

## Mortgage meltdowns, monsoons and shipping costs impact tropical timber in last quarter of 2007 and early 2008

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**P**RICES OF LOGS, sawnwood and plywood in many countries were impacted by the sub-prime mortgage crisis beginning in the us and spreading to other regions. In December 2007, housing starts in the us fell 14% from November 2007 levels, hitting a 16-year low. In August 2007, Japan housing starts dropped 43% lower than August 2006 levels and the lows continued through the second half of 2007. After seeing gains immediately after the first half of the year, prices for many Malaysian and Indonesian species fell as international markets became more volatile. Prices were further affected by the monsoon season in October and November, which limited availability of logs. Despite these impacts on demand and prices, some countries such as China showed strong results in the second half.

### Housing starts slow

us sub-prime mortgage losses significantly impacted the us housing market in 2007 (Figure 1). Some experts expected a further drop in housing starts in 2008. us housing projections for 2007 were estimated at 1.354 million units. Analysts speculated that the us economy was headed for a recession, which would impact housing and financial markets overseas. The decline in the us housing market was also causing demand for wood-based panels to drop (especially Oriented Strand Board), with panel producers scaling down, delaying their growth plans or canceling new mill construction altogether. Experts noted that as the us housing crisis worsened, there would be further deterioration in homebuilding and buying, which would impact markets for hardwood products. This, coupled with the falling value of the us dollar, has continued to impact the global hardwood market in early 2008.

Japan's housing starts and panel imports also plunged in the second half of 2007 (Figure 2). Analysts suggested the main reason for the drop in housing starts was due to confusion associated with new application procedures for building approval enacted in June 2007. Plywood imports fell with housing starts and also as a result of Japan's increasing reliance on domestic sources for plywood materials and the

rising costs of imported raw materials (Figure 3). Plywood continued to be imported at low levels until the end of 2007 due to continued weak demand. The Japanese yen was also appreciating during this time, weakening market prices for certain types of logs. Imports of Southsea logs from January to September 2007 were 828 450 m<sup>3</sup> and total 2007 imports of tropical logs were likely to be the lowest in many years. Lumber imports dropped 15.1% in volume, mainly due to declining hardwood imports with softwood lumber sustaining the previous year's levels of imports.

The uk housing market also appears set for a correction. House sales stalled in late 2007 due to the credit squeeze and as a result of the Christmas holidays. House building also slowed and experts anticipated that housing price inflation in 2008 would reach near zero levels.

Europe showed a renewed interest in certain species from West Africa in late 2007, including iroko, afrormosia, azobe, douka and sapele. Prices rose for sapele sawnwood imported by eu countries, as Congo and Central African Republic reduced their supply of logs and Congo and Gabon worked to implement their log export quotas.

Freight rate changes also impacted timber prices (Figure 4). The London-based Far East Freight Conference (FEFC) enacted higher freight rates to major Asian ports effective 1 October 2007. Under the new system, once additional surcharges were added, shipping costs in 40-foot containers had in some cases increased by us\$700 per container. Higher freight rates impacted prices for okoume and redwood logs in West Africa. The higher freight costs had temporarily halted purchases of lesser used species in West Africa and traders were more focused on okoume and other premium timbers shipped in smaller vessels.

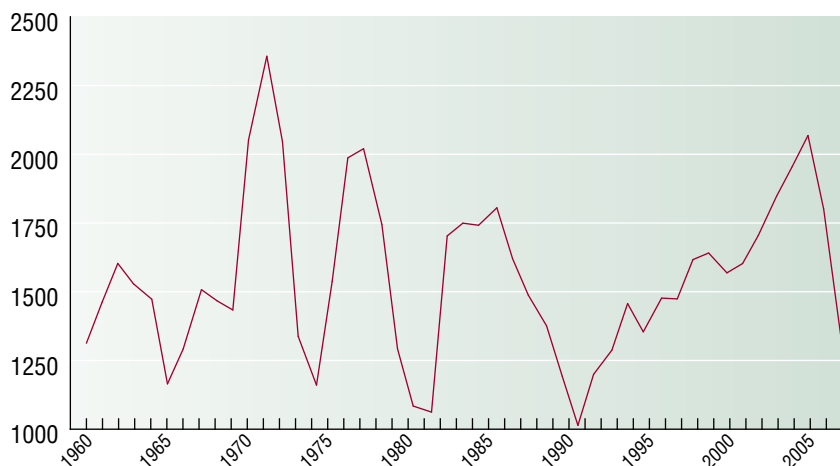
From June to October 2007, Indonesian and Malaysian prices for logs and sawnwood rose and many analysts expected the positive trend to continue. However, prices for Indonesian plywood and peeler logs dropped at the start of the monsoon season in October. Malaysian prices for sawn timber and logs rose modestly in the second half due to the monsoons, which limited availability of fresh logs (Figure 5). The monsoon season also affected areas of Northern Congo and the Central African Republic, which struggled to obtain raw material in the wet conditions.

### China continues to shine

Despite the volatility in global markets, China continued to show strong growth during the second half of 2007. Chinese experts estimated that the total value of China's wooden door output would exceed RMB 40 billion (us\$5.4 billion) by the end of 2007, with the value of wooden door exports reaching us\$700 million. Wooden furniture imports and exports grew 10.5% during the first three quarters of 2007 from the same period in 2006, with the total export value of wooden furniture (us\$4.78 billion) rising 4.5% from the same period in 2006. During the first three quarters of 2007,

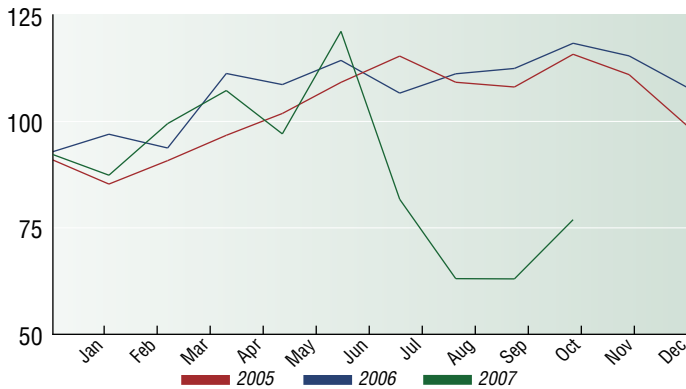
### On the way down

Figure 1: US housing starts, 1960–2007



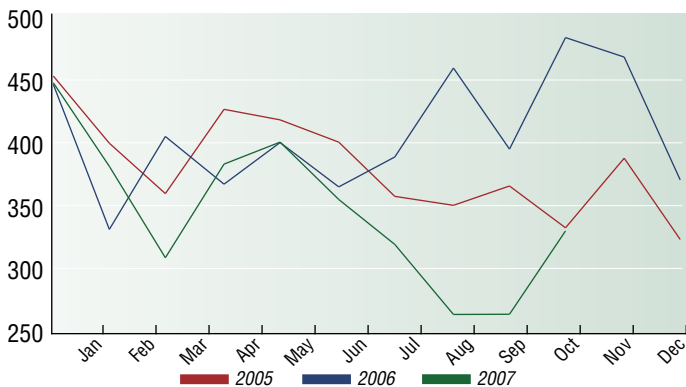
## Summer doldrums

Figure 2: Japan monthly housing starts ('000 units, 2005–07)



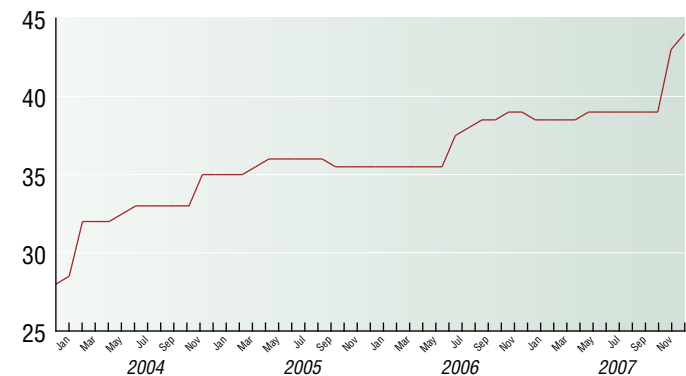
## Volatile

Figure 3: Japan monthly plywood imports (m<sup>3</sup>, 2005–07)



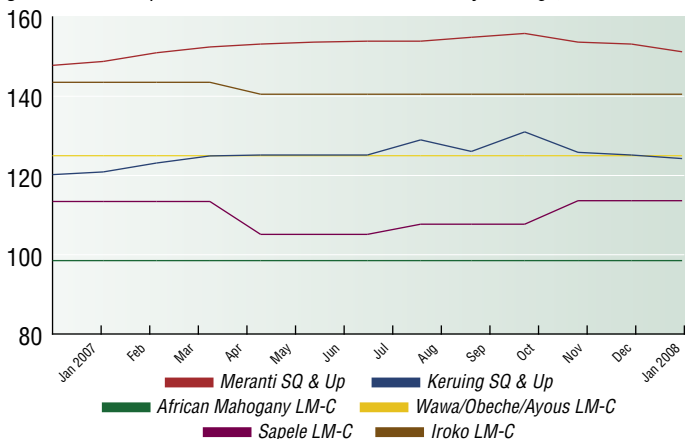
## Shipping up

Figure 4: Sarawak to Tokyo ocean freight rates, 2004–07



## Logs steady

Figure 5: Selected price trends for West African and Malaysian logs, 2007



the total value of China's major wood products imports and exports rose 31.9% to US\$42.43 billion.

## Other exporters mixed

During the second half of 2007, however, results from other regions were less positive. Reports from Brazil indicated that the forest sector was contributing less to the state of Para's GDP, in part due to the slowing approval of forest management plans. Other Brazilian reports also drew attention to the increasing amount of illegal log transport, due partly to a lack of military police to conduct inspections on logging trucks.

In November 2007, exports of Brazilian wood products (excluding pulp and paper) increased 2.7% compared to the same month last year, growing in value from US\$344.8 million to \$353.9 million. The price of elliotis pine plywood also slumped in the second half, due to the uncertainty surrounding the us dollar and corresponding changes in plywood prices. During the second half, the price of pine plywood in the us was nearly 10% lower than in Europe (pine plywood prices in Europe have traditionally been lower than those in the us).

In other areas of South America, Guyana's forest products exports increased 3% in volume, or by approximately US\$2 million when compared to 2006. Total value of forest products exports for 2007 was US\$61.5 million. Sawn timber, round logs and plywood accounted for the bulk of the products exported. Other important exported products included garden furniture, shingles and doors.

Bolivia's wood exports slowed due to fuel scarcity during the period of August to September 2007. There were problems with fuel supplies in the autumn, which at times cut Bolivian companies' production capacity in half. Nevertheless, it was estimated that Bolivia's wood exports reached US\$115 million in value in 2007, a 10% increase compared to 2006. High-value added products accounted for 62.5% of total wood exports in 2007, compared to 55.5% in 2006.

Due to the response of the Myanmar government to civil unrest in 2007, the EU imposed (and the us strengthened existing) bans on timber from Myanmar and restrictions on other investments. Prior to the EU announcement, Myanmar log prices slumped in late September/early October. When the EU ban was implemented in mid-October, it prohibited European imports of logs from Myanmar and prevented European companies from providing machinery to and investments in Myanmar timber companies. In late December, the us Senate approved the Burma Democracy Promotion Act, outlawing the import of Myanmar timber by the us. Despite these actions, demand for Myanmar's natural teak remained strong, with prices rising for higher grades in December 2007, while prices for lower grades declined.

At the close of 2007, tropical timber trade slowed due to the Christmas and New Year's holidays in most markets. The holiday season and economic conditions (including increasing transport costs) continued to slow tropical timber demand in most markets into the first quarter of 2008.