

We have a Dilemma

By Peter Fitch

I have touched this subject many times in my articles and yet we find ourselves faced with the same situation where we are creating a potential imbalance or at least generating volatility in the Supply and Demand of composite wood panels. It is almost as if business leaders have chosen to forget the most basic economic principles by which profits are made and returns on investment maximised in a free market. This principle in its purest form depends on the dynamics of Supply v's Demand.

I find it incredible that following my earlier postings on potential new projects that a total of 6 Particleboard Lines and 3 MDF Lines will be built within South East Asia by the end of 2017 and still others are in the planning stage for 2018. These lines will not be small as most will boast a potential capacity of 1,000m³ per day. Outside of South East Asia but within the sphere of influence of our markets new Particleboard and MDF lines have been announced for India, Bangladesh, Pakistan, Iran, Russia, China, Turkmenistan, and Australia. Elsewhere in the world the consolidation process is continuing in Europe with the American Company Arauco taking up significant shares in producers there. Arauco a company that was originally founded in Chile has become a major player in the composite wood panel business both in North and South America.

Perhaps the MDF and Particleboard producers in South East Asia know something that I do not, but for me I can predict with a high degree of certainty that it will be very difficult to sell the full potential of this new capacity into the current market.

The financial year of 2015 was generally a good year for SE Asian composite panel manufacturers. It must be pointed out that this was mainly due to the strengthening of the US Dollar and lower commodity prices which helped keep wood, glue, energy and transport costs down. Markets were also by enlarge stable with demand able to take the current capacity. We could say the market was 'balanced'.

The dynamics started to change in 2016. The proxy battles in Syria & Yemen, the sustained low oil price and a weakening USD all paid its toll on our most important market – The Middle East. Demand was severely curtailed in the large markets of Saudi Arabia and Iran. Luckily some of this excess volume was diverted to South Asia as the economies of India, Pakistan and Bangladesh improved. That process is still on going with the hope that demand will also slowly recover in the Middle East. My estimate is that by the middle of 2016 we will once again reach a near balance in the Supply v's Demand for composite wood panels and prices will stabilise.

We may enjoy a healthy market situation to the end of 2016. The crunch will come as the new lines come on stream and the first commissioning panels and then the 'A' Grade material comes to market. If Demand in our critical key markets cannot keep up with the Supply then the market is forecast to crash in a spectacular fashion.

If one was to be optimistic we could predict the following conditions could justify the investments in new plants, but I will leave the reader to make their own mind up whether this will be the case:-



- Peace finally returns to Syria and Yemen, the new governments together with the international community help undertake a massive nation rebuilding exercise.
- Rapprochement, between Saudi Arabia and Iran leading to stability and renewed investment into the Middle East.
- A return to a more stable and middling price of Crude Oil boosting investment in the oil producing countries.
- A rapid opening up and deregulation of the Indian market, to achieve a similar spectacular growth as that achieved by China 15 years ago.
- A more rapid transition in converting the Chinese economy from a manufacturing base to become more of a consumer economy.
- ASEAN to realise its full market potential and boost domestic demand.
- The Euro crisis to be resolved leading to the resumption of sustained growth in the European Economies.
- The refugee crisis in Europe turns into an opportunity to boost growth.
- Sanctions are dropped against Russia and the Ukrainian issue is settled between vested interests.
- The next US President to re-align government policies to be inclusive of the majority of the population as opposed to only benefiting the business elite. Thus stimulating real economic growth as opposed to fiscal growth.
- The opening up and engagement of new developing markets in the African Continent, South American Sub-continent and countries such as Myanmar and North Korea.
- Japan to finally exit its 'lost decade' and to engage in reflationary growth.

So with a strong following wind and some good luck, there could be sustained growth in the Demand for Composite Wood Panels. Unfortunately, I think that some of the global issues we face will take many years if not decades to solve.



As a final word of warning to those that are embarking on new capacity investments and a point of concern for those that remain within the business. A key element of our industries survival is the sustainability of our wood supply. Wood supply in Malaysia is already strained with costs being typically double that of Thailand, Vietnam and Indonesia. With the new lines and their huge appetite for wood fibre, this will undoubtedly increase the price of wood material across the whole of SE Asia and especially in Thailand and Vietnam. We must also ask ourselves for how much longer will oil prices, freight rates and exchange rates work in our favour?

By 2017 or earlier our industry will find itself in a dilemma of high costs and low selling prices. Investment returns will be very poor.