



Briefing #11: Timber prices will remain high in 2022 - here's why

*Prepared by Tim Woods
of IndustryEdge:
November 2021*



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Timber prices will remain high in 2022 – here’s why

From Tim Woods at [IndustryEdge](#)

For some time now, every public conversation about houses has included discussion of timber prices. The entire nation has an opinion about housing markets and by proxy, they also have a view about timber supply and the price of timber.

While many have just used the opportunity to complain about timber prices, we know that for most in the industry, the cost of timber is a serious issue that has to be understood and even predicted as best as possible, because the future of businesses relies on it.

So here, in this year-ending piece on housing markets and timber supply, we want to take a sober look at timber pricing, present our expectation and explain why we expect timber prices to remain at or near current levels throughout 2022.

Current timber prices at all-time highs

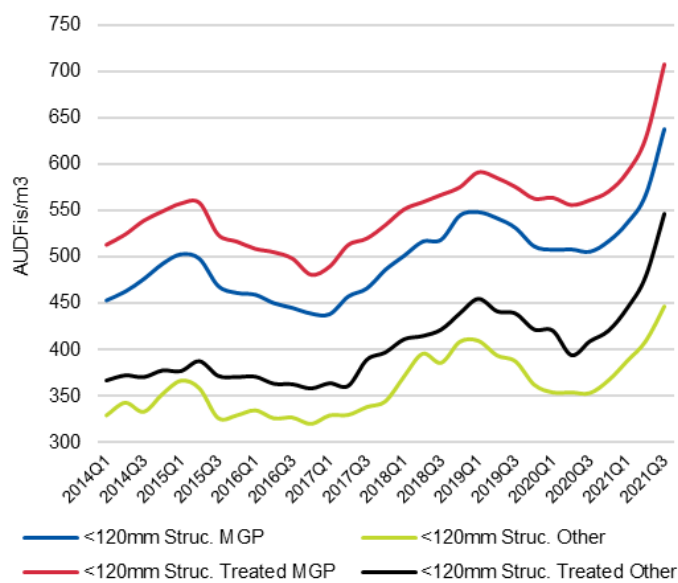
The price of timber has risen across Australia over the last year, as has been the case across most of the world.

Because of its importance to the Australian housing economy – more important than any other building product, in our assessment – we focus mainly on sawn structural softwood and specifically the grades that are <120 mm (the modern 4 x 2).

Prices for locally produced structural grades lifted over the last year by between 26.0% and 33.7% according to the latest data from [Forest & Wood Products Australia \(FWPA\)](#). Prices are at record levels and as an example, in the September quarter, the Treated Structural MGP grade lifted to \$708/m3.

This very useful and deceptively simple data series is the weighted average pricing of the contributors, and it is quarterly, which smooths out many of the most absurd ‘moment in time’ movements. That means, as the chart and table below demonstrate, that it also identifies real movements in prices, like those experienced over the last year.

Sawn Structural Softwood Prices: MQ’14 – SQ’21 (AUDFis/m3)

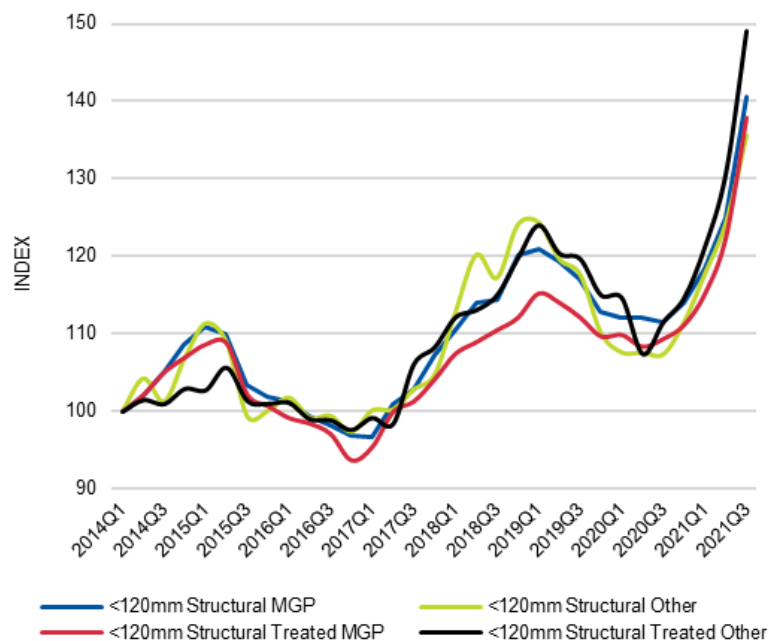


Source: FWPA

AUDFis/m3	SQ'20	JQ'21	SQ'21	SQ'21 v JQ'21	SQ'21 v SQ'20
<120mm Struc. MGP	506.02	567.22	637.63	12.4%	26.0%
<120mm Struc. Other	353.59	409.40	446.56	9.1%	26.3%
<120mm Struc. Treated MGP	576.75	639.10	737.44	12.6%	26.0%
<120mm Struc. Treated Other	561.67	628.49	707.87	14.1%	33.7%

Because the products have different values – despite being quite similar – the index chart below is also important to see the comparative movements between these grades.

Sawn Structural Softwood Prices: MQ'14 – SQ'21 (INDEX: MQ'14 = 100)



Source: FWPA & IndustryEdge

The index chart shows that for the most part, the prices of structural timber grades have moved consistently with one another and in fact, the increases have been more uniform over the last year, than in prior years.

Demand outstripping supply has pushed prices up, for domestically produced sawn softwood.

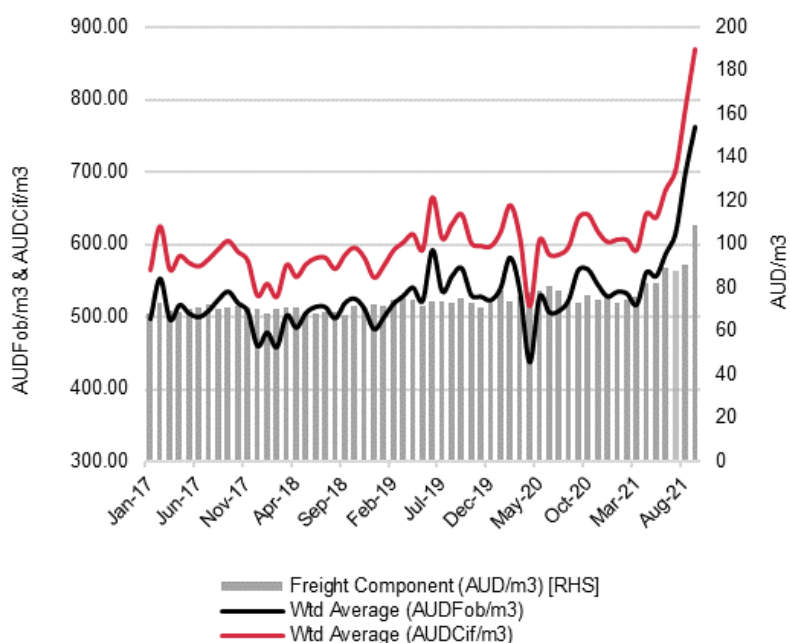
But, what about imports?

In the next chart (following page), we can see the weighted average price of sawn structural softwood products has grown on a fairly similar trajectory to that of the local products. In fact, in September 2021, the weighted average price was AUDFob761/m³, up 35.0% on September 2020. By contrast, the landed or 'Cif' price was an eye watering AUDCif870/m³ in September 2021.

This reference to 'Fob' shown on the black line and the higher price recorded as 'Cif' is important. The Free-on-Board (Fob) price is essentially the price of the goods before shipping. The Costs, Insurance & Freight (Cif) price includes the cost of shipping the goods to the wharf in Australia.

So, the chart shows both these prices, and the grey bars show the cost of freight per cubic metre. That has been getting out of control recently. We will discuss this element of total cost a little later in this analysis.

Imported Sawn Structural Softwood: Jan '17 – Sep '21 (AUDFob/m³, AUDCif/m³ & AUD/m³)



Source: ABS and IndustryEdge

The drivers for these huge – and largely consistent – price increases have been the coincidence of global demand spiking unexpectedly in most major markets at the same time, coupled with mainly global supply disruptions.

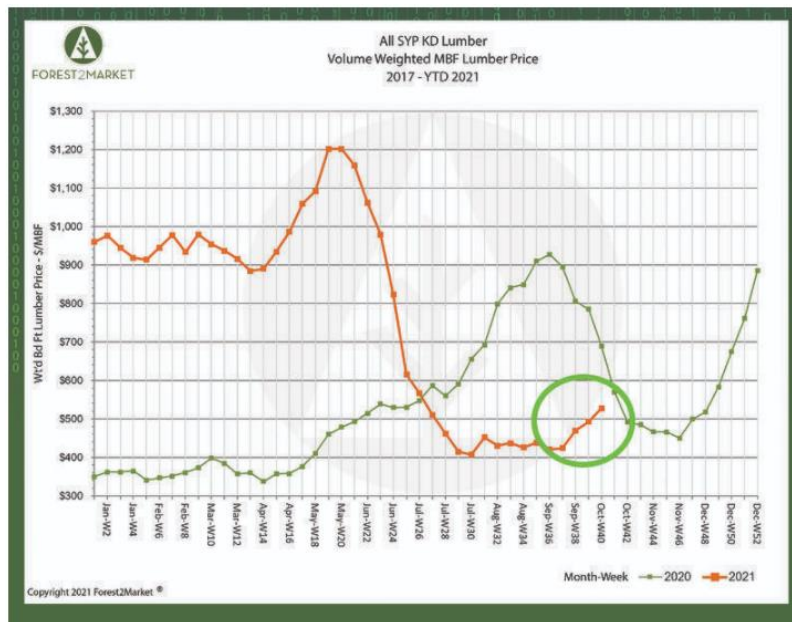
These reports from IndustryEdge, for FTMA Australia have discussed these drivers in much greater detail over the last year. Members of FTMA can review the previous analysis separately, rather than us repeat them here.

In summary, having seen the price of timber – both the local supply and imports – increase over the last year by a bit more than 30% on average, we need to understand how that has compared with the global experience?

Global timber pricing trends are more volatile, but on trend

It is no secret global timber prices have lifted dramatically over the last year. The stand-out market is the USA of course, where timber is openly traded and nearly all jurisdictions allow materials price increases to pass-through to end-users, including home buyers.

Though not a direct comparison, the chart on the following page from our partners [Forest2Market](#), shows the sharp rise in prices that started in April 2020 (the green line) and has been through two steep cycles, including hitting stratospheric new peaks in June of 2021 (the orange line), before crashing by around 70% and then commencing to climb again in recent trade.

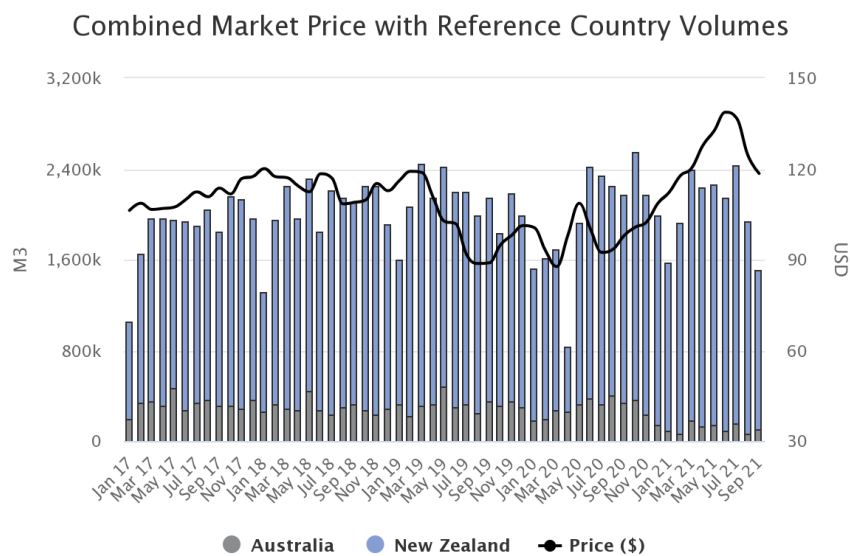


IndustryEdge struggles to comprehend a market where prices move so viciously and rapidly. How exactly would Australia cope with those conditions, is the question that comes to mind. Not very well!

Just as relevant, log prices are continuing to shift up in the US, and in Europe, just as we have experienced in Australia and New Zealand. Higher log prices feed directly into higher timber prices, as everyone in the supply chain understands.

There may be some evidence of slight moderation in international log prices. IndustryEdge's new Australasian Log Price Index (to be launched in December) shows the weighted average price of logs exported from Australia and New Zealand.

As the chart from the 'beat test' shows, the weighted average price (dominated by New Zealand's volumes) dipped in August and September, but at an average USDFob118/m3 in September, prices are far from cheap and remain around previous peaks. What may be more important is that the September price is around 25% higher than a year earlier.



©2021 IndustryEdge, Source: ABS

There may have been some moderation in log prices, and international lumber prices, from their all-time peaks, but prices are still at record levels.

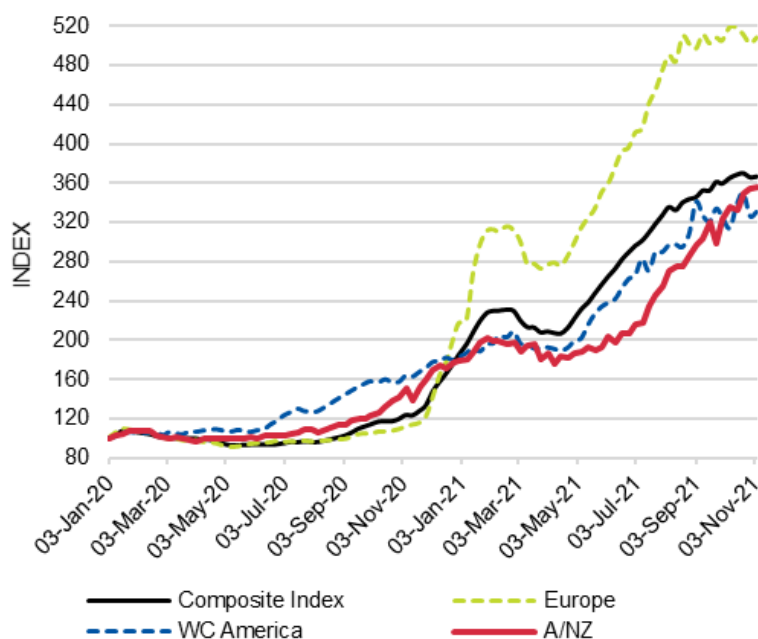
Shipping and freight debacle to continue

The cost of shipping, as we introduced earlier in this analysis, is spiralling upwards, with every piece of market feedback adding to the inflationary sentiment on shipping costs. The suspicion overall must be that the global shipping and freight market is now running itself up based on perception, as much as, if not more than reality.

For timber imported to Australia, the data shows that in September, the cost of shipping lifted to an all-time high of AUD109/m³, a 49% increase on September 2020.

The index chart below shows the cost of containerised freight from Shanghai to key locations around the world. The red line shows that to Australia and New Zealand (the reference port is Melbourne), the cost of containerised freight has increased 158% over the year to 5th November 2021, and we are not alone. Spare a thought for those shipping to Europe!

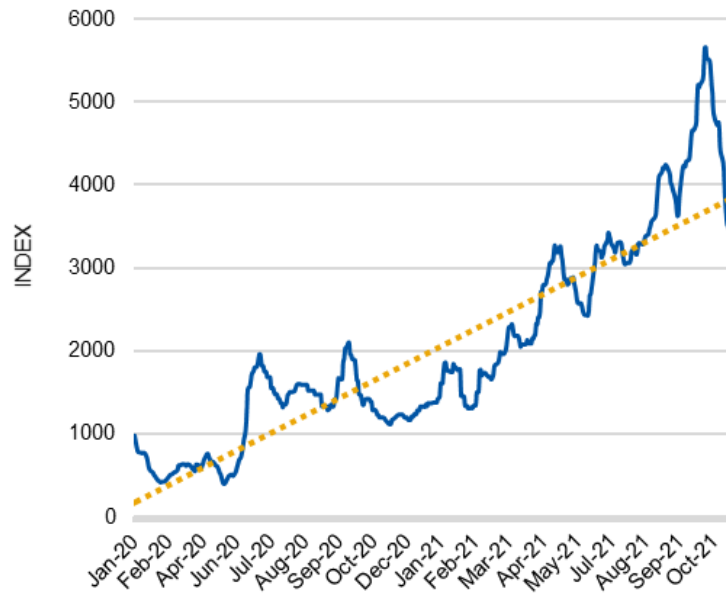
China Containerised Freight Index: 3 Jan '20 – 5 Nov '21 (INDEX: 3 Jan '20 = 100)



Source: CCFI & IndustryEdge

For bulk shipping as distinct from container freight, the situation is little different as the leading indicator, the Baltic Dry Index (BDI) shows (following page). The welcome relief that has seen massive falls in bulk shipping costs in recent weeks helps, but there is also every chance it will bounce up again in coming weeks and months.

Baltic Dry Index: Jan '20 – Nov '21 (INDEX: 3 Jan '20 = 100)



Source: Bloomberg

Fuel prices continue to move up

One reason the BDI is likely to continue to move up is the relative strength of fuel prices right now. Fuel is the largest input to shipping costs, and as we can see here, after plunging in the early part of 2020, the cost of petroleum – in this case, West Texas Intermediate Crude Oil – has lifted very dramatically. From a low of USD17/barrel in April 2020 to USD81/barrel in October, the nearly four-fold increase has added significantly to all transport costs.

West Texas Intermediate Crude Oil: Jan '20 – Oct '21 (USD/barrel)



Source: Forest2Market

These factors are feeding into the great concern of the economic moment: where is inflation headed?

Inflation – is the genie out of the bottle?

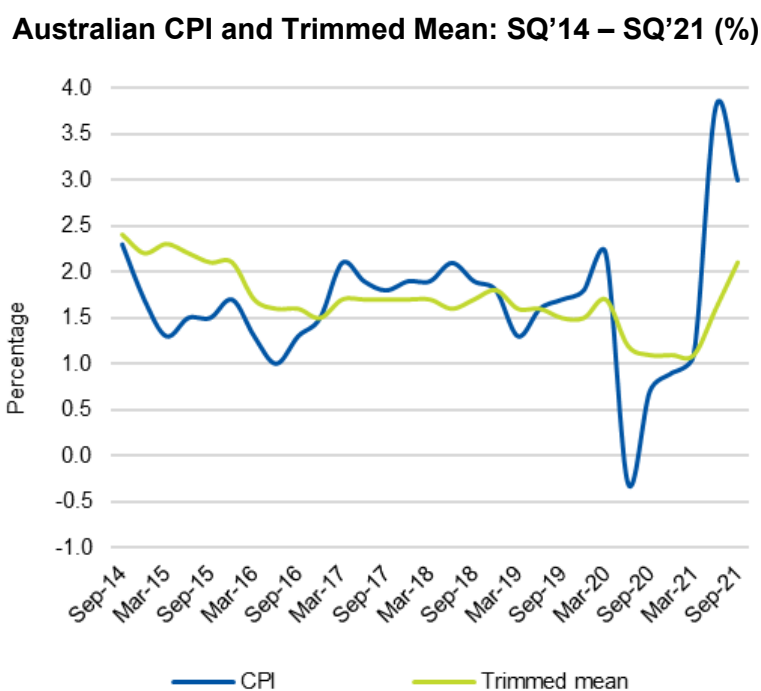
There is a lot of economic news – the world over – about inflation right now. Inflation is often not well understood. Sure, it means prices rise, but really what it means is prices rising relative to the purchasing power of money.

Generally, a level of continuous but orderly price increases is important for economic progress because that sends signals that other factors need to increase as well: wages and social security payments being key among them.

When economies are hit by shocks, the magnitude is measured a number of ways. One is the Consumer Price Index (CPI) or the measure of price growth for the things that households typically buy.

Australia's CPI plunged at the onset of the pandemic and has subsequently sky-rocketed, ending the September quarter at an annualised 3.0% - inside the Reserve Bank of Australia's (RBA) target band of 2-3% per annum. The chart shows this and also the 'trimmed mean' which removes the impact of volatile outliers, like say fuel price increases.

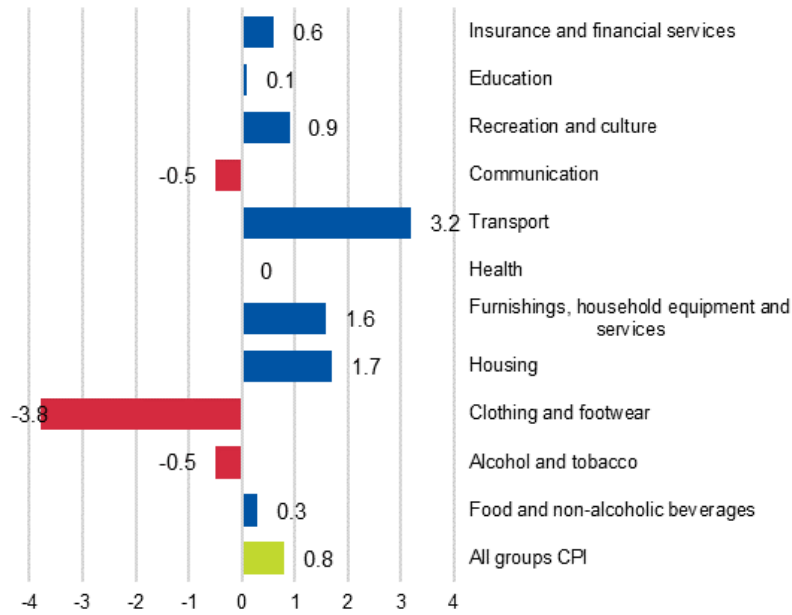
Sure, the trimmed mean at 2.1% makes sense in normal times, but these ain't normal times, so perhaps the headline CPI of 3.0% is more real than the trimmed mean right now?



Source: ABS

Analysis of inflation is not complete unless we look at what caused it in each period. In the September quarter, inflation lifted 0.8%, and as we see on the next page, transport (yep, fuel included) saw prices increase a huge 3.2% and housing costs by 1.7%, for example.

Contributions to Australian CPI: SQ'21 (%)

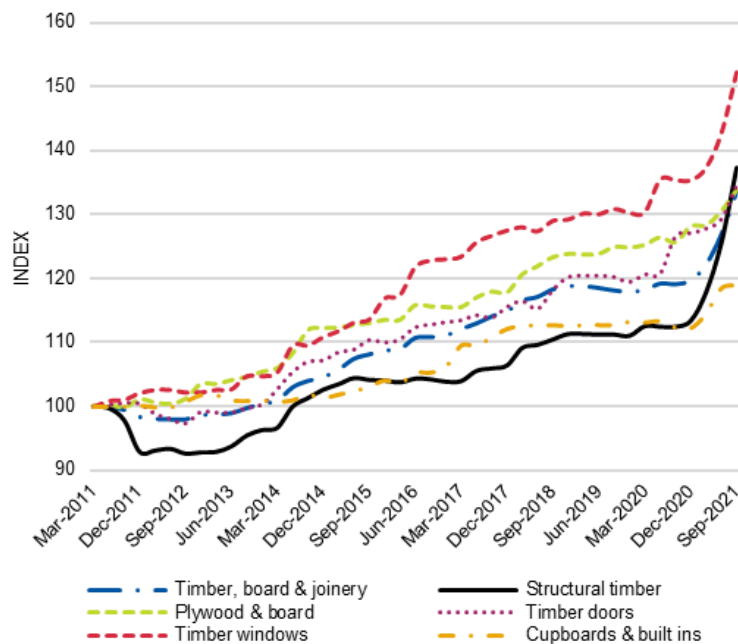


Source: ABS

So, no shock, consumer prices are going up and households face inflation. But that does not mean the businesses supplying them have filled their boots at consumer's expense. Sometimes it does, but generally, the consumer prices increase because producer prices have increased.

We can see that is the case below, where for home building, the Producer Price Index (PPI) rose 8.0% over the year-ended September, with structural timber prices up 22.1% and other timber, board and joinery up 12.2%.

Housing & Construction Industry: Producer Price Index: MQ'11 - SQ'21 (INDEX: MQ'11 = 100)



Source: ABS & IndustryEdge

The point here is simple enough. The prices being experienced through the timber supply chain are being felt in the main end-market.

One of the factors that drives inflation is momentum and the expectation of price increases. Those are very real right now – and for good reason. We should anticipate prices for timber and wood products will continue to rise for a while yet, before flattening out.

But, the caution is that the genie has escaped the bottle on inflation, and after years of suppressed wages and over 2022 when labour and materials will be in short supply, watch out for further pricing surprises in every day life, both at home and at work.

How long before a timber price correction?

If we are correct that price rises for timber still have a little way to go and will remain high through 2022, what will bring them down again, will be demand and supply coming back into balance.

For that to happen, the biggest pipeline of building work in history has to reduce to the point where there is over-supply. We don't think that can possibly happen until very late 2022, and possibly 2023.

If there is one thing that would bring the demand to a close faster it would be a sharp rise in interest rates brought about by the Reserve Bank of Australia (RBA) pulling the brakes on because inflation is out of control. In early November, amidst a lot of discussion on inflation, the RBA said 2023 was the earliest it would push interest rates up. Its clear preference is 2024.

With no end in sight to shipping disruptions, high international prices for logs and timber, rising general inflation, increasing housing sector inflation and labour shortages, timber prices are likely to remain high until the pipeline of work is built out.

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