WOOD MARKETS MONTHLY
AUGUST 2020

Forest Economic Advisors

MENA MARKET OVERVIEW

UPDATE ON EUROPE'S LARGEST EXPORT REGION

The Middle East/North Africa (MENA) region is an economically diverse area that includes both the oil-rich economies in the Gulf and countries that are resource-scarce in relation to population, e.g., Egypt and Morocco. While the countries comprising MENA may seem similar culturally, the use of timber varies across the region. Each country has its own particularities with regard to how their construction companies employ softwood.

Following macroeconomic and political development in the MENA countries, sawn softwood imports to the region have tended to fluctuate near 12 million m^3 per year, sourced largely from Europe. To track the trend, it is vital to keep a close watch on the political and economic situation in Egypt, Saudi Arabia, Algeria, Morocco, and the UAE. Together, these five countries account for more than 70% of the total volume imported into MENA. Out of these five countries, only one—Egypt—remains a key market: when Egypt does well, softwood imports to the MENA region do well.

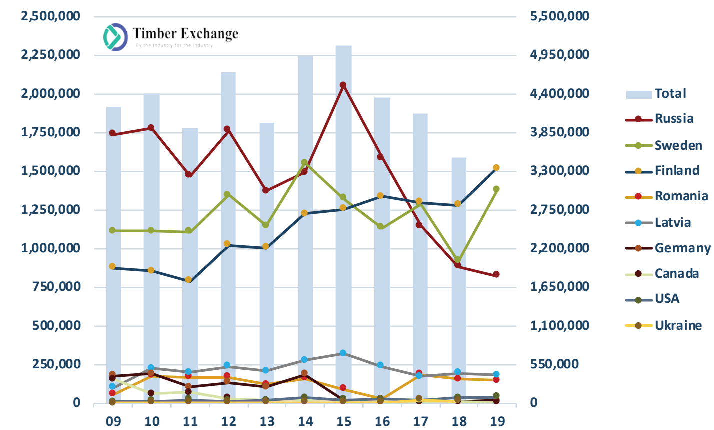
The World Bank expects MENA's economic growth to continue at a modest pace of about 1.5–3.5% for the period 2019–21, a fraction of what is needed to create enough jobs for the fast-growing working-age population. Even in those few countries that have enjoyed periods of higher growth, poverty failed to decline; this suggests a need for reforms to instill fair competition and promote inclusive growth.

EGYPT

Egypt is the most populated country in MENA, with a population of ~104 million and GDP that is expected to grow by 2% in 2020. Egypt had been on a path to recovery and showed steady increases from 2017 to 2019, but it is now likely to have its growth cut in half due to COVID-19.

With a young population, a diversified economy, many different industries, and a strategic location on the Suez Canal, it is no wonder the country is one of the largest timber importers in the world. Egypt possesses a true ecosystem and traditions around wood that are employed by the country's many small and medium-sized companies. Egypt is among the world's largest markets, importers and users of softwood. Russian and Scandinavian redwood (pine) and whitewood (spruce) are the major types of softwood lumber imported, and softwood consumption is divided into 75% redwood/25% whitewood.

FIGURE 1 Egypt: Annual Timber Imported Volume (m^3)



Egypt's overall timber imports have been in a downward trend since 2015, due primarily to a decline in exports from Russia (now down to a 23% market share). A new trend has emerged in the region: increased timber coming from Finland. Shipping primarily pine, Finland competes directly with Sweden and Russia. In 2020Q1, Sweden and Finland collectively exported 648,685 m^3, some 22% of their total 2019 exports to Egypt.

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Egypt's housing market is one of the best-performing markets in MENA. To support its growing population, the government plans to target more than one million homes for low-income households by 2024; already, 287,600 units have been established in the state's social housing program. The World Bank has also announced US$500 million to support efforts to improve housing affordability for low-income households, with subsidies recently increased by 31%. However, due to COVID-19, demand has declined as a result of reduced cash flow and an attendant slowdown in construction activity. There are also credit issues in the market that have forced importers to lower prices in order to clear inventory. This is being accentuated by high inventories, a situation expected to last at least six months due to the slowdown in consumption.

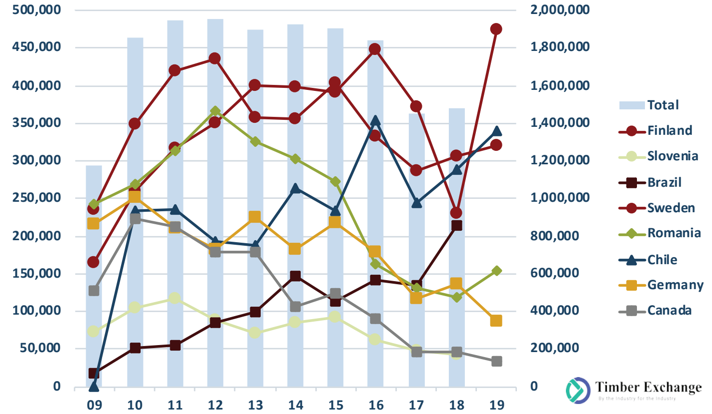
In terms of other construction activity, there is a push by the government to finish pending projects. As a result, private sector building has been halted in four governates, including Cairo and Alexandria, for a period of six months. This impacts consumption of *schaalboard* (side boards of standard thickness and 75–125mm in width) and *fillery* (used mainly in scaffolding construction). It should be noted that most of the large-scale and state construction projects use steel and plywood, so timber might not be as highly impacted due to its low demand. On the other hand, inner-city, small-scale, and illegal market construction all rely heavily on timber.

SAUDI ARABIA

Saudi Arabia is diversifying its economy in an effort to free itself from oil dependency. To support this strategy, the country is combining government spending cuts with a major change in economic focus that includes investing massively in green energy and opening the country to foreign investors. To limit its budget spending, the government has introduced austerity measures and, in 2018, imposed a value-added tax on selected items. As a result of these changes, the construction sector is quite slow. Saudi Arabia imports around 1.5 million m^3 of timber each year. In recent years, Finland, Sweden, and Chile have been its major suppliers, while traditional suppliers such as Romania and Canada have decreased their market presences. In 2020Q1, Sweden and Finland collectively exported 187,309 m^3, approximately 24% of their total 2019 exports to Saudi Arabia.

FIGURE 2

Saudi Arabia: Annual Timber Imported Volume (m^3)



COVID-19 has taken a toll on the Saudi timber market. The country is contending with above-normal stock levels due to the plunge in consumption, but overall demand is stable at present and has not fallen sharply; in addition, there is an expectation of reasonable demand in the coming months for whitewood sideboards for construction, and higher consumption is anticipated by the end of the year as activity picks up. This is helped by the fact that there are no credit issues in the market at the present time and conditions are considered relatively normal.

As a result of COVID-19, government ministries have been instructed to cut spending by 20%. Since the cuts affect mostly capital expenditure and new projects, the move has had a marked impact on the construction industry. A series of government-backed "giga-projects" that had been poised to move into the construction phase at the start of this year have been affected, a situation exacerbated by prevailing labour shortages. In 2019, there were 5,200 construction projects with a value of US$819 billion, some of which may now face suspension or cancellation due to the pandemic.

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There have been factory closures and a decline in tourism and retail activity in Saudi Arabia as well. To cope with the loss of tax revenue, the country tripled its value-added tax rate from 5% to 15% starting in July. This is expected to increase revenue by US$27 billion amid plummeting oil prices.

The GDP of Saudi Arabia grew by 0.5% in 2019 versus the previous year. It is expected to fall to 2.3% in 2020 and then rise in 2021 to 2.9%. The Kingdom has seen its revenues drop by 22%, with the deficit reaching US$9 billion as crude exports decreased to 6.82 million barrels per day in 2019 (the lowest level since 2010).

Acting on its vision to revitalize the economy and eliminate its oil dependency by 2030, Saudi Arabia is working on several giga-projects:

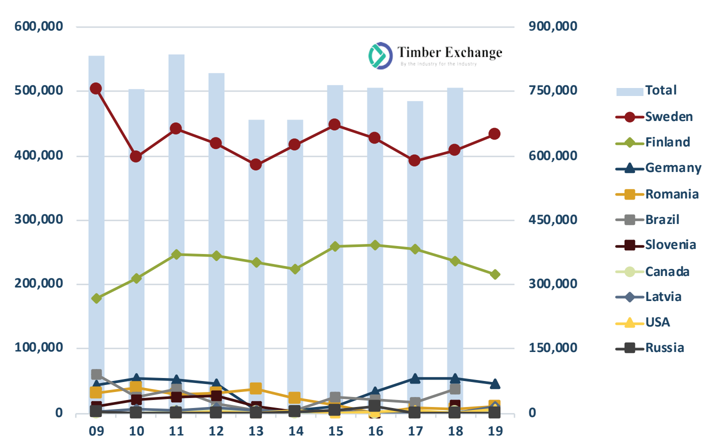
- Construction of 19 hospitals and 500 schools and universities with a value of US$85 billion.
- Al Faisaliya City, at US$25 billion, to be developed in seven phases between 2030 and 2050.
- KAEC, an industrial and logistics hub costing US$100 billion and due in 2035.
- NEOM, to be the world's first "smart city" and costing US$500 billion; reportedly, construction has already begun.
- Jeddah Economic City, a financial hub in the western region and a cornerstone of the 2030 vision for a tourism and wellness destination that will attract visitors from all over the world.
- Qiddiya, an entertainment city (large theme park), due for completion in 2022; at 340 square kilometres in area, it will be 15 times the size of Disneyland Paris!
- The Red Sea Project, which will cover 28,000 square kilometres in total (including 200 kilometres of coastline).
- A Red Sea luxury development project called AMAALA, targeted to create an all-new concept for ultra-luxury tourism that focuses on wellness, healthy living, and meditation.

MOROCCO

Morocco's economic growth has been on a downward trend for the last two years. GDP growth decelerated sharply in 2019, dropping to 2.2% (from 3% in 2018), driven mainly by a contraction in agricultural output of 5.4% and modest non-agricultural GDP growth of 3.3%. The COVID-19 pandemic is expected to impact the Moroccan economy negatively in the medium term, with the economy also expected to suffer a recession this year (its first in more than two decades).

FIGURE 3

Morocco: Annual Timber Imported Volume (m³)



With the exception of a downward trend between 2011 and 2013, Morocco's annual timber exports have remained steady. If we look at the overall timber market, sales have been negative since March due to the pandemic. In March and April, market demand fell by 30% and 70%, respectively, on already extremely low demand due to reduced consumption (that has led to high inventories). Consumption is anticipated to improve after September/October, with the pallet sector the only one showing stability at present.

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In the housing sector, Morocco's housing market is declining sharply amid slowing economic growth. Property prices are now beginning a gradual decline and transactions are plummeting, with the mortgage market shrinking continuously. Plans are to build about 100,000 homes per year; this is some 40,000 below the actual annual demand level of 140,000. In May 2017, the government announced its intention to build 800,000 housing units by 2022; however, due to COVID-19, National Federation of Builders and Public Works (FNBTP) turnover has fallen by 75%, leading builders to ask for government assistance to revive the sector (in the form of a stimulus package).

ALGERIA

Algeria faces the same challenge as Saudi Arabia as it similarly seeks to diversify its economy away from oil dependency. The Algerian government made the decision to implement some heavy import limits, as well as freeze projects and increase taxes. Once a promising market, Algeria has been going through tough economic times in recent years due to political instability. The country has relied almost entirely on oil and gas exports to finance an ambitious infrastructure investment program. Now, with oil and natural gas accounting for 95% of export revenues and 60% of total government revenues and driving economic growth, declining oil prices have severely hurt government finances.

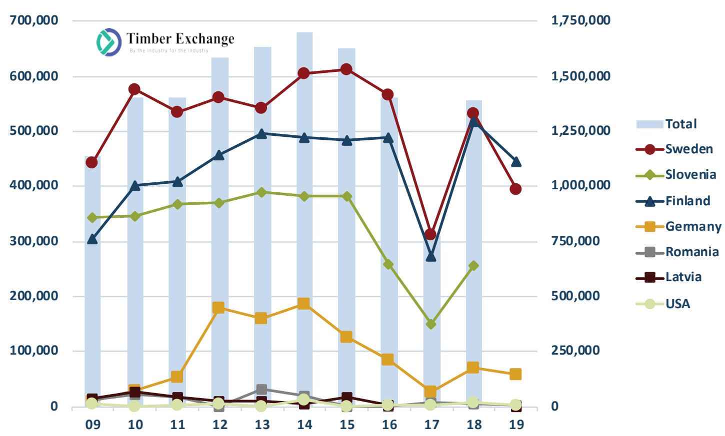
If we look at GDP figures, the Algerian economy is forecast to contract in 2020 due to subdued domestic demand on a pandemic-related faltering of private consumption. Given the ongoing political tensions, volatile oil prices and diminished global demand are key risks to exports. The growth seen during 2018 was driven mainly by the recovering oil and gas sector.

In 2020Q1, Sweden and Finland collectively exported 176,831 m^3 to Algeria, approximately 21% of their 2019 volume. Spruce (whitewood), imported mostly from Germany and Slovenia (from its port in Koper), are used mainly in construction for concrete forming, i.e., in the early stages of construction.

Some industry participants fear the government could reintroduce a licence quota on timber imports similar to what was imposed on cars, cement and steel rebar in March. In the case of cement, imports were limited to 1 million tonnes per year even though annual demand is some 3 million tonnes. Since local cement factories were not efficient enough to fill the gap, reduced cement imports have meant that the country will require less spruce lumber for concrete shuttering. Timber exporters had accumulated heavy volumes in the port of Koper in the hope of shipping it to Algeria. However, with pressure to sell quickly at a time of scant demand, prices had to be discounted.

FIGURE 4

Algeria: Annual Timber Imported Volume (m^3)



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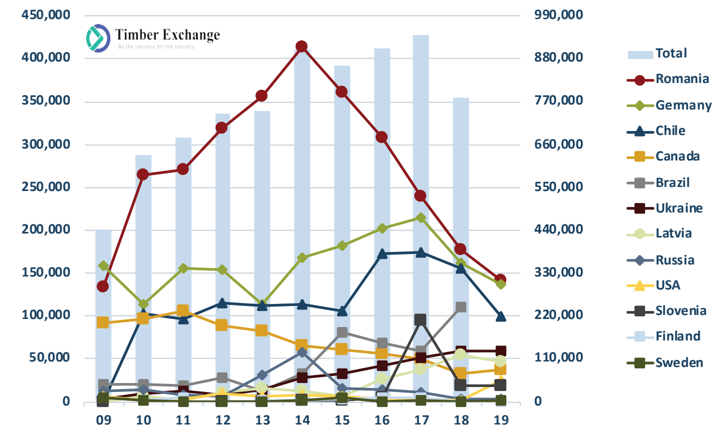
UNITED ARAB EMIRATES

The wood industry in the United Arab Emirates (UAE) had been expected to boom over the next two years as the country ramped up construction activities ahead of Expo 2020 in Dubai. Now, given the COVID-19 situation and postponement of the Expo, the market is in downturn. The UAE's GDP declined in 2019 to 1.3%. Further contraction is anticipated in 2020, mainly as a result of both the oil and non-oil sectors shrinking amid dissipating global demand (due also to COVID-19).

FIGURE 5

UAE: Annual Timber Imported Volume (m³)



The UAE had seen a rising level of timber imports until recently, notwithstanding the fact that its major importing partner, Romania, has been recording constant declines since 2015. Other major partners, such as Germany and Chile, saw contractions in timber exports in 2019; this was a departure from steady increases in previous years. In terms of the overall timber market, demand is currently reported as "weak," with contracts supposedly on hold as major projects are mothballed due to the coronavirus. Consumption is also weak at 25% of normal activity. In addition, the credit situation in the UAE market is unclear. Unstable conditions caused by the reduction in demand have led to high inventories, a state of affairs expected to last until September.

Due to the halt in major projects, construction activity is currently at only 30% of capacity in the UAE. With many engineers and labourers having become infected with the coronavirus, municipalities have been forced to close several construction sites.

In terms of ongoing work, Dubai developers are endeavoring to complete more than 300 property projects and 90,000 housing units. Some 40% of these homes are under construction and likely to be completed this year. A major concern, however, is housing affordability: only 20% of all homes are deemed "affordable," whereas demand is around 40%.

By Amir Rashad, CEO, Timber.Exchange, Sweden (www.timber.exchange). Adapted from a presentation at the 10th Annual Global Log & Lumber Conference, held virtually on June 18, 2020

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