



**Hancock  
Asset  
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Brasil**

*A Manulife Asset Management Company*

# Hancock Timberland Investor Brazil

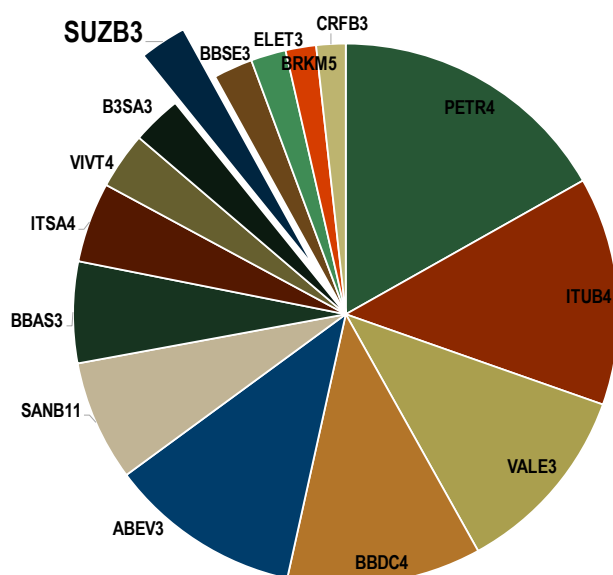
April 2019

One year following the announced merger of two of Brazil's major pulp and paper producers: Fibria Celulose S.A. (FIBR3) and Suzano Papel e Celulose S.A. (SUZB3), a giant integrated business has emerged. The new Suzano S.A., has a market capitalization of BRL 63 billion and is now the eleventh largest company by market cap on the Ibovespa<sup>1</sup>.

Suzano's dominant position in global market pulp was highlighted this past January in an environment of otherwise weak underlying demand: global producer stocks of bleached chemical market pulp hit record highs, yet Suzano was able to hold the line on price and actually achieved some modest price increases in China for both softwood and hardwood grades<sup>2</sup>.

The new company has seven pulp mills with a combined capacity of 10.9 million tons of market pulp—the largest market pulp capacity of any single company worldwide<sup>3</sup>. The successful creation of the new Suzano should help dispel the cloud of uncertainty surrounding the possible paths for the expansion of Brazil's market pulp sector over the coming decade. Previously discussed projects shelved during the merger process might move forward. If undertaken, the construction of a green-field world-class pulp mill would have direct positive implications for pulpwood markets and timber plantation values in the region of Brazil where the mill would be located.

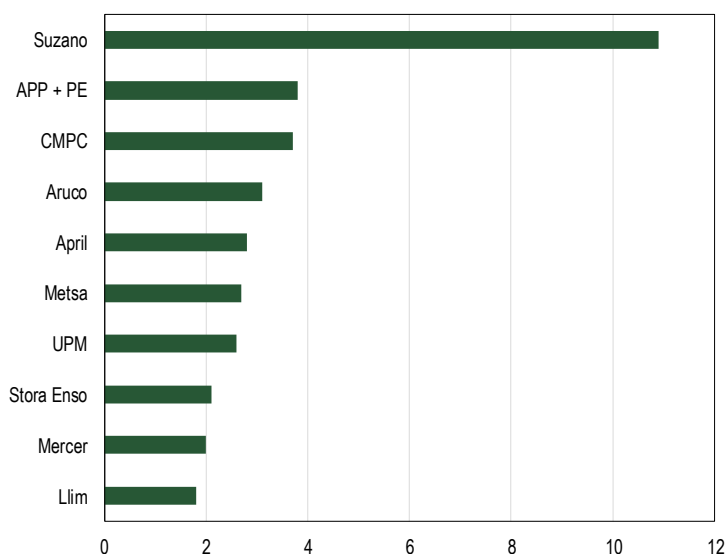
## A Giant is Born: Suzano is now the eleventh largest company by market cap on the Ibovespa



Source: Bloomberg, April 2019

## Suzano is the largest producer of market pulp globally

Global Top 10 Pulp Producers (Million Tons)

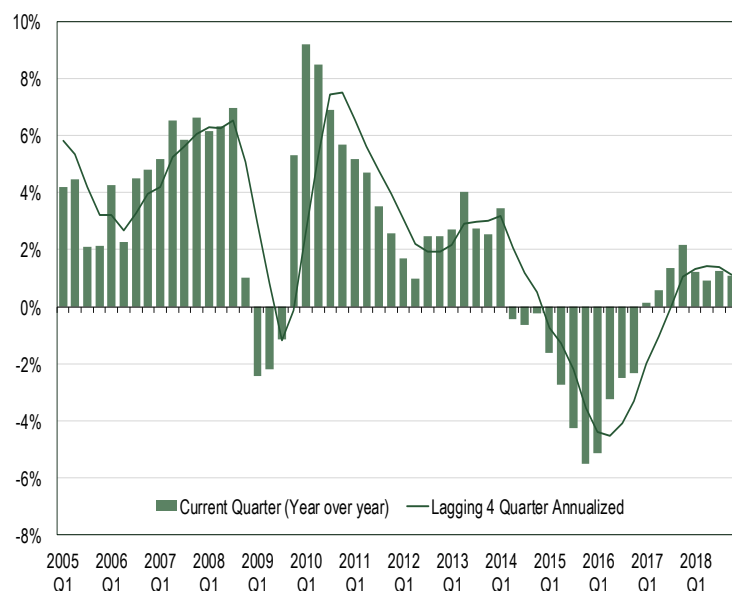


Source: Suzano, Bradesco BBI 6th Annual Brazil Investor Forum, April 2019

<sup>1</sup>Bloomberg, January, 2019 <sup>2</sup>Hawkins Wright Pulpwatch March 2019 <sup>3</sup>Suzano, Bradesco BBI 6th Annual Brazil Investor Forum, April

## Sluggish but Still Positive

Figure 1: Quarterly Brazil Real GDP (Percent)



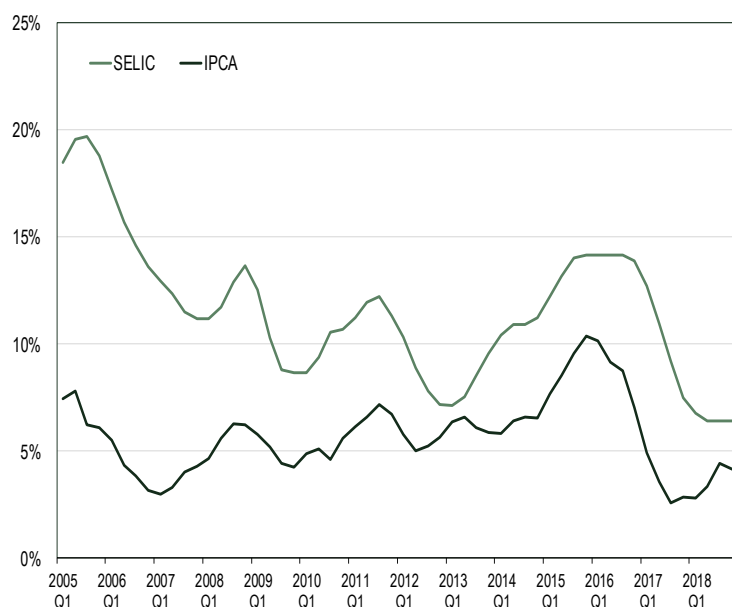
Sources: IBGE, Macrobond as of December 2018

Brazil's economic growth slowed marginally in the fourth quarter of 2018, advancing 1.1 percent year over year—down from a revised 1.3 percent third quarter, year over year—with a contraction in government spending in the fourth quarter contributing to the slow growth<sup>5</sup>.

<sup>5</sup>Trading Economics, <https://tradingeconomics.com/brazil/gdp-growth>

## Inflation Remains within Target Band while Borrowing Costs Still Historically Low

Figure 2: Quarterly Brazil Interest Rates and Inflation (Percent per year)



Sources: IBGE, Macrobond as of December 2018

Note: IPCA measures consumer price inflation. The SELIC rate is the benchmark overnight bank rate calculated from daily rates for a quarterly average

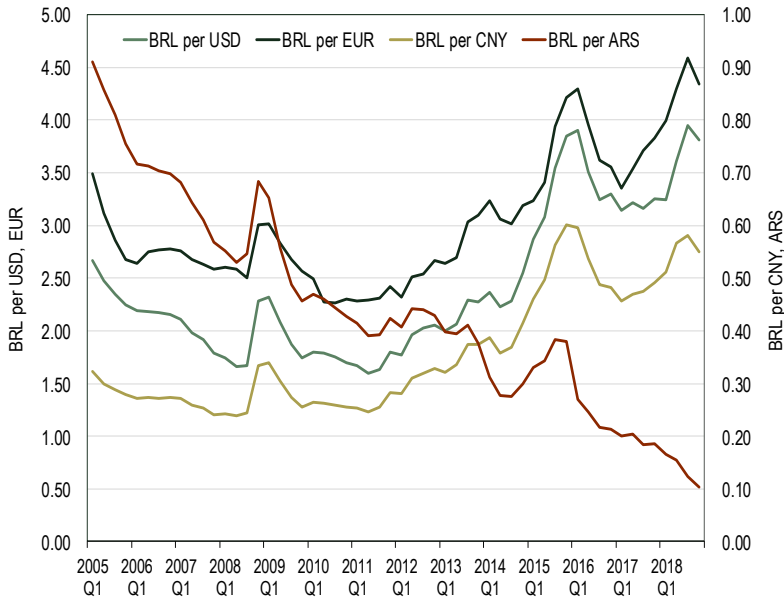
Consumer inflation, measured by the benchmark IPCA index, averaged 4.1 percent in the fourth quarter, a slight decline from third quarter's 4.4 percent. Averaging 3.75 percent for the year, inflation registered in the lower range of analysts' expectations and within the target band of 3.0 to 6.0 percent<sup>6</sup>.

At the Central Bank of Brazil's March 19–20 meeting, the Monetary Policy Committee (Comité de Política Monetária, COPOM) unanimously decided to hold the benchmark SELIC interest rate at its record low of 6.50 percent, where it has remained since the Central Bank put a pause on its long and aggressive easing cycle in March 2018<sup>6</sup>.

<sup>6</sup>The Brazilian Report, December 14, 2019, Focus Economics <https://www.focus-economics.com/country-indicator/brazil/inflation>

## BRL Strengthens Post-Election

Figure 3: Quarterly Brazil FX

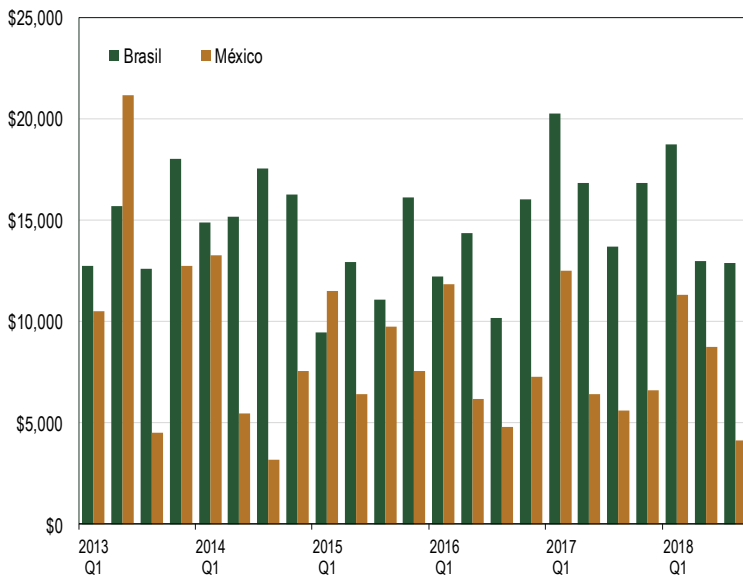


Source: Macrobond as of December 2018

The Brazilian real (BRL) strengthened in the fourth quarter following Brazil's national election, gaining greater momentum relative to these four currencies: the U.S. Dollar (USD), the Euro, the Chinese yuan (CNY) and Argentinean peso (ARS). But, the recovery of the BRL relative to the USD in the fourth quarter (3.6 percent) could not fully correct for the sharp drop it experienced in the third quarter, leaving the BRL at a 2018 final quarter average of 3.81 BRL/USD. From the third to the fourth quarter, the BRL's strengthening over the other three currencies was 5.1 percent against the CYN, 5.4 percent against the Euro and 17.2 percent against the ARS.

## Foreign Investment Steady

Figure 4: Quarterly Foreign Direct Investment – Net Capital Flows (USD Millions)



Source: OECD as of December 2018

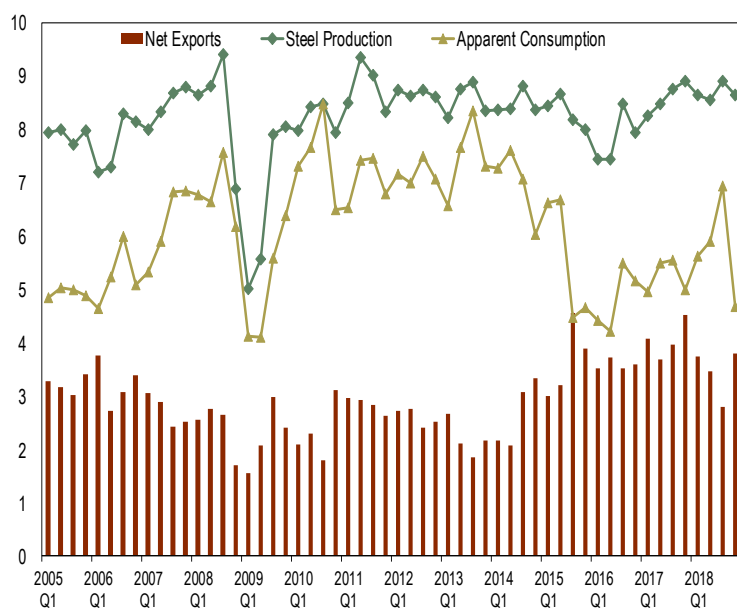
Note: FDI reports lag one quarter

Third-quarter foreign direct investment (FDI) into Brazil remained flat at the second-quarter level (USD 13 billion), but was close to 40 percent off 2017 first quarter highs. On the other hand, fourth quarter FDI in Brazil remained quite favorable compared to Mexico's.

Note: FDI reporting lags several quarters.

## Export Demand Supports Production, Despite Weak Domestic Consumption

Figure 5: Quarterly Brazil Steel Production, Exports and Domestic Production (Million MT)

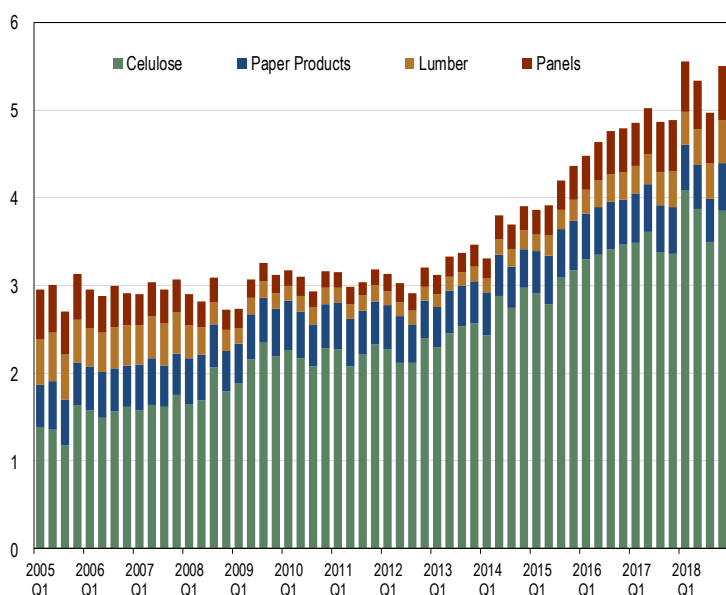


Sources: Brazil Ministry of Industry, Foreign Trade and Services, December 2018

Fourth-quarter Brazilian steel production of 8.6 million MT compares favorably with historical quarterly production of an average 8.2 million MT per quarter since 2005, but was down 3 percent from the fourth quarter last year. At 4.7 million MT in the fourth quarter, domestic steel consumption experienced a 6 percent drop from the same period last year, and a 33 percent drop from the previous quarter. However, with the United States the largest export market for Brazil's semi-finished steel products, a 36 percent increase in steel exports to 3.8 million MT partially compensated for the significant fall-off in domestic consumption.

## Forest Product Export Volumes Bounce Back

Figure 6: Quarterly Brazil Forest Product Exports (Million MT)

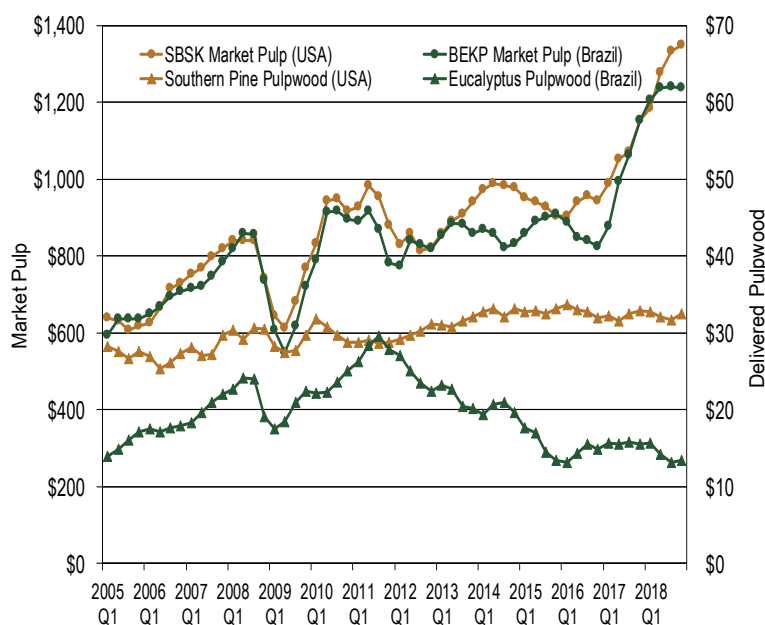


Sources: Brazil Ministry of Industry, Foreign Trade and Services, December 2018

Fourth-quarter Brazilian exports of forest products rose 11 percent compared with the third quarter, and were up 13 percent over the 2017 fourth quarter, with cellulose, lumber, panel and paper export volumes all increasing for the quarter. Lumber exports showed the largest gains, increasing over 20 percent from the third quarter and 20 percent year-over-year. Cellulose exports increased 10 percent from the previous quarter and were up 15 percent compared to the same period a year earlier.

## BEKP Market Pulp Prices Stall at Last Quarter's Level

Figure 7: Quarterly Prices for Market Pulp and Pulpwood (USD/MT)

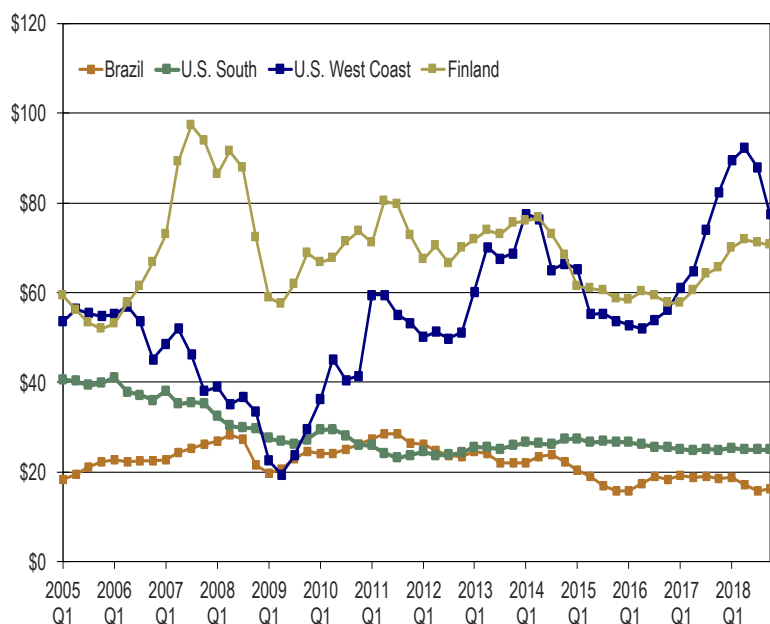


Sources: Hawkins Wright, STCP, and Timber Mart-South as of December 2018

Global pulp markets lost forward momentum in the final quarter of 2018, as China's overall economy and demand for pulp imports slowed. Global pulp inventories also bulked higher in the fourth quarter, adding to the downward pressure on pulp prices. The price of Brazilian Bleached Eucalyptus Kraft Pulp (BEKP) was flat in the fourth quarter, but despite the weaker pulp markets, the price of Brazilian Eucalyptus pulpwood on a USD basis, showed a modest up-tick, supported by the rebound in the Brazilian real.

## U.S. West Coast Sawtimber Prices Correct from Recent Highs

Figure 8: Quarterly Sawtimber Stumpage Prices for Timber (USD/m3)



Sources: STCP, Timber-Mart South, RISI as of December 2018

Reflecting a collapse in North American softwood lumber prices, U.S. West Coast softwood sawtimber prices continued to correct downward in the fourth quarter, dropping 12 percent from the previous quarter. Although the U.S. is an increasingly important export market for shipments of Brazilian Pine, sawtimber prices were relatively untouched by the weakness in North American lumber prices, even managing a small gain in USD terms, driven by the appreciation of the Brazilian real in the final quarter of the year.

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