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April 2023 Market Update

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Opinion Piece

Sometimes things seem too good to be true and the March export log prices were a perfect example of this phenomenon. March price increases saw A-Grade export push through $140/m3 which gave us a similar euphoric feeling to that which Chris Hipkins would have had immediately after getting the top job. However, this feeling was short lived after April's offerings dropped around $20/JAS into the mid $120's/m3, much lower than we all expected, resulting in a general feeling of queasiness, similar to how the newly minted Prime Minister would have felt once he had realised what he had inherited.

This price drop was driven by a number of factors and the current situation is still in a state of flux as many exporters still don't really know which way the market will head in the next few months. China pricing is very sentiment based and if you sit back and look at the fundamentals, the March prices were probably pushed too hard in the upwards direction in the face of static demand and very average Chinese economic data. On port softwood log inventories in China have been reducing nicely since the beginning of the year and are at what is considered as a low level of around 3.7Mm3 which is around 50 days' supply. It appears that some exporters have been talking up the supply levels from NZ as a result of the cyclones which has led customers to believe that supply will increase rather than decrease. It's hard to see that own goal playing out as the supply into the affected ports of Napier and Gisborne are still stilling around 70% and it's unlikely that Gisborne will be back to full deliveries this quarter.

The salvage of the 6,000ha of wind damage in the Taupo region has started and the clock is ticking on the viability of this volume in meeting the export phytosanitary requirements. Quick cigarette packet numbers would indicate a supply hole of between 300,000 and 400,000m3 over the past few months due to the cyclone and, due to the 5–6-week timeframe from stump to market, this hole will only be coming to fruition in China now. Even if we could significantly ramp up harvest levels in the wind damaged regions, there is only a limited number of log trucks in the system. The cyclone flooded a chunk of the Hawkes Bay trucking fleet and it's not like we can go to the truck supermarket to get any more. Kiwirail has been doing its best to reduce their scale by increasing rail rates to a point that in some regions, rail is 15-20% higher cost than trucking. The net result of this is less volume on rail and more on trucks which stretches the truck fleet further and reduces our ability to react to supply increases. Any increased road freight component only compounds delivery efficiency as ports get congested, truck wait times increase and the number of loads a truck can complete per day reduces.

A quick glance at the following graph would think it was measuring a drug addicts' pulse rate, but unfortunately, it's the export log price over the past 12 years. While there was a period where we went into rehab between late 2015 and early 2019 and things ticked over nicely, the rest of the time has been one hell of a trip. If this makes you wonder how you can run a business that relies on China for around 55% of its demand, you'd be right. While larger forest owners can play the long-term averages game, smaller forest and woodlot owners have a much higher exposure to short term price fluctuations and trying to line your harvest up with the market is about as opportunistic as catching the Interislander.

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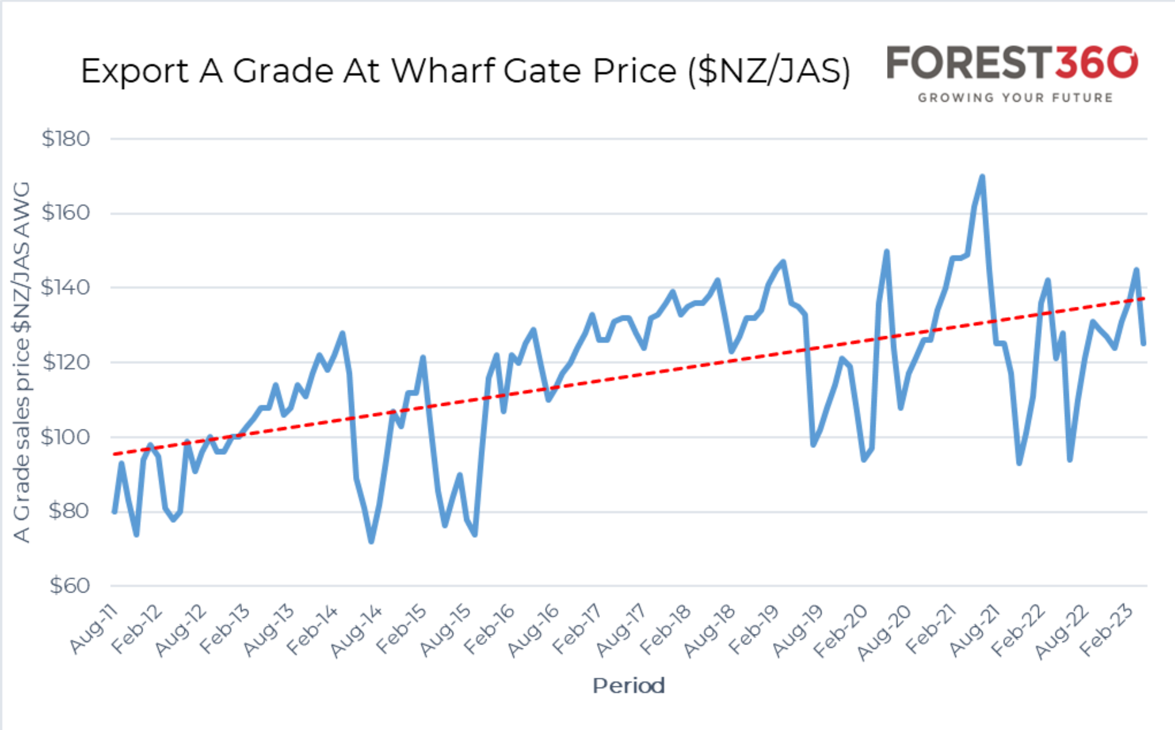

This is where the Government's Industry Transformation Plan comes into play as the more volume we can remove from the export supply chain, the more stability we can expect in pricing. Probably the quickest wins we can get as an industry is throwing the lower grade export logs down the chipper to provide fuel for industrial heat requirements. Most industrial heat requirements are fueled by coal and gas which are the Putin of climate change. Broad brush estimates are that the average large agricultural processing plant (milk and meat processors) has an annual energy demand of around 2 million gigajoules. This energy demand converts into around 210,000 green tonnes of woodchips/logs per plant if they converted solely to wood-based fuel.

It would only take one of these plants in each provincial region to convert to wood-based fuel to utilize the majority of the lower grade export logs (Ki and KIS) therefore removing around 15% of the total export log supply. It doesn't take a rocket scientist to realise that there are generally more than one of these plants in each region and once the decision to switch to wood-based fuel is made, there will be a lack of available supply. We all know how the supply and demand graph works in terms of price. The viability and speed of these conversions sits around the carbon price and the external pressures of the processing plants customers around demand for carbon neutrality; however, the smarter operators should see the writing on the wall and move lock up the fuel supply first.

The next few months will be interesting to see what the actual supply situation is into China. There's very little argument that the Chinese economy has the medium-term buoyancy of the Titanic and there's little chance of a significant increase in real log demand in the next few months. We had pinned hopes on a China rebound post covid with various stimulus packages announced but to date there hasn't been a corresponding increase in housing demand. Should supply reductions eventuate in the next few weeks there may be an opportunity of upwards price pressure but at this point it's a waiting game.

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