

Regional Timberland Investment Study – Europe

As of 2008, the European Union comprises 27 member states. IWC analyzed each country for a variety of different parameters driving timberland investment returns and concluded with a short list of countries that currently provide desirable risk-return profiles; the majority are in Eastern Europe.

1 Economics

The European Union has a strong influence on the national legislation in each of the member states as well as on political and macro-economic conditions. This applies even more for countries within the monetary union, all utilizing the Euro as the common currency, as it implies fiscal policy restrictions. Countries that recently joined the EU made significant reform progress in advance of their accession, some have lost momentum since, but further improvements can be expected.

- The European Union's economy accounts for about 23 percent of the world's total economic output as measured by Gross Domestic Product and is thus the largest economic entity in the world.
- Economic growth rates have been above US levels for the last couple of years but the EU economy is stagnating as the international economic slowdown following the US subprime crisis reduced economic growth rates from 2.8 % in 2007 to an expected 1.8 % in the near future.
- In the monetary union, one common target is maintaining inflation below 2 %. Generally, new member states show higher levels of inflation than older ones, but predictions are the inflation rate will average around 2.4 %.
- The growth rates of the new eastern member states have been considerably higher than in the rest of Europe, with some of the rates comparable to emerging Asian countries.
- Foreign Direct Investment activity increases with a country's entrance into the Union. The investment level signals approval of the countries' economic activity and positive expectations for future development.
- The Euro has recently gained considerably against the US dollar. Despite the negative effect this has on exports, the monetary union's entry criteria generally lower the risk of investment.

2 Forest Sector

165 million hectares, or more than one third of the EU, is covered with forests of which approximately two thirds are privately owned. However, public ownership is predominant in Eastern Europe due to the inheritance from former centralized and communist regimes. Restitution of land that was nationalized after the Second World War is an ongoing process and will generally increase the availability of private timberlands.

- Timberland markets in Eastern Europe are still immature, thus allowing knowledgeable buyers to benefit from the inefficiencies.
- Europe's forests contain a large variety of different tree species among which spruce, pine, birch, beech and oak are commercially the most important. Annual growth rates average 6.4 m³ per hectare, but can be up to three times as high depending on site and species. Only about 60 % of the annual increment is harvested, indicating the potential of higher yields.
- Costs of production are varying among the member states, but education and forest technology are generally highly developed, making silvicultural practices very cost-efficient. In Eastern Europe, costs of production are significantly lower than in the western member states.

>> Continues on next page



>> continued from front page ...

When it comes to timber markets, the status of the domestic timber industry (primary conversion) clearly has the most direct impact on timberland investments. On the other hand, timber has become a commodity that is traded worldwide, thus development in countries outside of Europe forms another relevant aspect.

- Investment in sawmilling capacity is now moving toward Eastern Europe and significant new capacities are being built. Western Europe's timber industry is restructuring, making mills more efficient and globally competitive.
- The production and consumption of pulp and paper has become stagnant in the Northern Hemisphere. New investment is focusing on South America and Asia due to significantly lower costs of feedstock. However, the pulp produced in Europe is different from that from South America, thus hampering its substitution.
- Russia initiated increases in export taxes for unprocessed logs starting in mid-2007 in order to incentivize the enhancement of value-adding capacities of its domestic timber industry. The export tariffs, which will increase further until 2009, have driven up timber prices in Europe and other parts of the world as volumes of coniferous roundwood available from Russia are drastically reduced.
- The US housing market, which is a key global demand driver for structural lumber and panels, has declined due to the mortgage crisis in 2007. However, this market is expected to steadily recover within the near future as underlying fundamentals indicate.
- There is a possible emerging log shortage of industrial roundwood developing in the Northern Hemisphere because of competition among panel, pulp and bioenergy producers all utilizing the same kind of raw material. Furthermore, prices of industrial roundwood have increased because the downturn in US housing starts has meant that less sawtimber is harvested, which decreases the availability of the joint-product pulpwood.
- European and North American government policies in response to climate change and energy security concerns are accelerating the demand for wood as fuel to meet renewable energy targets.
- Eastern European countries have an increasing mid-term need for wooden building materials in the construction and refurbishment sector of residential and commercial building construction.

3 Conclusions


The mid to long term outlook for Europe's timber markets is positive due to investments in milling capacities as well as increasing demand from retail markets within and outside the European Union.

Despite negative effects from the US housing downturn and the shift in pulping capacity, Russia's log tariffs as well as increasing demand from the bioenergy sector tend to keep prices buoyant.

Europe's economy is the world's largest and features stable and reliable characteristics. Its legal framework keeps risks at a comparably low level.

In comparison with fast growing plantations in the Southern Hemisphere, biological growth rates are generally lower. But the region features a large variety of species some of which can only be found in Europe and are appreciated worldwide. In addition, the quality of timber produced in Europe is often superior.

The availability of timberland is generally good and one finds both mature and less developed markets. Furthermore, the restitution of nationalized lands holds significant upsides for timberland investors.

It is worth noting that the diversity of European countries provides differing national traits, which is one of the challenges but even more so one of the region's upsides. 



World Forest Products and Timberland News

Ghana And EU Sign Landmark Deal on Illegal Timber

The European Union (EU) and Ghana signed a Voluntary Partnership Agreement that is designed to stop illegally felled timber from Ghana from entering the EU market. The agreement was regarded as a landmark deal to fight illegal timber exports from Ghana by ensuring that all timber exported from the country is certified as legal. Current statistics indicate that in recent years about 60 % of logging across Ghana has been classified as illegal, according to the World Bank. Under the agreement, the Government of Ghana will impose stricter controls on logging from trees felled in remote forests to timber loaded onto cargo ships. The EU, which consumes more than 50 % of Ghana's timber exports (more than USD400 million a year), will ban entry to shipments of Ghana timber that are not verified, audited and licensed. (Source: ITTO)

Norway Pledges USD1 Billion to Brazil Amazon Fund

Norway will donate USD1 billion to Brazil's Amazon protection fund through 2015 to help Brazil fight deforestation. Norway, the first country to pledge money to the fund, will donate as much as USD130 million next year. But the money will only be handed over if Brazil shows deforestation was reduced in the previous year. Brazil launched the international fund in August. It aims to raise USD21 billion over 13 years to finance conservation and sustainable development in the Amazon. The Amazon Fund will support forest conservation through scientific research and sustainable development projects including forestry management. (Source: Reuters)

US Lumber Production in 2007 Hits 11-Year Low

With the housing market in trouble, lumber production at Western U.S. sawmills in 2007 slipped for the second straight year, according to final production figures prepared by Western Wood Products Association. Mills in the 12 Western states produced 16.32 billion board feet of softwood lumber in 2007, down 9.3 percent from the previous year. The estimated wholesale value of the lumber was USD6.1 billion, compared to USD6.8 billion in 2006. The volume was the lowest since 1996. U.S. lumber consumption fell by 14 percent to 52.2 billion board feet from 2006 totals. Since reaching an all-time record of 64.3 billion board feet in 2005, lumber demand has dropped by 12 billion board feet – equivalent to the annual production in Oregon, Washington and California. Housing starts totaled just 1.36 million for 2007, far lower than the 2.07 million starts recorded two years earlier. Production in the southern U.S. decreased 9.2 percent to 16.99 billion board feet. Lumber imports declined more steeply, falling 19.4 percent to 18.39 billion board feet. Canada, the largest lumber supplier to the U.S. market, shipped 17 percent less lumber to the U.S. in 2007. Non-Canadian lumber imports from Europe, South America and New Zealand plummeted 35.5 percent. (Source: WWPA)

China's Log Imports to Decline, Lumber and Woodchip Imports to Increase

RISI has predicted that China's log imports will decline by 13 million cubic meters between 2007 and 2012, but the country's total wood fiber deficit (including logs, woodchips and the roundwood equivalent of its wood product and pulp imports) will increase by 22 million cubic meters, a 26 % increase during that same timeframe. China's Timber Supply Outlook 2008 - 2012 study author, Robert Flynn commented, "Mainly due to the impending Russian log export tax, China will see a significant decline in softwood log imports between 2007 and 2012, but imports of softwood lumber will more than double. Russia will be the primary new source of softwood lumber for China, but Canadian lumber exports to China will climb rapidly as well. We also expect to see potentially a threefold increase in woodchip imports as China attempts to feed its growing pulp industry." (Source: RISI)



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Follow up on the Singapore office

In our last newsletter, we informed you about the opening of IWC's first off-shore office. We are glad to confirm that since August 1, 2008, Mikkel Brings Nielsen, Forest Acquisition Manager, is working on deal sourcing and timberland acquisitions in Asia from the address.

We already observe the numerous advantages of being locally present in Asia through an increased deal pipeline in the region. 

IWC internal news

IWC congratulates

Karsten R. Petersen


In June 2008, Karsten R. Petersen was awarded the Graduate Diploma in Business Administration (Finance) [HD(F)], which is a four-year part time study at bachelor's level from Copenhagen Business School. His thesis was about mitigation banking in the United States as an investment opportunity for a Danish pension fund.

Karsten is now the Legal Counsel and Economist at IWC. 



IWC welcomes Esben Brandt


Esben Brandt joined IWC in September 2008 as a Forest Acquisition Manager working with IWC's Investment Development and Analysis team. Esben is responsible for deal sourcing and due diligence for direct forest investments, with a focus on Africa.

Esben holds a MSc in forestry from the Royal Veterinary and Agricultural University of Copenhagen. Prior to joining IWC, Esben worked with COWI, an international consulting company, as a coordinator and project manager in COWI's development assistance division. With his development aid and consulting background, Esben brings hands-on experience of doing business in Africa to IWC. 



Falck

First Aid & Fire Safety course at IWC

In September & October 2008, half of IWC's staff was trained by Falck, to react correctly under difficult conditions if accidents or fires occur at the office, during forest visits, or on the road. Another session is planned for later this year so that all of IWC's employees are better trained to properly respond in an emergency situation. 

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