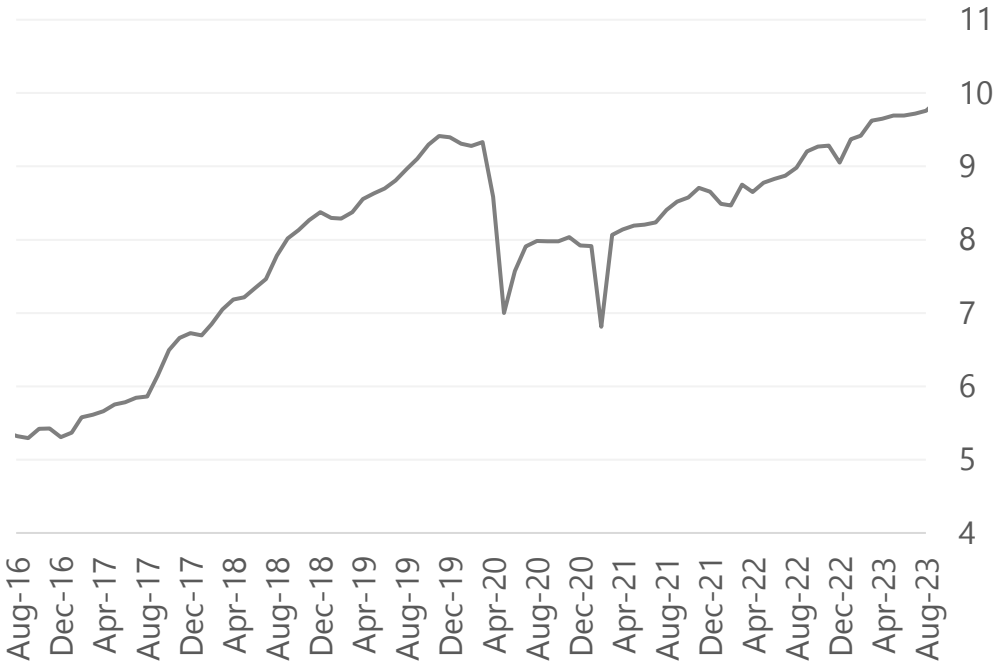
- According to EIA, US shale oil production has likely peaked. Now that the easiest-to-reach crude has been extracted, and with higher cost inflation, drilling wells and increasing output is getting more expensive.
- **With smaller SPRs and decelerated output growth, U.S. ability to influence oil prices has diminished.** This should mean more market power for OPEC+.

US Oil Production (Total)



Sources: Bloomberg, Santander.

US Shale Production (mm bpd)

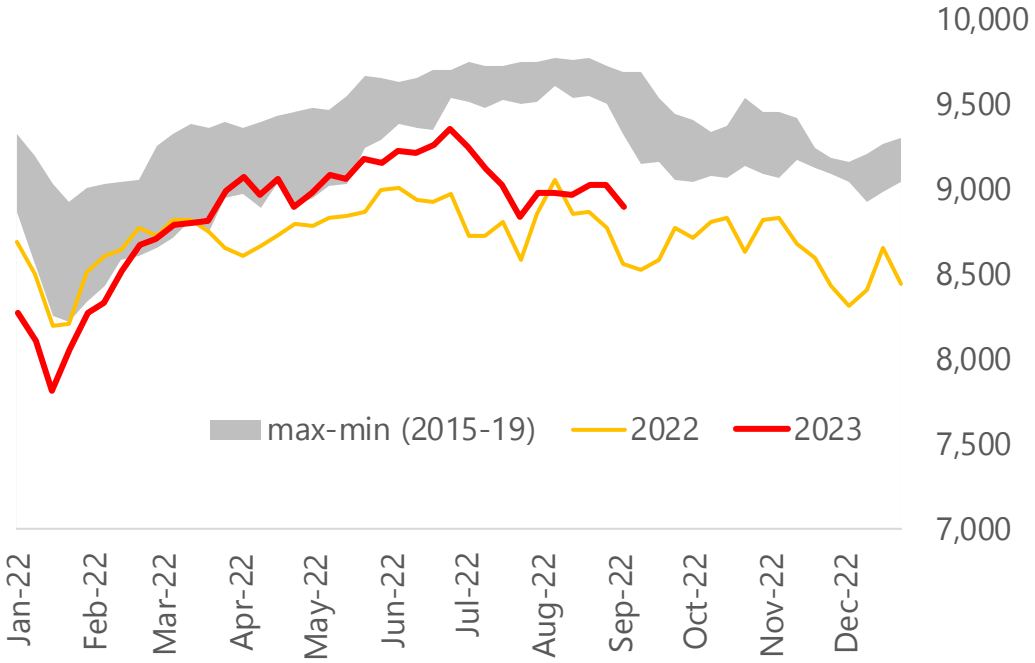


Sources: Bloomberg, Santander.

Oil: U.S. gasoline pump prices at the highest since November 2022

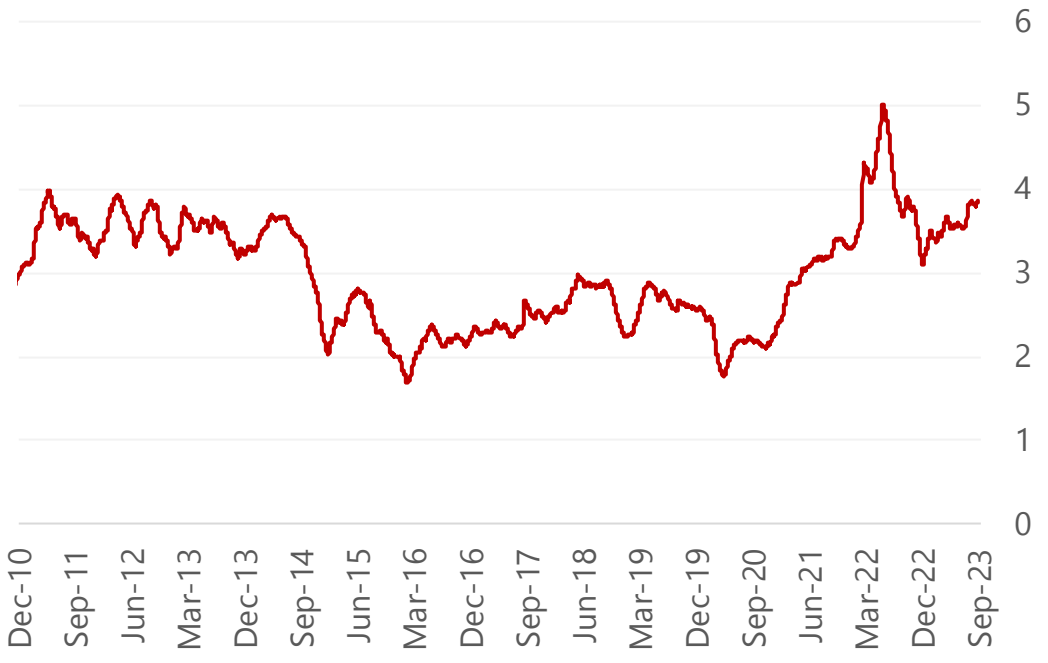
- It is unusual to see gasoline prices rising this time of the year, after the end of the summer driving season that boosted demand.
- Yet U.S. gasoline pump prices rose to U$ 3.86/gallon, following crude's rally.

U.S. Finished motor gasoline – Product supplied (k bpd)



Sources: Bloomberg, EIA, Santander.

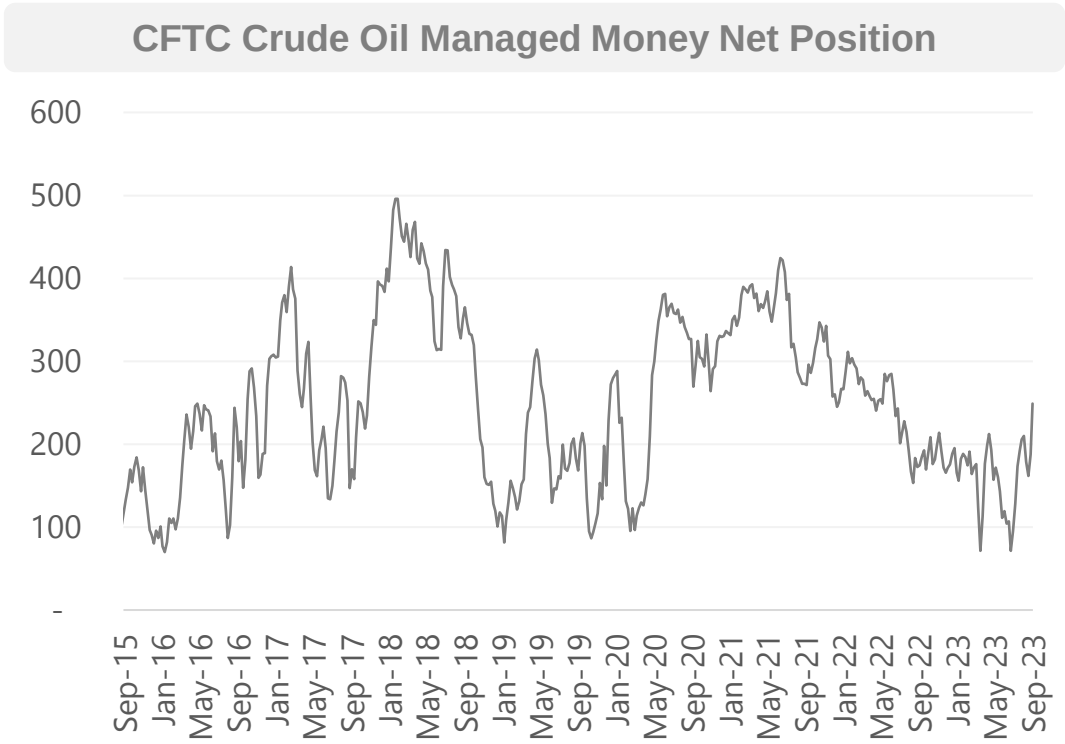
U.S. National Average Gasoline Price – Retail (USD/gallon)



Sources: Bloomberg, Santander.

Oil: Investors raise their bullish bets on crude

- Speculators raised they net long U.S. crude futures and option positions to the highest level since April 2023.
- The shift coincides with the production cuts announced by OPEC+.

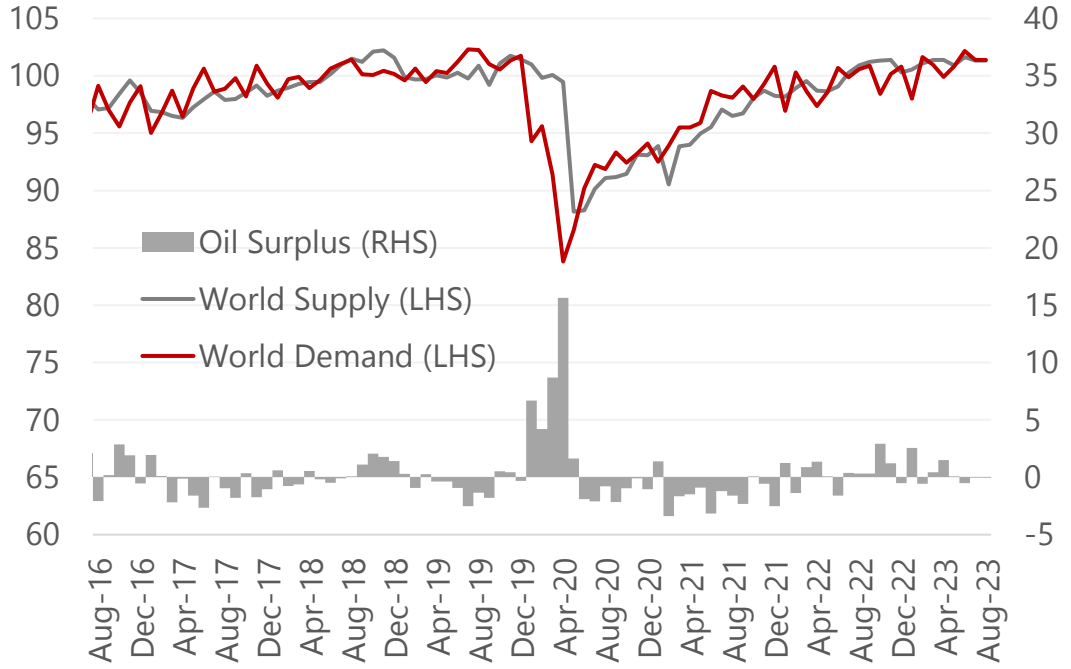


Sources: CFTC, Santander.

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

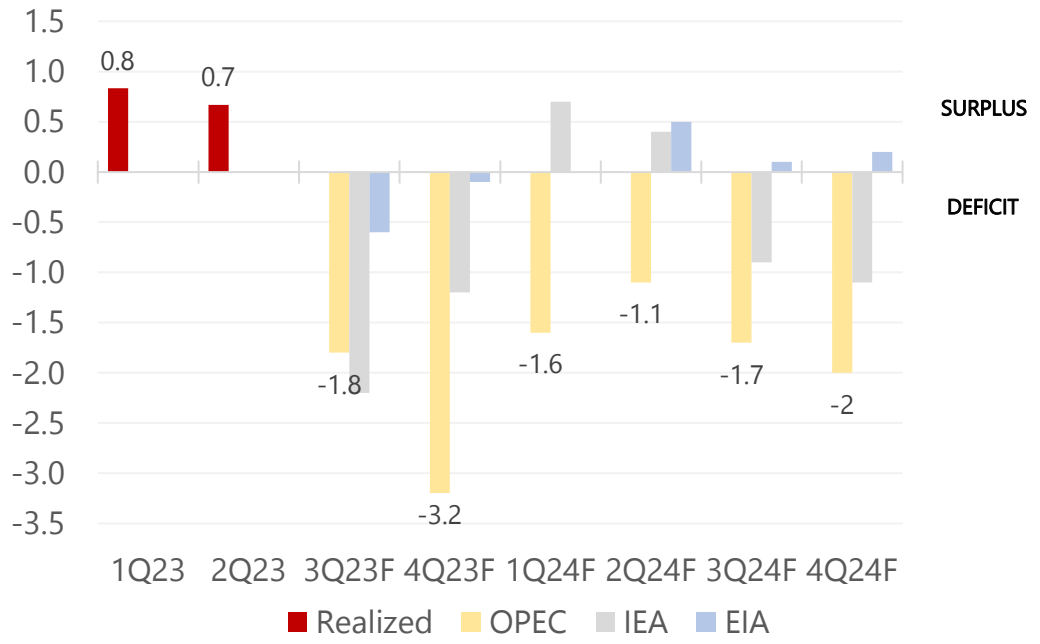
- Key agency reports forecast a tightening in global oil balance in the coming quarters.

World Oil Supply x Demand (mm bpd)



Sources: Bloomberg, Santander.

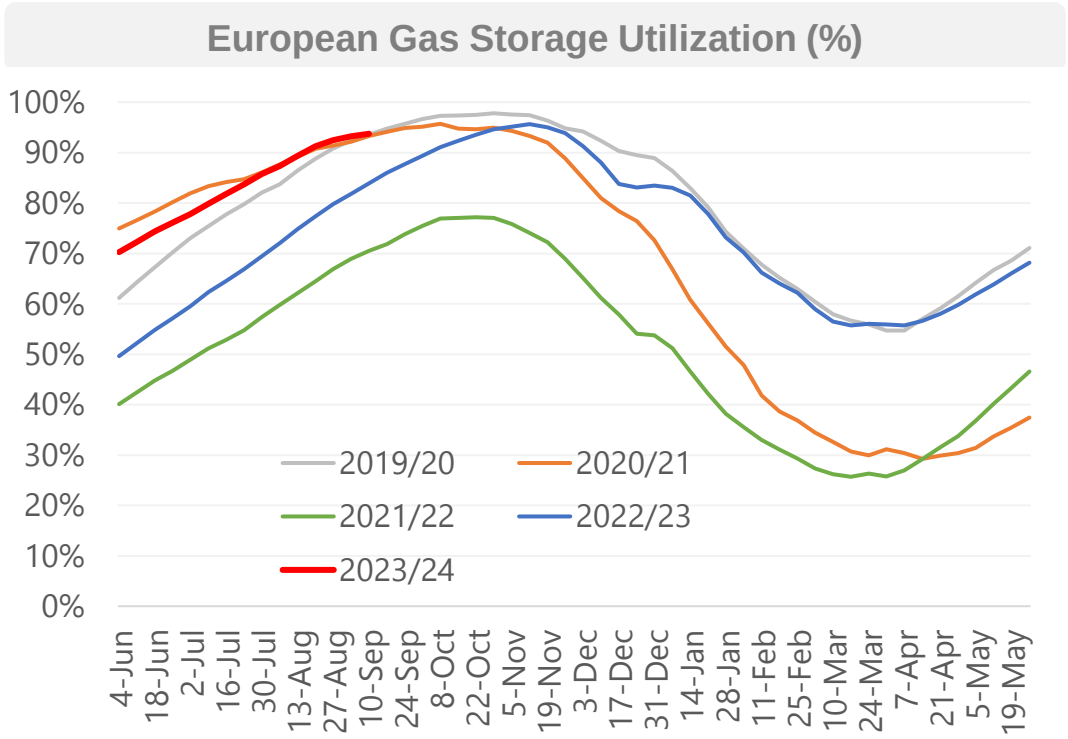
Global Oil Balance Forecast (million barrels)



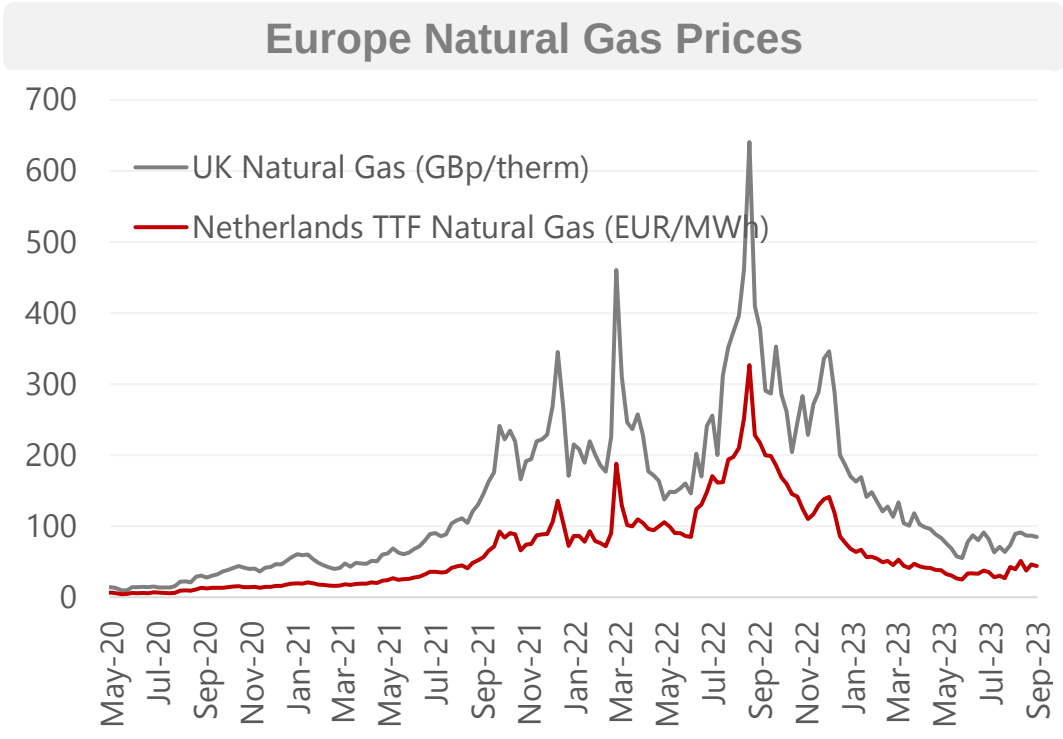
Sources: OPEC, IEA, EIA, Santander.

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

- Europe has been successful in pivoting away from Russian gas imports, as LNG imports (mainly from the U.S.) have been running high, and inventories are at 93% ahead of the coming winter.
- Worth to remember, last year Europe suffered with gas shortages, industrial paralysis and compulsory rationing.



Sources: Bloomberg, Santander.



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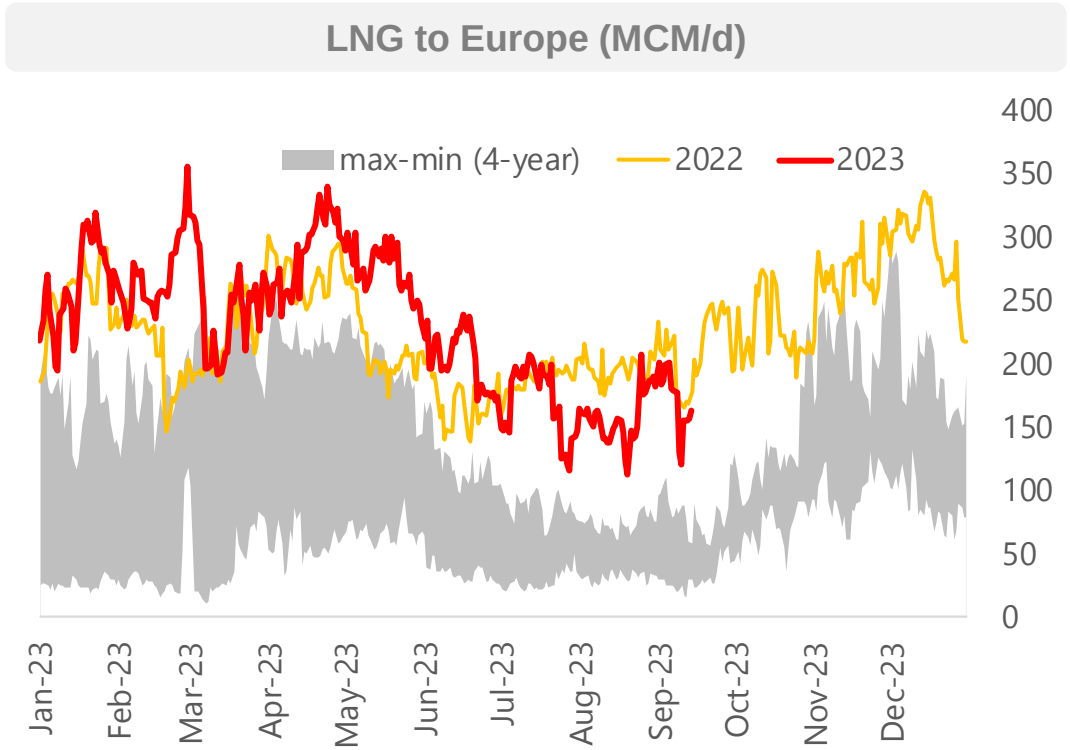


Sources: Bloomberg, Santander.

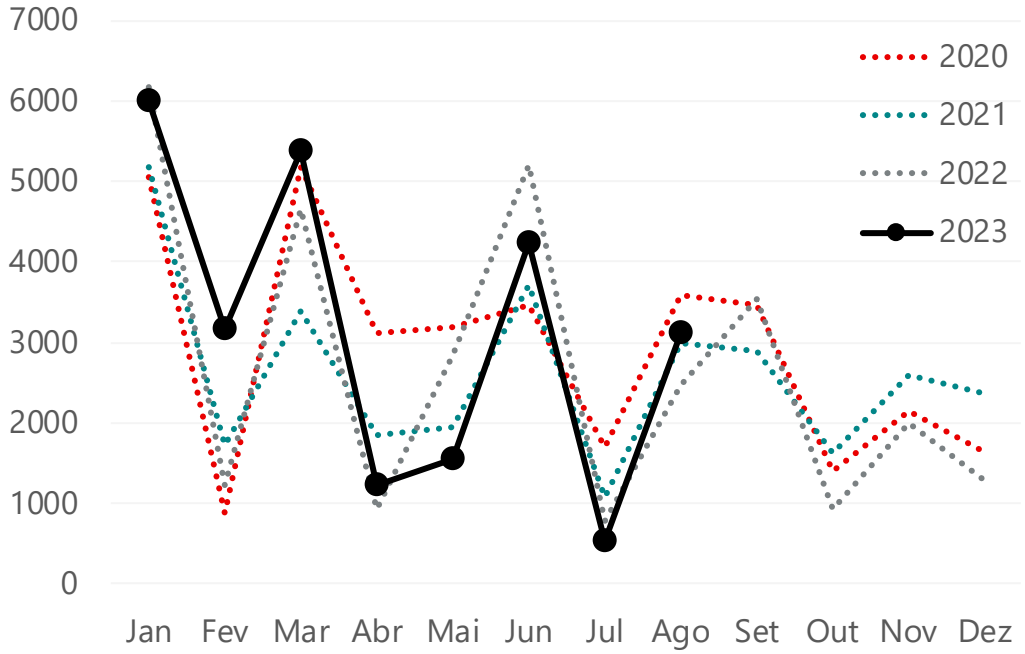
METALS

04

Metals: Activity is weak, but improving at the margin

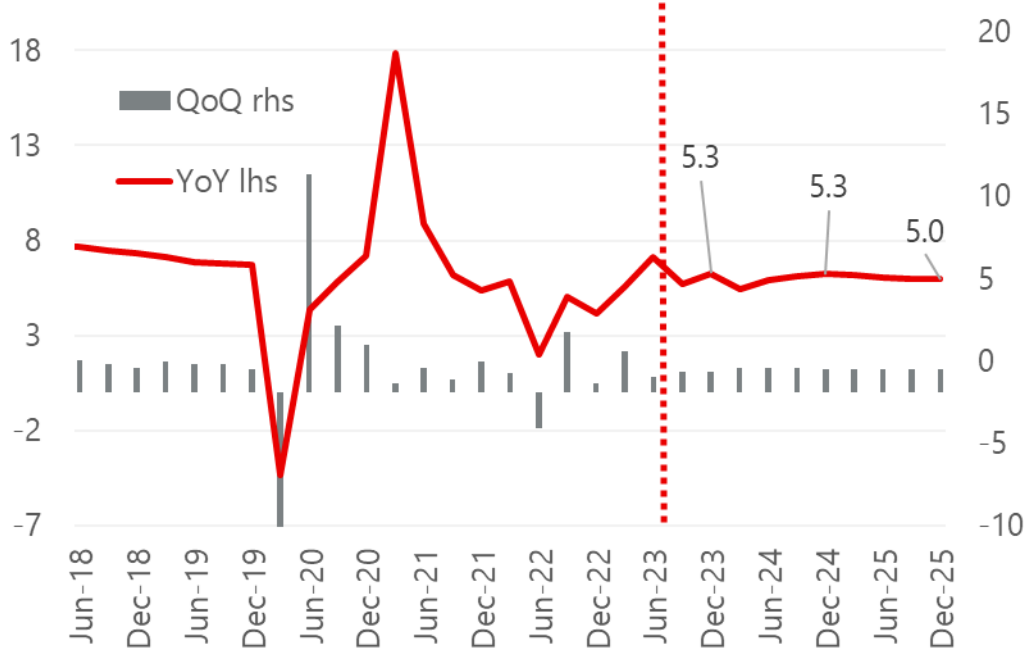
- Economic activity was very weak in Q2, and markets were revising lower growth forecasts for 2023.
- Government has been announcing several stimuli to contain activity slowdown. Data at the margin is improving and growth target for 2023 (at around 5.0%) should be met

Credit expansion accelerated in August



Sources: Bloomberg, Santander.

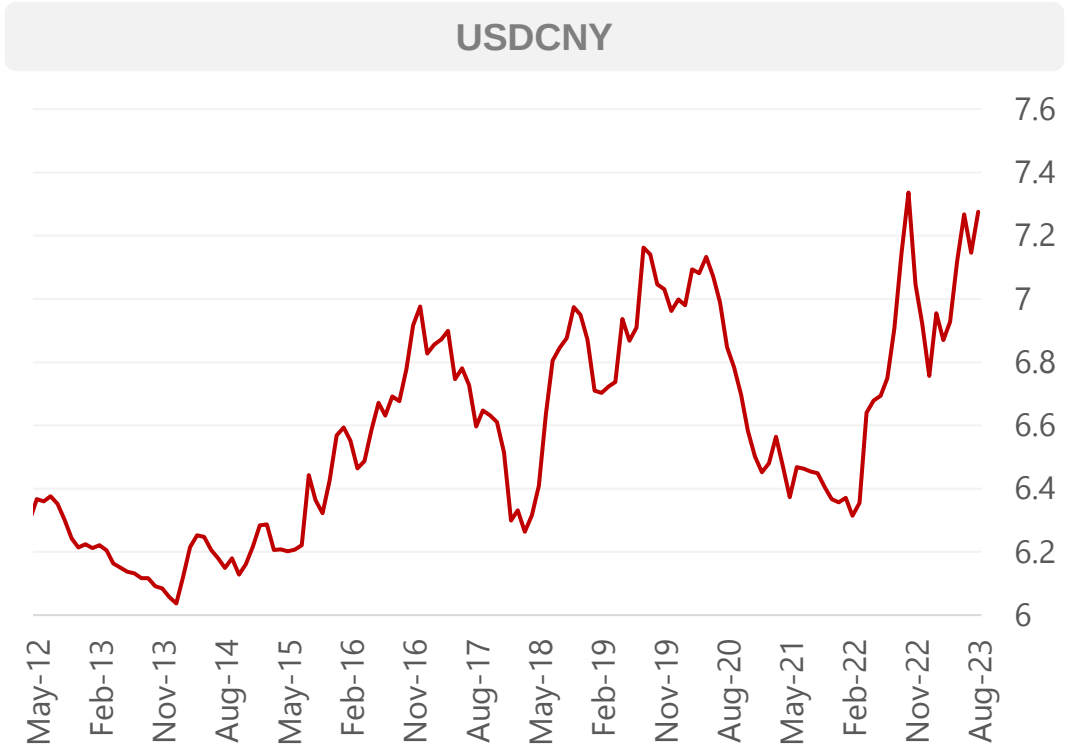
Economic recovery lost momentum in Q2



Sources: Bloomberg, Santander.

Metals: A weak CNY hinder demand for commodities

- A weak yuan makes imports more expensive, hence cooling demand for commodities.
- It is also not encouraging for property development firms in China that have borrowed in USD, as their debt repayments will increase.

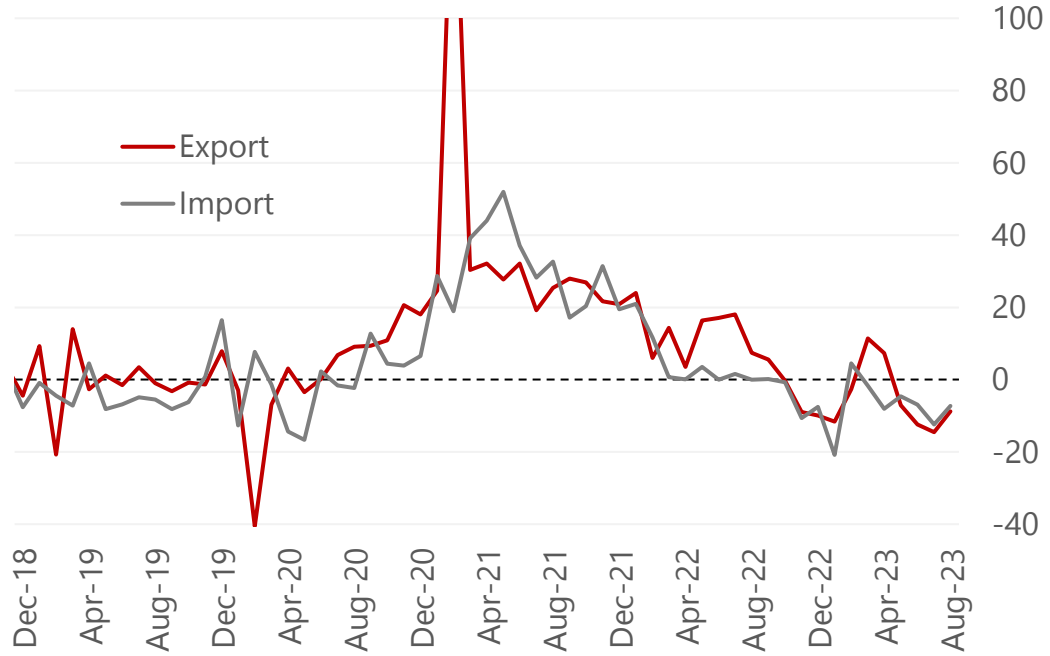


Sources: Bloomberg, Santander.

Metals: After a deterioration in Q2, economic data suggest a stability

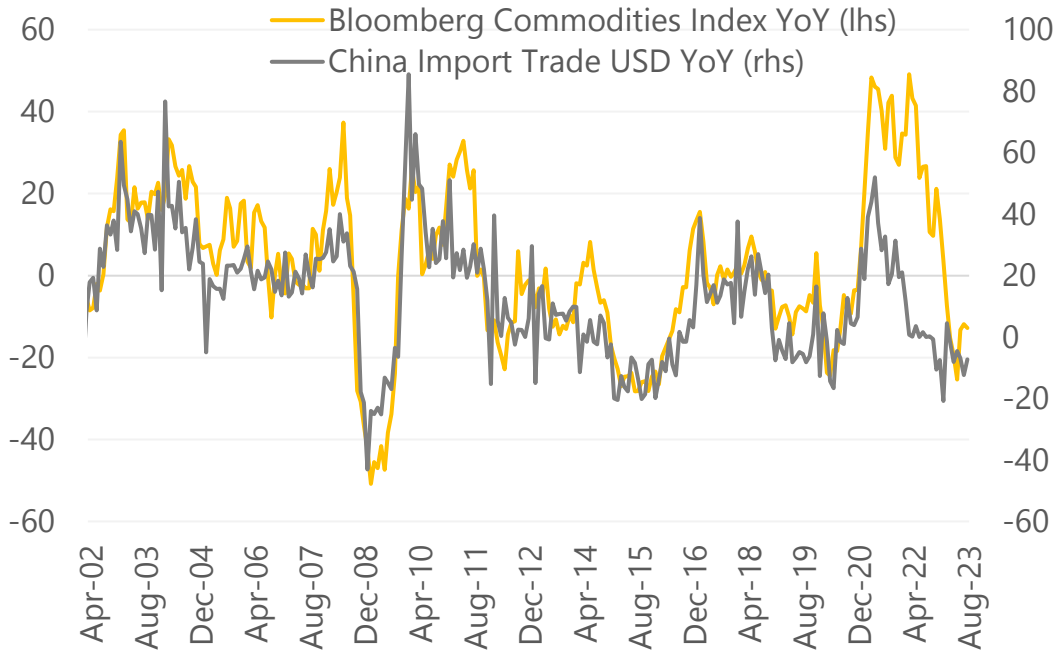
- China's imports and exports fell in August – though showing signs of a stabilization at the margin - as weak domestic and abroad demand threatens recovery prospects.

China Trade USD (YoY)



Sources: Bloomberg, Santander.

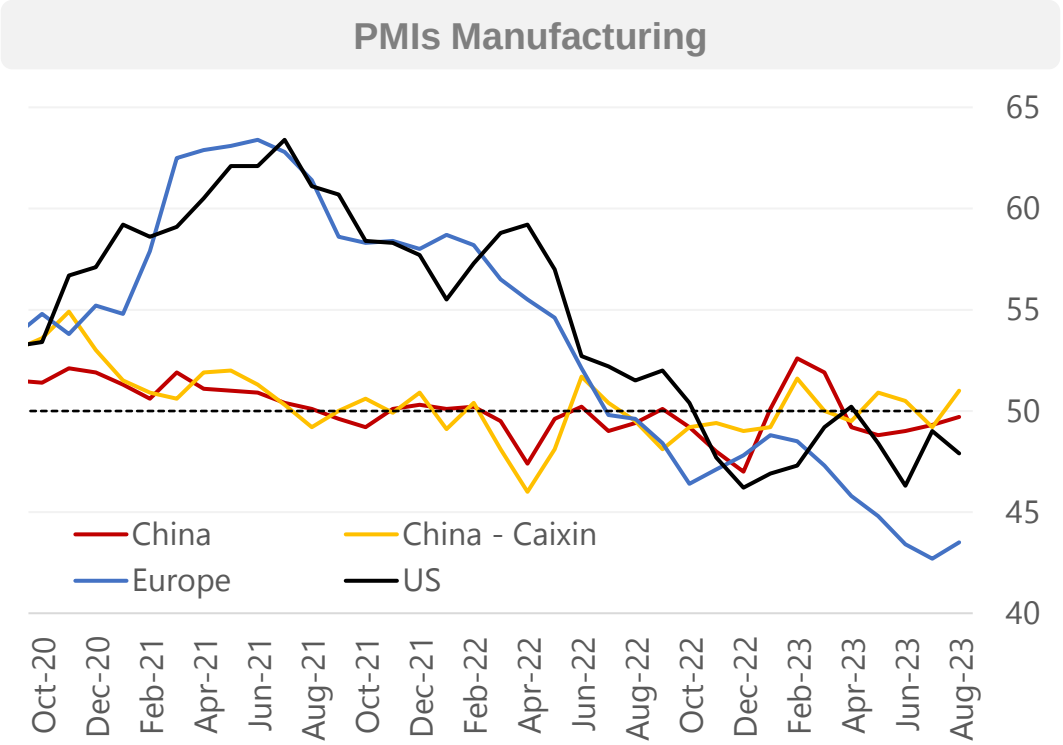
China Import Trade x Commodities Index



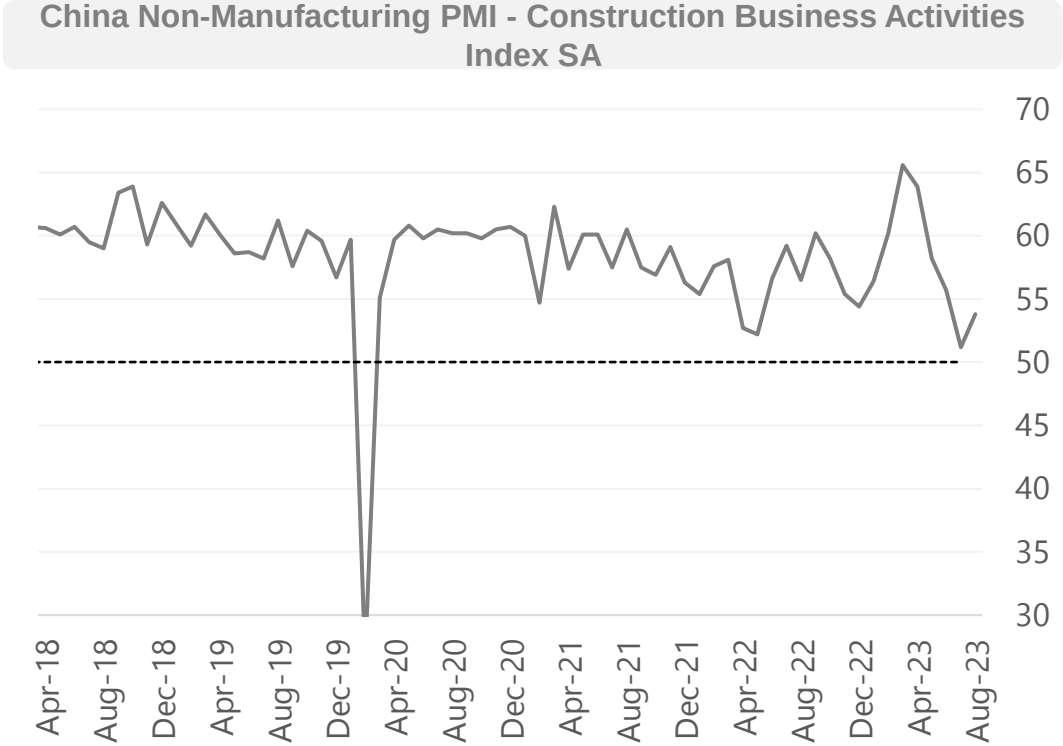
Sources: Bloomberg, Santander.

Metals: After a deterioration in Q2, economic data suggest a stability

- China's manufacturing activity indexes (both official and Caixin) have expanded in August.
- The sub-index for the key construction sector is down sharply from a high in March, though it rebounded at the margin.



Sources: Bloomberg, Santander.

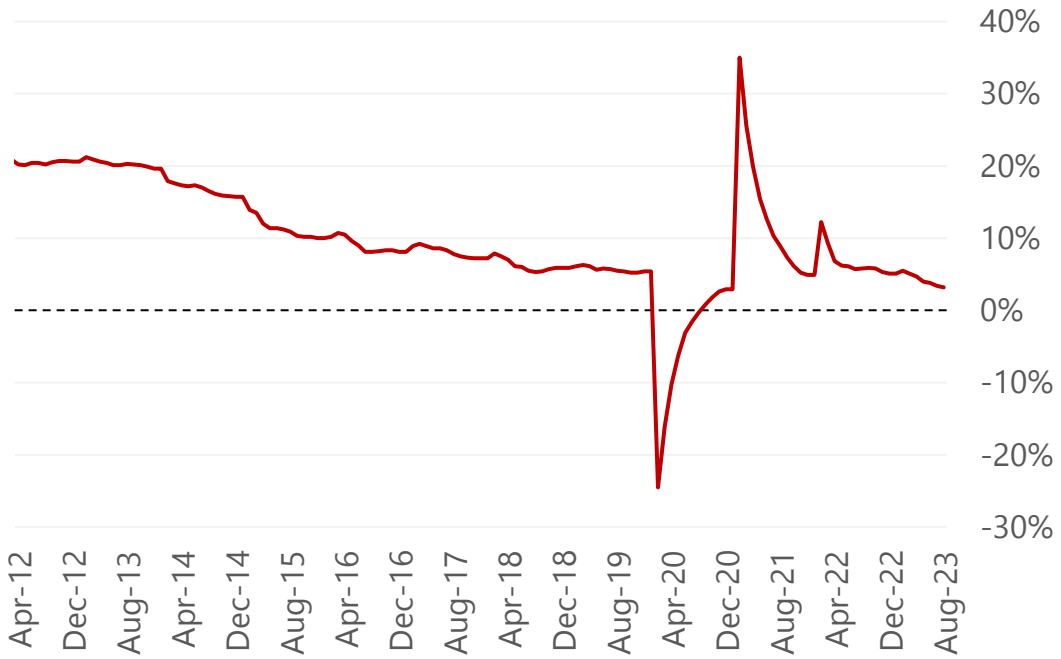


Sources: Bloomberg, Santander.

Metals: After a deterioration in Q2, economic data suggest a stability

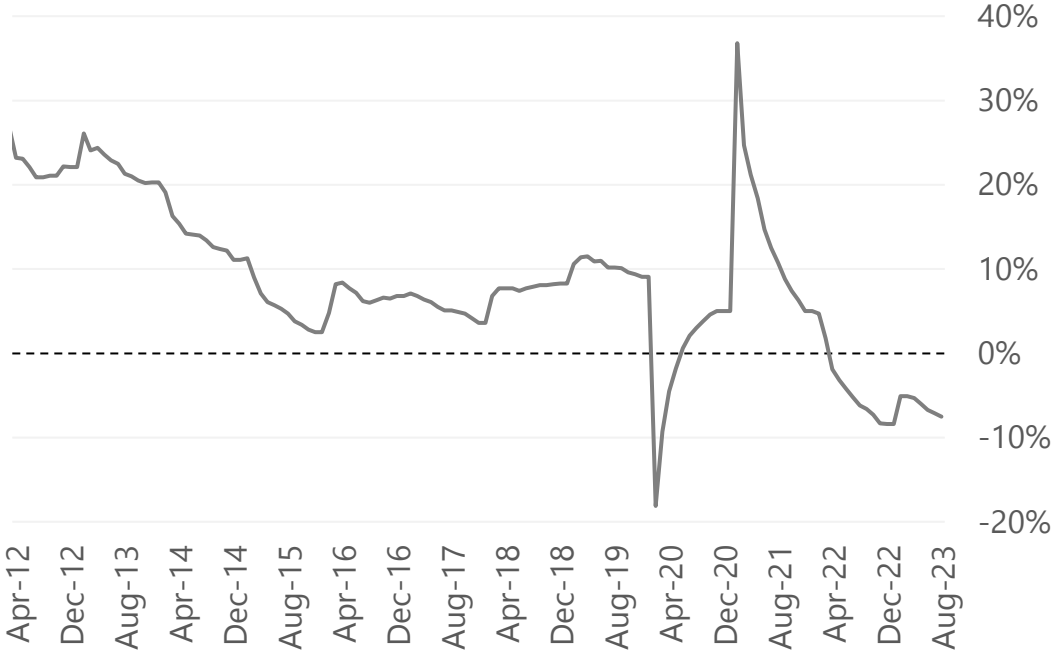
- China's fixed asset investment (FAI) increased 3.4% YoY in August.
- FAI in real estate decreased -7.5% YoY.

China Fixed Assets Investments (FAI) YoY



Sources: Bloomberg, Santander.

China FAI - Real Estate YoY

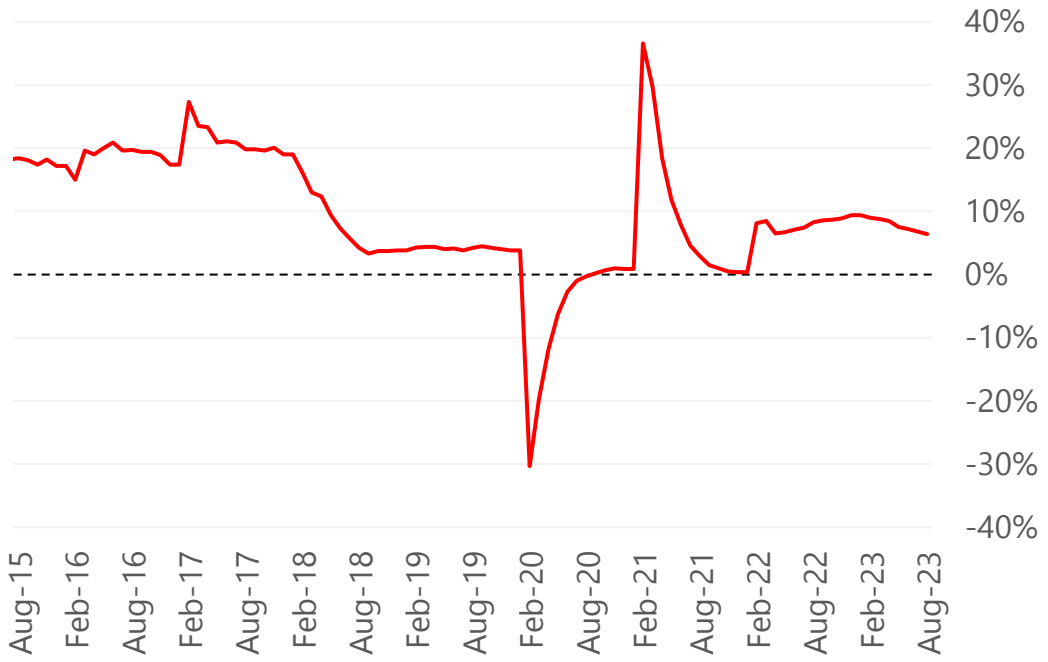


Sources: Bloomberg, Santander.

Metals: After a deterioration in Q2, economic data suggest a stability

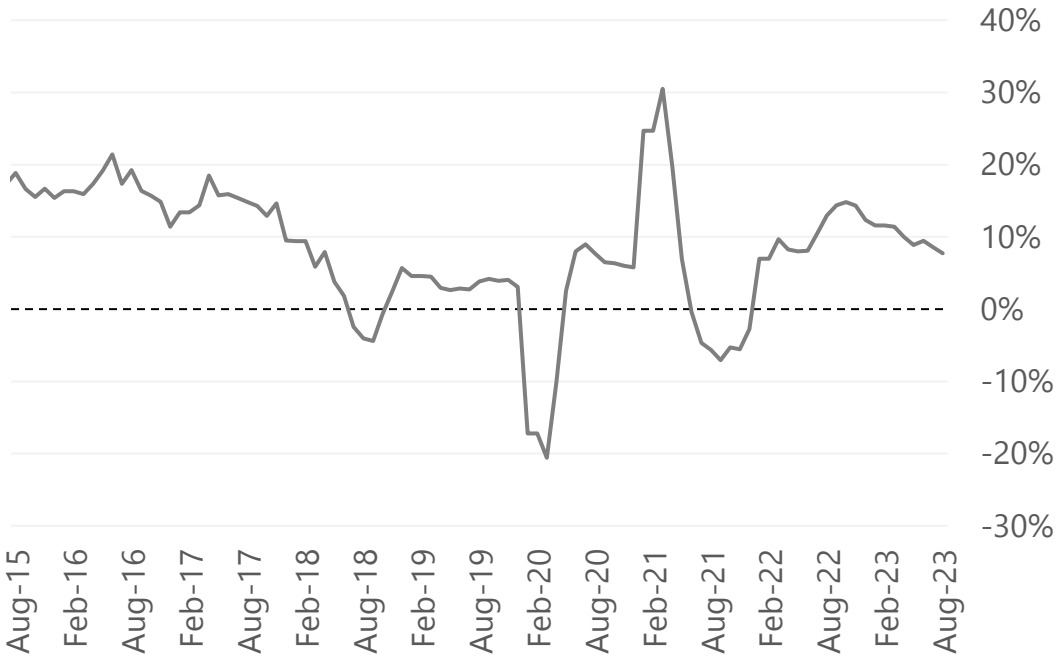
- FAI in infrastructure increased 6.8% YoY in August, and it has been slowly decelerating since January 2023.

China FAI - Infrastructure (excluding electricity) YoY



Sources: Bloomberg, Santander.

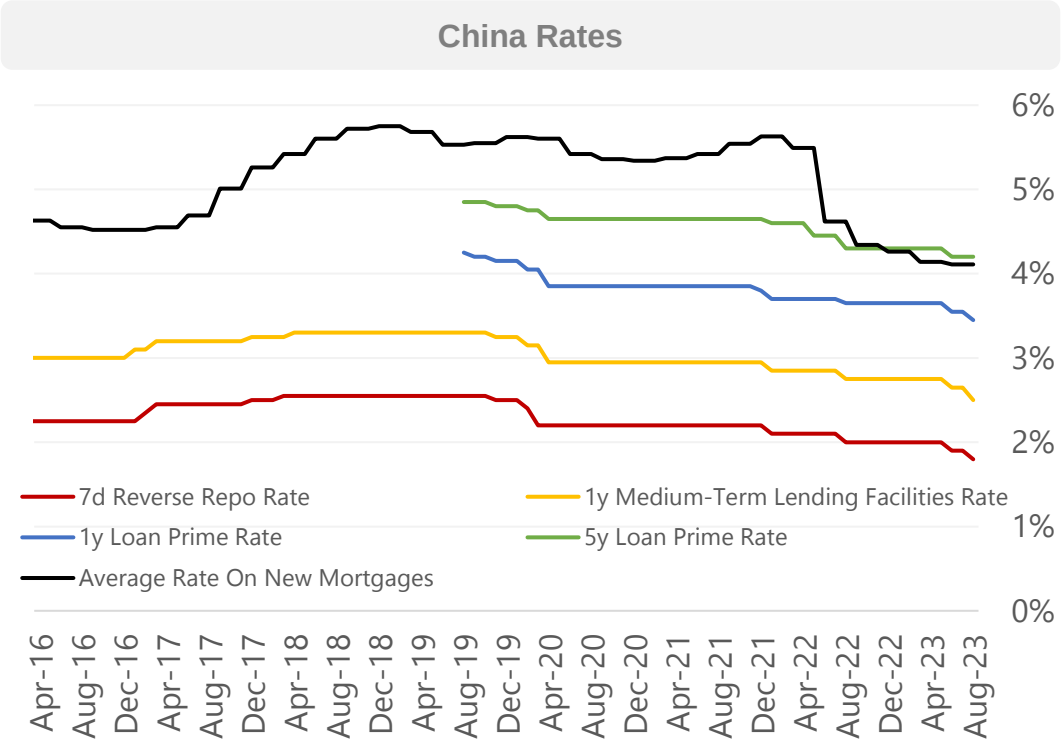
China Infrastructure Investment YoY



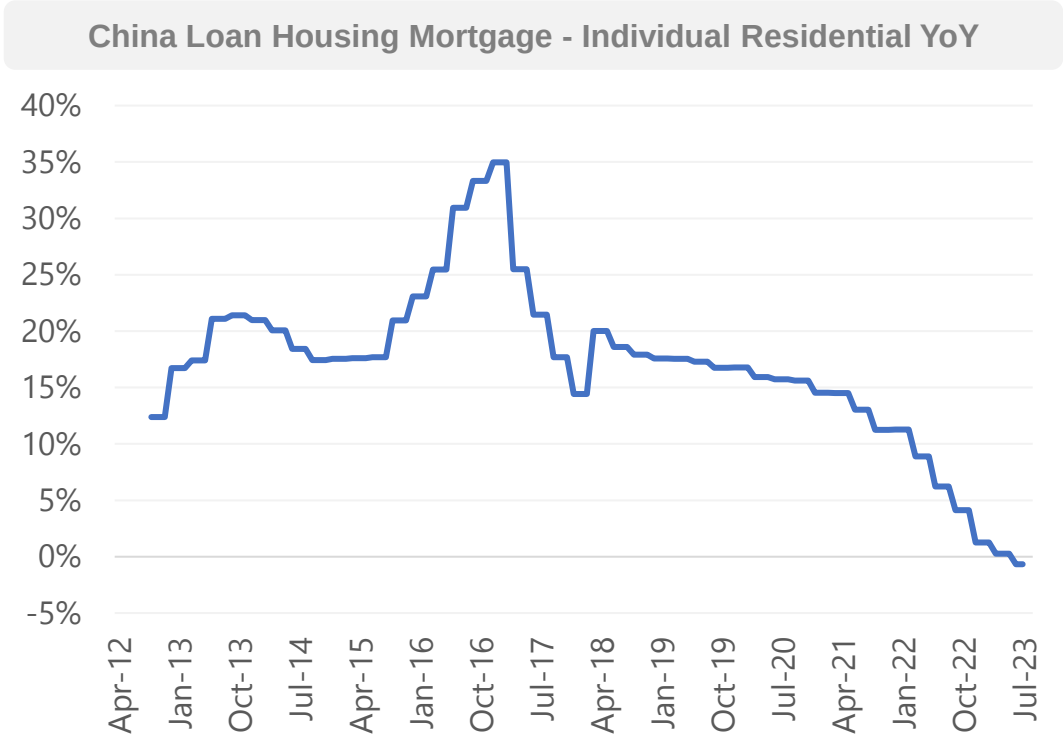
Sources: Bloomberg, Santander.

Metals: As recovery disappointed, China has cut key interest rates

- China's central bank has cut several interest rates for a second time in the last months, as the country attempts to shore up the economy.
- Rate cuts were likely limited by concerns of additional downward pressure on the CNY.



Sources: Bloomberg, Santander.

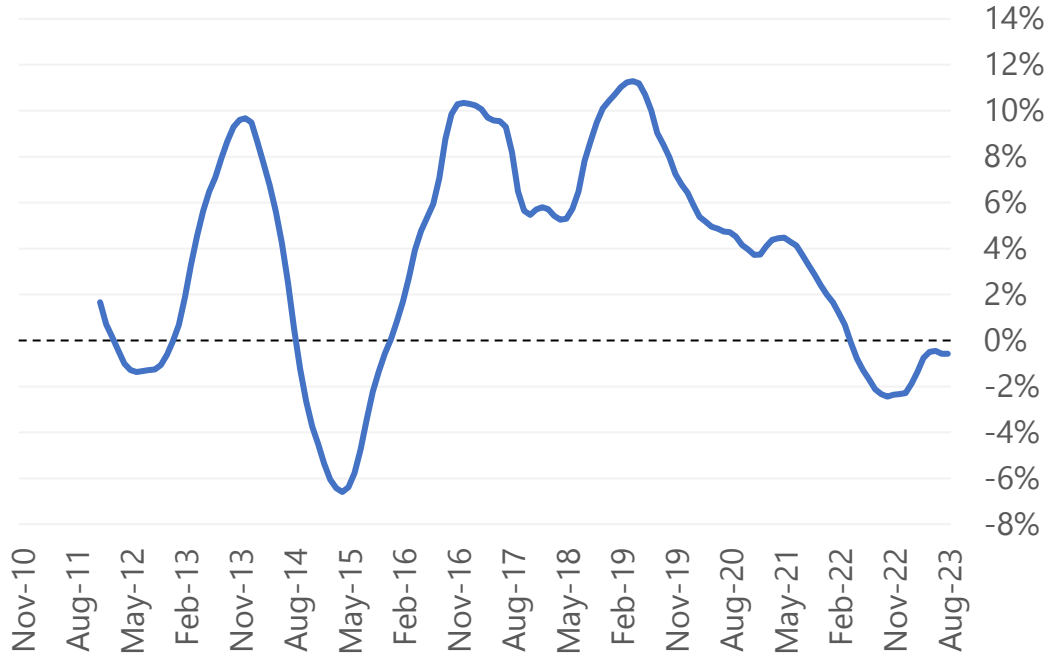


Sources: Bloomberg, Santander.

Metals: New home prices in China fell in August

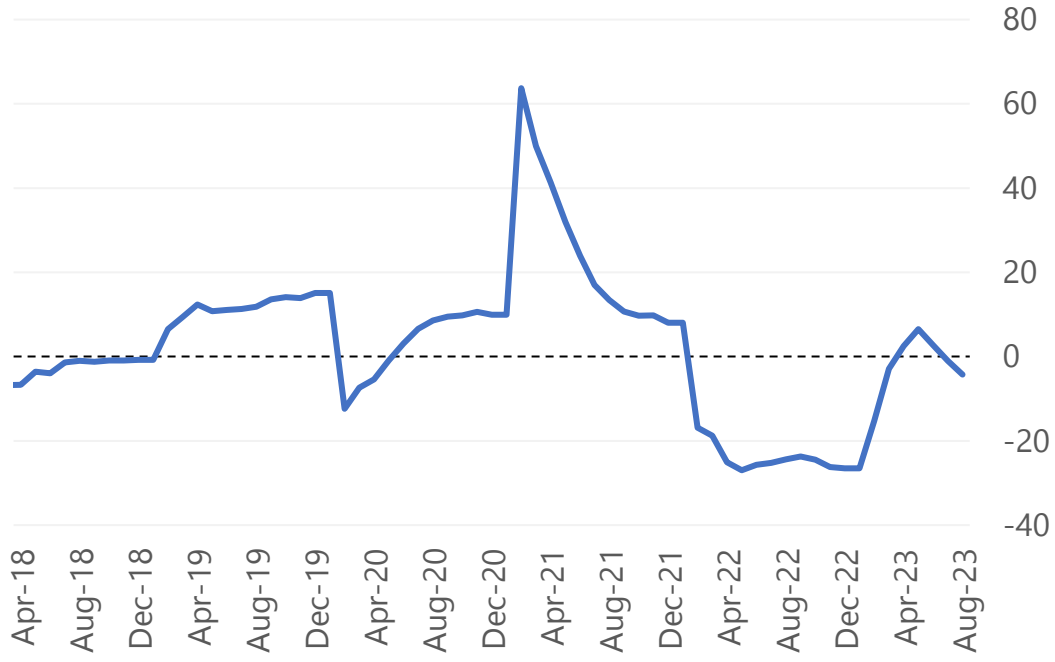
- Recently announced easing measures (e.g. cuts in mortgage rates and down payment for homebuyers) may have only a short-lived effect on property sales.
- Reduction in the reserve requirement ratio could also inject some liquidity, but a small cut would do very little to help property developers in trouble.

China 70 Cities Newly Built Commercial Residential Buildings Prices YoY



Sources: Bloomberg, Santander.

China Property - Personal Mortgage - YoY

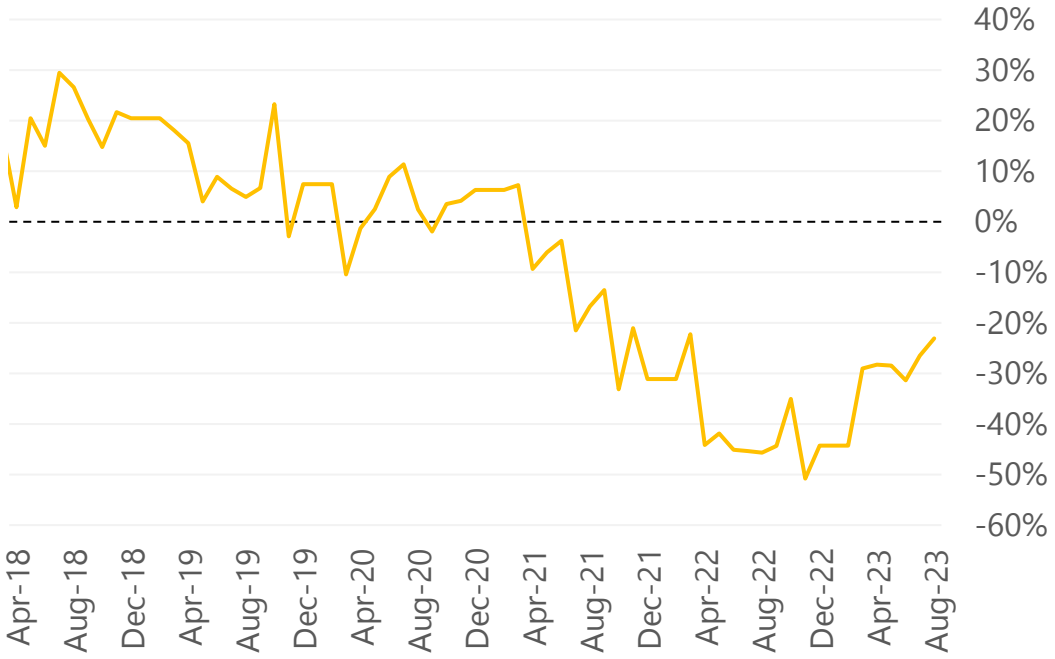


Sources: Bloomberg, Santander.

Metals: A bottom for property activity?

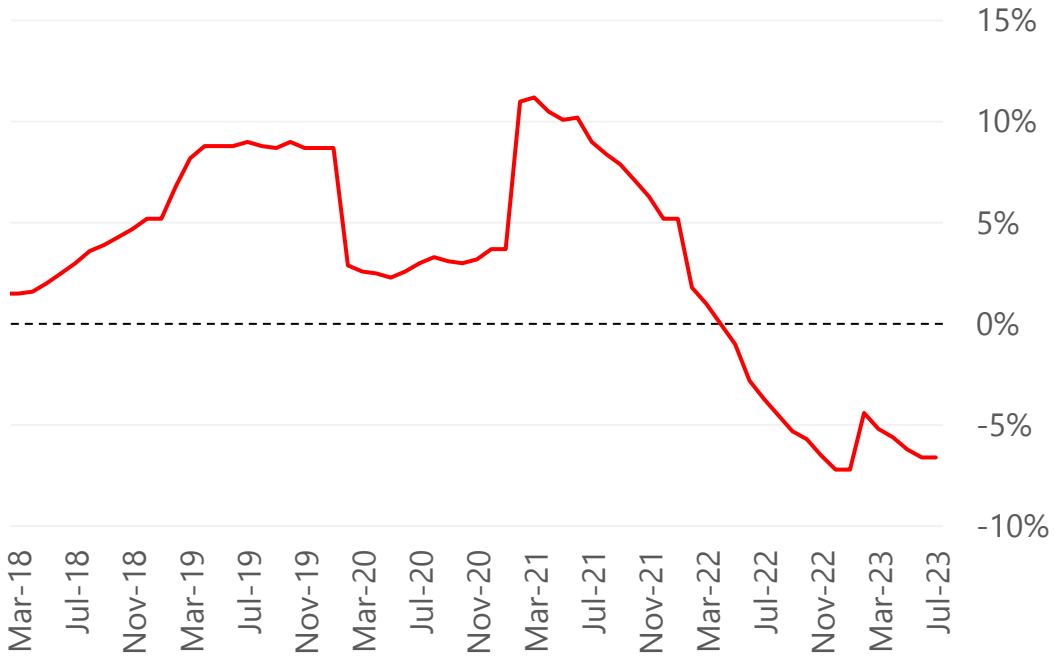
- New starts are still contracting in YoY, but reducing at the margin, while buildings under construction are relatively flat since the beginning of the year.
- Home sales rose a tad in July, with the value of new home sales falling -24% YoY in July.

China Property - Floor Space of Houses Newly Started YoY



Sources: Bloomberg, Santander.

China Property -Floor Space of Buildings Under Construction YoY



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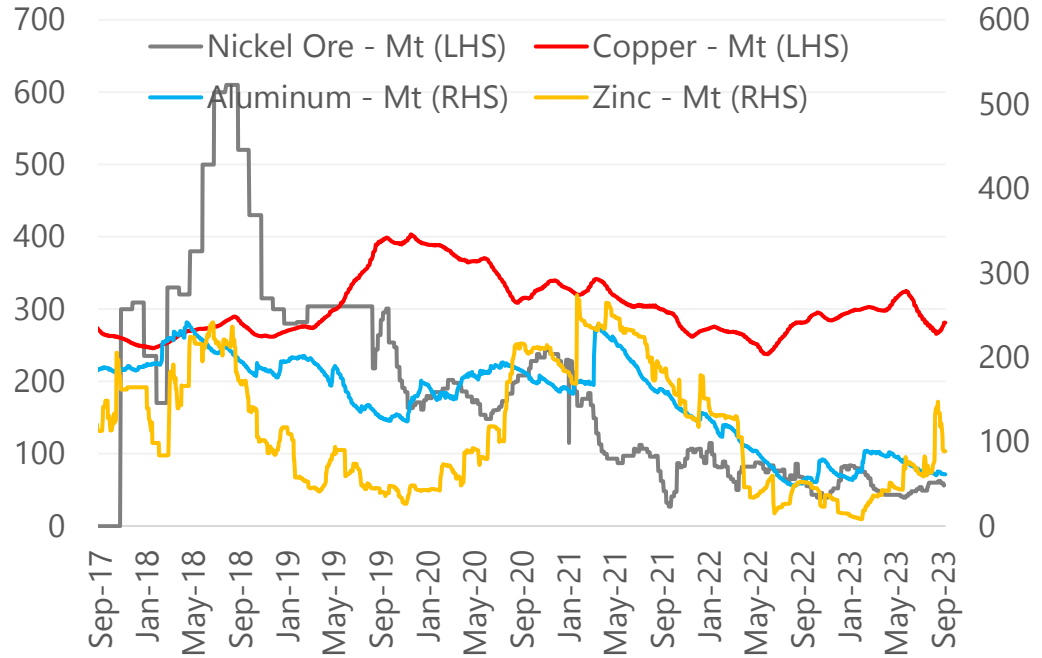
Metals: Depleted inventories for base metals

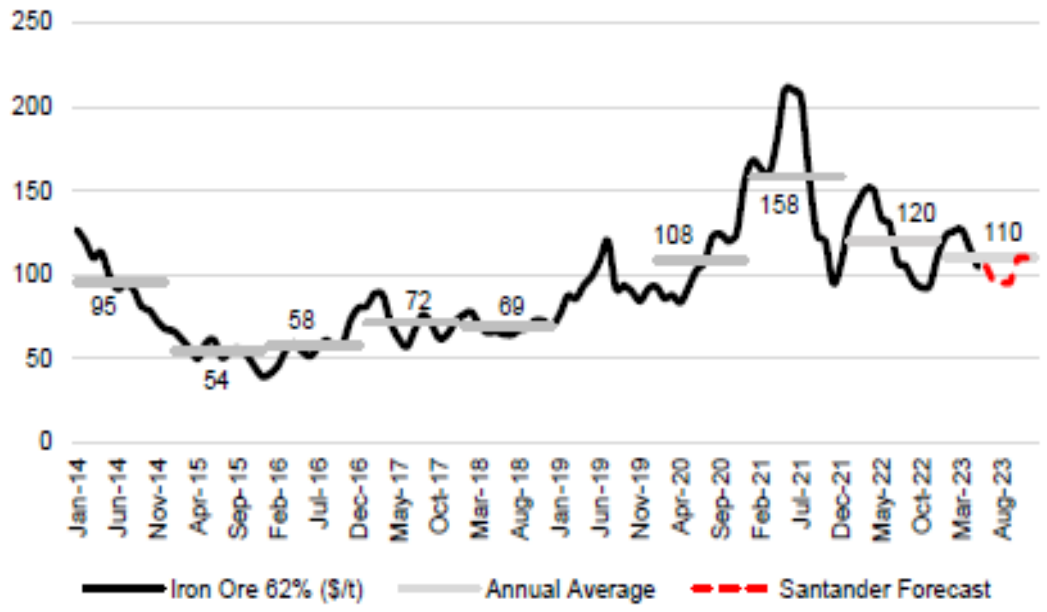
- Metals inventories remain near-record levels, but the weak demand of China is prevailing in the outlook for metals.
- As for iron ore, with exports from key producing countries (Brazil and Australia) flowing at a decent pace, we see little room for further gains in iron prices.

Base Metals Inventories



Sources: Bloomberg, Santander.

Iron Ore Price Forecast



Sources: Santander.

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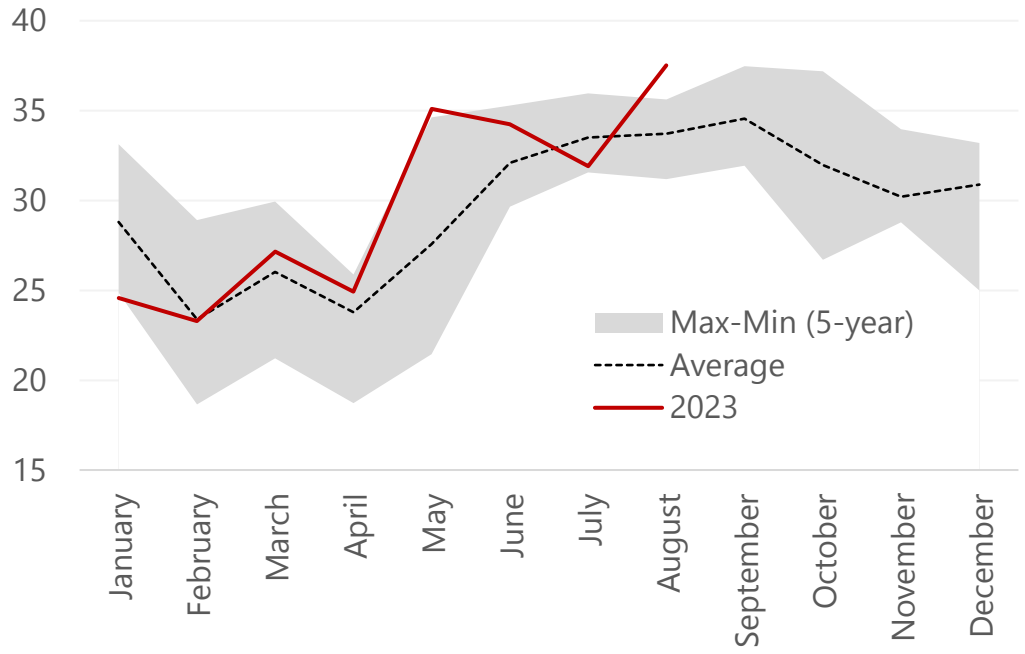
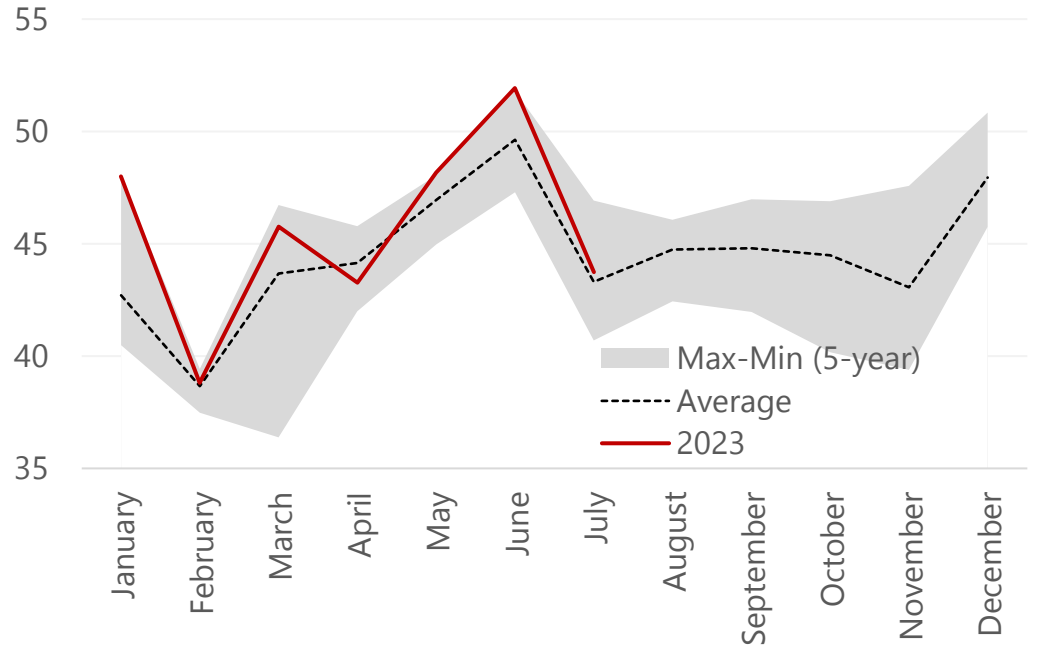
Brazil Iron Ore Monthly Exports (ton)



Sources: Bloomberg, Santander.

Australia Iron Ore Monthly Exports (ton)



Sources: Bloomberg, Santander.

Macro Scenario - Forecasts

Macroeconomic Variables		Previous		Current
GDP (%)	2023E	1.9	↑	2.5
	2024E	1.0	→	1.0
	2025E	1.5	→	1.5
IPCA (%)	2023E	4.9	↓	4.7
	2024E	3.9	↓	3.8
	2025E	4.5	→	4.5
Selic Rate (% end of period)	2023E	11.75	→	11.75
	2024E	10.00	↓	9.50
	2025E	7.50	→	7.50
FX Rate - USDBRL (end of period)	2023E	5.20	↓	5.10
	2024E	5.35	↓	5.25
	2025E	5.40	↓	5.30
Current Account Balance (% of GDP)	2023E	-2.5	→	-2.5
	2024E	-2.7	→	-2.7
	2025E	-2.7	→	-2.7
Primary Fiscal Balance (% of GDP)	2023E	-1.0	→	-1.0
	2024E	-0.9	→	-0.9
	2025E	-0.7	→	-0.7
Gross Public Debt (% of GDP)	2023E	77.0	↓	76.5
	2024E	81.1	↓	80.5
	2025E	83.9	↓	83.2

Note: Our previous forecasts date from August 4, 2023 (Scenario Update: "Better Growth Outlook in 2024 Given a Less Contractionary Monetary Policy" – Available on: https://tinyurl.com/Std-scenreview-aug23).

The forecasts refers to our latest Scenario Review

"Adjustments to Reflect Past Surprises; Same Trends Continuing Ahead"
(sent on September 15, 2023)

For the full report click on the link:

https://bit.ly/std-sce-review-Sep23

Macro Scenario - Santander Brazil's Global Macro Assumptions – Summary

Global Macro Scenario												
	2018	2019	2020	2021	2022	2023E		2024E		2025E		
Global GDP (%)	3.5	2.8	-3.5	5.9	3.4	2.4	→	2.2	→	2.8	→	
China GDP (%)	6.7	6.0	2.3	8.1	3.0	5.2	↓	5.1	→	5.0	→	
US GDP (%)	3.0	2.2	-3.5	5.7	2.1	2.1	↑	0.1	↑	1.8	→	
US Inflation (Core PCE, %)	2.1	1.6	1.5	4.9	5.0	4.0	↑	2.5	→	2.0	→	
US Interest Rate (FFR, %)	2.50	1.75	0.25	0.25	4.50	5.50	→	4.00	→	2.50	→	
US Interest Rate (UST10y, %)	2.7	1.9	0.8	1.8	3.9	4.0	↑	3.5	↑	3.0	→	
Dollar Index - DXY	96	96	90	96	104	103	↑	100	→	100	→	
Commodity Prices - CRB	409	401	444	571	558	528	→	474	→	445	→	

*Core PCE is referred to the y/y variation for Q4.

Source: Santander

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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

Brazil Macroeconomic Research Team

Ana Paula Vescovi
Chief Economist
anavescovi@santander.com.br
+55 (11) 3553-8567

Adriano Valladao
Economist – Inflation
adriano.ribeiro@santander.com.br
+55 (11) 3553-9828

Ana Júlia Carvalho
Economist – Special Projects
fana.carvalho.silva@santander.com.br
+55 (11) 3553-8071

Daniel Karp Vasquez
Economist - Inflation
daniel.karp@santander.com.br
+55 (11) 3553-9828

Felipe Kotinda
Economist - Commodities
felipe.kotinda@santander.com.br
+55 (11) 3553-8071

Gabriel Couto
Economist – Activity
gabriel.couto@santander.com.br
+55 (11) 3553-8487

Gilmar Lima
Economist – Modeling
gilmar.lima@santander.com.br
+55 (11) 3553-6327

Henrique Danyi
Economist - Credit
henrique.danyi@santander.com.br
+55 (11) 3553-8071

Ítalo Franca
Economist – Fiscal Policy
italo.franca@santander.com.br
+55 (11) 3553-5235

Jankiel Santos
Economist – External Sector
jankiel.santos@santander.com.br
+55 (11) 3012-5726

Patrícia Bonilha
Business Manager
pacardoso@santander.com.br
++55 (11) 3553-5235

Tomas Urani
Economist – Global Economics
tomas.urani@santander.com.br
+55 (11) 3553-9520

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