



**Hancock
Asset
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Brasil**

A Manulife Asset Management Company

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Hancock Timberland Investor Brazil

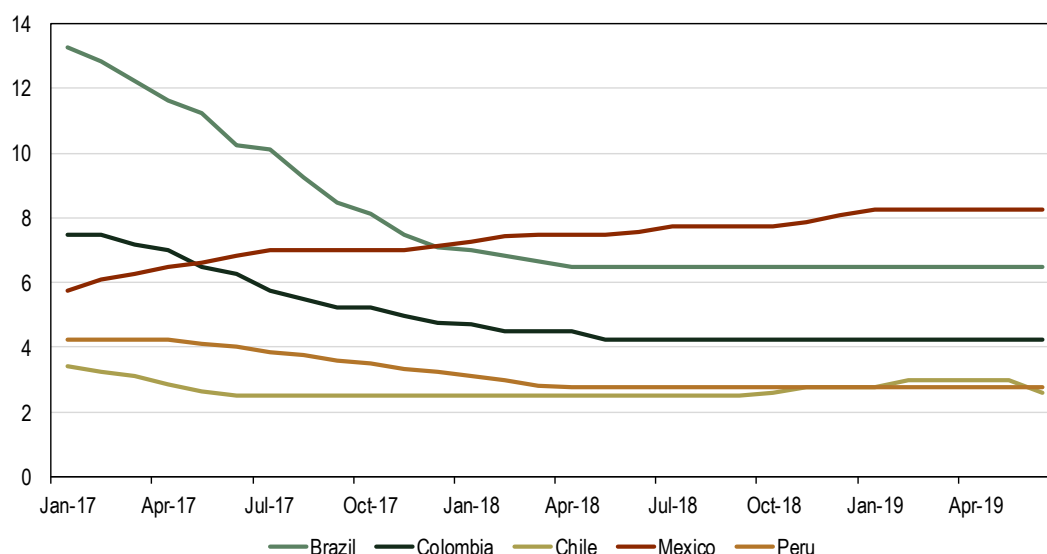
Over the past year, Brazil, along with other major Latin American countries, has seen extremely stable interest rates. Current economic weakness in Brazil in parallel with a slowing global economy, however, almost certainly spells impending interest rate cuts. Interest rates in Brazil have remained historically low at 6.5 percent since April 2018 – after multiple rate cuts in 2017 from double-digit highs. Brazil's current rate is competitive with other Latin American economies such as Colombia at 4.25 percent, Chile at 2.6 percent and Peru at 2.75 percent.

With Brazil's central bank scheduled to meet in late July, several factors indicate a rate cut could be in the cards. May industrial production fell by 0.2 percent month over month, with the most dramatic slowdown being the production of consumer goods, which is evidence household spending is starting to lose steam¹. May's contraction is the second industrial production setback this year, after March production lost ground by 1.4 percent month over month following the Brumadinho dam tragedy.

Brazil GDP ended a nine-quarter run of economic growth by contracting in the first quarter by -0.2 percent quarter over quarter, stoking fears of a slowdown and adding pressure on the Central Bank to prime the pump. A contributor to the economic outlook will be the progress of the pension reform bill, passed by the Chamber of Deputies of the National Congress of Brazil on July 10 and now awaiting a second vote by that chamber before heading to the Senate². Internationally, the ground is being set for global interest rates to ease in the coming months. The U.S. markets anticipate the Federal Reserve will implement a rate cut at its July meeting. Several Latin American countries, including Mexico and Chile, are expected to follow suit, easing credit conditions in the coming months.

Brazil Rate Cut Expected

Quarterly Interest Rates (Percent)



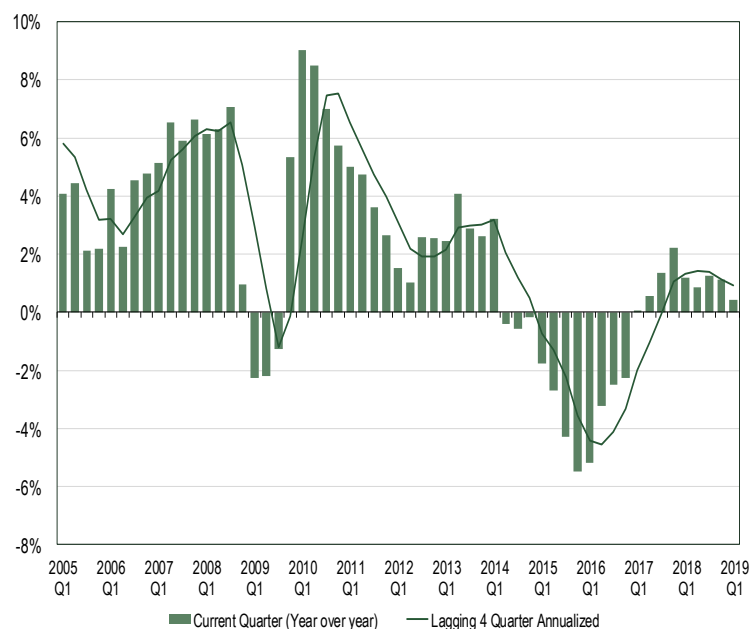
Source: Macrobond, June 2019

¹Capital Economics, Latin America Data Response, July 2, 2019

²Capital Economics, Latin America Economics Weekly, June 28, 2019

Sluggish but Still Positive

Figure 1: Quarterly Brazil Real GDP (Percent)



Sources: IBGE, Macrobond as of March 2019

Brazil's first-quarter GDP growth rate was 0.45 percent compared to the first quarter last year – 0.9 percent annualized growth over the past four quarters. First quarter economic growth contracted -0.2 percent from the previous quarter, bringing a halt to nine consecutive quarters of quarter-over-quarter growth. The Primary contributors to Brazil's weak first quarter economic performance was sluggish industrial production related to curtailed mining activity as a result of the tailings dam accident and some uncertainty about the progress of pension reform as it moves through the legislature.

With Inflation Flat, Borrowing Costs Remain Historically Low

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



Sources: IBGE, Macrobond as of March 2019

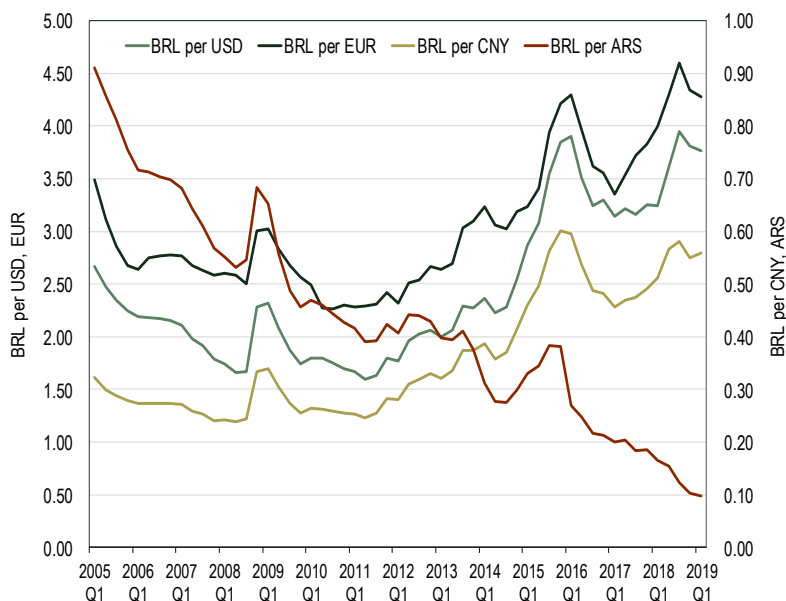
Note: IPCA measures consumer price inflation. The SELIC rate is the benchmark overnight bank rate calculated from daily rates for a quarterly average

In March, Brazil's annual inflation rate was the same as the previous quarter – 4.1 percent. Early June data suggests inflation is easing and second-quarter inflation may fall below the central bank's target rate of 4.25 percent for the year³. June inflation is expected to decline compared to the same month a year ago, since last May and June's supply chain disruptions related to the trucker strike drove a temporary upward tick in inflationary pressures. Interest rates remain at historically low levels – 6.5 percent through the first quarter of 2019. However we believe a number of factors will likely be critical to further reductions in the coming months: the Brazilian economy showing signs of distress; pension reform legislation advancing; the global economy slowing; and the U.S. Federal Reserve expected to lower the Fed Fund rate in July.

³Capital Economics, Latin America data Response July 10, 2019

Brazilian Real Mixed

Figure 3: Quarterly Brazil FX

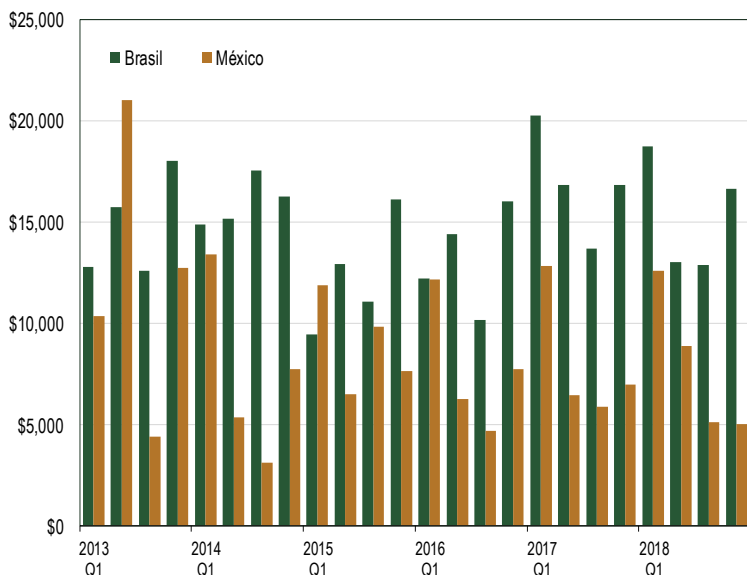


Source: Macrobond as of March 2019

The BRL made slight first-quarter gains against the USD (-1 percent), reflecting post-election optimism regarding the outlook for the Brazilian economy. The BRL strengthened against the Argentinean peso (-6 percent) and the Euro (-1 percent) but weakened slightly against the Chinese renminbi (1 percent), with the U.S.-China trade conflict impacting the Chinese currency's strength against the USD.

Renewed Foreign Investment

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



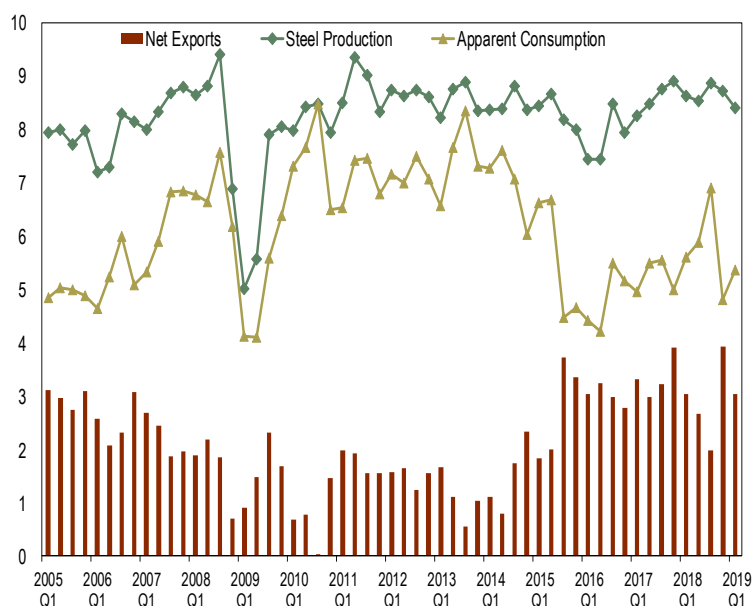
Source: OECD as of March 2019
Note: FDI reports lag one quarter

Foreign direct investment (FDI) in Brazil strengthened in the final quarter of 2018 to USD 16.6 billion, up 30 percent from the previous quarter, though 18 percent below the cyclical peak of USD 20.2 billion achieved in the first quarter of 2017. Total FDI net flows over the 12 months to December 2018 accounted for 4.7 percent of GDP, the highest contribution since June 2001 according to Brazil's Central Bank⁴. While lingering economic uncertainty is a negative factor, the country's sheer size gives it a huge advantage as a destination for FDI.

⁴<https://www.reuters.com/article/us-brazil-economy-current-account/brazil-current-account-deficit-doubles-fdi-inflows-rise-in-2018-idUSKCN1PM1JZ>

Steel Production Declines for Second Consecutive Quarter

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

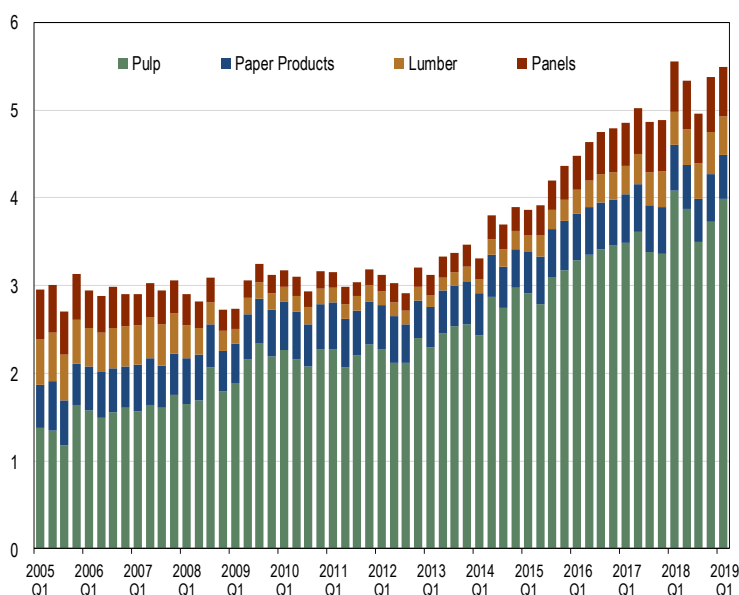


Sources: Brazil Ministry of Industry, Foreign Trade and Services, March 2019

Steel production contracted, again, from 8.7 million metric tons in the fourth quarter to 8.4 million metric tons in the first quarter and was down 3 percent or 240 thousand metric tons compared to the first quarter of 2018. This first quarter decrease is the second consecutive quarter of production declines, with steel net exports falling 23 percent from the high level achieved in the final quarter of 2018. At the same time, Brazilian steel demand, measured by estimated consumption, rose 12 percent from last quarter's low levels.

Pulp Export Volumes Move Higher

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



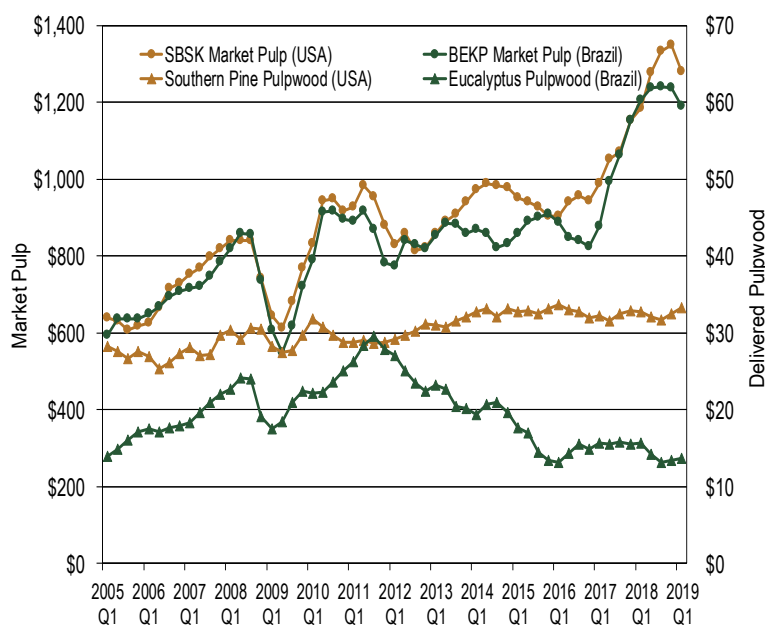
Sources: Brazil Ministry of Industry, Foreign Trade and Services, March 2019

In the forest product sector, Brazil exported 5.49 million metric tons in the first quarter of 2019, a 2-percent rise in total forest product exports from fourth quarter 2018, though a 1-percent dip from the record-high volume in the first quarter a year ago. Brazil's chief forest product is pulp, and despite weaker global demand for market pulp, as well as declining prices for eucalyptus market pulp in China, Brazil pulp export volumes rose 7 percent this quarter over the previous quarter. But while pulp export volumes during the month of March reached new highs⁵, wood panel, lumber and paper product export volumes were down first quarter, falling almost 10 percent from volume levels shipped in the last quarter of 2018. At the same time, first quarter lumber exports rose 17 percent this year above lumber exports in the first quarter of 2018.

⁵Pulpwatch, Volume 25 No. 10. May 3, 2019

Brazil Market Pulp Prices Turn Lower after Historic Run Up

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

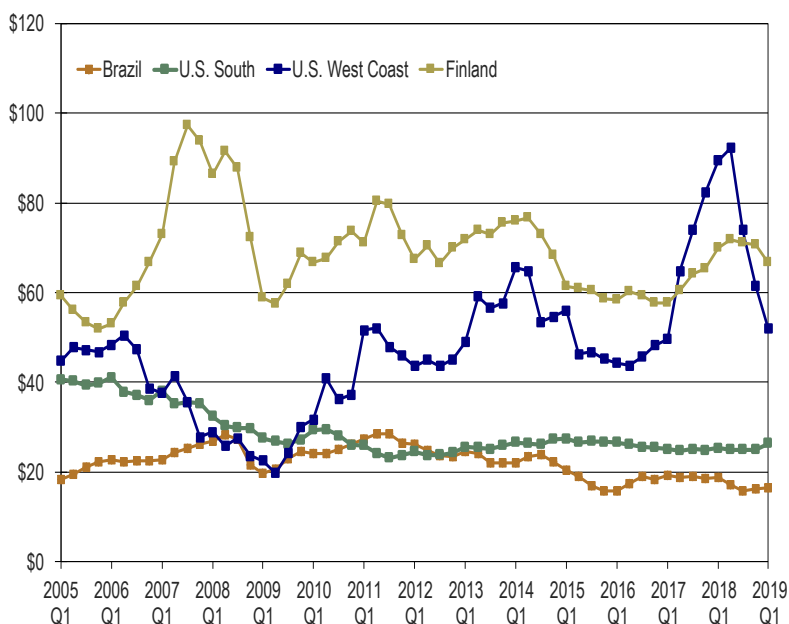


Sources: Hawkins Wright, STCP, and Timber Mart-South as of March 2019

Prices for Bleached Eucalyptus Kraft Pulp (BEKP) and Southern Bleached Softwood Kraft (SBSK) turned lower in the first quarter of 2019. BEKP USD prices were down 4 percent compared to the previous quarter and SBSK USD prices slipped 5 percent for the same time period. China imported record volumes of pulp over the past year, and this has swelled inventories and generated oversupply. Pine pulpwood delivered prices in the U.S. South rose 3 percent in USD over the previous quarter, largely due to the pervasive wet weather this past winter and spring, which restricted harvesting and in turn constrained supply. First-quarter gains in pulpwood prices in the U.S. South are nonetheless vulnerable, since southern pulp mills can access ample fiber supplies by tapping into the burgeoning production of manufacturing residuals generated by the region's lumber mills. In the case of Brazilian eucalyptus pulpwood, delivered prices moved up 2 percent in USD from the previous quarter.

Sawtimber Prices Lower Globally

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



Sources: STCP, Timber-Mart South, RISI as of March 2019

First quarter Brazilian pine sawtimber USD prices rose 2 percent from the previous quarter, though were down 13 percent from the first quarter last year. Measured in local currency (BRL), Brazilian pine sawtimber prices were flat first quarter⁶. U.S. West Coast prices for softwood sawtimber continued to fall from the record highs reached in the second quarter of 2018, plummeting 42 percent year-over-year in the first quarter of 2019. The price of southern pine sawtimber in the U.S. South rose by USD 1 per cubic meter (5 percent) in the first quarter over fourth quarter prices – an increase not seen since the first quarter of 2013. Extensive wet weather in the U.S. South hampered the region's harvesting activity, which lifted prices. Finnish softwood sawtimber prices moved lower again first quarter, falling USD 4 per cubic meter (6 percent) from last quarter as storm-damaged timber salvage continues to depress prices⁷.

⁶STCP Wood Price Outlook Jan/Feb 2019 and March/April 2019

⁷Wood Resources Quarterly, 1Q 2019

Disclosures

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