

## UNECE Timber Committee Statement on Forest Products Markets in 2007 and Prospects for 2008

The UNECE Timber Committee adopted the entire official text below on 11 October 2007.

### I. Overview of forest products markets in 2007 and 2008

The first joint UNECE Timber Committee and International Softwood Conference Market Discussions emphasized the new market situation developing from governments' commitments and industries' actions to fight climate change, mainly through the promotion of renewable energy sources, especially woodfuels. All wood markets are affected, both positively and negatively, and new opportunities and challenges are evolving for the sector, from forest owners, to wood processors, to wood energy consumers. Forest products markets are forecast to decline in North America, and dramatically for sawn softwood, due to the crash in the United States housing market, in contrast to positive developments in Europe and Russia.

Policy decisions and markets are interacting in complex ways, developing new opportunities and constraints for market actors. One example is policies to promote bioenergy, which, together with the high oil price, have already caused a steep rise in the consumption of wood for energy, and opened the prospect of significant new markets. This is the topic of the policy forum organised in connection with the Committee's session (see separate press release).

**Public procurement policies.** Increasingly, procurement policies, by public agencies or private firms (for instance large publishing groups or building supplies wholesalers and DIY outlets), are adding other criteria than price and performance to the decision making process. Many purchasers are now insisting that forest products must come from sustainable, or at least legal, sources, and that this be verifiable, in order to maintain credibility with public opinion.

In the UK, for example, the Government announced that from April 2009 its central departments will purchase only timber and timber products that derive from sustainably managed forests or are licensed under the EU Forest Law Enforcement, Governance and Trade (FLEGT) regulation; from April 2015 only sustainably produced timber will be purchased. This policy is at present under consultation and may be modified. Purchasers also aim to minimise the environmental impact of whole systems, for instance through "green building" requirements aimed to reduce energy requirements of creating and occupying buildings. How these requirements, whether for sustainability of forest management or for energy efficiency, are specified in detail is already influencing markets for forest products.

**Corporate social responsibility.** The private sector is responding to purchasing requirements by developing its own best practice guidelines: the UK Timber Trade Federation (TTF) issues specific guidance on buying compliance through its Code of Conduct for purchases from high risk countries. Companies are also developing more ambitious corporate social responsibility (CSR) policies, aimed at demonstrating the positive social impact of their operations, including safety and health, avoidance of "conflict timber", respect for indigenous peoples, children, and local populations. It is to be expected that the social dimension of companies' operations will become subject to more intense scrutiny in the future. Such policies can be a means for shaping consumer perceptions, and gaining a competitive edge, as well as international recognition and an improved perception of the company. The Quebec Wood Export Bureau called for mutual recognition of trade associations' CSR policies in order to facilitate trade between importers and exporters. It was suggested that the Timber Committee be more involved in CSR.

**Russia.** Russia has made changes in its forest sector policies which will influence conditions for trading partners, in particular the imposition of duties on exported logs, scheduled to reach prohibitive levels by 2009, in order to encourage domestic processing of wood, and investment in the Russian wood processing industries. Importers of Russian roundwood and other market actors are considering how to adapt to the changed supply situation. The new Russian Forest Code, adopted in January 2007, unifies national forest policy and promotes structural reform.

**Wood promotion.** There was broad agreement that the time was ripe to promote wood's role in tackling climate change. Several countries, mainly in Europe, have successfully raised public awareness through promotion campaigns though there is still a need to persuade key influential groups, such as parliamentarians. The 2010 Vancouver Olympics and the 2012 London Olympics represent a major opportunity to showcase wood. There is a need also to establish confidence in standards of forest management to counter the idea that using wood is bad for the environment, a message that the concrete and steel lobbies have presented in misleading marketing campaigns. Certification was highlighted as an important communication tool. The need for a consistent approach in describing specifications for wood to aid the choice of wood for construction was identified.

**Certified forest products.** Certified forest area is approaching 300 million hectares worldwide in mid 2007, with most in the UNECE region's forests. Chain-of-custody – tracing wood products back to their origins to verify legality and sustainability – is important

to achieve the full benefits of certification. In North America, most chain-of-custody certificates are held by the paper industry, which along with publishers, are key drivers of certification. Another driver is the US Green Building Council which developed the Leadership in Energy and Environmental Design (LEED) rating systems which specify certified wood products, although it accepts only the Forest Stewardship Council system. Trade associations stressed the need for green building rating systems to have a more inclusive approach and accept all internationally recognized sustainable forest management (SFM) standards such as CSA (Canadian Standards Association SFM Standard), PEFC (Programme for the Endorsement of Forest Certification schemes) and SFI (Sustainable Forestry Initiative) and also have a life-cycle analysis based approach. Almost half of LEED projects are by government agencies, mostly due to mandatory requirements. States' forestland is increasingly certified in the US, and the federal forestlands are under consideration for certification. Acceleration in certification for woodfuel, in conjunction with fire reduction, was forecast to drive further certification in the US.

**CE marking and stress grading.** The availability of new techniques for non-destructive testing of sawnwood and engineered structural components is enabling wood to compete in new markets where it could substitute for steel or concrete elements. The adoption of stress grading will be essential to comply with the European Union directive on CE marking for construction timber, which is due to take effect from 1 September 2008, having been postponed at the industry's request from 1 September 2007. The state of readiness of producers to comply with CE marking varies widely but users were adamant that buyers would become more selective and would expect producers to be ready to implement CE marking in 2008.

**Markets for modified softwood.** New processes that overcome some of wood's traditional weak points, such as moisture sensitivity, dimensional instability and lack of resistance against fungi, are creating 'new materials' that open up new marketing possibilities for both softwood and hardwood, which should allow wood to take market share from competing building materials.

## II. Economic situation

Growth in the global economy is strong, over 5% in 2007, with a slowdown of growth in the US, a levelling off in Europe and Japan and rapid growth in Latin America, Africa and Asia. Growth rates in EU15 and North America in 2007 are expected to be around 2.5%, with higher rates (5-7%) in eastern Europe, Caucasus and central Asia. Similar growth rates are expected for 2008. The high price of oil and the financial turmoil linked to hedge funds are slowing down growth. The US dollar has fallen steadily since 2001 against the euro, the Canadian dollar and other currencies, and is

expected to fall further as reaction to the continuing US current account and budget deficits. The US housing market is experiencing serious problems, with falling house prices, growing inventory of unsold houses and housing starts now below 1 million per year (annual rate). Housing permits as of August 2007 are also down by over 40% compared to August 2005. Europe shows some symptoms of a similar problem in the housing market, but by no means so severe as in the US, although it is already feeling the effects of the housing crisis in the US, transmitted through the financial markets. Higher interest rates and declines in house prices affect the broader economy through reducing demand for new homes, reducing consumer wealth and generating financial turmoil due to mortgage defaults.

## III. Market sector developments

**Wood raw materials.** Strong sawnwood and pulp markets in 2006 brought roundwood prices into record highs. Total removals in the UNECE region reached 1.3 billion m<sup>3</sup>, only marginally below the exceptional level of 2005 that was influenced by significant volumes of storm-damaged timber, especially in Sweden. European removals are forecast to increase by 5.4% in 2007 as Swedish removals recover from the post-storm level of 2006. Looking ahead to 2008, removals are forecast to remain almost unchanged, in spite of the drastic reduction in housing starts in the US. The introduction by Russia of rising export taxes on roundwood, with the full impact for softwood being felt by January 2009 and for hardwood (mainly birch) by January 2011 will undoubtedly cause a significant reduction in exports. Russian exports of roundwood are expected to peak in 2006: softwood log exports at 20.5 million m<sup>3</sup> are forecast to halve to 11.0 million in 2008. Some countries have come to depend heavily on Russian-sourced roundwood and already have begun to look for other sources, as well as investing in Russia.

**Wood energy.** The increasing use of wood for energy throughout the UNECE region, driven by policy measures and high oil prices, is reshaping markets for wood and presents both a challenge and an opportunity for the forest and wood processing sectors. The rapidly evolving market dynamic presents a challenge also for public policy development, which will have to try to balance the needs of the established wood products sector and the bio-energy sector.

Demand for processed fuels such as wood pellets is at record levels, resulting in shortages and higher prices in parts of Europe. Manufacturers, who until now have relied on sawdust as their main raw material, are having to look to other materials, such as wood chips and roundwood, to keep pace with the burgeoning demand. One source is the expanding volume of trees killed by the mountain pine beetle in British Columbia, Canada. Currently about 80% of pellet production from North America is exported to Europe.

Recent efforts to improve data quality have revealed that in many countries much more wood is used for energy than previously reported. Official figures often do not include: 1. wood that was harvested and used by individuals and which did not enter the market, and 2. wood from outside forests and recovered wood.

**Sawn softwood.** Overall in the UNECE region, sawn softwood markets are forecast to decline from record levels in 2006, due to the collapse in the US housing market. From a high annual rate of construction of 2.3 million housing starts in early 2006, the Timber Committee heard a forecast for only half that amount in 2008. US consumption of sawn softwood is expected to fall by 10.8% in 2007, and a further 2.3% in 2008, down to 90.9 million m<sup>3</sup>. Production in North America (US and Canada) is predicted to fall by 5.8% in 2007, and another 1.0% in 2008, down to 116.1 million m<sup>3</sup>. US imports are forecast to fall even more, by 17.1%. With low sawnwood prices, and a weak US dollar, many European exporters have withdrawn from the US market, and although the US remains Canada's prime export market, Canadian suppliers are exploring opportunities in offshore markets. Low sawnwood prices have also triggered the maximum export charges provided for under the renegotiated Softwood Lumber Agreement (SLA) on Canadian shipments of sawn softwood to the US. A SLA dispute in autumn 2007 is being submitted to an arbitration tribunal. North America is forecast to return to being a net exporter of sawnwood.

In contrast to North America, European sawmillers are forecast to increase production in 2007, by 4.3%, and another 0.4% in 2008, to a record 116.2 million m<sup>3</sup>. European mills which had in 2006 experienced log supply problems and higher prices, to some extent driven by energy policies, suddenly found a reversal in January 2007 when two windstorms caused heavy damage to forests in Austria, Belgium, Czech Republic, France, Germany, Poland and southern Sweden. As roundwood supplies returned to normal levels over the year, prices rose, along with sawnwood prices. European consumption of sawn softwood is forecast to grow too, peaking in 2007 at 108.1 million m<sup>3</sup>.

The Russian sawmilling sector expects benefits from export taxes on roundwood, and both foreign and domestic investment. Production is forecast to leap by 8.9% in 2007 and by a further 11.8% in 2008, to reach 24.1 million m<sup>3</sup>. Most of the increase is destined for export markets, which could rise by 9 to 10% in each of the next two years, reaching 18.4 million m<sup>3</sup> in 2008.

The Committee discussed the new requirement that structural timber in the European Union have a CE mark from September 2008. Companies in several supplying subregions, including many in Russia, were not ready for this requirement and this could constrain Russian exports to Europe.

**Sawn hardwood.** Sawn hardwood markets are forecast to remain buoyant in the UNECE region. European markets are forecast to grow by about 2.4% in 2007 for both consumption and production, with little changes in trade. In North America, sawn hardwood production, similar to sawn softwood, is forecast to fall in 2007, but by much less, only 1.7%, to 28.5 million m<sup>3</sup>, and a recovery is forecast for 2008. Europe, US and China are demanding European and American white oak, and sawnwood prices rose in 2007. Beech demand is up too, with a rise in prices. A new study in the US aims to ensure hardwoods are traded with confidence in terms of legality, coinciding with a proposed Senate bill to combat illegal logging. Developments in tropical sawnwood according to the International Tropical Timber Organization include a slowing decline in forest cover, a decrease in log exports in favour of value-added processing and continued illegal logging. Tropical sawn softwood trade is not currently significant on global markets as the majority of plantation-produced softwoods are used domestically.

**Wood-based panels.** European panel markets are forecast to continue growth in 2007 and 2008 in production and consumption, despite rising energy and wood raw material costs and global competition. Rising wood prices, in part driven by renewable energy policies, and resulting uncertainties with regard to wood availability, as well as difficulties to source supply from small forests owners are challenges confronting the European woodworking industries. MDF and OSB are expected to increase production and expand market share at a fast pace, due to higher demand from the construction industry, the revival of the furniture sector, packaging and flooring. Plywood production is expected to remain stable, facing difficulties because of severe competition from South American and Asian countries. The production of particleboard, by far the most important panel type in Europe, has been increasing steadily, though it lost market share due to the rapid expansion of other panel types. It is forecast to reach a record 47.5 million m<sup>3</sup> in 2008. Capacity expansions mainly in eastern Europe are projected, mostly to satisfy domestic demand.

North American panel markets are forecast to remain relatively stable at 2006 levels, with slight increases for 2008, despite a sharp decrease in construction activity. After a decline of particleboard production in 2007, an increase in 2008 is forecast. OSB production is expected to continue gaining market share from plywood. Plywood lost market share, mostly to imports, especially from China.

Russian particle board and MDF production is forecast to grow in 2008 by 8% and 52%, respectively, over 2007 levels, although they remain low in comparison with other subregions. Until 2008, increases in production are forecasted for domestic use by the construction and furniture industry and exports, mainly to neighbouring

CIS countries. The trend of increasing production of plywood is forecast to continue, to satisfy export markets, mainly in the EU. Plywood is by far the most important panel type in the Russian Federation, which produces and exports more plywood than any other European country.

**Paper, paperboard and woodpulp.** The paper and paperboard sector in the UNECE region is marked by expansion in Russia, where consumption is forecast to increase by 5.1% between 2006 and 2007, contrasting with the situation for other regions where little change is expected in production or consumption.

European consumption will remain around 97 million m.t. from 2006 to 2008, and North American consumption just below 101 million m.t. over the same

period. In other parts of the world, stronger increases were reported for many grades. Asian production grew by 9% in 2006, compared to 3.2% for Europe and 0.1% for North America. Capacity expansion for paper has been correspondingly stronger in Asia and Latin America than in Europe or North America. Pulp consumption is expected to remain stable in all three sub-regions, although European pulp production is forecast to increase by over 1 million m.t. and exports by 0.6 million m.t.

The Confederation of European Paper Industries (CEPI) reported that in its member countries (most of western Europe) in 2006 consumption of recovered paper exceeded consumption of virgin pulp for the first time, despite exports of recovered paper to Asia of over 7 million m.t.