

Signs mount of economic slowdown in Europe

Signs are mounting that this may be a difficult year for the hardwood trade in Europe. Economic forecasts are becoming more gloomy. According to this week's Economist journal "the facts suggest that Europe is not weathering the global financial storms well. Figures released on February 14th reveal that the euro-area economy slowed abruptly at the end of 2007. GDP rose by only 1.6% at an annual rate in the fourth quarter-stronger than in America, admittedly, but still a lot slower than before." The Economist goes on to note that GDP growth in the two largest euro-zone economies, Germany and France, was weaker than the euro-area average. Figures for Italy are not yet out, but existing indications are that the economy may have shrunk in the last quarter of 2007.

What makes matters worse is that although the strong euro has weakened Europe's export competitiveness, the slowdown seems to be more a result of failing domestic demand. The European Commission's gauge of consumer confidence has fallen by 10% points since July 2007, the sharpest drop since early 2003. European consumers are becoming less inclined to spend. Housing markets have been slowing and rising oil and food prices have eroded spending power. In interviews in early February, the President of the European Central Bank confirmed that the ECB thinks that the risks to the economy now "lie on the downside". As a result the ECB has stopped hinting about the possibility of an interest-rate increase. However, with concerns that inflation might persist above the 2% upper-limit of the ECB's target range, there is not much likelihood of a reduction in interest rates as a measure to boost demand.

Prospects do not look much rosier outside the euro-zone. UK economic growth in the last quarter of 2007 was respectable, hitting 0.6% and only marginally down on the previous quarter. However indications are of falling economic momentum in 2008. On 22 January in a speech to a group of businessmen, the Governor of the Bank of England said that "To put it bluntly, this year we are probably facing a period of above target inflation and a marked slowing of growth". The UK housing market has been wilting as banks have responded to financial uncertainty by tightening the terms on which they make mortgage loans and buyers are taking fright at the prospect of falling prices. That augurs ill for consumer spending.

European veneer sector points to slowing hardwood demand

To get a clearer idea of how economic conditions may impact on the hardwood sector, it's worth keeping an eye on the sliced veneer sector. The sliced veneer industry is pivotal to the hardwood sector as a whole, since it influences the price and availability of the highest quality logs in many species. And because of the sensitivity of sliced veneer demand to shifts in fashion, and the huge capital investments required, veneer producers have to keep a particularly close eye on market trends. For these reasons, it is often said that trends in the veneer sector are a good barometer of likely changes in the hardwood sector as a whole.

The news from the European veneer sector tends to confirm the generally gloomy picture painted by the economic data. According to a report in the EUWID, the Germany-based "European Economic Service", sliced veneer manufacturers in Germany are currently operating at only 70%-80% of full capacity. Operating levels are greater at some Eastern European sites but still below full capacity. Manufacturers stock levels are relatively high everywhere. According to EUWID, the German veneer market is "especially problematic" due to the weak situation in private

residential building which is hitting sales to the German internal door industry. Demand for corporate and government offices is stronger, but volumes required in these sectors are relatively low compared to the residential market. Demand from the German furniture sector is described as “stagnant”.

With respect to other European countries, EUWID states that “declines in the German market are currently not being compensated by sales in other markets in Europe or overseas as here, too, selling potential for veneer has for example been dampened by declining building activity and a general holding back on the buying side, as well as insecurity in international financial markets. Sales possibilities in Spain, Greece, Italy, France, the Benelux countries and North America, are repeatedly described as tending to be slow. Some veneer producers report a somewhat more lively demand from various Eastern European markets, such as the Czech Republic and Slovakia, although some veneer prices there are under severe pressure.”

Fashion shifts open the door to tropical hardwoods

Over the last decade, sales of tropical hardwood in Europe have suffered from a major shift in fashion away from darker species towards much lighter temperate hardwood species. White oak has been particularly dominant, to such an extent that prices for this species have risen consistently and dramatically as supply has fallen well short of demand. Data from FEP, the European Flooring Federation, suggest that this trend has if anything intensified in recent times. Between 2005 and 2006, the share of tropical hardwood in European real wood flooring manufacturing fell from 16.6% to 13%. In 2006, oak accounted for a massive 56% share of all real wood flooring produced in Europe.

But while the trade data may not yet be registering any shift back to tropical hardwoods, there is some anecdotal evidence to suggest such a change may be imminent. In a recent article for Panels and Furniture Asia, Michael Buckley of consultancy company World Hardwoods – a close follower of hardwood fashions around the world over many years - makes the following comment: “cycles in the furniture market often give the clue to where the flooring market may be heading in terms of look. There is very clear evidence that furniture is getting darker in colour again and thus one could expect species such as teak, iroko and some South American species such as ipe to become more popular”.

Similarly an article in the UK Timber Trade Journal (TTJ) on fashions in the European wood flooring market notes that there is a growing reaction against the use of low grade wood or imitation wood floors that have flooded the market at budget prices. Consumers are beginning to look for something a little different and “more adventurous”. TTJ quotes a representative of a leading UK flooring supplier: “As part of this market trend, we are experiencing higher demand for more exotic woods such as walnut, panga panga and wenge.”

The TTJ article also notes, however, that European flooring manufacturers are responding to the trend as much by experimenting with new finishes on temperate hardwoods as they are by using more tropical wood. For example, manufacturers are offering more “antique oak” which has been stained and has a brushed and distressed finish.

Another important feature of current design trends is to sharply contrast light and dark colours. Dark flooring may be contrasted with light furniture and vice versa.

Therefore the increase in dark colours may also be matched by an increase in demand for very light species, such as beech and ash.

Both Buckley and the TTJ article stress that the extent to which tropical suppliers are able to exploit the new opportunities emerging from these fashion changes will be heavily dependent on their ability to provide appropriate environmental assurances. European manufacturers are willing to develop and promote tropical hardwood products if they can obtain regular supplies of certified raw material. The TTJ article notes the example of the 6000 m³ of FSC-certified jatoba block flooring recently procured as part of the £800 million project to restore the Eurostar Terminal in London.

UK plywood market remains sluggish

In mid February, the UK TTJ reports that the UK plywood market has made a steady but unspectacular start to the new year, with business confidence levels markedly lower and margins tighter than at the start of 2007. Availability of plywood is generally regarded as sufficient to meet this level of lacklustre demand, partly as a result of overbuying during 2007 in response to supply concerns. TTJ reports that the price advantage of Chinese shippers in the UK market is narrowing as rising freight, labour, raw material and veneer import costs have asked producers to ask for more money. This is already leading to some buyers shifting back to Malaysian and Brazilian hardwood plywood. Also for the first time in many months, there are reports of Indonesian mills picking up limited orders in the UK market.