FORESTRY & FOREST PRODUCTS INDUSTRY OUTLOOK FOR 2020

1. ECONOMIC ENVIRONMENT’S IMPACT ON THE FOREST SECTOR

1. LOCAL ECONOMY
The South African economy has significantly underperformed its peers for at least a decade. Low GDP growth rates, increasing unemployment, low levels of investment, burgeoning Government debt, the fall out from the State Capture project and the increasing likelihood of a further ratings downgrade. Despite this, the Government seems incapable of making the necessary structural reforms needed to improve growth for fear of upsetting its alliance partners. It would appear that there is no end in sight and that these unfavourable conditions will prevail throughout 2020.

This unfavourable economic climate has had a severe impact on the SA Forest sector, in particular the Sawmilling Industry, Mining Timber Industry and the Pole treating Industry i.e. those Industries that the dependant on the local market for the sale of their products.

2. GLOBAL ECONOMY
The South African economy has not been isolated from the events taking place in the global economy and the uncertainty that these are creating. Most important of these are the ongoing US / China “Trade War” and BREXIT. The former issue has, in particular, had a significant impact on the Pulp and Paper and Woodchip Industries which are very much export focused Industries. Prices, in dollar terms, have fallen significantly (up to 25%) which, despite the depreciation of the Rand, has and will continue to put enormous pressure on local pulpwood prices, thereby negatively affecting growers of this product. It is likely that unless the threat of an all-out trade war is resolved, this negative situation could well continue throughout 2020.

2. FORESTRY INDUSTRY

1. Developments in 2020
• On a positive note, the Industry looks like it will rebound slightly from its low point (from a production point of view) as the demand for pulpwood (60% of the market) appears to have turned the corner. Other positive developments include the introduction of a new certification scheme (PEFC) in 2019. This will hopefully lead to an increased number of small and medium-scale growers practising sustainable forest management and a likely improvement in the Industry’s transformation credentials and agreements reached with Government which should ease the issuing of water use licences.
• On the negative side, there are a few overall developments which could cause problems during 2020. These are as follows:
➢ The implementation of the National Minimum wage on 1 May 2018. This has put added pressure on growers to possibly increase the mechanisation of their operations further which would not be good from a socio-economic perspective but as labour costs increase, makes increasing economic sense.

➢ Continuing uncertainty surrounding the land reform process (e.g. possible implementation of land ceilings, foreign ownership of land, expropriation and the chaos brought about by the re-opening of the land claims window). With regards to EWC, the Industry does not, however, see this as a current threat.

➢ The continual threat from forest pests and diseases.

➢ Increased incidents of the theft of timber and equipment.

➢ The increased planting of avocados and macadamia nuts on forestry land thereby reducing the plantation area further.

• In addition to the abovementioned, the impact of the fires in the Southern Cape that occurred in July 2017 and in September the following year by another devastating fire in the same area needs special mention as its affects will be felt for many years to come in that it will have a profound impact on the long-term supply of sawlogs and in fact, the sustainability of the Industry and associated value chain in this region. The former DAFF / now DEFF has, since the first fires, not come to the party with regards to the funding / assistance to replant those areas burnt nor to fund the re capitalisation of the “V-Con” areas (20 000 ha of plantations that were originally earmarked as part of the exit area of 40 000 ha but are now to remain in production).

• In terms of the conditions attached to the issuing of water use licences and the issue of what is the definition of “Existing Lawful Use” in terms of the National Water Act” are two stumbling blocks to further afforestation which need to be resolved between the Industry and the Department of Human Settlements, Water and Sanitation. At least the implementation of the Presidential Public Private Growth Initiative (PPGI) in 2019 has led to significant progress to resolve this stumbling block.

2. Production Outlook for 2020

• Pulpwood production is expected to increase during 2020 as a result of the increased dissolving pulp capacity installed at Saicccor (eventually by 400 000 tons by 2022) which will lead to increased demand for hardwood pulpwood. Softwood pulpwood production is expected to decrease as the shift towards hardwood pulpwood (driven by the mills), continues apace.

• Sawlog production is driven by local demand, primarily for housing applications. As the housing construction Industry is static at best (or decreasing) we could see sawlog production either remain static or in fact decrease slightly. However, due to the fires in the Southern Cape in 2017 & 2018, production there initially spiked but has now levelled off but at far lower levels than prior to 2017. This will remain at this subdued level during 2020. The situation in the rest of the country should also remain as is, with a slight shortage of larger logs (C&D) but an over-supply of smaller logs (A&B).

• Mining Timber production is likely to see a continued decrease as demand for mining timber from the mining industry continues to decrease.

• Pole production is expected to remain static or even fall slightly due to drop in demand from Eskom and the building Industry.
3. **Price Outlook for 2020**
   - **Pulpwood** prices, which are determined by international “pulp prices”, will be under severe potential downward pressure due to the significant drop in the US$ price of all grades of pulp during 2019 (+/- 25%).
   - **Sawlog** prices are expected to increase by between 4% and 5%.
   - **Pole** prices are expected to remain unchanged.
   - **Mining timber** prices are expected to increase less than inflation or drop slightly.

4. **New Market Opportunities for 2020**
   - As the Saiccor expansion ramps up, demand for hardwood pulpwood will increase.
   - Bio-energy production from plantation by-products will gain traction. A few projects have already been initiated (e.g. York Timbers’ planned bio-refinery) and we expect more such projects to begin in the coming years, especially in areas where there are limited markets for pulpwood - e.g. Limpopo.
   - Due to depressed local demand, it is likely that the export of “oversized” sawlogs will continue.

3. **SAWMILLING INDUSTRY**

3.1 **Developments in 2020**
   No major developments. There may be a few closures of marginal mills or even takeovers or change of ownership but volumes produced should remain close to 2019 levels.

3.2 **Production Outlook for 2020**
   Production not expected to increase and may even decline slightly.

3.3 **Price Outlook for 2020**
   It is expected that the price of structural timber will increase by probably 4% to 5%.

3.4 **New Market Opportunities for 2020**
   None anticipated.

4. **PULP & PAPER INDUSTRY**

4.1 **Developments in 2020**
   - Ramping up of dissolving pulp at Saiccor will continue (until 2022).
   - There will be an increased focus on recycling.
   - The cost of energy will continue to place pressure on both production costs and volumes on the Industry, especially those entities who are wholly reliant on Eskom power.

4.2 **Production Outlook for 2020**
   - Production of fine paper, newsprint and tissue (which already has excess capacity) will probably decrease.
   - Dissolving pulp production is expected to increase annually until the Saiccor expansion ramps up to full production in 2022.
   - Woodchip export volumes are expected to remain static or in fact decline in 2020 due to substantial decrease in the $ price of market and dissolving pulp.
4.3 Price Outlook for 2020

- The price of all types of pulp are set by the “world price”. During 2019 prices of hardwood bleached kraft fell from $800 / ton to $600 / ton. Those of dissolving pulp fell from $950 / ton to less than $700 / ton. The Rand prices of these products have not fallen as much due to the depreciation of the Rand against the US$. Nevertheless, this is causing significant potential downward pressure on local pulpwood.
- The price of woodchips in US$ terms is expected to decrease for the rest of the year and into 2020, thus putting downward pressure on pulpwood prices.

4.4 New Market Opportunities for 2020

Those entities that are able to do so will continue to diversify away from traditional Pulp & Paper core products and invest in the production of bio-products that are becoming more accessible through improved technology. This is where the future of the Industry lies.

5. POLE TREATING INDUSTRY

5.1 Developments in 2020

There are likely to be no new developments in 2020. On the negative side, the proliferation of illegal pole “treaters” is of major concern as is the theft of poles and the reduced demand from Eskom for transmission poles and a significant decline in export orders for transmission poles.

5.2 Production Outlook for 2020

Production is expected to remain static despite the continued high demand for shade netting poles (for the local agricultural Industry).

5.3 Price Outlook for 2020

Stable.

5.4 New Market Opportunities for 2020

Due to a significant fall-off in demand, especially for transmission poles, treaters are looking at new market opportunities in hitherto un-serviced markets further afield.

6. MINING TIMBER INDUSTRY

6.1 Developments in 2020

The fortunes of the MT Industry are linked with those of the gold and platinum mining Industry. As these mining activities are in gradual decline, so too is the MT Industry.

6.2 Production Outlook for 2020

Current production of 352 000 tons is likely to decline further.

6.3 Price Outlook for 2020

Stable to negative.

6.4 New Market Opportunities for 2020

Most mining timber is grown in Limpopo and Mpumalanga. Alternative markets are limited. As the demand for mining timber continues to decline, new opportu-
nities in bio-energy generation may present themselves or to supply hardwood pulpwood to Ngodwana (depending on lead distance).

Roger Godsmark
Operations Director
September 2019