

Log Market Analysis

As at 27 February 2020



Photo 1: Hauler crew at Landing 65 in Te Hau Forest, Wairarapa. February 2020.

The content of this Log Market Analysis is produced monthly as part of a suite of documents that comprise the regular reporting to log market owners during harvest. This standalone document is made available to other forest owners approaching harvest to keep them informed on market conditions. We have prepared this February communication after a break arising from the Christmas period holidays.

We have included log price series separately for Wairarapa and Gisborne forests, as the price series differ for reasons including different customers, log specifications and locations.

Forest Enterprises (FE) is currently harvesting approximately 650,000 tonnes of logs per annum for Wairarapa and Gisborne forest owners. We now harvest and deliver a further 350,000 tonnes for a private fund manager client in the same regions.

Our harvest volume has grown with the additional client volume, but in this month, specific production levels are falling as we deal with the Covid-19 crisis.

IMPORTANT

Every effort has been made to provide current accurate information in this document, which is for information purposes only. Any opinions and views expressed are those currently held by Forest Enterprises, however the reader accepts that where they are opinions and views in respect of future prices, they may subsequently be proven incorrect. The nature of the international log market is that of price fluctuations, and these fluctuations can be material, and material changes can arise due to factors not previously able to be foreseen.

Overview

We returned from our Christmas holidays expecting that normal problems would arise and be solved as they routinely are. This year we have a new problem. A global pandemic is not something we have planned for because it's unlikely. But right now it's a lot less unlikely than usual.

In this Log Market Analysis, I will try to set out what we believe to be likely and some of the impacts we are already seeing. These are very difficult times, and everyone is suffering to some extent. Stumpage is down, payment terms are uncertain, contractors are on reduced work rates, and people are fearing for their livelihoods.

Our first duty, as always, is to manage the investment to maintain or grow value. The steps we take in this crisis are intended to preserve investment value over the long term as well as the short term.

The expectation set out by our export agents is that a reduction in log supply is necessary to settle market sentiment. The Covid-19 flu has essentially stopped sawmilling and construction in China, as well as most industrial activity. The Chinese need to get back to work and earning again and we expect to see workers in sawmills next week.

It will take time to run down the high stocks of logs in China and consequently log production levels need to stay low for weeks if not months. Some loggers can survive lower levels of production; others with high debt levels may not be able to make ends meet. We will carry on a lower level in order that when log demand firms up we can return to normal production levels. Stopping logging completely will mean that any subsequent restart programme will be very difficult and take a lot of time and expense to work through.

What we don't know is how Covid-19 will spread and when it will be contained. So, we wait, and we are cautious.



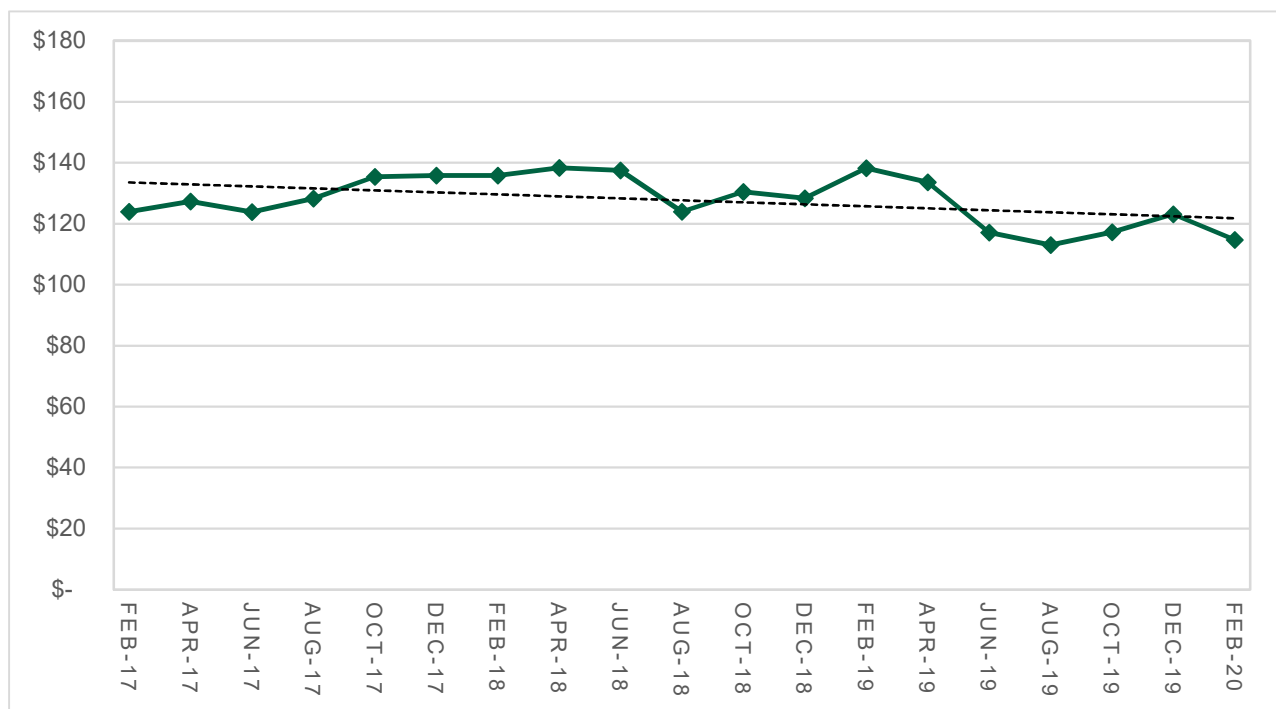
Photo 2: People in China are staying home. The Shanghai Transrapid train (the Maglev) runs between Pudong in the eastern part of the Shanghai urban area, to Pudong Airport, the main international airport in Shanghai. Usually full, the Maglev was empty mid-morning on Thursday 20 February 2020. Photo taken by a family member of Forest Enterprises staff, on their way home to NZ.



Wairarapa Log Prices Per Tonne

Grade	Forest Enterprises Feb-20	Forest Enterprises 36 Month Average	Current vs 36 Month Average	Percentage of the 36m Average
Export P40	\$160.00	\$183.30	(\$23.30)	87%
Export P30	\$125.00	\$146.10	(\$21.10)	86%
Export A	\$102.00	\$135.00	(\$33.00)	76%
Export K	\$94.50	\$119.85	(\$25.35)	79%
Export KI	\$85.00	\$112.85	(\$27.85)	75%
Export Pulp	\$78.50	\$97.75	(\$19.25)	80%
Domestic P35	\$170.00	\$175.60	(\$5.60)	97%
Domestic S30	\$117.00	\$121.15	(\$4.15)	97%
Domestic S20	\$102.00	\$106.15	(\$4.15)	96%
Domestic Pulp	\$31.00	\$31.00	\$0.00	100%
Export sales units are volumetric (JAS) while domestic sales units are paid per tonne. The Export JAS prices have been converted to tonnes. Refer to page 5 for more detail on the JAS to Tonne Conversion.				
Index Log Price	\$114.75	\$128.60	(\$13.85)	89%
Index Log Price is calculated using inventory measurements from our Wairarapa forest crops and establishing an average log grade recovery for our typical Wairarapa Forest. Applying these estimates to our long run prices per grade has derived an Index Log Price. This index price helps to estimate the average logs sales predicted for a typical forest.				

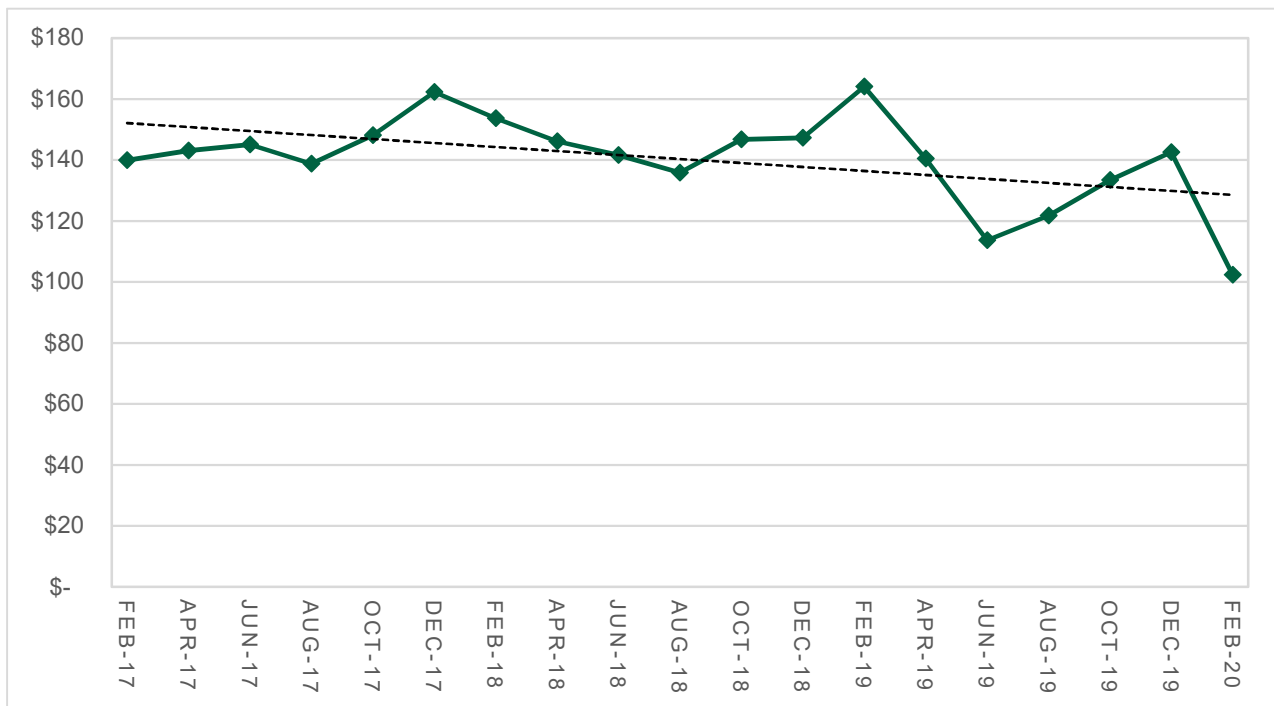
Index Log Price for our typical Wairarapa Forests



Gisborne Log Prices Per Tonne

Grade	Forest Enterprises Feb-20	Forest Enterprises 36 Month Average	Current vs 36 Month Average	Percentage of the 36m Average
Export P40	\$146.10	\$181.25	(\$35.15)	81%
Export P30	\$108.30	\$148.25	(\$39.95)	73%
Export A	\$98.20	\$140.20	(\$42.00)	70%
Export K	\$84.75	\$125.45	(\$40.70)	68%
Export KI	\$75.60	\$116.40	(\$40.80)	65%
Export Pulp	\$68.70	\$103.05	(\$34.35)	67%
Domestic P35	\$175.00	\$179.15	(\$4.15)	98%
Export sales units are volumetric (JAS) while domestic sales units are paid per tonne. The Export JAS prices have been converted to tonnes. Refer to page 5 for more detail on the JAS to Tonne Conversion.				
Index Log Price	\$102.35	\$142.05	(\$39.70)	72%
Index Log Price is calculated using inventory measurements from our Gisborne forest crops and establishing an average log grade recovery for our typical Wairarapa Forest. Applying these estimates to our long run prices per grade has derived an Index Log Price. This index price helps to estimate the average logs sales predicted for a typical forest.				

Index Log Price for our typical Gisborne Forests



The trend shown on the charts is that Gisborne returns are more volatile than in the Wairarapa. This is largely due to the smoothing influence of the relatively large domestic sawmill market in the Wairarapa. We have added domestic customers in the Gisborne region recently which will make price less volatile.



Factors Influencing Current Log Price

Key:

↑ More Benefit to the Investor

↓ Less Benefit to the Investor

↔ Neutral

Price, Costs and Logistics

↑ Foreign Exchange (Forex)

Export logs are priced in USD. FE's rate in February was forecast at 0.6550. We last shipped at a rate of 0.6335 which is in our favour. Exchange in NZD typically fall in response to commodity price falls as investors lose confidence.

FE takes no forward position or hedge in currency trading. Hedging imposes transaction costs without giving certainty of improved outcomes.

↑ Shipping

Shipping cost has fallen dramatically; unsurprising, as there is very little activity in the short term bulk freight volume forecast. Shipping cost will increase as the markets firm up in response to demand.

↑ JAS to Tonne Conversion

JAS-to-tonne conversion rates are very high with the very dry summer season, increasing to an average of 107% for all export grades during February 2020. This is a good result and improves returns to growers.

Export logs are sold in Japanese Agricultural Standard cubic metres (JAS). JAS is a measure of useable log volume rather than weight. Payments to most contractors are made based on weight, which is appropriate for handling heavy material. This means the return to the forest owner is affected strongly by the conversion of weight to volume in the logs.

Conversion has seasonal trends and varies between log grades, length and log quality. Accounting for conversion is necessary to report comparable values from different sales options. Our convention is to report all prices converted to the 'per tonne basis', which would appear different if compared with a per cubic metre (JAS) series. Hence why our harvest reports show monthly JAS/tonne conversion per forest.

↓ Log Price, Export CFR

CFR (Cost and Freight) is the price in USD paid by the end user/buyer.

China Rapid price falls, little or no current log usage.

South Korea Low price and demand. Better than China but volume constrained.

India Taking some overflow from China, though with limited ability to take any more volume.

Japan Relative to China, Japan looking not as bad; imported lumber price falling, stocks quite high.

Log Demand

↓ Export Log Inventory in Market

China Inventory of logs in China is a leading supply/price indicator. Inventory levels in China are growing as log ships continue to arrive and has been estimated at about 6 million JAS. Daily sales is being variously reported as 3000, or up to 20,000 JAS per day, but essentially very little. Days of stock is inventory divided by usage and can't be measured easily, but is more than 3 months normal supply and is regarded as very high. The speed that logs turn to lumber and lumber turns to cash drives market sentiment. European spruce lumber represents additional stock in inventory above the conventional metrics but this supply has stopped as the containers used spruce for return loads to china are no longer leaving China loaded for Europe.

South Korea Flat and slow.

India Probable oversupply.

Japan Some relief from imported lumber freeing up milling of imported NZ logs.

↑ Pruned Log Grades

No change; plenty of demand for pruned logs.



↔ NZ Domestic

Local sawmills still need logs and are buying from us at normal rates. We have secured more business in Kawarau and Putaruru for mill and pruned logs which reduces our reliance on the Gisborne export port. Sawmills do rely in part on export options for lumber though, so there is a relationship there to watch.

↔ Housing and Business

Housing drives panel, lumber and furniture sales and therefore log demand. Housing timber use has two primary markets: new house starts, or remodel and renovate. These two uses have different cycles based on relative consumer optimism. Construction in China stopped over Chinese Lunar New Year holiday and has not restarted for over 4 weeks now due to Covid-19 quarantine issues.

↑ Domestic Construction

Not enough low-cost houses being built.

Log Supply

NZ

Woodlot logging stopped largely; corporate forests operating at about 60-70% capacity. NZ total perhaps 50% of normal.

Australia

Fire salvage operations take priority; very little being exported.

Europe and Russia

The European beetle damage remains a concern for the Europeans. But the transport links carrying spruce into China have stopped so lumber is currently moving very slowly out of Europe.

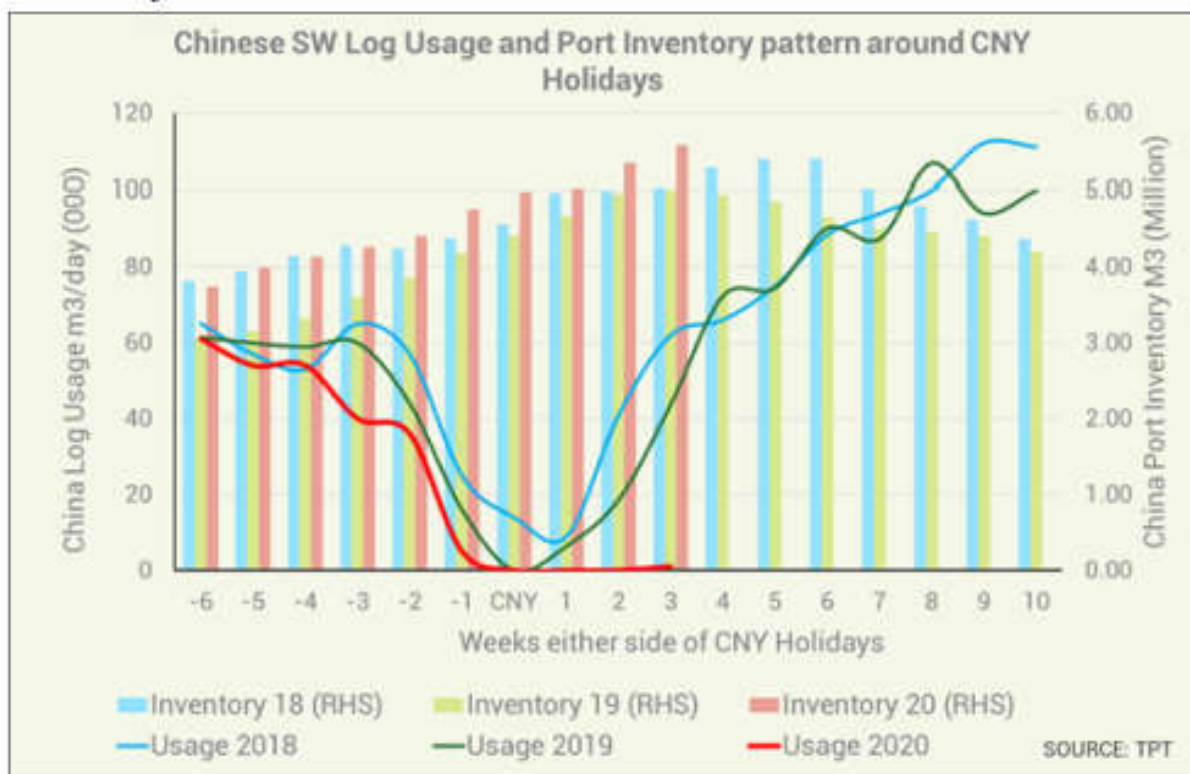
Pacific Northwest (PNW)

President Trump reduced the US China trade balance so the US business is now internally focussed.

Other

Uruguay now regular exporter to India, low margin business.

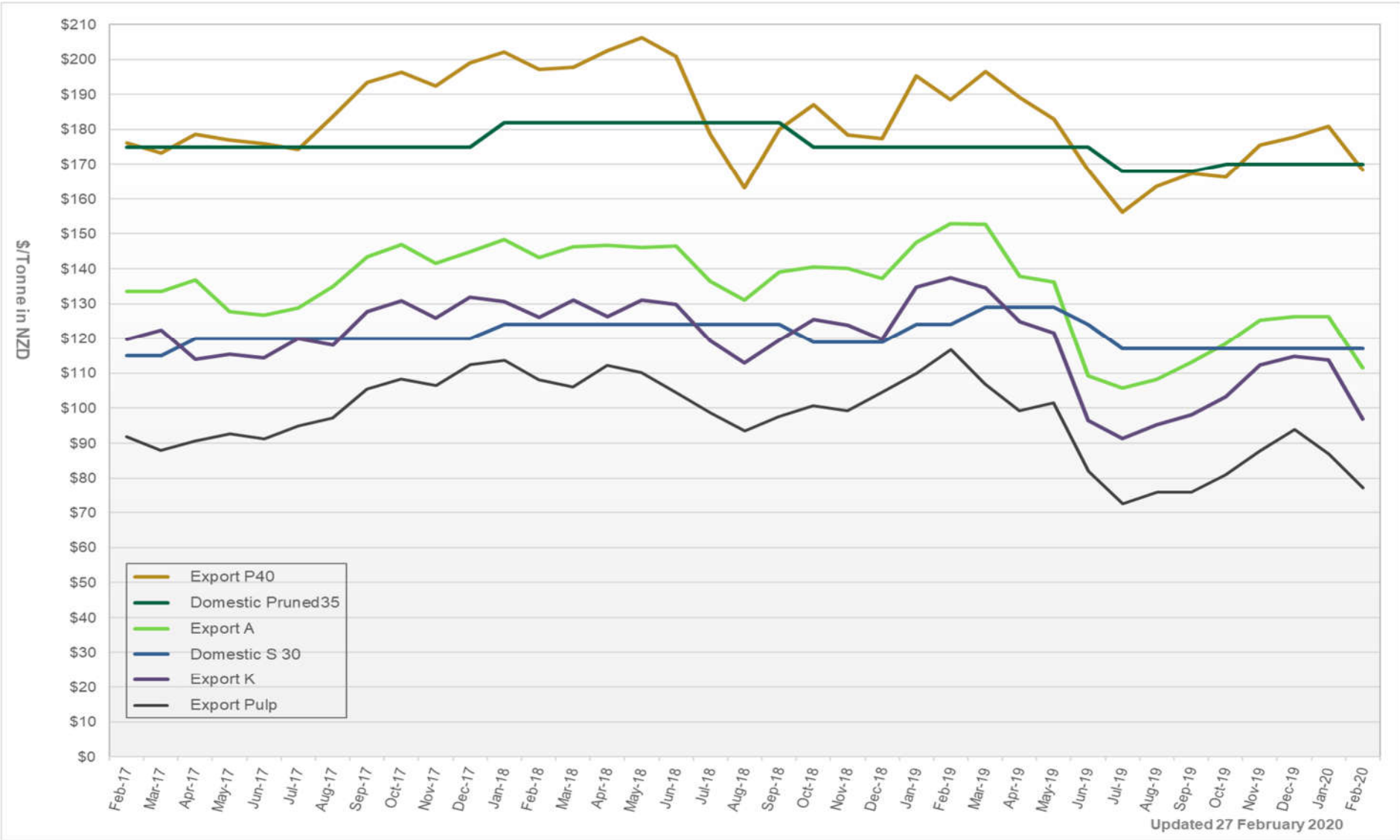
Point of Interest



Graph supplied by TPT Forests, our log export partner out of Port of Wellington.



Lower North Island Log Price Graph per Tonne



Log Price Graph: Tracks the key log prices for a 37-month period. The first 36 months are the months which comprise the average referred to under Log Prices per Tonne above. The 37th month shows the indicative prices scheduled for the current month. Export sales units are volumetric (JAS) while domestic sales units are paid per tonne. The Export JAS prices have been converted to tonnes.



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Our forests are a renewable resource offering real returns to investors
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For our latest forest investment opportunities, contact us
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Creating wealth Naturally

