COVID-19 puts Europe on a knife-edge

The COVID-19 situation in Europe is on a knife edge. The numbers of new cases and deaths have stabilised and are beginning to decline in the worst affected countries, which include Italy, the UK and Spain. This has led to calls for the lockdown measures, which have been in place now throughout large parts of Europe for over six weeks, to be eased as the detrimental effects on economic activity, education, mental health and general well-being are becoming increasingly obvious.

Against this, the authorities must balance the very real possibility that easing of the lockdown measures too soon could trigger a renewed rise in coronavirus cases. The reality of these concerns was confirmed following the German government's decision to begin relaxing restrictions on 20 April to allow small businesses to open. Germany now faces the prospect of having to restore stricter lockdown measures as its number and rate of coronavirus infections have grown again.

Whatever decisions are taken now, the economic effects look certain to be nothing short of catastrophic. The IMF latest projection, issued on 14 April, is that world output will decline 3.0% this year, down 6.1% in advanced economies and 1% in emerging and developing economies. IMF observe that "for the first time since the Great Depression both advanced economies and emerging market and developing economies are in recession".

IMF warn that this is a baseline scenario and that "the pandemic may not recede in the second half of this year, leading to longer durations of containment, worsening financial conditions, and further breakdowns of global supply chains". Under these conditions, say the IMF, global GDP may fall even further, possibly by an additional 3% in 2020 if the pandemic is more protracted this year.

Western Europe has been the epicentre of the pandemic in March and April and 2020 IMF projections reflect this fact. The steepest declines in GDP this year are expected in Italy (-9.1%) and Spain (-8.0%). Large declines are also forecast in France (-7.2%), Germany (-7.0%) and the UK (-6.5%). Total eurozone GDP is expected to fall 7.5% in 2020.

Prospects for global trade are equally grim. The WTO's trade forecast report for 2020 issued earlier in April projects that total world trade will fall by between 13% and 32% this year.

European timber importers put orders on hold

Accurate estimates of the specific effects on timber trade volumes this year will only become apparent when more countries publish trade data for the first quarter (data for European trade during that period is due be published in mid-May).

Anecdotally, reports suggest most European timber importers were putting orders on hold in the second half of March and during April as they struggled to deal with a build-up of stock that couldn't be shifted as manufacturers, retailers and construction sites have gone into lockdown.

Shipper and forwarder groups in Europe have been calling on carriers and terminals to exercise restraint before issuing detention and demurrage charges for goods ordered before the lockdown that were still on the water and due to arrive in April and May.

Adding to the uncertainty, freight rates have become volatile, rising sharply on some routes (e.g. from Europe to China and East Asia) and falling on others (e.g. North America to Europe). Containers shipping cargoes from Asia to Europe, the US and other countries have been severely reduced, with no empty containers transporting timber back. Shipping companies have cancelled hundreds of vessels in response to the fall in demand.

According to a report by Bollore Logistics, European ports are continuing to operate despite difficult conditions and containers are being processed for onward movement, although clearances by some customs authorities is slower and there are border bottlenecks. Most shipping companies continue to operate, although they are adding surcharges and available space and equipment has become very restricted.

Within Europe itself, the borders of the Schengen area and between the European Union and the rest of the world are partially or completely closed. However, the flow of goods is free from these restrictions and continues to be authorised to ensure supply chains can be maintained.

Land transport of goods is continuing in Europe, subject to disruptions and slowdowns due to increased border control, sanitary measures (such as health checks on drivers) and special arrangements (including closure of certain border posts and detours, limited driver availability).

Steepest fall in European business activity ever recorded

During this period of heightened uncertainty, there is much focus on the IHS Markit Purchasing Managers Index (PMI) for early insights into the impact of COVID-19 on European market conditions.

The latest 'flash' PMI assessment for April (published early based on approximately 85% of the final number of replies received every month) suggests that the eurozone economy suffered the steepest falls in business activity and employment ever recorded during April as a result of the COVID-19 lockdown measures.

The eurozone PMI index plummeted to an all-time low of 13.5 in April, down from a prior record low of 29.7 in March, to indicate by far the largest monthly collapse in output recorded in over two decades of survey data collection (the PMI operates on a scale of 0 to 100 and any score below 50 implies a contraction in output when compared with the previous month). By comparison, the lowest reading seen during the global financial crisis was 36.2, reached in February 2009.

The service sector bore the brunt of the impact from the lockdown measures, with the eurozone business activity index sliding from 26.4 in March to just 11.7 in April. Companies operating in sectors such as hospitality, accommodation, restaurants, travel and tourism saw especially steep falls in activity, with vast numbers of such companies in enforced shutdowns or severely limited in terms of their ability to operate.

Manufacturing also saw a record fall in production, the PMI output index slumping from 38.5 in March to 18.4, with many non-essential businesses having closed and others reporting either dramatically reduced demand or being constrained by shortages of staff and inputs.

By region, the unprecedented scale of the collapse was broad-based, with composite flash PMI output indices hitting all-time lows of 17.1 and 11.2 respectively in Germany and France (down from 35.0 and 28.9 in March), while the rest of the region saw the composite PMI slide from 25.0 to 11.5.

Commenting on the flash PMI data, Chris Williamson, Chief Business Economist at IHS Markit said: "April saw unprecedented damage to the eurozone economy amid virus lockdown measures coupled with slumping global demand and shortages of both staff and inputs.

"The extent to which the PMI survey has shown business to have collapsed across the eurozone greatly exceeds anything ever seen before in over 20 years of data collection. The ferocity of the slump has also surpassed that thought imaginable by most economists, the headline index falling far below consensus estimates.

"Our model which compares the PMI with GDP suggests that the April survey is indicative of the eurozone economy contracting at a quarterly rate of approximately 7.5%", concluded Mr Williamson.

PMI data for the UK is equally sobering. The IHS Markit/CIPS Flash UK Composite Output Index was at 12.9 in April, down from 36.0 in March, indicating that the combined decline in manufacturing and services was considerably worse than the 38.1 experienced at the height of the financial crisis in 2008/09. 81% of UK service providers and 75% of manufacturing companies reported a fall in business activity during April.

The UK services PMI fell to 12.3 in April from 34.5 in March, the sharpest reduction in service sector activity since the survey began in 1996. Customer-facing service providers reported a complete shutdown of business operations in April whilst many other respondents stated that they had weaker demand due to closures from clients. The UK manufacturing PMI was 32.9 in April, down from 47.8 in March, the lowest since the survey began in January 1992.

Based on history, this would correlate to more than a 6% contraction in GDP in the UK during the second quarter of 2020. IHS Markit note that even this is probably too optimistic since these PMI exclude some key sectors such as retail.

Other projections for the UK economy this year are certainly more pessimistic, despite the fact that most forecasters still assume a 'V' shaped recession - a sharp fall in activity during the first half of 2020 followed by a swift recovery in the second half of the year.

On 16 April, HM Treasury published recent UK macroeconomic forecasts across City and non-City forecasters. The average fall in GDP during 2020 is expected to be 7.4%, ranging from the most optimistic estimate of only 3.6% fall to the most pessimistic estimate of 12%.

ETTF and EOS: COVID-19 impact on European wood market "severe and wide-ranging"

On April 15, the European Timber Trade Federation (ETTF) and the European Organization of the Sawmill Industry (EOS) organised a joint conference call to take stock of the effects of the COVID-19 crisis in the timber market and to gauge what the situation will be in the coming months. Representatives from eleven European countries contributed to the discussion.

Participants concluded that the impact of the COVID-19 outbreak on the timber sector is wide-ranging and severe and the legacy is likely to be long-lasting. However, there are significant differences between European countries, indicative both of variable spread of the virus and policy responses.

The construction sector, a fundamental market for the timber industry, has taken a hit in several countries, notably Spain, Italy, the United Kingdom and France, and this has impacted on timber suppliers and other business elsewhere in Europe which have a high level of exposure to this group of countries.

In other parts of Europe – including Scandinavia, Germany, and the Netherlands - the local construction sector has been less affected. However, a crunch period for these countries might yet be on the cards in the third quarter of 2020.

The impact has also varied between market sectors. Sectors connected to logistics, such as pallets, are performing comparatively better than sectors connected to manufacturing, such as the furniture and joinery industries.

In response to struggling demand, European wood processors have introduced double-digit production curtailments, with reductions in Scandinavia generally being less than in Central Europe.

Participants in the conference call expected that the Do It Yourself (DIY) sector will help to prop up the European timber market during a period when people are confined to their homes. Larger DIY stores are also one of the few categories of retailer that have been permitted to remain open during the lockdown and are therefore better placed to support sawmills and trade.

For both EOS and ETTF members, overseas markets are very important. Participants in the call stressed that China, as both a critical client and producer, has been recovering in the last few weeks, while sales to the United States are dropping. They noted also that the Indian market is completely closed, while there are also considerable difficulties on both the demand and supply side in some South-East Asian countries.

Looking forward, both organisations agreed that the length and intensity of the crisis will be crucial as to the pattern of recovery. If the lockdowns and other measures prove successful in controlling COVID-19 in the coming months, there is some hope for a return to an almost business-as-usual situation. It was noted that the timber sector was performing well in Europe in the first quarter of 2020. Such a “V-shaped” outcome represents a best-case scenario.

However, if there is a prolonged contraction in the general economy and the construction sector in the second half of 2020, it will take a heavy toll on the timber industry, even in countries that so far have managed to weather the storm. There are also likely to be very significant structural changes, still largely unpredictable, in both the wider economy and the timber sector as a result of the pandemic.

COVID-19 halts positive developments in European wood flooring sector

A similar narrative unfolded when the Board of Directors of the European Federation of the Parquet Industry (FEP) discussed the first impacts of the Covid-19 crisis during a conference call in April. FEP concluded that “the European parquet markets generally started the year well showing stable to slightly positive trends in January and February. But March and the arrival of the Covid-19 virus on the European territory put an end to this positive move.”

Compared to the same period last year, FEP’s provisional results for the three first months of 2020 indicate stable parquet consumption in Scandinavia (except in Sweden due a decline in new build activity), the Baltic States and Germany – all countries where economic activity continued for the time being.

In contrast, the South of Europe which is experiencing tougher COVID-19 restriction measures was already reporting very significant declines in wood flooring consumption: “Although right now it is impossible to predict when activities will restart and how consumption will then evolve, it is obvious that this crisis will have long-term and significant impacts on the European economy and industry,” FEP explains.

Eastern European construction carries on for now

Growth in European construction is forecast to drop to -1.4% in 2020, according to the latest report from industry analysts at GlobalData. The report, which follows decisions by many of Europe's leading industrial nations to extend lockdown measures, suggests that continuing activity in Eastern Europe may offset a sharp decline in Western Europe. However, GlobalData also emphasise that this preliminary forecast may prove to be optimistic.

Construction activity in Western Europe is forecast to contract by more than 5%, with GlobalData applying the caveat that things will almost certainly be worse if containment measures are further extended.

GlobalData highlight that the situation in Eastern Europe is currently less severe, noting that the virus is yet to take hold in some countries in the region. Moustafa Ali, Economist at GlobalData, said, "While the impact of the virus has so far been limited [in Eastern Europe], the health situation is expected to deteriorate in the coming months. The major Eastern European construction markets are also set for severe disruption in the first half of 2020."

UK hardwood trade suffering from lack of finance and poor margins in time of COVID-19

A report on the UK hardwood market in the Timber Trades Journal (www.ttjonline.com) notes that the sector was not in total lockdown in April, but activity was radically reduced by the Covid-19 epidemic.

Most hardwood companies responding to the TTJ survey said that they had taken advantage of the new government grant scheme to furlough personnel. One leading importer/distributor said they had 'downsized' in line with demand. Others had shut their doors entirely, initially for three weeks.

"Some customers are continuing to operate for the time being, and we're still getting orders," they said. "Some construction sites are still working and joinery companies are staying open to supply them and there's also DIY demand, presumably with people staying at home in the lockdown.

There were reports of some customers actually increasing orders early to mid-March, seemingly as a hedge against suppliers curtailing operations. But that came to a halt after government announcements of restrictions on public gathering and closure of restaurants, pubs and other amenities.

Smaller companies are also reported to be disproportionately affected by customers extending payment terms during the crisis, citing cashflow reasons. "It tends to be bigger buyers, so you have little choice but to comply," said one agent/importer. Another business agreed. "Almost our sole focus currently is getting paid," they said.

Some companies expressed concern about logjams building up at UK ports, with importers running out of storage themselves unable to take incoming cargoes. However, one importer/distributor, which said they were continuing to take both containers and breakbulk from ports, thought this was not a 'significant risk to date' and that port operators might use nearby overspill storage areas if it became a problem.

In terms of supply, most companies consulted said that they were asking for orders not yet dispatched to be pushed back a month to six weeks. Overseas suppliers were generally reported to be accommodating.

Looking forward, UK hardwood businesses were not sugar coating the pill. The next three months, and possibly longer, are expected to be very difficult. “The profit we made at the start of the year has already been wiped out,” said one importer.

There was also an expectation that the pandemic would result in permanent changes; accelerating the trend to remote working, more online trade and less overseas travel and face to face supplier contact.

Inevitably, it is feared, the current crisis will also lead to job losses and some industry concentration. “This has not been a very profitable business for a number of years and companies have not built up a financial safety net, so there will be casualties,” said one importer.

“Hopefully, when we emerge on the other side, the trade as a whole will press for better margins. We’ve been selling hardwood too cheaply for too long.”

Other news from the UK highlights the vulnerability of the hardwood sector during the COVID-19 lockdown and its aftermath. Most producers and traders are small companies that sell into other sectors, such as high-end joinery and furniture manufacturing, equally dependent on smaller operators.

The problems for small and medium-sized contractors in the UK were clearly highlighted in a Federation of Master Builders (FMB) survey published on 17 April. Almost two thirds (65%) of small building companies stated that they would not be able to last more than two months without grants from the government while almost a quarter (24%) said they would struggle even to get through four weeks.

The UK government had announced over four weeks before the FMB survey that new loans would be available under the Coronavirus Business Interruption Loan Scheme (CBILS). However, only 4% of builders who had applied for the CBILS had been successful.

The FMB survey also highlighted that 68% of builders had stopped at least 91% of operations and new enquiries had dropped by 64%. Of stopped work, 80% said this was due to lack of availability of products and materials while 65% experienced problems maintaining social distancing rules on often small, domestic sites.

Unlike other European government, the UK government has so far resisted calls to loosen the country’s lockdown. After returning to work on 27 April following his recovery, Prime Minister Johnson - the first world leader to fall victim to coronavirus - urged caution and gave no clue as to how or when businesses might return to normal, calling this the time of "maximum risk" of a second wave of infections.

Following his statement, and under pressure to set out a timetable for easing of lockdown measures, the UK government stated that this will happen only when five tests had been passed: the number of coronavirus deaths are clearly falling; the NHS is able to cope; the rate of infection is coming down; there are enough supplies of personal protective equipment (PPE) and COVID-19 tests; and the government must be confident lifting lockdown measures won't result in a second peak.

Sharp fall in German construction despite policy to continue building

In Germany, Chancellor Angela Merkel has maintained that construction should continue, calling it an “essential pillar of the domestic economy, which must be maintained”. With the IMF predicting that the Germany economy could contract by 7% this year, the country is looking to construction to help ease it out of recession in 2021.

DIY shops have remained open in most parts of Germany during the lockdown, while many building contractors and installers have kept working, with restrictions. Smaller shops were allowed to open from 27 April, although this move may be reconsidered with a subsequent rise in coronavirus cases.

Despite the political focus on keeping the construction sector operational, IHS Markit data shows that Germany's construction activity decreased at the sharpest rate in seven years in March with declines in all sub-groups as firms cut jobs amid weaker demand due to the coronavirus outbreak.

The German Construction PMI fell to 42 in March from a 25-month high of 55.8 in February. The construction sector shrunk for the first time in seven months. Housing activity logged its worst decline since March 2013, while commercial activity fell the most in over eight years.

Signs are that the economy slowed even more dramatically in April. Germany’s Flash PMI Composite Output Index was at 17.1 in April, down from 35 in March, a record low. The services PMI activity index was at 15.9 (Mar: 31.7), while the manufacturing PMI was only a little better at 19.4 (Mar: 41.0). Firms’ expectations towards activity over the next 12 months remained deep in negative territory in April.

France ponders possible easing of lockdown from 11 May

French President Emmanuel Macron announced on 13 April a possible exit from COVID-19 confinement on 11 May, subject to strict compliance with gradual social distancing measures. Until that time, economic activity in France must remain at a low level. This has already put more than 8 million workers in partial activity and resulted in a 6% decline in GDP in the first quarter of 2020.

Most industrial activity in France has been at a standstill since 17 March. Industrial joinery, carpentry, furniture and panel factories have stopped producing almost 90% of their production. The building and public works sector is also at a standstill, with only maintenance and repair activities continuing.

The IHS Markit ‘flash’ PMI for April posted a reading of just 11.2, eclipsing March’s historic result of 28.9 and a fresh series low. The overall reduction in activity was driven by both manufacturers and service providers, with the latter registering the sharper decline. Both sub-sectors recorded their fastest contractions in output since composite data collection began 22 years ago.

Amid widespread expectations of a global economic recession, French firms surveyed by HIS Markit in April were pessimistic towards the 12-month business outlook. The degree of negativity was the most severe since composite data were first available in July 2012. Both manufacturers and service providers recorded record lows for sentiment, with goods producers the more pessimistic.

According to IHS Markit, there are two key areas of focus going forward: “firstly, how quickly will measures be lifted as the gradual easing of restrictions begins on the 11th of May? This will give the clearest indication on how fast we can expect activity to recover in the short-term. Secondly, will the easing of restrictions lead to a second outbreak of the virus? If so, any remaining hopes of a so-called ‘V-shaped’ recovery will vanish.”

Some insight into hardwood product consumption is provided by FEP, the parquet wood flooring association who note that, compared to the first three months of 2019, French parquet consumption fell by 15 to 17% during the first quarter 2020. FEP note that “January and February were normal months of activity, but the French parquet market collapsed in March. All shops are closed. All factories have stopped their activities".

Economic activity still tightly constrained in Italy

Italy was the first European country to experience a significant outbreak of COVID-19 and was the global epicentre in February. Northern Italy, where most of the country's factories are based, has been the worst affected region. The country's vital design sector was brought to a standstill, with Milan's Salone del Mobile postponed and later cancelled.

Only a limited amount of economic activity has continued. Shipping lines are operating despite difficult conditions and cargo can be moved, although challenged by limited container availability, blank sailing in imports, and surcharges.

On April 10, Prime Minister Giuseppe Conte extended Italy's full lockdown to at least May 3. There were some government concessions allowing timber companies and other strategically important activities to continue, but factories were to remain closed for the time being.

This decision came despite pressure from the Italian furniture sector that has been calling for operations to be allowed to restart as soon as possible. In the first week of April, representatives from nine Italian furniture firms—B&B Italia, Bisazza, Boffi, Cappellini, Cassina, Flexform, Giorgetti, Molteni Group, and Poltrona Frau—issued a manifesto asking that their factories be allowed to reopen.

While emphasising that 'health comes first', the Italian firms stressed their concerns about a mounting backlog of orders and competition from other countries with fewer current restrictions on production. They believe this could end up causing long-term devastation to Italy's furniture industry.

If factories remain closed for much longer, the manifesto warns, "we could lose 20–30% of our industrial heritage and witness serious damage to the industry. All of this would inevitably result in the loss of tens of thousands of jobs." In conclusion, the group asserts that "it could take 20–30 years to recover what we would lose in a few weeks."

The petitioning firms highlighted several structural characteristics of furniture production and sales that could make it possible to get back to work while maintaining social distancing. Beyond more typical measures, like the use of certified personal protective equipment, temperature scanning, and regular deep cleanings, the companies note that "our plants are safe spaces, thanks to the layout of the production areas that respects social distancing." Additionally, the location of their factories allows employees to reach work without relying on public transportation.

More recently, the Italian government has been signalling its intention to ease the lockdown. In an interview published on 26 April, Prime Minister Conte told Italian daily La Repubblica "we are working in these hours to allow the reopening of a good part of businesses from manufacturing to construction for May 4".

Mr Conte said that some companies considered "strategic", including export-oriented businesses, could reopen in the last week of April if local prefects give them the green light. Perhaps partly to acknowledge the furniture industry manifesto, Mr Conte added that exporting businesses need to reopen sooner to avoid the risk of being cut out of the production chain and losing business.

On 16 April, the Italian construction forecasting body CRESME said that construction activity this year could fall by almost 23%, which is more than double the decline in 2009, the worst year of the financial crisis. That represents a loss of €34 billion in investment in construction for Italy this year. According to FEP, the Italian parquet market declined by 10% during the three first months of the year.

Spain plans to end lockdown measures by the end of June

Despite having more confirmed COVID-19 cases than any other European country, Spain began to ease some lockdown measures from 13 April, allowing workers in manufacturing, construction and some services to return to work.

On 28 April, the Prime Minister Sanchez outlined a fuller de-escalation plan with four phases, each expected to last about two weeks. He said the process would take a minimum of six weeks, and hopefully no more than eight.

"By the end of June, we as a country will have entered into the new normality if the epidemic remains under control," he said.

Before the plan kicks in, there will be a preparatory "phase zero" from 4-11 May, in which businesses that take appointments can reopen, restaurants can offer take-away services, and professional sports leagues will go back to training.

Mr Sanchez said provinces would progress to less restrictive phases based on their infection rates, local hospital capacity, and how well distancing measures were being observed.