

# A further look at further processing

## **ITTO producers are increasing their share of the secondary processed wood products export market**

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**I**NTERNATIONAL trade of further processed tropical timber has grown rapidly in the last decade while, simultaneously, the trade of primary tropical timber products—logs, sawnwood, plywood and veneer—has started to decline. The growth of further processed tropical timber products is therefore a phenomenon of immense importance for the tropical timber trade and warrants close monitoring.

This article discusses current trends in the trade of tropical secondary processed wood products (SPWP), updating and complementing an article that appeared in *TFU* 11/1 some 18 months ago (Tissari 2001) with data from ITTO's *Annual Review and Assessment of the World Timber Situation*. The primary categories of tropical SPWPs considered here are wooden furniture and parts, builders' woodwork (doors, windows and their frames) and other processed products (for domestic/decorative use, packaging/pallets, coopers' products and other manufactured products such as tools, handles and brooms). Cane and bamboo furniture and parts are included as a fourth category given their growing importance in the exports of many ITTO member countries.

### **The pace of trade growth in ITTO producers**

Figure 1 shows that the value of exports of further processed tropical timber by ITTO producer countries grew more than three-fold in the last decade to just under US\$5.9 billion in 2001, while the value of their exports of primary tropical timber products declined by 18% after 1993 to an estimated US\$9.6 billion in 2001. Much of this growth has been driven by multi-fold increases in exports in Malaysia (up 1368%), Brazil (up 726%) and Indonesia (up 579%). The upward trend in SPWP exports from ITTO producer countries is reflected in an increased share in the global market, up from 9% in 1992 to 16% in 2001.

Apart from a larger contribution to foreign exchange earnings, a greater focus on added value products also pays off in times of market turbulence. During the 1997–98 Asian financial crisis, prices of value-added timber products were much less severely affected than prices of primary timber

products and recovered more quickly. Forest sectors in countries such as Indonesia and Malaysia, whose export strategies aim at downstream processing, fared better than countries exporting only primary products.

Figure 2 shows the breakdown of SPWP exports of the top ITTO producer exporters in 1999, the reference year for SPWP in ITTO's 2001 *Annual Review*. The figure shows that four of the top five ITTO producer exporters of SPWP are Asia-Pacific countries. The top five accounted for almost 97% of total ITTO producers' SPWP exports in 1999, with Asia-Pacific countries making up 85% of the total; Latin America, led by Brazil, accounted for most of the balance (14%). Brazil has developed a large-volume industry based on further processing located largely in the temperate zone of the country (where the domestic markets and the plantation estate are concentrated). Downstream timber processing is still minimal in Africa, due largely to a lack of capital and infrastructure. Nevertheless, countries such as Ghana, Cameroon and Gabon are making the development of secondary processing a priority. Practically all the export-oriented further processing industries in Ghana are foreign-owned and many produce components for the captive markets of their overseas owners.

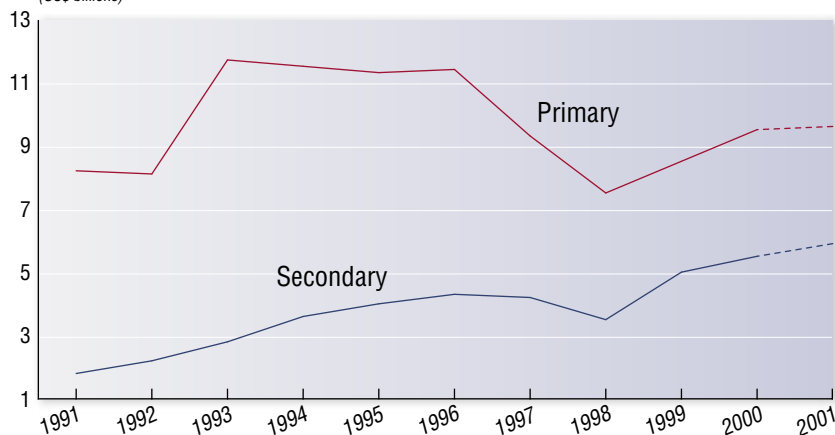
Figure 2 also shows that furniture is the mainstay of exports, accounting for over 55% of total value. Malaysia is by far the largest supplier of furniture among ITTO producers, with exports of products in that category worth over US\$1 billion; Indonesia shows a more balanced portfolio of export products. Most Malaysian exports of further processed products originate in Peninsular Malaysia, while exports of primary products come primarily from Sarawak. In Brazil, furniture—mostly aimed at the exterior furniture market—has been gaining a larger share of total exports at the expense of builders' joinery.

Malaysia's main trading partners in 1999 were USA (35%), the European Union (EU; 18%) and Japan (13%). Indonesia shipped nearly three-quarters of its SPWP to these three destinations, the EU accounting for 34%, the USA 22% and Japan 16%. Thailand's main trading partners were the USA (38%) and Japan (33%) in that year. Thailand was the main supplier of furniture to Japan in 1999, capturing 20% of Japan's US\$1.2 billion market for this product. Malaysia and Thailand have demonstrated the possibilities offered by plantation wood by using plantation rubberwood for 80% of their furniture exports. Brazil's SPWP exports go predominantly to the EU (45%) and the USA (37%). Brazil's SPWP production is based mainly on pine and, to a lesser extent, eucalypt plantations in the southeast.

Figure 3 shows that, overall, most SPWP exports from ITTO producer countries go to the USA (37%), the EU (32%, led by the UK, Germany, France and Netherlands) and Japan (14%). In terms of market share, these figures represent one-fifth, one-tenth and one-third respectively of the markets in those countries. The market shares held by ITTO producer

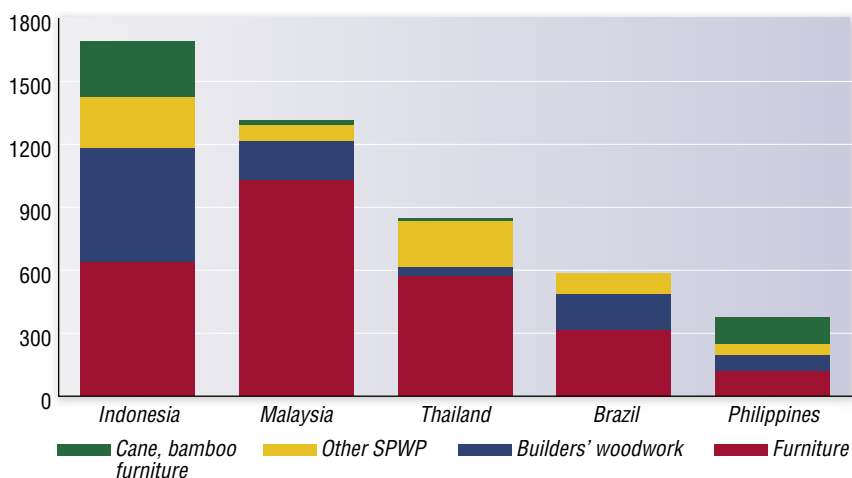
### **The rough and the relatively smooth**

**Figure 1:** The value of ITTO producer exports of primary and secondary tropical timber products (US\$ billions)



## Five of the best

**Figure 2:** Top ITTO producer SPWP exporters in 1999 (million US\$)



countries are gradually declining in the USA and increasing in the EU, while the Japanese market share is relatively stable. Transportation costs, tariff levels and regional marketing relationships play a role in the differences in market share held by ITTO producers in the major markets for SPWP, but there is clearly a substantial opportunity for all producing countries to continue increasing their market share, particularly in the enormous European market.

## ITTO consumers still lead the trade

Although SPWP trade is a growing source of foreign revenue for ITTO producer countries, ITTO consumer countries still dominate the SPWP export marketplace. The combined value of all SPWP exports from ITTO producer countries fell short by 15% of Italy's SPWP exports in 1999, though this gap narrowed in 2000–01. Figure 4 shows the breakdown of the world's top five SPWP exporters in 1999, which collectively accounted for around two-thirds of total ITTO consumer SPWP exports; EU countries made up 69% of the consumers' total. Italy is by far the world's largest exporter of SPWP, comprising about one-third of the US\$19.6 billion of EU SPWP exports. Furniture is the dominant product, accounting for over 69% of total value and 89% of Italy's SPWP exports. The bulk of Italy's SPWP shipments go to other EU countries (54%) and the USA (15%). Italy is particularly successful in furniture markets because of its high-quality, fashionable designs, skilful labour, state-of-the-art technology, good service and exceptional access to high-value markets.

Canada, Germany and China are other major SPWP exporters. While Germany's exports have been stable or declining over the last decade, Canada and China experienced phenomenal growth in SPWP trade, with exports growing four-fold and three-fold respectively in the same period. Virtually all Canada's SPWP exports are absorbed by the USA.

## China: the new competitor

China is by far the top exporter of SPWP in the developing world and is expected to soon overtake Germany as the third-

largest exporter globally. Most of China's SPWP exports in 1999 went to the USA (39%), Japan (19%) and the EU (14%).

The economic growth seen in China in the last few years has attracted foreign investment in the SPWP sector, mainly from the USA and Taiwan but also from other traditional Asian producers. This has been facilitated by low wages and a policy towards encouraging downstream

timber processing. SPWP manufacturers based in China have been successful in penetrating high-value markets such as Japan and, particularly, the USA with their furniture. China has developed a special ability to provide products well suited to changing fashions in the USA at highly competitive prices.

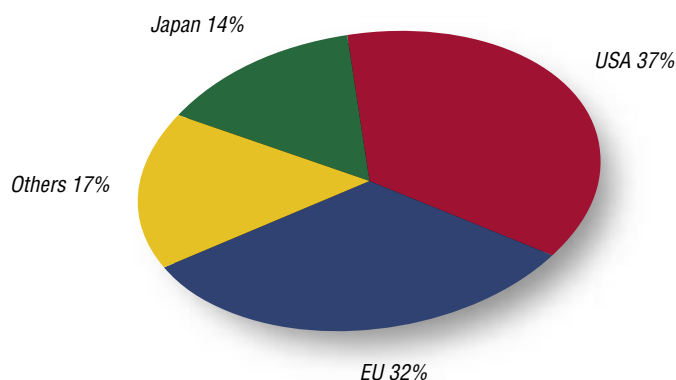
US imports of Chinese wood furniture have increased three-fold since 1992; China is expected to soon overtake Canada as the largest supplier of furniture to the US. The impact of this on the US domestic industry is being seen in the closing or restructuring of furniture plants. Over the next few years, many US furniture companies will more than likely shift their production to the Far East and focus on marketing and distribution at home. From the point of view of ITTO producers, China is a major competitor in its main export outlets; in fact, China overtook Thailand in 2000 as Japan's largest supplier of furniture.

## Future outlook

It is apparent that developing countries have been able to expand their participation in the international trade of SPWP at the expense of industrialised countries and this trend is expected to continue. For example, Malaysia is moving from OEM (original equipment manufacturing) to ODM (original design manufacturing) and aggressively

## The SPWP pie

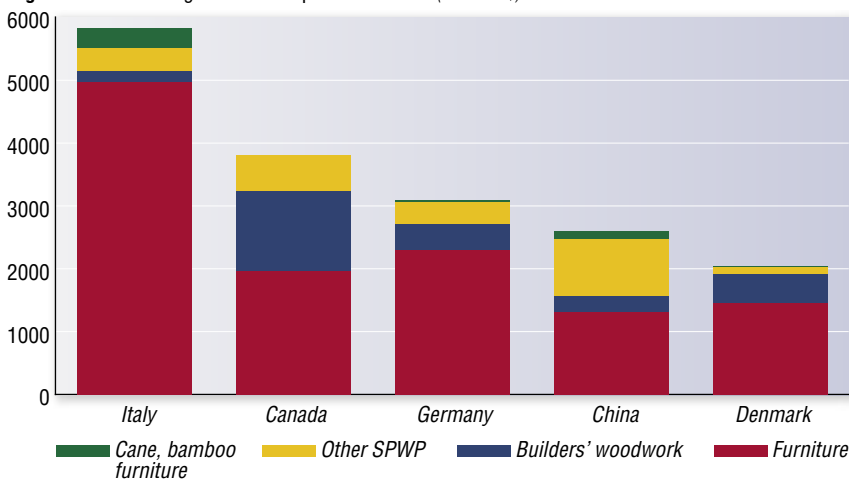
**Figure 3:** Major markets of ITTO producer SPWP exports in 1999 (% of US\$4.98 billion)



seeks new market outlets for its higher-value products. The driving forces behind the expansion of developing countries in international SPWP trade include the widening availability of good-quality plantation timbers, lower wage costs, improved technical and managerial skills and technologies, systematic market promotion efforts and supportive institutions and rational policies. The growth of the SPWP sector in China presents a significant challenge to the sectors in ITTO producer countries: China has the potential to greatly erode the market share of tropical producers as its production continues to grow.

## Tall timbers

**Figure 4:** World's largest SPWP exporters in 1999 (million US\$)



## The benefits of downstream processing

Downstream timber processing and trade in producer countries are important earners of revenue and sources of local employment. These are, in turn, key multipliers that contribute to the economic growth of countries. Trade strengthens the capacity of developing countries to generate foreign exchange, which empowers them, in particular, to alleviate poverty and to address pressing development challenges. If appropriate domestic forest policies are in place, the timber trade and the processing industry on which it is based bestow value to forests, which would otherwise be vulnerable to conversion to competing land-uses that generate more immediate income.

Although SPWP trade is growing in developing countries, it is still well below its potential. Tariff differentials are one reason for this. Most developed countries apply higher import tariffs to SPWP than they do to most primary timber products. Tariffs for wood-based panels, builders' woodwork items (windows, doors, frames), furniture, other value-added products and various types of paper products are in the range of 10–15% in many countries (particularly the EU) but less than 5% for products such as logs and sawnwood. These tariffs become particularly burdensome for distant suppliers since duties are usually charged on the cost-and-freight (CIF) price. Tariff escalation discourages the development of domestic value-added wood processing and encourages the export of less processed forms.

However, the USA, Canada, the EU and Japan are all expected to de-escalate tariffs on some SPWP products by 2005 under the General Agreement on Tariffs and Trade, and this will likely lead to further boosts in SPWP exports from ITTO producer countries. A gradual tariff de-escalation is expected to primarily benefit countries such as Malaysia, China, Thailand, Indonesia, the Philippines and Brazil that have established policies for encouraging the expansion of downstream processing capacity and export.

Another element that restrains further growth of SPWP exports for ITTO producers is product design. With few exceptions, most of the further processed products currently exported by ITTO producers are made-to-order, with little innovation or design input, which is often provided by the buyer. There is a growing need to infuse technical and design know-how into these industries and to create larger and stronger units capable of capturing international markets.

The further processing sector will continue to expand, partly because of the eventual de-escalation of import tariffs and continual improvement in product design. However, given the declining availability of large-sized timber, the sustainability of this growth will depend on new end-uses being found for lesser used species, new techniques to meet the technical and aesthetic appearance requirements of markets, and on new technologies to make efficient use of smaller dimension logs from fast-growing plantations.

## References

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