May 2017
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THE MIDDLE EAST & NORTH AFRICA (MENA)

Economic and Wood Market Trends 2017

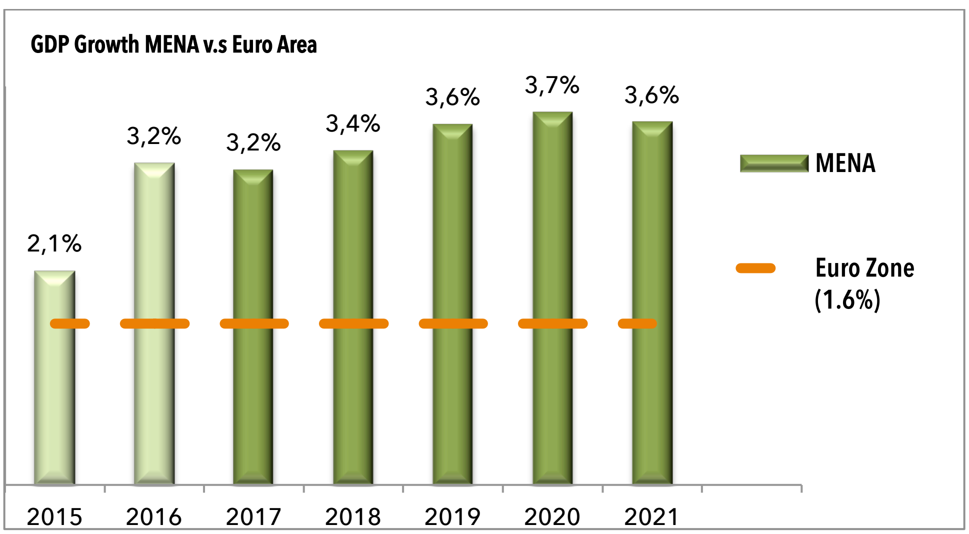
A NEW NORMAL AHEAD, TIME TO RETHINK BUSINESS & DEVELOPMENT MODELS, LESS POLITICAL VOLATILITY, AND A YOUNG & DYNAMIC POPULATION

In a Nutshell:

- Since the collapse of oil prices, actions must be taken by governments to "disrupt" the current situation and rethink their countries' growth model.
- A quite diversified economy (oil & gas, mining, tourism, agriculture, construction, and finance, etc...) with a GDP (Purchasing Power Parity) of $7,989 billion, which grew by 3.2% in 2016.
- An excellent long-term economic outlook driven by a young population: 35% is between 15 and 24 years old.
- Less political volatility. However, exchange rate, sovereign non-payment and supply chain disruption risks remain.
- Corruption and competition from the informal sector negatively impact the business environment.
- A lack of sustainable forests make timber imports a necessity.
- In 2016, Sawn softwood imports decreased by 12%, reaching 11,624 million cubic meters.

The Catalyst: A young and growing population and a developing economy, relying almost entirely on softwood import for construction, furniture manufacturing, carpentry, and other needs.

MIDDLE EAST & NORTH AFRICA ECONOMY: THE FATE OF OIL & THE OPPORTUNITY TO DEVELOP NEW GROWTH MODELS



Sources: IMF / Company data, Comarbois weighted average estimates

The Middle East & North Africa "MENA" region gathers a group of countries, which share a similar culture, Islam as the main religion and Arabic in various dialects as a language. Regrouping such many nations *(Morocco, Algeria, Tunisia, Libya, Egypt, Lebanon, Jordan, Syria, Saudi Arabia, Iraq, Kuwait, Yemen, Qatar, UAE, Oman, Bahrain & Iran)* allows to diversify the economical landscape: oil and gas, tourism, construction, banking, agriculture, mining, telecom and various heavy industries contribute to its growth domestic product.

With 360 million inhabitants – over 1/3 below 24 years old, and a population growing at 1.7% per year, the economical outlook should be outstanding. However, in 20,16 MENA's GDP grew only by 3.2%. It is certainly not enough for a "frontier market" which needs to absorb the ever-growing numbers of young people looking for jobs.

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Back in 2010, the "Arab Spring" and public dissatisfaction with incumbent politicians brought a great political instability in the area, but this time is now over. The political remnants of the Arab Spring, is called ISIL, the Islamic State, or Daesh. Taking advantage of the power vacuum in countries like Libya, Syria, Iraq and Yemen, this group proliferated and gained control of local economies. This has had a highly negative impact on business trade, as it has become increasingly difficult to find a safe port and reliable partner to export goods in Syria or Libya.

The political volatility greatly influences an important source of income for MENA: tourism. Some countries such as Tunisia and Egypt have lost a significant number of foreign tourists as long as their essential cash.

Another significant challenge, reshaping forever the development model of Middle East & North Africa came in 2014.

THE FATE OF OIL

With the development of the shale drilling revolution, green/renewable energy and a slowing Chinese economy, oil prices have fallen over the last few years, triggering a new threat, not only for oil producing countries. Oil always has been "too easy money" for the Gulf Cooperation Council or GCC countries (Saudi Arabia, UAE, Qatar, Oman, Kuwait & Bahrain), Algeria, Iraq and Libya.

Algeria, for instance, has been relying almost entirely on oil and gas exports to finance an ambitious infrastructure investment program (60% of Algeria's budget is dependent on energy income). However, with WTI Crude Oil trading at $45 a barrel, the country has to pump into its foreign exchange reserve (around $116 billion in 2016, 41% down or $195 billion since 2014) to cover demand for imported goods. Oil defines Algeria's economic forecast. The Algerian government is now taking action to reduce its budget, impose import licenses, increase VAT to 19% and promote other fiscal measures as energy revenues decrease rapidly. However, these actions seem too shy and nothing has been done yet to really disrupt the situation. The political decisions are unstable, easy to put in place, but even easier to remove. The recent import license impacting our timber trade is a perfect example: in less than a week, licenses were applied, then removed and finally put back. No bill with long-term effects to open the country up to the World has been engaged yet.

With oil prices at the current level, Saudi Arabia and other Gulf nations also face huge budgetary shortfalls. Plus Saudi Arabia has to finance a costly war in Yemen. But under the leadership of Saudi Deputy Crown Prince Mohammed Bin Salman, the kingdom accepts low oil prices as a new standard. A new growth model is then needed: opening the country to foreign investors, preparing the IPO of the State owned oil company Saudi ARAMCO, introducing a VAT and austerity measures or announcing plan to diversify its economy, all will contribute to better develop this nation.

The volatility of this natural resource's prices reveals a systemic risk: over the year an ecosystem surrounding oil & gas has spread around. Countries importing petroleum like Morocco or Egypt have been waiting for the money (direct investments or donations) from their wealthy neighbors (Saudi Arabia) to fill up their budget.

In 2017, oil exporters in MENA should see their budget deficits shrink as austerity measures, taxes and stable oil prices finally start to take effect. On the long run, the Middle East & North Africa economic development looks extremely promising.

Political volatility or commodities prices may have a negative effect on the possibility of growth in the region. Nevertheless, with land covered by only 2% of forest area, MENA relies entirely on timber imports for all projects.

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The Use of Softwood in MENA:

While the countries constituting MENA may seem similar culturally, the use of softwood varies across the region. Each country has its own particularities with regards to how their construction companies employ softwood. We can divide softwood consumption in three different categories:

(1) CONSTRUCTION / SHUTTERING / CONCRETE: Construction, shuttering, and concrete forming are a prime end-use for timber. With growth in direct correlations with the construction sector - along with concrete and steel rebar - softwood is ubiquitous in the construction processes at several sites in MENA. Steel concrete forming systems and other substitutes are entering this market as well, which represent a potential threat for timber import to the region fostered by a step decrease in steel prices and the modernization of construction techniques. However, the value, ease of use, and versatility of timber is inestimable. Each country adapts their construction methods to their climate, culture, and preferred timber species. For instance, in Egypt, companies mainly consume pine (redwood), while in Algeria and Morocco, they tend to utilize green spruce and maritime pine. Meanwhile, in Saudi Arabia, KD spruce is preferred due to the extremely dry climate.

(2) FURNITURE / DOORS / WINDOWS / INTERIOR DESIGN: Inhabitants of MENA love to use timber as part of their home. Chairs, Arabian sofas, doors, and window frames all employ a great amount of pine in various dimensions and qualities. Egypt is a key destination for rejects grade wood, while higher quality wood has a great market in the Middle East and Algeria. The dimensions are also important components of design and style: While 75x150 (mm) center cuts are popular in Algeria, a more balanced specification with boards is prevalent in neighboring Morocco. Wood is the primary material in the creation of window and door frames, though aluminum and PVC have also crowded the market in the last couple of years.

(3) PALLET / CABLE DRUMS / PACKING: A niche market that is growing nonetheless, pallets, cable drums, and packing manufacturers use maritime pine, spruce, and pine in reject quality. With the development of logistics, retail chains, and manufactured products, we are confident about growth in this sector in the coming years.

OVERALL, 77% OF THE SOFTWOOD IMPORTED IN MENA IS PINE, 21% IS SPRUCE, AND 2 % IS MARITIME PINE.

What are the top softwood exporting countries to MENA in 2016?

Sweden (25%) market share, Finland (23,4%), and Russia (23,2%) are primary pine exporters to MENA. At fourth, Austrian/Slovenian softwood (principally spruce used for construction) accounts for 9% of the volume imported.

TOP EXPORTERS TO MENA IN 2016	TOP EXPORTERS TO MENA IN 2015
#1: Sweden (25%)	#1: Russia (25%)
#2: Finland (23,4%)	#2: Sweden (24%)
#3: Russia (23.2%)	#3: Finland (20%)
#4: Austria/Slovenia (9%)	#4: Romania (10%)

Source: WOODSTAT AB

Scandinavians have a large market share in Egypt and Algeria, while Russia caters to Iran and Egypt and Romania serves Saudi Arabia and the Emirates. In 2016 Finnish sawmills have shipped more softwood to this strategic region.

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WHAT MAKES CERTAIN COUNTRIES SO HOSPITABLE TO SOFTWOOD TRADE WITH MENA?

Like in any market, the presence of a brand or product depends on:

- The global demand for the goods and the willingness of the seller to strategically promote it.
- The willingness of the buyer to obtain the products based on brand recognition, quality, availability, and the price of substitutes.
- Tax or trade agreements between countries and foreign currency valuations.
- The efficiency of the supply chain and logistics that connects sellers to buyers.

This last point has become critical. Some timber exporters have developed extremely well organized logistics, which increases export volume for certain countries. They have managed to build positive momentum by developing networks from sawmills to export platforms (usually in a port), shipping large bulk vessels to decrease freight cost per unit and, in so doing, becoming competitive sellers.

For example, one of the main timber exporters to Algeria is Slovenia. Shipping more than 563,000 cubic meters of softwood in 2016, a handful of traders have leveraged the infrastructure and location of the Koper port to ship substantial volumes of timber from Slovenia and neighboring countries like Austria, Croatia, and Bosnia, to Algeria.

YESTERDAY - TODAY - TOMORROW

Historically, sawn softwood imports in MENA fluctuate at around 12 million cubic meters per year following macroeconomic and political development in the area. To track the trend, it is vital to keep a close watch on the political and economic situation in Egypt, Algeria, Saudi Arabia, and Morocco. Together, those four countries account for 73% of the total volume imported in MENA. **Out of these four countries, only one remains key: Egypt. When Egypt does well, softwood imports in MENA follow, and vice versa.**

After a record year in 2015 when MENA's softwood import reached 13.2 million cubic meter, the volume decreased by 12% to settle at 11.6 million cubic meter in 2016. Indeed, last year, softwood's export to Egypt, Algeria, and Saudi Arabia slumped respectively by 14%, 15% & 15%. Moroccan's imports stayed stable.

A new trend arises in this region: Finland timber exports are getting market share in this area. Shipping primarily pine, Finland compete directly with Sweden and Russia, two countries which delivered 10% and 20% less softwood in 2016 compared to 2015. Finland has been aggressively marketing its timber to MENA, while Swedish and Russian (mainly Siberian) sawmills seemed to focus on Far East i.e China.

Indeed, Siberian mills can efficiently convey their timber via train to China while Swedish factories opportunistically used cheap containers and interesting softwood prices to deliver their goods. However for the last couple months, containers' price to China has been skyrocketing.

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ALGERIA, SAUDI ARABIA AND MOROCCO IN 2016 & 2017

Algeria & Saudi Arabia share the same challenge. They are both in the urgent need to diversify their economy to free it from oil prices fluctuation. And they both selected two different approaches: the Algerian government decided on some heavy import limitations, projects freeze, increasing taxes while Saudi Arabia combines its government spending cuts with deeper economical changes (investing massively in green energy, opening the country to foreign investors…). With regards to Algeria, softwood imports went down by 15% in 2016 at 1.7 million cubic meters.

To better understand, what happened in this key Algerian market in 2016, we must differentiate two segments:

First, Spruce (white wood). This timber, imported mostly from Germany & Slovenia from its port of Koper, goes mainly into construction for concrete forming, meaning it is used at the early stage of a construction project.
With the current oil situation, the Algerian government has decided to cancel, or put on hold, the vast majority of the scheduled projects: social housing, hospitals, infrastructures…
In 2016 there were also an "indirect" license quota on timber (white wood). Since March, there were licenses quotas on cars, cement & steel rebar.
For example, they have limited cement imports to 1 million ton per year while the demand is around 3 million. And local cement factories were not efficient enough to fill the gap… so if you import less cement, you will need less spruce for concrete shuttering.
Imported volume from Slovenia collapsed by 26%. There was a strong pressure on white wood prices. Timber exporters had accumulated heavy volumes in the port Koper hoping to ship it to Algeria. At the same time, Slovenian port authority put a charge (up to 1,5 Euros/m3) per day, to limit the number of days timber exporters can warehouse spruce in the port. There were a pressure to sell quickly but with no demand, prices had to be discounted.

Second, in 2016 pine (red wood) export to Algeria showed some resistance. Red wood, especially higher qualities, comes later in a project to make joineries, windows, doorframes or furniture. So there was a positive momentum: housing & apartments which had been built over the last two or three years needed to be furnished!!

In 2017 in Algeria, this momentum is gone. Softwood export to this country should decrease by more than 17%! Not only spruce but also pine volume should tumble. The Algerian government generalized the import licenses even on timber. At first, they applied it only to importers who wholesale the goods; and then they extended it to industrial firms… took it off and put it back again in less than a week.
As always in Algeria, political decisions are unpredictable and may change from one day to the next.

Saudi Arabia softwood import is also difficult. To limit its budget spending, the government has introduced austerity measures, soared municipality licenses price and will impose a value added tax on selected items in 2018. As a consequence, the construction sector is quite slow.
In 2016, timber export to Saudi Arabia settled at 1.4 million cubic meters, down 15% compared to 2015. Finland became the main Saudi softwood supplier (448 000 m3 vs. 333 000 m3 for Sweden). In 2017, the difficulties to find containers to ship timbers to Saudi, and the ongoing economic downturn will weight on pine and spruce imports. We expect timber imports to decrease by minimum 5% this year and start growing again in 2018.

The Moroccan case is different. Ten years ago, the country understood it had to diversify its economy and started to launch programs to attract investments in various sectors: tourism, mining, car industry, logistics… Morocco is now the world's largest producer and exporter of phosphate, Renault set a gigantic factory and Peugeot is now building one. In addition, the country has one of the largest solar plants in the world. Nevertheless, a major part of the economy is still correlated to agriculture and in 2016 with little rain, the harvest season has been weak. A reason why the GDP is grew by only 1.8% that year.
Morocco has difficulties to find the money to finance its ambitions. And the ongoing liquidity crisis started in 2012 is still here. The State doesn't pay on time, banks restrain credits so construction is slowing down and it has become a custom habit to pay softwood importers after 150 days on average. 2016 was an election year, which means some projects got delayed waiting for the new government to be elected. And on top of all that, the Moroccan Dirham may devaluate in 2017 following a new law making it freely convertible. At the end of 2016, the overall stock level in the country was high and while Scandinavians imports are slightly on the downside, two countries have been delivering more spruce to the kingdom: Austria/Slovenia & Germany (a correlation of the spruce situation in Algeria). This year in Morocco, softwood imports should slide by 5%.

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TIMBER MARKET – Sawn Softwood Import in the MENA Region (1 000 M3)

	2013	2014	2015	**2016**	Est. 2017	Est. 2018	Est. 2019
EGYPT	3 742	4 610	5 113	**4 390**	3 658	3 878	4 071
ALGERIA	1 885	2 036	2 010	**1 710**	1 425	1 539	1 582
SAUDIA ARABIA	1 657	1 531	1 682	**1 429**	1 361	1 429	1 481
MOROCCO	955	960	995	**996**	949	996	1 028
UAE	612	744	696	**699**	659	680	703
IRAN	747	658	780	**714**	800	833	868
TUNISIA	300	400	369	**345**	319	335	349
LEBANON	260	335	264	**204**	216	222	230
JORDAN	326	326	244	**217**	207	214	223
IRAQ	243	301	257	**243**	413	434	455
OTHERS (SYRIA, BAHRAIN, SUDAN, YEMEN, KUWAIT, QATAR, LIBYA)	1 075	1 031	807	**677**	636	689	730
TOTAL	11 802	12 932	13 217	**11 624**	10 644	11 249	11 719
% CHANGE		10%	2%	**-12%**	-8%	6%	4%

Sources: WOODSTAT AB / Company data, Comarbois estimates

A SPECIAL CASE: THE EGYPTIAN MARKET IN 2016 AND 2017

Egypt is the most populated country in the Middle East & North Africa region with around 93 millions inhabitants. With a young population, a quite diversified economy, many different industries and a strategic location on the Suez Canal, it is no wonder why the country is one of the largest timber importers in the World. Egypt posses a real ecosystem and tradition around wood with many small and medium companies are working with this material.

Over the years, the Egyptian's softwood imports have been fluctuating following the country's political and macro economical decisions. In 2015, the Egyptian Central Bank (ECB) decided to impose tight restrictions on the amount of US Dollars that can be deposited in cash at banks. With these new regulations, intended to fight the illegal currency exchange black market, one could only deposit a maximum of $50,000 per month, per bank. On top of that, terrorist

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attacks have a deep negative impact on the revenue coming from tourism. International currencies (especially US Dollars) have become scarce in the banking system. Many timber exporters based in Scandinavia or Russia who financed their Egyptian customers selling them on credit, had difficulties to collect the money. However, in 2015, Egyptian timber importers filled up their yards and vessels continued to flock into Alexandria Port. That year, softwood exports to Egypt reached 5.1 million m3 (11% boost compared to 2014) for mainly two reasons:

(1) the year started with a lack of timber.
(2) some rumors about a possible Egyptian Pound devaluation encouraged companies to "gamble" and buy much more than the market needs.

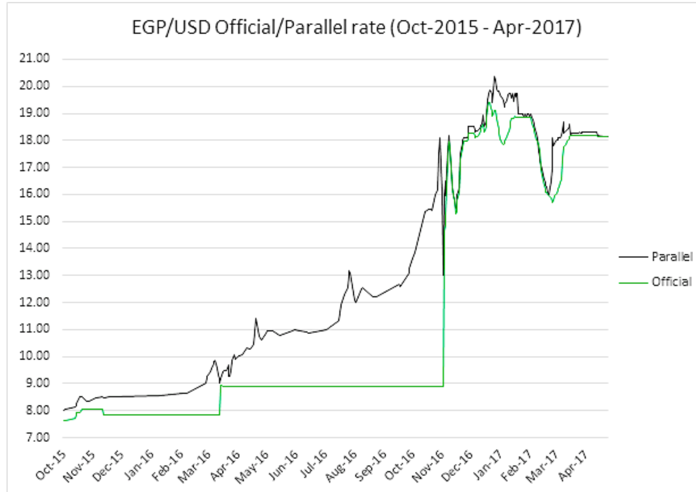
And this trend, primarily based on uncertainties, kept going in 2016… at least for the first half of the year. Until June, timber exports were shifting up. But starting in August 2016, the government scraped the usual 5% Sales Tax to establish a Value Added Tax for sawn timber: a 13% VAT had been applied temporarily. It will be set at 14% on August 2017.

TOP EXPORTERS TO EGYPT (1 000 M3)

	2015	2016
Sweden	1327	1136
Finland	1254	1339
Russia	2061	1577
Germany	15	3
Romania	91	24
US	18	24
Canada	14	9
Baltics	333	275
Austria-Slovenia	0	3
Total	5113	4390

Source: WOODSTAT AB

Egypt also took the spectacular step of allowing its currency to trade freely as it was supposed to be a way of stabilizing an economy paralyzed by a dollar shortage. In November 2016, the Egyptian Pound (EGP) depreciated immediately going from 9 EGP for 1 USD to 18 EGP and soon 20 EGP. Over 100% drop in value. It shows how determined the government is about reforming the country and tightening the gap between official and parallel exchange rate.



Sources: ELSHAL TIMBER, Company data

Costs to build housings and infrastructures double, people are looking for smaller surfaces and naturally many projects got cancelled. Finally in 2016, we saw a 14% drop in Egyptian softwood imports. Earlier in 2017, Egypt decided to lift the $50,000 restriction that could be deposited in cash at banks. The ECB canceled the limitation for "necessity goods" or "raw materials manufactured in Egypt": food, pharmaceuticals and sawn timbers fall into those categories! This should allow Egyptian softwood dealers to have fewer difficulties to pay for the goods.

This year, there are less "barriers" to ship wood to Alexandria; nevertheless we expect a serious drop in Egyptian timber imports again. The construction industry is still weak. For instance, an interesting dimension to monitor is the 25*100 VI and Shall.

"This size is primarily used for concrete forming, scaffolding and represents the most efficient thermometer of the Egyptian building sector."

Over the last nine month, Egypt put a break on this item buying-spree, which can be found available all around Scandinavia. Egyptians' warehouses stocks are now at the "right" level reflecting the real demand in the country. The EGP decline still puts pressure on imports and local clients need to get familiar with new prices. Within the next two months the situation should stabilize. Unlike what used to happen in the past, Egyptian timber merchants avoid to "gamble" buying more than what they could sell based on expected rumors. The business seems to become healthier.

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To satisfy the local demand, we expect Egypt to finally import 325,000m3 softwood per month. Overall, in 2017, softwood export to Egypt should fall approximately by 20% to settle at 3.6 million cubic meters.

RUSSIA, SCANDINAVIA AND CHINA

Historically, Russian softwood (mainly pine from Siberia), has been highly available in Egypt. However, in 2017, timber imports from Russia are at a really low level. Russian sawmills prefer to use a cheap and efficient logistic, shipping sawn timber to China via train.

Since the beginning of the year, Russia is no longer the main Egyptian softwood supplier… Finland is now leading the way! Over the last two years, Finish firms have looked to boost their presence in MENA. They also dramatically increased their exports to China but with the recent shortage of containers (and sharp price inflation) to China, the trend may soon reverse.

WHAT TO LOOK FOR IN 2018 AND BEYOND

The geo-political situation in Middle East & North Africa has been challenging over the last few years. The governments finally understood the urgent need to find new revenue streams and disrupt their old business model relying almost entirely on oil or raw material exports. It may still take some time but MENA is headed toward the right direction. Opening the region to the World, making it easier to do business, fighting corruption and diversifying the economy will guaranty a better future. The softwood business in this strategic area with no forests will follow!

Based on the GDP and population growth in MENA, we do expect this market to grow by an average of 6% annually in 2018 and afterward. The "big four," Egypt, Algeria, Saudi Arabia and Morocco - will continue to import in great volumes. With the end of certain sanctions in Iran, the softwood trade should begin to grow as well.

The most interesting surprise (a drastic increase of softwood imports) could come from countries such as Libya, or Yemen though this is contingent on the peace and stability in the region.