



FORESTRY MARKET REPORT

Key Points

- Still steady locally
- Stabilisation after a big fall at the wharfgate
- Drop unlikely to be repeated
- NZ log exports to India bounce around again

S1 DOMESTIC LOGS (NZ\$/TONNE)	A-GRADE EXPORT LOGS (US\$/JAS (CFR))	SHIPPING – CHINA (US\$/JAS)	CARBON (NZ\$/NZU)	USD:NZD
137	133	29.5	25.1	0.657



VIEWPOINT

Just a bump in the road?



Reece Brick

The Chinese log market has again dominated talk in the NZ forestry industry amid its sudden depreciation these past two months. Purely from a data perspective August and early September don't make for pretty reading. In-market rates on unpruned logs tanked by a level unheard of since the first half of 2015, with the volatility even more exaggerated for pruned logs.

In spite of this fall market sentiment has stayed quite positive, as just a single factor, the CNY:USD rate, has accounted for all or close to all of the weakness. After free-falling by 7% in the two months to mid-August, the exchange rate has managed to stabilise for a period of four weeks at the time of writing. Factors such as port-level inventories, offtake rates and shipping rates otherwise point towards healthy fundamentals for NZ log trading in China. Consensus among the majority of traders is that we've settled at the bottom of the market for at least the time being, and some are even preparing for a firming unpruned log market from October. A recovery for pruned logs is looking less likely.

“...just a single factor, the CNY:USD rate, has accounted for all or close to all of the weakness.”



Sam Laurenson

What the future looks like will largely be dictated by the actions of the Trump administration. The latest round of 10% tariffs covering \$200b of Chinese products is yet to be felt within the log industry. The main headache, however, is that there's no end in sight for the trade war. It's expected the latest tariffs will be lifted to 25% by Christmas, while Trump has threatened to extend these tariffs to another \$267b worth of Chinese products. Given log demand is so closely tied to economic growth, we can only hope these two power-houses can settle their differences sooner rather than later. Just don't count on it.

NEW ZEALAND DOMESTIC MARKET

Sideways path set for Q4

All the volatility beyond NZ's shores has essentially evaded sales into local mills. For the most part log values tracked sideways with the odd reduction here and there. Many trades were locked onto Q3 contracts though. The standard range for structural (S1) logs in the North Island was \$130-\$143/t, whereas the South Island was covered by \$123-\$135/t.

The impact of the subdued wharfgate market has varied from region-to-region. Mills in parts of the South Island in particular have found relief from logs being diverted away from export markets, however any reductions in pricing were small. Not all the increased supply is market related though, with better weather conditions adding to log availability through improved harvesting rates.

Local mills have contended with mixed market conditions for timber in recent weeks. There's yet to be a proper revival in NZ construction from the winter low's, however there is confidence that everything will follow a standard trend in good time. Steady year-on-year sales for a number of NZ mills through winter has reaffirmed this stance.

Common consensus from both mills and log sellers is that Q4 contracts will remain very similar to the levels agreed upon for Q3. With that said mills are keeping an eye on what happens at the wharfgate, particularly since values are being heavily subsidised by the low NZD:USD rate.

Supplies of pruned logs through the North Island are reported to sit somewhere between in-balance and mild over-supply. In additional producers of clearwood timber sold locally have experienced a tougher spell due to a mixture of subdued local construction and in some instances competition from imported product. Both factors saw North Island pruned (P1) logs

“Supplies of North Island pruned logs sit somewhere between in-balance and mild over-supply.”

soften a degree to \$189-\$201/t, with the odd exception lower. Export clearwood traders are still finding good success, most notably with sales into Europe. Demand for pruned logs is matching supplies in the South Island, where a steady \$175-\$187.50/t is being paid.

The market for pulp logs edged upwards yet again. National average prices for August and early September came out at \$53.1/t, marking the highest point since early 2012. Nearly all months since September 2012 have seen pulp logs average \$48/t-\$51.50/t.

Carbon breaks through \$25/t

The NZ carbon market is edging further and further into brand new territory by ranging across \$25-\$25.1/t since the beginning of September. This is a long way from the \$1.6/t that carbon sank to in early 2013.

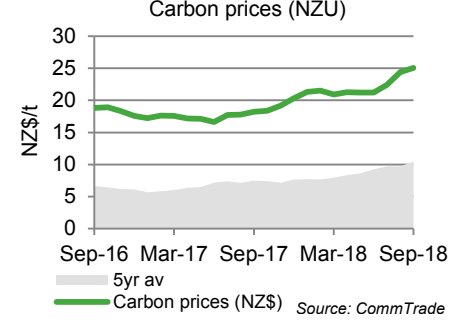
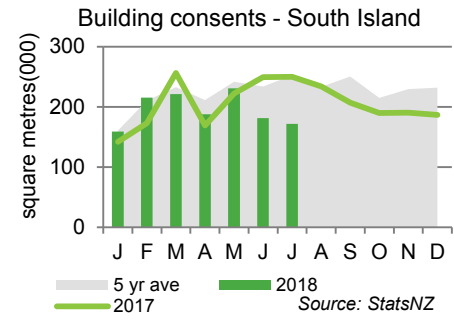
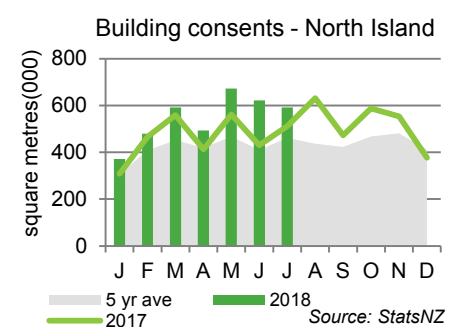
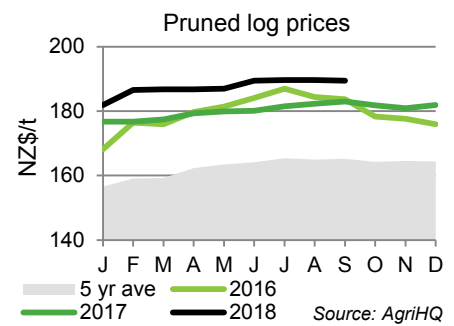
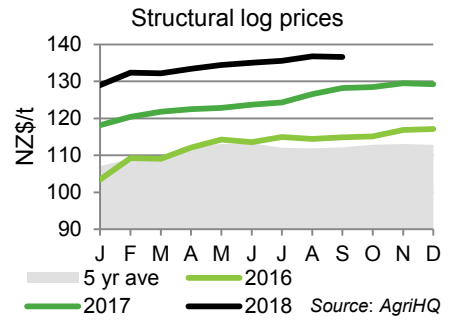
These constant lifts have begun to reignite conversations around forestry conversion on NZ sheep and beef farms. It's estimated that 1 million hectare of marginal farm land exists in NZ. The combination of the higher carbon price, the governments' joint-venture program announced earlier in the year to farmers, and the ongoing contraction of NZ's sheep farming industry could all push for increase in the conversion of NZ land into forestry use.

high lights

\$130-\$143/t

\$25-\$25.1/t

S1 logs close to steady in the North Island
 NZ carbon price pushed into brand new territory



Lumber exports - 3 mths rolling average (cubic metres)				Proportion of total exports		
	2018	2017	2016	2018	2017	2016
July						
World	175,729	158,956	159,231			
China	45,671	39,800	36,140	26%	25%	23%
Australia	13,448	11,708	14,097	8%	7%	9%
US	20,572	20,230	17,778	12%	13%	11%
Southeast Asia	-	42,557	44,946	-	27%	28%

Forest harvest & Production - Quarterly				Percentage change	
Latest	Mar-18	Dec-17	Mar-17	Q-Q	Y-Y
Harvest (cubic metres)	7,834,420	8,940,808	7,346,990	-12%	7%
of which: Export logs	4,758,612	5,581,452	3,959,305	-15%	20%
Production					
Sawn timber (cubic metres)	1,004,240	1,052,740	1,123,080	-5%	-11%
Pulp (air dry tonnes)	288,797	363,327	369,218	-21%	-22%

NEW ZEALAND EXPORT LOGS

Stabilisation after a big fall

As expected, even more was taken out of wharfgate log values through August and early-September, however it does look like we've bottomed out for the short-term at least.

Encouragingly, variation in wharfgate pricing was much slimmer in this round of the AgriHQ Log Price survey, indicating some settling in the market. Although the upper-end of values came back significantly, the lower-end was essentially steady. A-grade logs in the North Island were traded in the US\$130-\$141/JASm3 range, whereas the South Island market sat at \$117-\$130/JASm3.

All of this weakness is directly related to the reduction in Chinese buying power, itself due to the depreciation of the CNY:USD. Exporters have been relieved to see this rate hold stable in the past four weeks. Neither India nor South Korea have provided significant relief for exporters either. India is in a very similar position to China in that the falling INR:USD has eaten into importers' budgets, creating a wave of uncertainty and causing additional issues around cash-flows when paying for orders. With this said, there have been increased sales into some Indian ports in recent weeks. Port-level inventories for India are in a positive position for NZ traders at least.

The latest Scion Forestry Business Outlook report shows market participants widely anticipate a weaker three-month period from August for export unpruned log sales, before prices make small positive movements throughout the coming twelve months.

Luckily for NZ exporters secondary factors, particularly the exchange rate, have protected export traders against the depreciation within China. The NZD:USD fell to a two-and-a-half year low of US\$0.652 in mid-September, but has risen a little since. For some context, if the

“... secondary factors, particularly the exchange rate, have protected exporters...”

NZD:USD was at the same level as a 12 months ago A-grade logs would be another \$10-\$11/JASm3 lower. Shipping rates to China retracted a little to US\$27.50-\$30.50/JASm3. There are signs that shipping capacity around the Pacific region is coming under pressure as a result of grain shipments into drought-affected regions of Australia. This is set to cause a small upswing in shipping rates for the short-term, though no major increase is anticipated.

Record breaking log exports in July

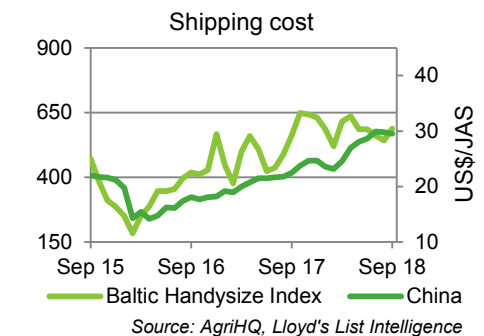
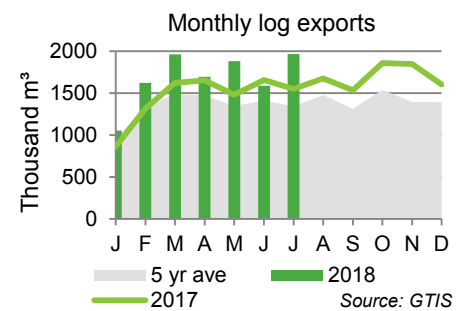
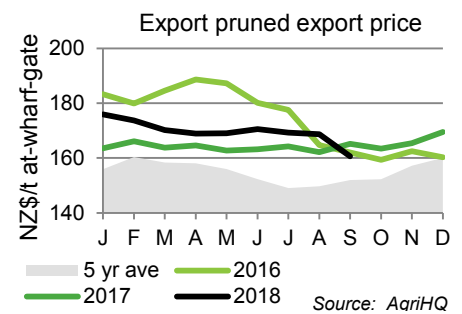
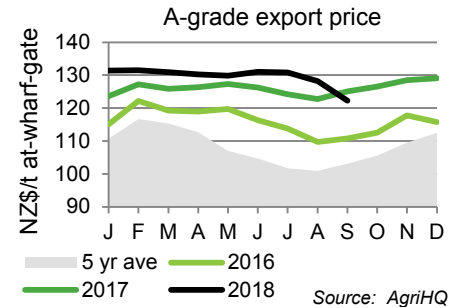
NZ softwood log exports were at a five year high in July, totalling 1,966,473m3. This was up 26.9% year-on-year and 14.3% on the three-month rolling average. The lift was across all major destinations bar China month-on-month. Year-on-year strength was from India and China. Exports are likely to remain steady in August despite weaker commodity prices, as the declining dollar offset the drop in prices.

Lumber exports were also strong at a three-year high, totalling 185,826m3, up 15.6% month-on-month and 8.4% year-on-year. A lot of the month-on-month strength came out of South East Asia, up 24.2% month-on-month and 19.2% year-on-year accounting for 27.3% of July's exports. All major destinations held steady over the past month.



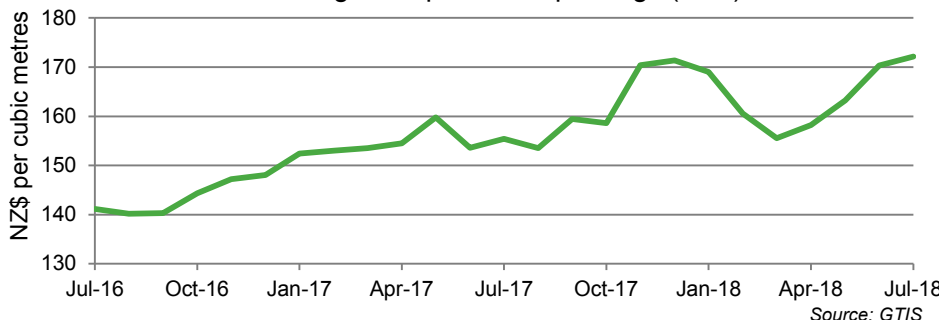
\$130-\$141/JASm3
A-grade logs take a hit at the wharfgate

\$27.50-\$30/JASm3
Shipping rates to China back a fraction



Log exports - 3 mths rolling average (cubic metres)				Proportion of total exports		
	2018	2017	2016	2018	2017	2016
July						
World	1,811,636	1,563,305	1,295,759			
China	1,265,293	1,107,198	880,316	70%	71%	68%
Korea	156,250	244,955	220,231	9%	16%	17%
India	122,851	151,651	139,774	7%	10%	11%
Japan	35,858	31,066	34,188	2%	2%	3%

Average unit price of export logs (NZ\$)



NZ dollar exchanges

	This mth	Last mth	Yr ago
USD	0.6568	0.65859	0.72122
AUD	0.9132	0.9066	0.9031
KRW	734.5	741.4	817.3
JPY	73.522	73.035	79.71
INR	47.036	46.11	46.346

CHINA

One sharp fall unlikely to be repeated

As mentioned on the front page, if it wasn't for the CNY:USD rate, China would be looking as healthy as ever. The squeeze on importers' budgets saw A-grade logs drop on average US\$8.5/JASm3 to US\$132-\$134/JASm3, while export pruned logs took an even larger hit, now trading for just US\$159-\$170/JASm3, back US\$9.5/JASm3. A drop of this magnitude is was last heard of more than three years ago, but in a historical context values remain firm. All grades are still trading around the levels reported in early 2017, when few were classing logs as under-valued.

Information from the ports paints a picture of solid underlying usage of logs, though reports vary from source to source. Some suggest a slight retraction in port-level inventories, whereas others have indicated the opposite. Either way 3.2 - 4 million m3 is the range. Everyone is in agreement that volumes out of South America and the Pacific Northwest are low, and this should at least steady stocks for the next few weeks.

Offtake rates are rebuilding some momentum too. Between 80,000 - 87,000 m3/day is being utilised as China transitions away from its hotter months. Areas closer to the equator are still quite warm though, suggesting more room for improvement in these figures.

China's housing index swings upwards

China's housing index rose significantly in July rising to 5.8% year-on-year growth.

This lift is the largest year-on-year gain since September 2017 due to the restrictions that have consistently been applied to curb prices. These curbs have been making it harder for potential buyers to purchase new homes. Property developers are trying to find ways around lending restrictions to ensure new developments are sold, going as far as offering perks, large discounts and lower deposit requirements that equate to more than 26% of the price.

“Further plans to rein in the skyrocketing housing prices have been given high priority.”

Surprisingly despite all the curbs Chinese government agencies have been putting in place over the past year it is predicted the prices will grow in excess of 5% over 2018 adding to the risk of a potential bubble. The current trade conflicts that China is experiencing will have little to no effect on housing prices with local supply and demand driving the market.

There remains a push to encourage properties to be used as rentals rather than sitting un-occupied. Despite the push expenditure on rental properties as a percent of total housing expenditure continues to lag behind most developed economies.

Further plans to rein in the skyrocketing



US\$132-
\$133/JASm3

+5.8%

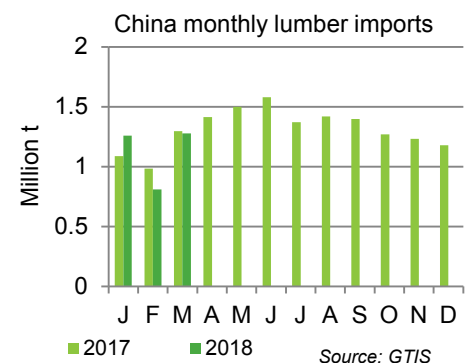
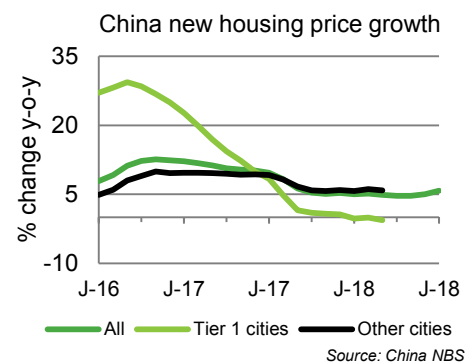
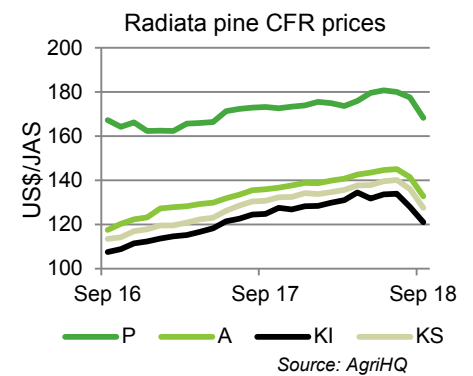
A-grade logs hit an 18-month low

China's housing index year-on-year in July

housing prices have been given high priority. One such plan is to implement a property tax, which will likely pass before the end of 2019. The concern surrounding such a policy is that market sentiment will be negatively affected.



Log imports - 3 mths rolling average (tonnes)				Proportion of total imports		
	2018	2017	2016	2018	2017	2016
World	2,618,180	2,371,557	2,036,468			
New Zealand	956,457	838,542	670,779	37%	35%	33%
Russia	600,979	652,218	683,084	23%	28%	34%
Australia	290,183	236,589	215,561	11%	10%	11%
US and Canada	401,508	473,455	339,349	15%	20%	17%



▶ SOUTH KOREA

Log imports continue to fall

Imports of softwood logs in July fell further to total 187,273t, down 9.3% on the three-month rolling average and 23.3% year-on-year. This was the lowest level imports has been since February last year. Despite this weakness in July, imports of NZ logs were up month-on-month lifting 1%, helping NZ to maintain an 84% share of imports.

South Korea employment market slows

The unemployment rate in South Korea continues to grow reaching the highest point since 2010, at 4.2% in August. This is on the back of a mandatory minimum wage growth, this is only adding to frustration surrounding economic policy. President Moon Jae-in's approval rating took a hard hit, now at the lowest since his inauguration. Minimum wage rates have grown 16% in 2018 the biggest jump this century. The rapid growth is discouraging employers from hiring any more staff.

▶ JAPAN

Log imports back up

July softwood log imports were back up as NZ re-entered the market. Totalling 277,659m3 imports were up 1.1% on the same time last year and 11.8% on the rolling three-month average. July imports from NZ were strong due to the timing of shipments, which meant zero imports the month prior. NZ logs made up 20% of July's imports while imports from the United States fell significantly accounting for 41% of imports.

Imports of NZ panels fell after a period of sustained strength, totalling NZ\$12.9 million, dropping 26.8% month-on-month, though more in line with 2017 down 3.7% year-on-year. This drop was the opposite of the overall NZ panel exports which increased 15.9% month-on-month, the majority of which headed to Australia.

▶ INDIA

NZ log exports to India bounce around again

Exports of softwood logs by NZ to India were up in July reaching a 12 month high at 175,811m3. This was more than double the average volume of logs exported to India in the first half of 2018 and up 42.2% on the same time last year. It is uncertain if the volatility can be removed from the market due to GST being required upfront at the port resulting in importers working on an as-needed basis. Demand from China is another driving factor as to whether NZ logs are a price effective product in India, with India making up any shortfall in exports to China each month.

Government attempts to rein in speculative housing bubble

Further attempts are being made to rein in the speculative housing bubble for which expensive homes are getting the blame. Despite current measures to curb speculative buying, apartment prices in some regions have accelerated rather than cooled. The government's plan is to impose tougher tax on property ownership for properties over 600 million won and multiple home owners.

The recent policy change to encourage rental properties in South Korea are set to be scrapped after it inflamed an additional price inflation rather than cooling it. In addition to scrapping this policy the government aims to increase the supply of housing in Seoul in response to the fastest increase in prices in more than a decade.

Abenomics missing 2% inflation target but still delivering growth

Despite Abenomics missing the current 2% inflation target it is still delivering good growth to Japan's economy. Since Prime Minister Shinzo Abe took office back in 2012 nominal GDP has risen 12%. The rate of growth is expected to ease in the coming months as concerns around protectionism weigh down on Japan. The Bank of Japan is focusing on protecting its local economy rather than solely pushing its inflation target. Despite this they continue to take small steps towards monetary policy normalisation.

India posts rapid growth brushing off trade war fears

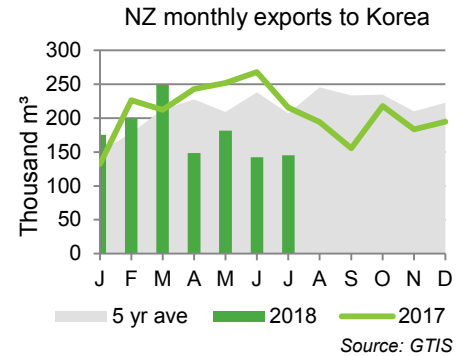
The annual GDP growth rate posted for the second quarter of 2018 was above expectations at 8.2%. This was the strongest growth rate posted in nine quarters and was the fastest growing major economy outpacing China. Further growth can be expected in the coming months as Prime Minister Modi tries to secure his party's prospects for general election in 2019. There are concerns that growth may be hindered by the weak rupee which has pushed petrol prices to record highs.



-9.3%

Log imports down on the three-month average

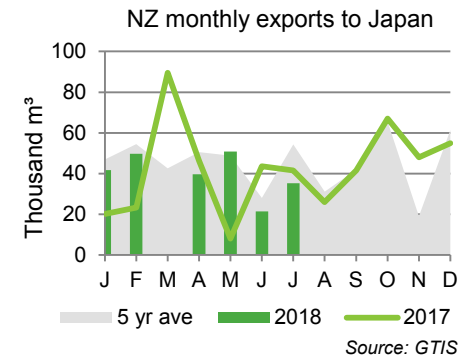
Unemployment reaches highest point since 2010



+11.8%

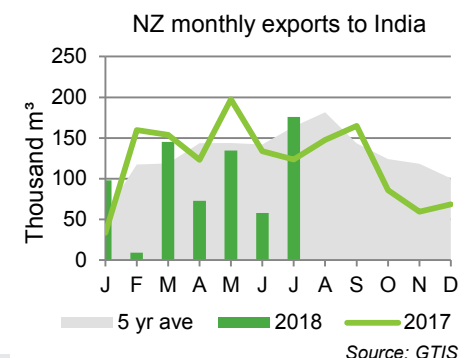
Log imports up on the three-month average

Good economic growth despite missing targets



July NZ log imports reach a 12-month high of 175,811m3

Q2 GDP growth exceeds expectations



▶ NORTH AMERICA

Canadian lumber exports hold strong

Exports of Canadian lumber remain strong as stockpiles are slowly dwindled down. These totalled 3,558,648m³ in July up 6.3% year-on-year but were down 5.3% on the three-month rolling average. Strength at this time of the year is abnormal with the summer months in Canada typically exhibiting a lower level of exports due to raging wildfires. This is not the case this year due to stockpiles grown during winter. Major destinations remain unchanged with the US receiving 80% of lumber exports.

Lumber future prices at 18 month low

Chicago Mercantile lumber futures have been trending downward in recent months and September was no different. Consistent downward momentum throughout September has resulted in lumber futures hitting the lowest point since February 2017. They are equivalent to US\$148.96/m³ on 20th September, nearly half the price witnessed in May.

“Consistent decreases through September led to lumber futures hitting its lowest point since February 2017.”

The recent slide in prices has been mainly driven by warning signs that the US housing market is slowing after a strong run. Prices should not fall by much more as wildfires in the US and Canada start to cut into the available supply of lumber.

High lumber prices have been insulating the Canadian market from President Trump's tariffs on Canadian lumber. The coming months will provide a better picture if the tariffs will have any impact on the Canadian market which has been relatively untouched to-date.

US Log exports in cubic metres (3 months rolling average)			
	2018	2017	2016
July			
World	825,921	717,808	775,585
China	489,346	418,185	467,715
Japan	144,326	137,249	135,125
Korea	30,704	48,425	34,182

Cost of building new houses in the US set to increase

The US is set to have further costs for new homes. On top of the rising costs for construction, labour and building materials they are now set to having rising furnishing costs. The latest list of retaliatory tariffs for the trade dispute between China and the US, essentially has a tariff of up to \$10 billion on goods used in construction of new homes in the US. Despite the headwinds that homebuilders continue to be hit with the most recent survey in September by the National Association of Home Builders showed high confidence within the industry.

There was continued weakness in housing permits issued in August, totalling 1,229,000 units (seasonally adjusted and annualised). This was down 5.7% on July and is the third month in a row of a low number of permits issued, suggesting a slowdown in construction is on the horizon. Despite weak issuance of permits in recent months construction starts took a turn upwards. August had an increase of 9.2% month-on-month to 1,282,000 units (seasonally adjusted and annualised), up 9.4% year-on-year.

North American Free Trade Agreement talks resume

North American Free Trade Agreement negotiations resumed in Washington mid-September. Very little time remains if a new agreement is to be reached before the new Mexican president takes office, the text would need to be generated by 30 September. Despite this, Canada has signalled that they are in no rush to accept a bad deal.

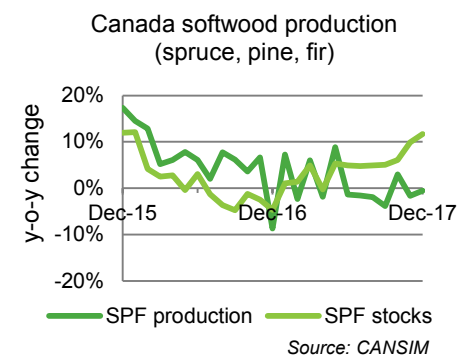
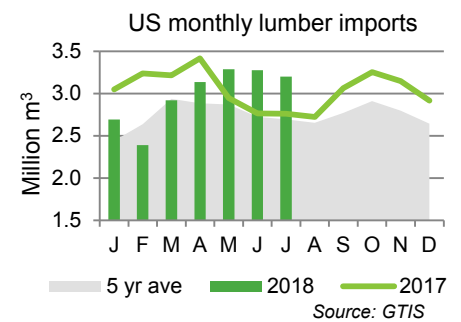
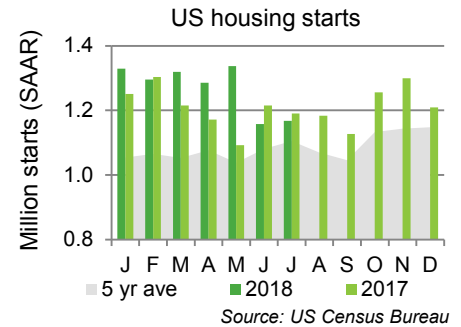
Progress continues to be made towards getting a new deal signed off, though challenges still remain. Major issues that remain are preservation of disputes panels and auto tariffs. President Trump continues to threaten that if a deal is not made by the coming deadline that the US will cut Canada out of the deal. The US and Mexico reached a preliminary deal in August.

Canada Log exports in cubic metres (3 months rolling average)			
	2018	2017	2016
July			
World	493,921	555,379	531,232
China	248,180	346,566	297,459
Japan	118,536	96,985	122,094
Korea	40,434	84,295	63,789

high
lights

Abnormally high lumber exports for Canada

High lumber prices insulating the Canadian market from Trump's tariffs



▶ AUSTRALIA

Lumber imports break through plateau

After three steady months of lumber imports, Australia appears to have pushed through the plateau and reached a new level of demand. Lumber imports reached a high totalling 80,375m3 in July, up 6.5% on the three-month rolling average and 53% year-on-year.

Log exports have eased in recent months as China's demand for lumber starts to fall back. July's lumber exports were in-line with the downgraded June figure, up 0.7% month-on-month, totalling 279,743m3. The eased demand has had two driving factors; the tightening housing market and weaker Chinese Yen. Both have decrease China's buying power.

Housing boom comes to an abrupt end

The current credit squeeze in Australia combined with unaffordable prices has halted Australia's housing boom abruptly. The tighter

credit has resulted in prices falling in major cities which had risen near 70% over the past 5 years. The ease to get credit in recent years has helped pushed household debt to one of the highest levels for a developed country, above 120% of GDP. Prices have yet to bottom out and will continue the downward slide for the foreseeable future as Australia enters its selling season and mortgage rates are lifted.

The Reserve Bank of Australia (RBA) reiterated in September that monetary policy will remain as is until such time the unemployment rates fall further and inflation picks up. Protectionist trade policies are

“The weak Australian dollar is currently helping to prop up its economy.”

high lights

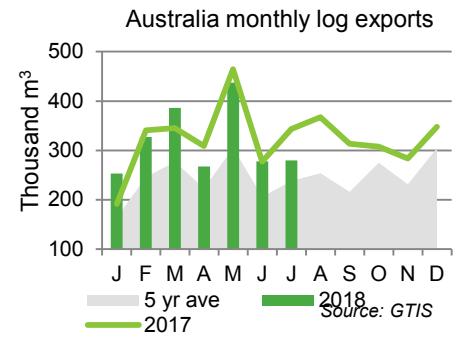
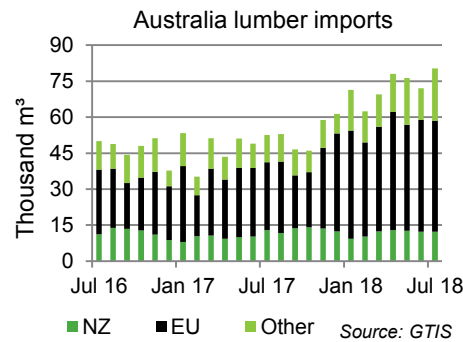
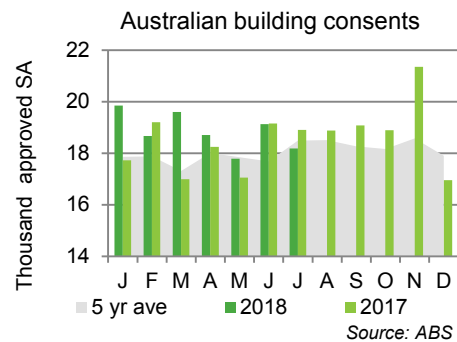
+53%

Big year-on-year increase in lumber imports for July

Credit squeeze combined with unaffordable prices halts Australia's housing boom

deemed as a material risk by the RBA due to the uncertainty it holds for the global economic outlook.

The weak Australian dollar is currently helping to prop up its economy. Towards the start of September the AUD:USD hit the lowest point since February 2016 at \$0.71. The weaker dollar however has helped make Australian assets more attractive to foreign investors. With its AAA rated status, Australian debt is viewed as a safe haven and relatively high yield investment.



▶ RUSSIA

US announce new sanctions on Russia

Exports of Russian lumber to China has remained strong for the first half of 2018 up 2.8% averaging 873,288t per month. The overall trend in WTI crude oil over the past month was upwards though turbulent. The current price was reached at the beginning of September before subsequently dropping before lifting back to US\$70.32/barrel. This price is in-line with those throughout July.

The United States plans to apply more severe sanctions in response to the nerve agent attack in the United Kingdom. The United States will continue to pursue this until Russia is willing to provide assurances that they will not use banned chemical weapons in the future. Current sanctions limit exports of US goods

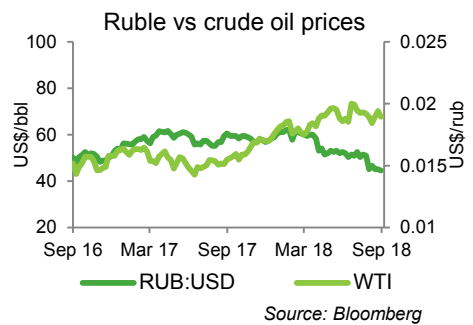
“The United States plans to apply more severe sanctions in response to the nerve agent attack”

considered sensitive to national security to Russia. Russia's Minister of Economic Development is not concerned about these sanctions, leaving growth forecasts unchanged despite the threat of sanctions. The major concern is contagion of the volatility in other emerging markets following through into Russia's economy.

high lights

Russia leaves growth forecasts unchanged despite the threat of sanctions

Exports of Russian lumber to China remained strong for the first half of 2018



DATA TABLES

CFR in-market log prices (US\$/JASm ³)							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
KI	121	128	-6%	131	125	-3%	108
KS	128	136	-6%	136	131	-2%	114
A	133	141	-6%	141	136	-2%	118
P	168	178	-5%	174	173	-3%	167

Carbon NZ\$/tonne							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
NZU	25.06	24.40	3%	20.90	18.20	38%	18.80

Shipping costs from NZ (US\$/JASm ³)							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
China	29.5	29.8	-1%	24.5	22.5	31%	18.1
South Korea	29.6	29.9	-1%	25.5	23.6	25%	17.8
India	39.3	38.8	1%	32.1	29.7	32%	24.4

Forex							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
US/NZD	0.6568	0.6586	0%	0.7255	0.7212	-9%	0.7389
AU/NZD	0.9132	0.9066	1%	0.9327	0.9031	1%	0.9671

Building activity							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
US	1168	1158	1%	1329	1190	-2%	1212
Australia	18,185	19,133	-5%	19,851	18,900	-4%	21,028
							000's approved
NZ	764	804	-5%	530	762	0%	724
Japan (wooden structured)	4855	4840	0%	3978	4909	-1%	5084
							000's m ²

Log import volumes from NZ							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
China (t)	1,172,849	563,065	108%	1,045,821	1,016,693	15%	945,367
South Korea (t)	156,427	155,260	1%	166,621	178,985	-13%	189,651
Japan (m ³)	56,042	0	-	41,205	43,467	29%	16,054

Source: GTT

NZ exports (m ³)							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
Logs	1,966,473	1,587,125	24%	1,051,866	1,550,038	27%	1,247,248
Lumber	185,826	160,810	16%	86,104	171,476	8%	167,854

Source: GTT

Chinese imports from PNW (t)							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
Logs	382,658	284,646	34%	614,977	508,838	-25%	361,733
Lumber	223,020	119,050	87%	245,376	268,263	-17%	316,633

Source: GTT

Chinese imports from Russia (t)							
	Latest	Last month	m/m change	6 months ago	Year ago	y/y change	2 years ago
Logs	607,119	606,975	0%	583,900	700,484	-13%	766,263
Lumber	801,367	580,117	38%	903,757	779,829	3%	632,674

Source: GTT

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