

# Commstock Report

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I spent a week traveling through much of Brazil's premiere farmland regions. Despite having a very good season, there still seems to be a lot of farmers looking for more debt capital. The farms are big, and so the demand for ag loans continue to increase consuming their liquidity. It was apparent to me on this trip that many of the farms that grew aggressively in the past decade, are now suffering from excessive debt. Several large farmers have filed for the equivalent of Chapter 11. Others tried to file for bankruptcy but were not granted approval because despite unhealthy debt levels, their equity was still greater than the debt. The farms that took a more conservative approach to growth, appear to be doing very well. What this means is, that while prices remain very favorable in Brazil, if they were to ever turn south, you would quickly find out who is doing well and who is faking it. Everyone appears to be wearing a bathing suit until the tide goes out.

The Brazilian mentality towards debt seems to be different than in the US. When grain prices boomed in 2007, there was a feeling of euphoria in Brazil. Farmers wanted to grow. Banks were giving them money because times were good. But eventually you have to pay that money back. The impression I get is most of those farmers really didn't think about that part. They were so concerned with buying the next farm, that they didn't do much cash flow planning on when and how they are going to pay it back. To be honest, it was almost as if they were planning on filing for Chapter 11 if it came down to it, so they could renegotiate their debts. Because in the end, they would still keep the farm. Many of them refuse to sell a farm to pay their debts. Preferring to enter Chapter 11 where they can then "renegotiate" their debts into something more manageable. I suppose you could almost compare it to the real estate crises in 2008. Home buyers took the lines of credit with no money down because they were offered it. However, the difference being, they had to give the home back when it was foreclosed on. Farm foreclosure is much more difficult to come by in Brazil.

I also noticed more Chinese names on the side of grain elevators than I did before. Obviously the Chinese buy US grain (or used to), but they don't necessarily set up shop in the Midwest. Or at least I don't see any Chinese symbols hanging next to the grain elevators around us. They appear to have a different strategy in Brazil where they openly buy and manage grain trading companies in the frontier farming regions. I am told their objective is not to buy and trade grain for profit, but to secure the origination of the product to bring home for food. I am not saying this is a direct result of the trade wars as one might suspect. But it does show that the Chinese are strategically positioning themselves to purchase more soybeans from Brazil.

Two important events happened while I was in Brazil. The first being the Brazilian federal police arrested former President Temer for bribery and corruption. This is the second of 7 Presidents to be jailed since Brazil began a democratic republic in the 80's. I expect there will be a third. Not exactly a great track record. I noticed that Brazilians are breathing a sigh of relief as the new Bolsonaro administration has taken over. I was told that if change was not made, Brazil would have followed Venezuela down the rabbit hole. Brazilians are now more optimistic about their future and they should be. The new President has been quick to make changes. I am told that the road from Mato Grosso to the northern port of Santarem only has 30 miles left before it is completely asphalted. That will mark a historical occasion worth celebrating.

The second thing that has happened, is that Brazil is expected to set another record for soybean exports. February was a record with 6 MMT. March is not done yet, but analysts believe it could reach 9 MMT. Their grain exports are on a strong upward trajectory and they know it. It is raining a lot now in Brazil, in

some cases too much. My brother-in-law has begun their harvest in Minas Gerais. While the yields are better than expected, the seed quality has been compromised from all of the rain. Since they raise seed beans, they pay as much attention to the germination quality as they do the yields.

The crops looked good overall. The soybeans in Mato Grosso had been harvested already, but the second crop of corn was on its way. Farmers complained of too much rain on the corn as opposed to too little. Field damage from rain was visible from the road as you could see some ponding and yellowing. But you also saw fields that looked excellent. Overall, analysts are calling for a good crop, some analysts expecting the second crop of corn to reach as much as 70 MMT.

It seemed that I saw a lot more cotton planted this year than in recent years. The cotton area is expected to increase dramatically in Brazil. Prices have been more favorable than corn. Last year saw cotton prices reach almost U\$1 per lb. Many farmers sold ahead three years out to take advantage of those prices. They now have really good cotton prices for a few years. They should make good money on this if they can produce well.

With more cotton area comes more infrastructure. I was shown the largest cotton gin under construction in South America. It is very close to the new corn ethanol plants being constructed. If you have read my prior reports, I have discussed how corn ethanol is taking off in Brazil. Brazil represents the largest destination for US ethanol exports. I wonder how much longer that will last. Hopefully the ethanol industry has a plan for that. If it were up to the oil industry, it would be the other way around where in ten years, the US would represent the largest destination for ethanol exports from Brazil.