

Timberland Market Update

Global Consulting Alliance

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Economic Developments

The COVID-19 pandemic has had an unprecedented impact on the world since the start of 2020. Being compared to the Great Depression, slated as being more destructive than the 2008 financial crash and defined as a once in a century event, the pandemic continues to inflict severe social and economic harm around the world. In its latest forecast, the IMF expects the global economy to contract sharply by 3% in 2020, with many countries seeing negative GDP growth projected for at least 2020. Global economic contraction is a reality and no country or region had been spared:

- The Euro area, according to the latest Economic Forecast issued by the European Commission, is expected to contract by a record 7.8% in 2020 and grow by 6.3% in 2021. For the UK, the Government is expecting a contraction of 5.8% in 2020 and growth of 4.1% in 2021.
- In the US, forecasters are now projecting a contraction in the range of -5.5% to -6.5% for the year 2020, predictions for recovery in 2021 range between 2.8% to a much more optimistic 6.3%.
- South American countries saw growth forecasts plunge between January and May 2020 (YEE) with Brazil and Uruguay expecting reductions from 2.3% to -6.0% and 1.7% to -3.0%, respectively. Sharp devaluation of the BRL (-40%) and UYU (-15.0%) currencies has helped to support exports.
- In the Asia-Pacific region, Australia's economic growth is expected to decline -4.7%, being Australia's first recession in 29 years. A partial rebound is expected in 2021 but it could take the remainder of the decade to return to GDP levels forecast prior to the onset of the pandemic. In New Zealand, the May Consensus Economics forecasts predicted -7% GDP growth for 2020 bouncing back to 5% in 2021.
- The IMF expects Asia's economic growth to come to a near halt for the first time in 60 years with growth in China and India decelerating to about 1.2% and 1.9%, respectively. China's economy is expected to see a rebound in activity later this year, with growth to bounce back to 9.2% in 2021. Real GDP in Japan is expected to decline by 5.2%, based on IMF forecasts.
- The World Bank's African Pulse Report of April 2020 reported adjusted growth forecasts for Sub-Saharan Africa of between -2.1 and -5.1% in 2020, resulting in the first regional recession in 25 years.

While global GDP growth is projected to recover in 2021 to 5.8% (Baseline Scenario), the IMF warns that the risk of a more severe outcome is substantial. For now, uncertainty reigns and the global forest industry, already affected by a slow downturn in the pulpwood market before COVID-19, must cope with reduced growth as well as the closure of international borders, domestic restrictions and demand shifts.

Asia-Pacific

- Lock down restrictions facing the Chinese industry in Q1 led to a large increase in port stocks peaking on 30 March at nearly 7.1 million m³. As China reopened again from early April, industry offtake exceeded imports (mainly due to the cessation of NZ supply due to the NZ COVID-19 lock-down) reducing log stocks to a more manageable level of 5.3 million m³ by the end of April. Log prices also rapidly increased from a low of USD105/JAS CFR for A grade to around USD128-130/JAS CFR by early May although this remains

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volatile. Exporters are also benefiting from low exchange rates and very low shipping costs (well below USD20/JAS). There is an increasing risk that as suppliers respond to these high price signals, a potential oversupply situation may evolve again in the next few months. This could cause problematic oscillations in volumes and prices for at least the balance of 2020.

- Chinese total imports of hardwood woodchip in Q1 2020 relative to Q1 2019 increased by 28.6%. At the individual country level, China's imports of hardwood chip from Australia increased by 9.7%, Vietnam by 48.7% and Chile by 25.2%. China's imports from South Africa dropped by 55.1%.
- Japan's total imports of hardwood woodchip declined by 14.9% from Q1 2019 to Q1 2020. At the individual country level, Japan's imports from Australia declined by 38.4% and South Africa by 34.4%. Japan's imports from Vietnam increased by 7.4% and from Chile by 11.9%.
- Australia's chip export prices reached USD182/BDMt FOB in 2019 but are declining in 2020. Price negotiations are protracted as both sellers and buyers try to factor in the impact of the COVID-19 pandemic. Pulp demand for tissue continues to grow in volume although Japanese tissue export prices have been declining over the last ~3 years, trending towards Chinese export prices. Uncoated paper prices are trading flat, but Chinese export volumes are seeing a sharp decline.
- During the 3rd week of March 2020, Australia's national cabinet announced the closure of all non-essential business and other social restrictions to curtail the spread of COVID-19. While there is a gradual re-opening of the Australian economy, unemployment is expected to increase to 8.1% by the end of CY 2020. The construction sector accounts for ~9% of all jobs in Australia and it is possible dwelling unit commencements (DUC) may drop as low as 116 000 during FY 2020/21. DUC peaked in FY 2015/16 at ~233 000. There is considerable conjecture around this outlook for DUC and various state-governments are likely to intervene to stimulate this sector through the construction of social housing and other projects.
- Anecdotal evidence suggests mixed signals from Australia's sawmilling sector during Q1 2020 with some slowdown in the frame and truss market segment reported but also an uptick in retail related to DIY projects during the period of social isolation.
- China's imports of Australian softwood logs declined from 846 113 GMt in Q1 2019 to 709 012 GMt in Q1 2020 (16.2% drop).
- The Resource Management Service, LLC (RMS) sold its ~21 000 ha *Eucalyptus nitens* plantation in Tasmania Australia to Global Forest Partners. Anecdotal evidence suggests a purchase price of AUD175-185 million
- In early 2020 Norske Skog sold its 18 000 ha radiata pine softwood plantation in Tasmania to New Forests at a disclosed price of AUD62.6 million.
- The strict lock down regulation followed in New Zealand from 25 March had a severe effect on the forestry industry, with operations stalled for 5 weeks coming on top of the earlier lockdown in the China market during February and March. A total constrained period of nearly 3 months with NZ unable to benefit from the restarting of the Chinese economy during April allowed competitors to gain market share that will take time to recover.
- Construction restarted from 28 April and the recovery budget includes a massive boost for public housing. The NZ government is also moving to adopt its election policy of wood first in public building construction. Although market expectations were for a significant reduction in house prices brought on by the crisis, this has yet to happen with a minor price uptick when sales resumed. The forest industry is also receiving somewhat of a shakeup with a rampaging Minister of Forestry introducing ill-conceived legislation under urgency to force all log traders and forestry advisors to become government registered and ultimately under the minister's control. Although this is portrayed as supporting the industries growth, the true purpose is to restrict log traders and forest owner's flexibility to export logs in favour of domestic processors. This is proving divisive for the industry with support coming from some processor

organisations and opposition from forest owner associations. Submissions on the legislation closed on 21 May.

- As a result of COVID-19, NZ pine exports to China decreased 10.3% to 3.33 million m³ in Q1 2020, compared to 3.71 million m³ in Q1 2019. Germany was the major gainer, up 266% to 1.4 million m³. Significant losers included; Australia down 15.3% from 0.83 million m³ to 0.71 million m³; USA down 29.2% from 0.71 million m³ to 0.50 million m³; Canada down 71.6% from 0.65 million m³ to 0.18 million m³; and Russia down 42.1% from 2.10 million m³ to 1.22 million m³. The warmer winter restricting forest access due to potential permafrost damage has been a major reason for the large decline in Russia's log exports to China. China's total imports for the quarter were down 9.3%, a surprisingly small affect from the nationwide lockdown in February/March. The large increase in European softwood logs exports from sanitary felling of dead and dying spruce forest resulted in a total of over 2.4 million m³ of imports for the quarter. Reports indicate that damage to European forests is accelerating with high pest counts and a dry summer predicted exacerbating the problems.
- CHH New Zealand decided to close its Whangārei sawmill in early April. The mill had a production capacity of ~210 000 m³/a. In May, CHH also announced that it will reduce its laminated veneer lumber (LVL) production at Marsden Point by about 2/3rds, now focusing on the domestic market only.

Europe

- Since March, pulp demand has increased significantly in Europe. According to a report published by Trade Tree, on March 30th, the consumption of tissue paper, the largest end use of bleached pulp, has increased by 5% since the beginning of 2020 due to the pandemic. The demand for absorbent hygiene products has been boosted by increased home use of diapers, wipes and other disposable hygiene products. As a result, Nordic pulp mills are operating at full capacity and maintenance stoppages have been postponed to autumn.
- The supply of BSKP was somewhat restricted by a strike in Finland and by the closure of a Canadian mill due to environmental issues. Some Nordic producers tried to push up prices earlier this year but the NBSKP prices has so far remained stable.
- The impact of the coronavirus on the packaging industry has been mixed. The crisis has led to some of the sharpest declines in recent times in demand for certain types of packaging while accelerating growth for others, i.e. boosting packaging for e-commerce shipments, groceries and healthcare products, which are largely based on wood fibre-based raw-materials.
- The European printing and writing paper markets have been negatively affected by the crisis. A handful of mills serving mainly the European markets directly or indirectly are suffering from weakening demand and have taken downtime to balance supply. For the time being, no dramatic drop in paper prices has occurred but the delivery volumes are critically low. There is a strong fear within the industry that the pandemic will cause a permanent shift in demand.
- The recovery of the sawmilling sector, which started last autumn was partially stopped in January 2020 because of tough measures in China to prevent the spread of COVID-19. The furniture industry in China is still suffering from COVID-19 due to slow market demand and dysfunctions in the logistics chain. China Q1 2020 furniture exports dropped by 84% year-over-year. Sawnwood prices in Europe are still under pressure due to abundant supply of sawnwood produced from bark beetle damaged trees in Central Europe.
- Recent reports from Central Europe suggests that a combination of windstorms, drought and spruce bark beetle damage has impacted more than 270 million m³ of standing timber between 2017 and 2019. After

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a mild winter and dry spring, bark beetle infestation numbers are expected to be very high during 2020 and will extend any salvage efforts well in to 2021 and beyond and continue to depress sawlog prices.

- The export of Central European logs to China from drought and bark beetle damage has continued during the 1st quarter of 2020, recording strong growth in the first two months of the year, despite disruptions to most supply chains. A drop in log exports of 25% was however observed in March 2020 compared with the same period last year.
- Sawnwood recovery will depend on government actions in Europe. If economic recovery is boosted by infrastructure investments the demand of sawnwood and plywood will recover faster. Without this capital injection, recovery in this sector will be slower than pulp, packaging and hygiene paper sectors. A full recovery of the sector may take several years. It is expected that sawnwood prices will still decrease and reach a bottom that is 15-20% lower than current prices.
- In April, the IHS Markit Eurozone Construction Purchasing Managers' Index or PMI fell to a record low, following already weakened figures from March 2020. Some of the most impacted countries in Europe are Italy and France in terms of construction output. This is mainly due to falling demand affected by lockdowns measures, stricter restrictions, and measures on business operations to protect worker health and supply chain issues disrupting raw material supply.
- The European Commission, 'Views on Construction – 2020 and beyond', stakeholder report identified energy efficiency and decarbonising the economy as one of its key priorities. This could greatly help wood as an environmentally friendly material as the EU transitions to greener buildings and more sustainable cities. There is a strong call from the European Sawmilling Industry for policies aimed at increasing the consumption and the use of wood.

North America

- American pulpwood remains stable as demand from tissue and hygiene products and fluff pulp sectors continues to be adequate. U.S. log and lumber exports have declined a modest 7% year-over-year to 143 MMBF, as demand from China weakened, but stronger demand from the Caribbean helped to stem losses. Pacific Northwest Douglas-fir log prices have been volatile and in March 2020 were down as much as 20% from their earlier Q1 2020 price of \$700-750/MBF. Export markets, primarily to China, have served as a floor for west coast prices. Increased competition from New Zealand resuming trade with China is expected to cause some volatility in log markets.
- Softwood mill curtailments in Q2 2020 have prevented price collapses by aligning supply with declining demand in markets. Higher sales to big box stores such as Home Depot have somewhat offset declining demand from the construction industry. Demand on lumber mills is projected to contract by more than 15% in Q2 and Q3 of 2020, and 10% in Q4. Logging hours have been reduced and shifted towards thinnings for pulpwood. Lumber and OSB prices and demand are expected to see significant declines in 2020 but rebound by the first half of 2021 as the housing forecast remains optimistic further out. One large TIMO has seen average U.S. South price declines around 10% for pine sawtimber and chip n' saw.
- Hardwood sawmill production from Eastern U.S. Hardwoods fell from 7.6 Bbf annually in 2019 to around 6 Bbf annually in April of 2020. January 2020 annual production rate was about 8 Bbf. Demand for exports to China and increased production of ties stand in contrast to an otherwise low-demand export and domestic lumber market caused by the pandemic's effect on the housing market, manufacturing, and industrial hardwood consumption.
- Demand for residuals, chips and roundwood is very low, with several pulp and paper factories halting purchases for 30 days or longer. Structural changes to the hardwood pulpwood industry are being

compounded and accelerated by the coronavirus, affecting prospects for this market's recovery. Unfinished Oak strip flooring shipments, the most impacted category of solid wood flooring, are down 50-65% below normal. Framestock, cants and board road producers have seen mostly poor demand and lowered prices on the low end of their ranges except for those supplying food distributors and the natural gas industry. Demand for grade lumber has decreased for most domestic markets and many export markets as the coronavirus suspends manufacturing and discretionary purchases by consumers have declined.

- Demand from China is returning since the timeline of the pandemic has allowed for manufacturing to resume earlier. Domestic, global and manufacturing centres that use U.S. hardwoods, such as Vietnam, are not ready to fully resume manufacturing yet. The speed of and the extent of recovery of grade lumber depends on how well economies perform in dealing with this crisis and how much spending capacity consumers have. In past economic recoveries, consumers have spent more money on the interior of their homes, which translates to higher hardwood demand
- U.S. Timberland transactions in the past 2 months have varied, with some moving ahead as planned, and others being cancelled or delaying closing to reorganize financing. Write-downs on appraisals are expected to be minor in Q2 2020, ranging from 1-4%. No distressed sales of quality timberland have been observed, meaning that small downward adjustments can be attributed to declines in timber markets. As an asset class, timberland remains attractive as a lower volatility diversifier. In the South, timberland managers are reacting to lower demand for sawtimber by doing more thinnings and less clearcutting. This practice yields more pulpwood for the select pulp and paper sectors where demand is higher and avoids the cost of site preparation and replanting. In the Pacific Northwest, managers are delaying or pulling sales off the market where local demand is down due to mill curtailments. Maintenance costs are also being deferred where possible.

South America

BRAZIL

- Similar to the trend in Europe, Brazilian pulp mills saw a significant increase in tissue and packaging paper consumption; along with a drop in printing and writing paper consumption. Additionally, the sharp devaluation of the BRL currency against the dollar (-40%) impacted the revenues positively but had a negative effect on those companies with high debts in USD. In the short term, companies expect a slight increase in demand and price, as they are facing a historic low since early 2019.
- Most companies in the composite panel industry have cut production drastically, closing most of their mills, because domestic consumption dropped around 80%. Although the companies are slowly resuming their operations, expectations for the second half of 2020 are negative.
- The charcoal Industry, against all expectations, has not been negatively impacted by the COVID-19 crisis yet. The remarkable recent export increase of pig iron to China by 20% of the industrial capacity, offset the plunge in domestic consumption caused by the sharp slowdown of the construction, automotive, and white line sectors.
- Within the lumber industry, companies producing wood for moulding, pallets, and food packages have performed well, and have a positive short-term expectation. In contrast, companies supplying the furniture and construction segments have faced a significant setback in Q2 2020, with prices declining by 10% to 15%. Furthermore, even with an external buyer-market and a favourable exchange rate, big sawmills are unable to produce because they have no destination for their chip production as the composite panel industry is halted.

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- In the plywood industry leading companies have implemented mandatory vacations in Q2 2020 as a strategy to address the steep decline in demand, with an export price drop ranging from 10% to 25%. As to the second half of 2020, a feeling of uncertainty and volatility predominate, and companies have no confidence in making market forecasts. However, it is expected that the exchange rate will continue to minimise possible declines in consumption and prices in the international market.
- The current crisis had a slight impact on Pine wood prices, specifically pulp and veneer logs (-5% to -10%) but has not affected sawlog prices. Eucalypt wood prices remains steady because of good performance in the pulp and pig iron industries.

URUGUAY

- During May, UPM finalized pending items with the new Government of Uruguay, allowing its growth project in the Centre region of Uruguay to proceed according to plan.
- Both the UPM1 and Montes del Plata (MdP) pulp mills continue to operate at full capacity despite the recent pulp price cycle. Both pulp mills continue to drive demand for eucalypt pulp logs from all Uruguayan regions, even though local foresters report a decrease in stumpage prices.
- The first wood chip exports of 2020 indicated a decrease in FOB price close to 10 USD per BDMT. As of May 2020, only 6 vessels were exported from Montevideo port, showing a large decrease of woodchips exports compared with 2019. The expectation for the second half of 2020 is also negative.
- Saw log exports to China increased during the last 3 months. As of mid-May, three vessels were exported to India and seven to China. FOB prices dropped ~10% between 2019 and 2020. Even though more pine logs vessels will be loaded during the next months, the expectation for the second half of 2020 is not so positive, based on concerns regarding China's demand. Uruguay's eucalypt saw logs exports continued during Q1 2020 with similar volumes as 2019 and stable prices.

Africa

- The South African construction sector has come to a standstill due to lock down restrictions aimed at reducing the spread of the COVID-19 virus. This has had a devastating effect on sawmills supplying structural timber, with most of these mills remaining closed.
- South African wood chip exports remained flat between January and March 2020 with an average volume of 140 000 tonnes per month exported mainly to Japan. In the same period pulp exports have declined from 93 000 to 79 000 tonnes per month.
- Tropical timber production in West Africa has been hampered by a lack of markets and strict lock down rules enforced by governments in countries such as Cameroon, DRC, Republic of the Congo and Equatorial Guinea, that brought production to a standstill. Buyers have also asked to delay orders or cancelled orders and in some instances, orders are stuck at portside or warehouses. Companies in Ghana report difficulty in implementing COVID-19 control measures related to protective equipment and social distancing.
- In East Africa, the market for transmission poles remains active, driven by domestic electrification programmes. The closure of borders between countries have, however, had a negative effect on the flow of timber between countries such as Tanzania, Kenya and Uganda. In Tanzania sawn timber prices have decreased as demand from private construction projects dropped. Government led construction projects are still ongoing offering opportunities for construction timber. Large construction projects in

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Kenya have stagnated and furniture demand has dropped off by 40 to 60%.

- Some of the major veneer peeling plants in Tanzania had to stop exports to China and are continuing at a reduced level to meet domestic demand. Exports of plywood to regional markets such as Zambia, Kenya, Rwanda and Burundi were reduced due to cross border trading restrictions. The situation worsened in May when Zambia's borders were closed followed by Kenyan border closings.
- Mozambique seems to have benefitted from the border lock down with South Africa, leading to improved domestic timber demand, although with limited timber supply and labour restrictions in place.

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