Timber Market Update

1Q 2019 – Executive summary

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Executive summary

IWC is proud to have its own in-house independent research team and considers this an integral part of our idea generation process, which enables us to develop opinions and provide insights in order to best guide our clients. Four times a year, at quarter-end, IWC publishes its Timber Market Update (TMU) produced by IWC's Investment Forestry Analyst, Øystein Juul Nielsen, in collaboration with our Foresters. Øystein is a Forestry PhD scholar with extensive experience in applied economics and econometrics, statistical analysis, survey implementation, and data management. While the full report is reserved for our clients, we would like to hereby share some of the major transactions and returns on the timber market, and highlight some of the most decisive regional price developments and market drivers during the first quarter of 2019.

Timberland transactions and returns

Overall, the quarter was marked by few US transactions, Hancock's sale of 38,000 acres of Douglas-fir plantation in Oregon being one of the most notable sales of the quarter. Meanwhile, US timberland returns were affected by capital depreciation in all regions but the Lake States, due to falling lumber prices and reduced exports to China. While the US South continues to underperform at 0.14%, annual returns for the Pacific Northwest (PNW) and Northeast (NE) remain stable at 7.75% and 4.56%, respectively. Outside the US, BTG purchased a large eucalyptus plantation in the Mato Grosso do Sul region of Brazil, while AXA added 4,000 hectares of Irish forests to their portfolio, making it the largest timberland transaction ever recorded in the country's history. Finally, SCA's acquisition of 10,000 hectares in Estonia increased their holdings in the Baltics, thus securing the supply of raw materials to their industries in Sweden.

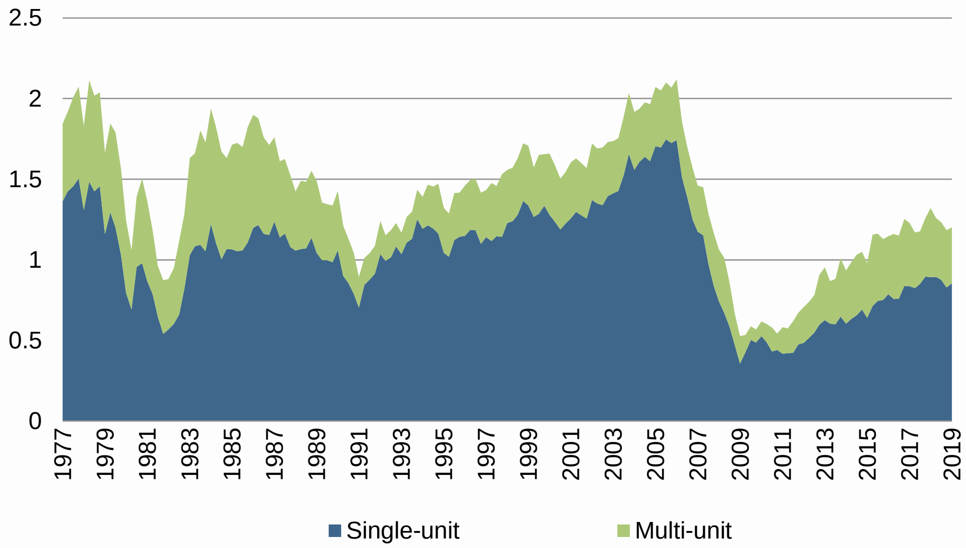
Figure 1 Quarterly transaction overview

Region	Price estimation* (million USD)	Hectares (000)
US	149.3	72.3
South	*72.4*	*23.5*
West	*58.4*	*38.0*
Northeast	*18.5*	*10.8*
Rest of the world	219.2	50.1

Regional price developments and market drivers

In the US, the marginal increase of 1.5% in housing starts, coupled with the decline in mortgage rates during the quarter, offered some improvement to the housing affordability., Lumber prices seems to have now stabilized and are expected to go up by as much as 8% in 2019. In Canada, several mill closures were announced in British Columbia (BC) with an additional 12 mills expected to close over the next 10 years. This, in turn, could support the development of mills in the US South, where wet conditions have constrained the supply, causing an increase in log prices for all grades in the region. Meanwhile, log prices in the PNW registered a decline in the first quarter.

Figure 2 US housing starts (million)*



Source: US Census Bureau (Seasonally Adjusted Annual Rate)

In Australia, housing starts declined further in the first quarter, mainly due to a 23% decrease in the multi-unit housing approvals. Although stable now, lumber prices are expected to fall due to the lag effect from falling approvals on the market. Hardwood chip exports and prices went up by 4.3% and 20%, respectively, thanks to global supply shortages and a weaker AUD.

To counterbalance the weakening Chinese demand and high inventory levels, Brazilian pulp producer, Suzano, announced that they would curtail production levels. Other producers are likely to follow this move, which could delay the harvesting of contracted pulp log supply. Despite a weakening pulp market, several new pulp investments in Brazil were announced during the quarter.

Meanwhile, in Europe, reduced lumber demand from the UK and ample supply from beetle infested spruce stands have affected log prices, though pulp log prices remained firm.

Finally, Chinese wood imports fell by 6% compared to last year, mainly due to a weaker RMB and uncertainties regarding new tariffs, which remains a developing issue going into the second quarter of the year.

*Quarterly averages are reported for US housing starts. Latest press releases are not reported, as these may fluctuate from month to month.

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