

# FICA 2011 Annual Conference

## Export Market Update

18 November 2011

# AGENDA

- Changes since last FICA update
- Supply
- Current market update
- 2012 Outlook

# A lot's changed since Oct 2009

- Its been 2 years on from the last conference update and 3 years on from the start of the Global Financial Crisis and the theme then was to be *Cautiously Positive*
- Although a few speed bumps along the way, its been a good 3 years:
  - China has developed to become the dominant player in the forest products sector leaving all other markets in its tracks
  - India has surpassed Japan as NZ's 3<sup>rd</sup> largest market so its now China, Korea, India and Japan
  - The Russian log supply remains relatively low
  - It's taken a while but the Americans have awoken to Asia's demand
  - Pacific Rim supply has hit record levels from all sources
  - NZ log export volumes have reached record levels
  - NZ returns hit record levels since 'wood shock' in the 90's
- Domestic log prices have been dragged up by the scruff of the neck due to the strong export conditions
- The disasters in Christchurch and North Eastern Japan haven't really provided any significant change in demand for logs or lumber . . . . . yet
- TPT now operating from NZ, PNW and Queensland
- But as the sayings go – all good things come to an end or what goes up must come down
- Most importantly - **the Webb Ellis RWC remains in the trophy cabinet for the next 4 years !**

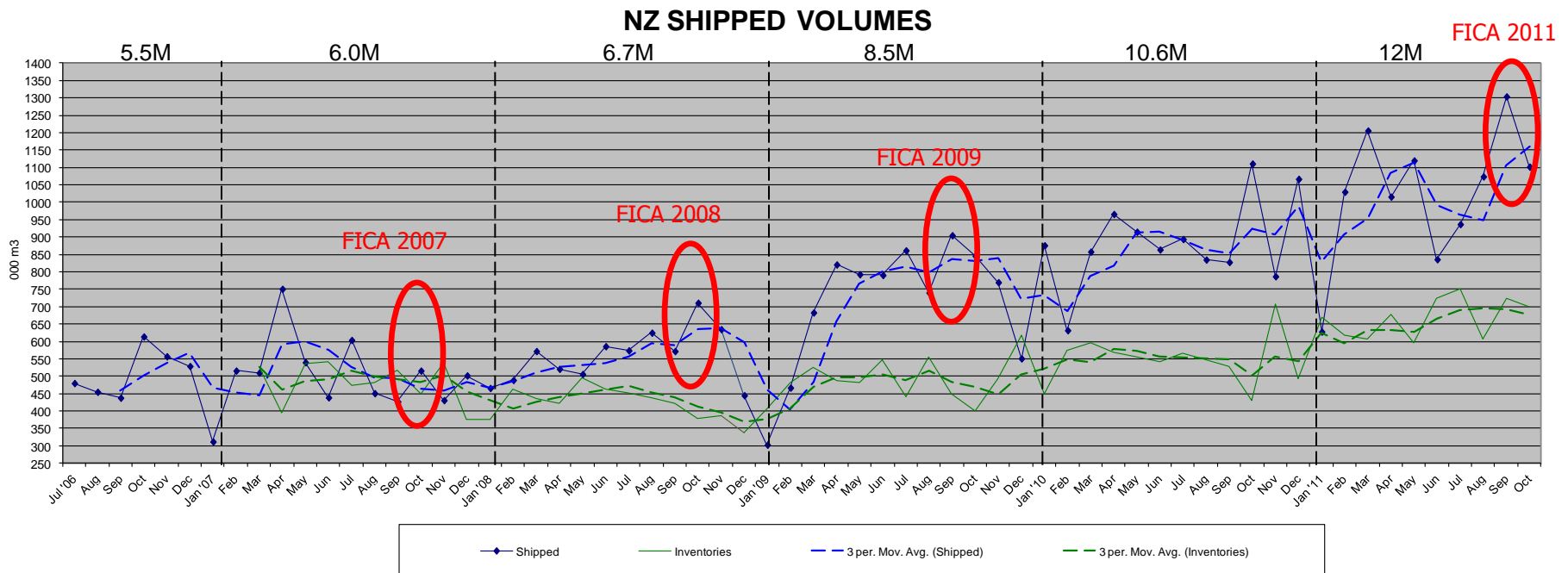
# 5 years of change

- First FICA conference for TPT was Oct 2007
- There's been many changes over the last 5 years
- The last 3 have been on balance very good for NZ primary industry – forest products and dairy
- China's been the 'rock' with Russia providing us the opportunity

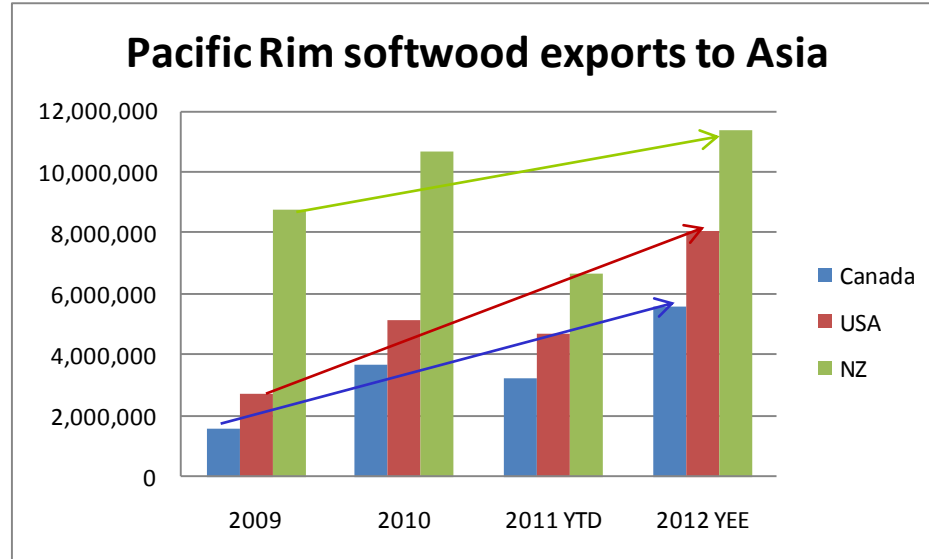
2007	2008	2009	2011
<ul style="list-style-type: none"> <li>• 2006 peak global activity</li> <li>• Russia dominance (23M)</li> <li>• Russian Tariff 20% (6.5%)</li> <li>• China developing</li> <li>• India emerging</li> <li>• Declining US supply</li> <li>• NZ supply static 5.5M</li> <li>• NZ infrastructure tops out at 7Mpm</li> </ul> <p><b>The perfect storm</b></p>	<ul style="list-style-type: none"> <li>• Start of GFC – Oct 08</li> <li>• Developed nations construction activity down (collapsed)</li> <li>• Russian Tariff 25%</li> <li>• High NZ supply – long Christmas</li> <li>• Freight and FX collapse</li> </ul> <p><b>Uncertainty but it will get better – when ?</b></p>	<ul style="list-style-type: none"> <li>• Still GFC impacts – 'U' or 'W' recovery</li> <li>• US economy slow</li> <li>• Russian Tariff supposed to hit 80%</li> <li>• Russian supply 50% (16M)</li> <li>• NZ supply at record levels</li> </ul> <p><b>Cautiously Positive</b></p>	<ul style="list-style-type: none"> <li>• China's dominance</li> <li>• India emerging</li> <li>• Russia WTO – Tariff 15% ?</li> <li>• NZ supply at record levels</li> <li>• North America supply at record levels</li> <li>• European economic issues, US no better</li> <li>• High in market inventory</li> </ul> <p><b>Tough and volatile</b></p>

# NZ supply is at record levels

- The message in 2008 and 09 was that supply had reached record levels, markets were over supplied and there was a need a long Christmas break - - - 2011 isn't any different - more records
- In 2009 NZ exported ~ 8.5M m3 for the year - 122% higher than the previous year and ~150% higher than the previous 5 year average
- Today, NZ export levels are 10.2M m3 YTD therefore running at new record levels of 12M m3 pa (10.6M in 2010)
  - ~140% higher than when we last met in 2009 and ~220% higher than the previous 5 year average (more than doubled)
- The four main ports of Tauranga Gisborne, Northport and Napier exporting ~75% of the volume (Tauranga and Gisborne ~50%) – Nelson ~6% of NZ total
- But its time for a breather again – there's too much wood and the market needs time to digest what its got



# PNW and Canada have increased as well



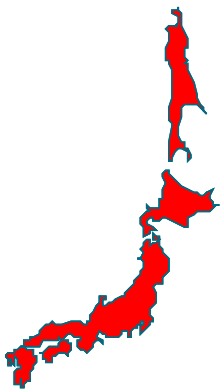
	2009		2010		2011 YTD	2011 YEE	
	Jas	Share	Jas	Share	Jas	Jas	Share
Canada	1,597,418	12%	3,691,430	19%	3,246,053	5,564,663	22%
USA	2,688,503	21%	5,103,648	26%	4,689,795	8,039,648	32%
NZ	8,749,869	67%	10,647,783	55%	6,635,591	11,375,299	46%
Total	13,035,790	100%	19,442,861	100%	14,571,439	24,979,610	100%

Pac rim supply points have grown ~190% over the last 3 years – CAN 348%, US 299%, NZ 130%

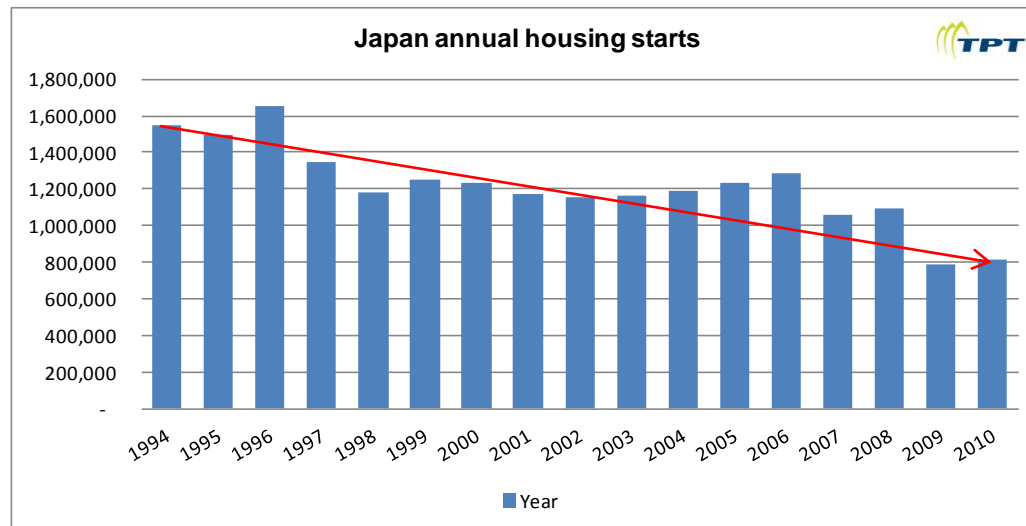
Look at Total, but also Canada and USA – combined now as big if not bigger than NZ

Lumber shows a similar picture from North America

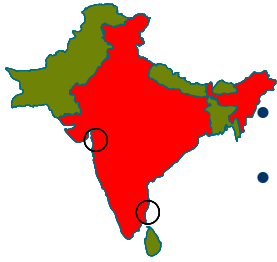
# Japan



- The strengthening Yen is helping import costs, however is severely impacting exports and Japans ability to remain competitive for manufactured export goods. This in turn is reflected in a weakening of packaging lumber demand and therefore NZ radiata A Grade logs.
- The Great Eastern Disaster of March 2011 has not provided any significant increase in demand for softwood log or lumber that has flowed through to NZ radiata. Temporary housing development is complete, however infrastructure remains an issue as is the fall out from the Fukushima power plant.
- Housing starts have improved slightly over recent months on the back of continued government stimulation packages (combined with the natural seasonal upswing), however still less than 900,000 starts per annum which remains ~25% reduction on the long run average.
- Plywood manufacturing capacity continues to be realigned between mills as the plants damaged during the earthquake and tsunami are slowing be recommissioned (3 out of 13 to date). Over-all production is slightly stronger as expected however domestic species remains the dominant supply source. There is no change in NZ radiata demand.
- The packaging sector remains stable in terms of demand, however all customers continue to struggle with international softwood prices and only the strength of the Yen keeping their head above water. USD FOB prices have increased 180% over the last 4 years.

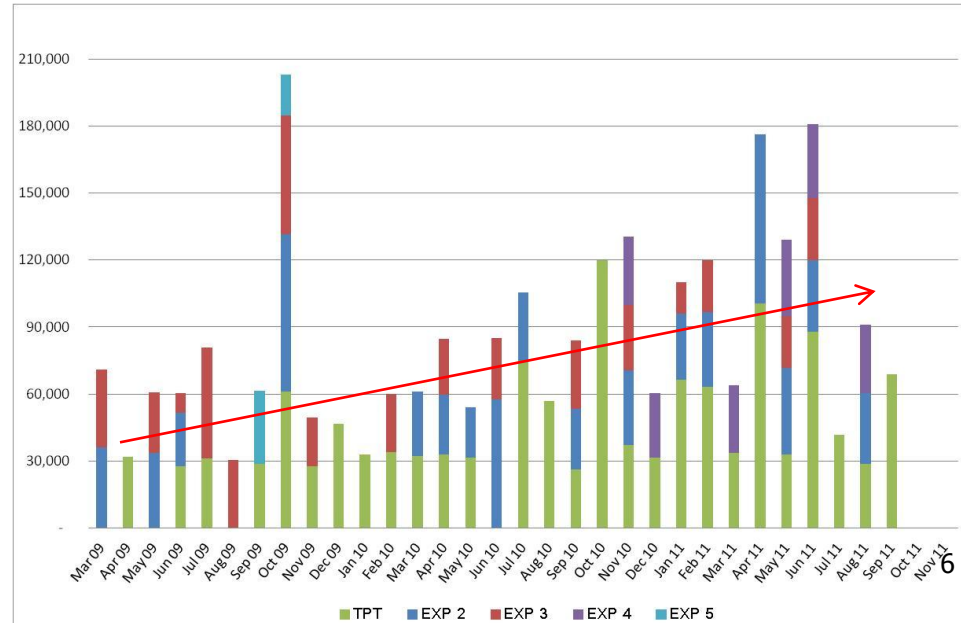
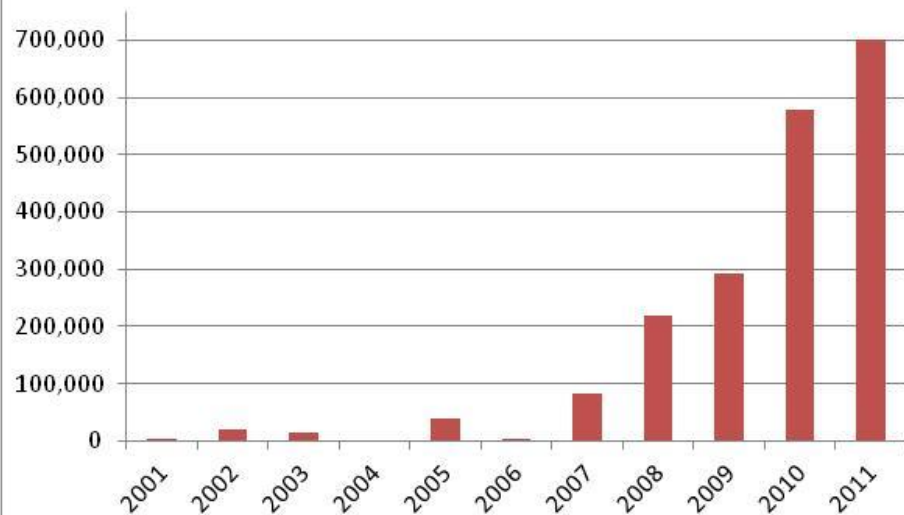


# India

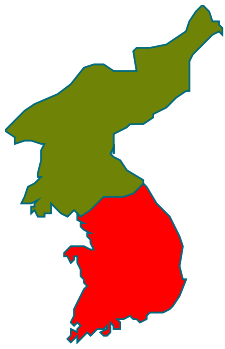


- India continues to perform well.
- The India market is still dominated by the Ghandidham region (Kandla/Mundra ports) with 80% market share, Tuticorin receives approx. 18%, with the balance going to a variety of locations in containers.
- To end September Ghandidham had received 981k Jas compared with a total of 935k in 2010 and 701k in 2009.
- The Indian market by current forecasts will consume 1.5m Jas in 2011 up 25% on 2010's 1.2m Jas.
- Infrastructure still remains one of the key issues in expanding supply into other areas of India.
- GDP growth for first half of 2010 is at 7.75%. The forecasts for the balance of the year is to stay flat.
- The general outlook for India is positive however NZ pine logs are under threat from lumber supplied from PNW and Sthn US. Demand will remain firm as long as NZ can remain competitive with these new supply sources.

**TPT's Annualised India Export Volume**

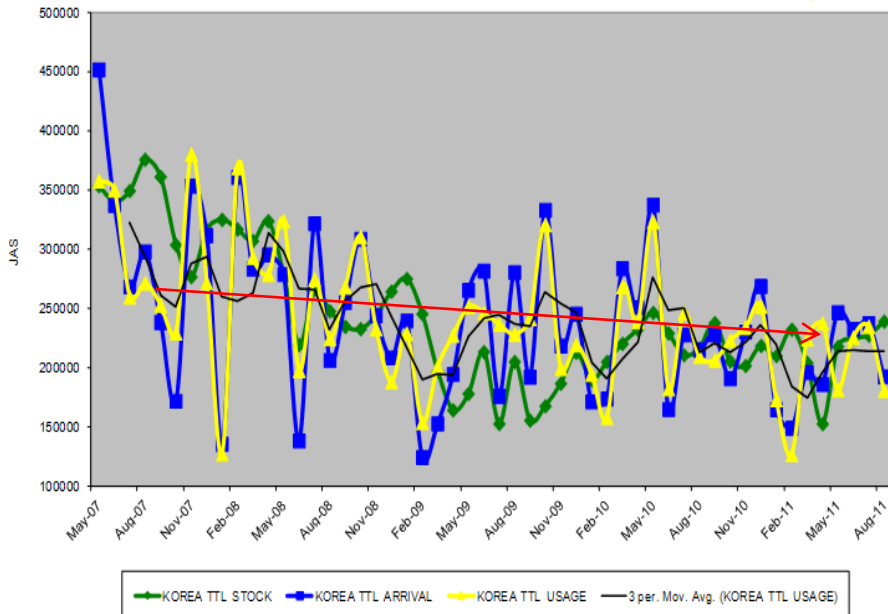


# Korea (1)

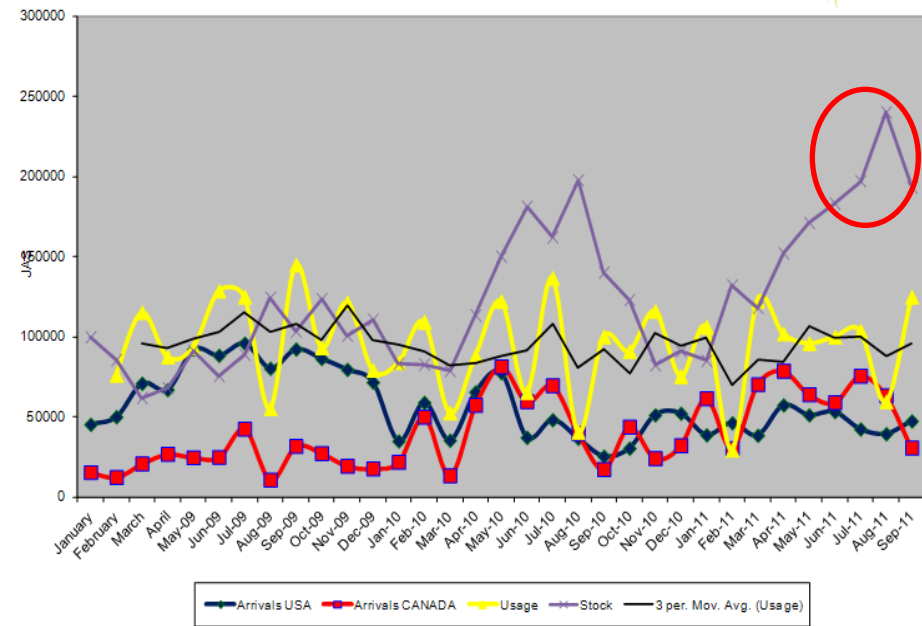


- Nothing of significance to report for Korea. In general Korea's economy continues to perform relatively well, however the construction sector remains subdued resulting in stable demand for NZ radiata
- The plywood speculation post the Japan Earthquake and Tsunami didn't eventuate and therefore Korea continues to hold high inventories of finished plywood
- Imported softwood log volumes continue to operate around 6M m3 per annum with NZ supply stable at ~ 3M m3 pa.
- Canadian log and lumber volumes continue to grow in Korea with competition with NZ radiata in some sectors and regions.

KOREAN CONSUMPTION - NZ/AUST Logs



KOREAN CONSUMPTION - US/CAN Logs





# China

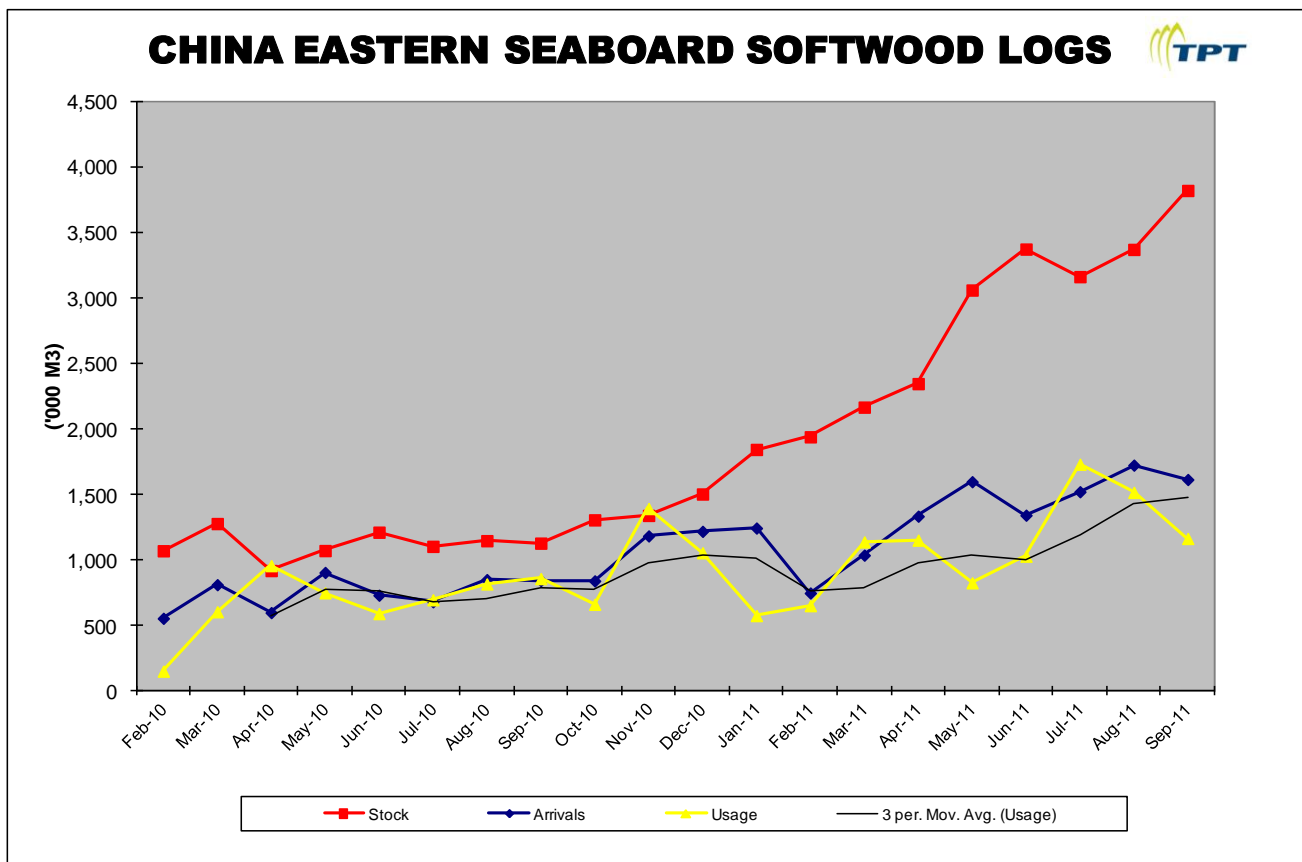
- China continues to be the dominant player for NZ softwood currently running at 7.15 M m3 pa representing 62 % of NZ's total export demand.
- Prices have fallen (A Grade basis) from around US\$30 CFR between September to October
- 2011 demand has increased 24 % for imported logs and lumber on an inventory adjusted basis (31 % increase in actual imports = building inventory)..
- 2012 is expected to be more difficult than 2011 with over established capacity in both imported log/lumber channels and eastern sea board processing capacity.
  - These two issues created positive market sentiment in 2011 and the 3 year period from 2008.
- The Chinese property market continues to come under sustained central government pressure to reduce housing costs as part of the general battle with inflation.
- Housing starts in 2012 (22 M m3 in 2011) are likely to decline as unsold apartments and falling prices weigh on the market. Falling house prices is a new concept for Chinese to grasp.
- The primary industry risk for 2012 remains over supply capacity from Pacific Rim processing countries. With the domestic economic outlooks in CAN/US/NZ and AUS remain difficult, pressure to place volumes is likely to result in stiff competition. This is likely to see the market continue to see periods of high inventories and associated price volatility as supply and demand levels rebalance.



# China (2)

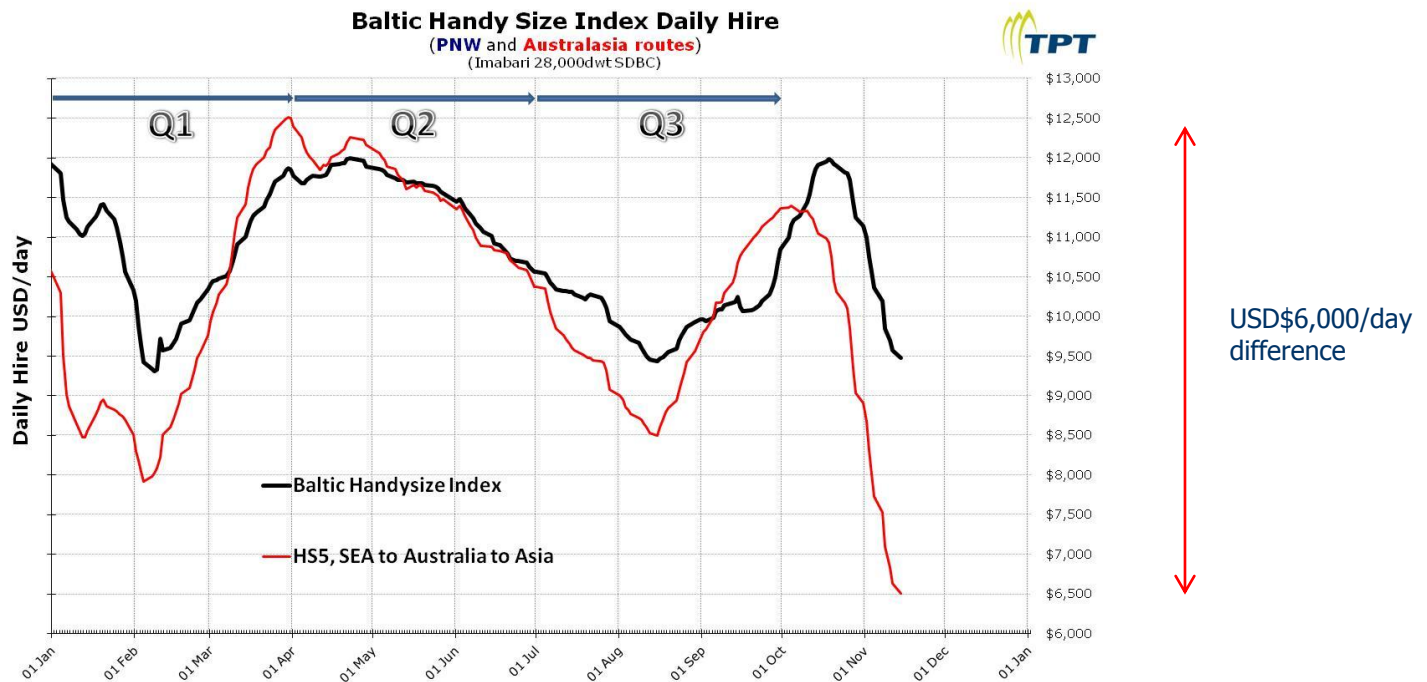


- This graph tells the complete story for China and the flow on to the rest of the markets
- Supply has been developing quicker than demand has been growing
  - Yellow line consumption
  - Red line inventory
- 3-4 months inventory – going into northern hemisphere winter and Chinese New Year



# Sea Freight

- Unit rates began the year in mid US\$30's/Jas, by June they were in the mid to high US\$40's/Jas
- Vessel fuel costs in 2011 have increased from US\$550/tonne to current levels of US\$720/tonne – an increase of 30%.
- Cost of fuel for a vessel steaming is more than the cost to hire the vessel -US\$17,000/day v US\$6,500/day.
- Daily Hire rates are now around US\$6,500/day – on the back of weakening demand out of China and increasing tonnage deliveries.
- Depending on the cost of an Owners fleet the returns are now at negative returns. A sustained market at these levels will see more receiverships and bankruptcies in the shipping industry



# 2012 Forward look

- The global economy continues to experience uncertainty as the developed nations struggle with debt, unemployment and general subdued economic activity. Accordingly this financial tension and uncertainty is likely to have a negative impact on general forest product demand as construction activity is expected to remain modest across residential, commercial and infrastructure sectors
- Underlying positive growth across Asia is expected to continue albeit at more subdued levels than experienced over 2009/2010. However, due to the increasing supply of softwood log and lumber to the Asian markets and the recent imbalance of consumption, supply and inventory, it's expected that the strong demand and pricing experienced over the preceding ~2 years will ease over 2012
- Due to size and dominance in the softwood log and industrial lumber market from the Pacific Rim supply point perspective, China is expected to continue to lead the markets in 2012. As experienced in late 2011, over-supply and seasonal consumption fluctuations will create price volatility which will drive supply behavior and other market pricing
- Supply competition is likely to intensify from all Pacific Rim log and lumber producing regions with all focusing on China as the only real growth potential region (India is more considered by Australasia only). Due to ongoing relative weak domestic construction markets in source countries, the continued strong supply to China is expected to continue throughout the year
- The ability of China to consume these ongoing high levels of supply is unlikely to continue into 2012 therefore the supply/demand and inventory balance will be a significant lead indicator over the year, as experienced over Q3 and Q4 this year.
- India will continue to play a role in the demand growth albeit from a low base, however supply/demand and subsequent inventory will be a critical indicator for pricing.
- Japan and Korea are expected to remain 'followers' from a price perspective while demand is expected to remain stable

# So what for FICA members ?

- Be cautious about the 'HYPE' early in the New Year about log market recovery – it may be short lived (watch the traders and international brokers)
- There's still uncertainty around the world and China remains the power house for a lot of global demand – Europe and the US don't look good and have a long way to go
- The export markets remain in very good shape for logs and lumber and demand continues to be at record levels for NZ radiata logs – but the supply balance will remain the determining factor
- The short to medium term will see volatility
- Our time will come again:
  - Asia's demand continues to grow at 7-9% per annum (2-3M per annum)
  - ✦ USA, Canada, Australia and NZ housing starts return to 'normal' levels
  - ⇒ Wood shortage
- ***The long term looks good***