

UN/ECE TIMBER COMMITTEE AND FAO EUROPEAN FORESTRY COMMISSION STATEMENT ON FOREST PRODUCTS MARKETS IN 2005 AND PROSPECTS FOR 2006

Abridged version - the entire official text of the Market Statement
was adopted by the UN/ECE Timber Committee
at its sixty-second session in Geneva, Switzerland, 30 September 2005
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Overview of forest products markets in 2005 and 2006

The UNECE Timber Committee reviewed the current major developments affecting forest sector policies and markets: illegal logging, inside and outside the UNECE region, the threats to economic viability of forest owners and industries from intense global competition, the challenge and opportunities presented by the growing demand for wood energy and the coming into force of the Kyoto Protocol. Governments, civil society and industry are working increasingly together to address these issues, for instance through public procurement policies, certification, corporate responsibility measures, “green building” schemes and improved communication.

The coming into force of the **Kyoto Protocol** in 2005 has brought attention to the multiple positive roles of forests and wood in carbon cycles: mitigation of the negative effects of climate change, sequestration of carbon, provision of a renewable carbon neutral energy source, substitution for non-renewable fuels or raw materials, and contribution to energy conservation. It should be better known that wood, coming from sustainable managed forests, is truly friendly to the environment: a much greater communication effort is needed to fix this impression in the public mind, replacing the many misconceptions there are at present.

The complex provisions of the Kyoto Protocol will influence all parts of the sector. Governments, the private sector and civil society should together analyse these consequences and take a proactive role in developing a strategic response to the challenges and opportunities. In the short term the main consequence has been the increased policy support for developing wood energy: many countries reported policy instruments in support of wood energy, driven by the Kyoto Protocol, but also by concerns for security and sustainability of energy supply and the high price of non-renewable energies. In some countries, prices for wood energy have risen, and there are indications that volumes have increased,

although the statistical system for monitoring this sector is still very weak. Representatives of the forest industries expressed concern that policy instruments in favour of renewable energy sources are distorting wood markets. It was pointed out that many parts of the economy were influenced by policy incentives, and that all actual or potential distortions should be taken into account, not only those linked to renewable energy. The Kyoto Protocol presents an additional opportunity to promote forests and wood products.

The **catastrophic windstorms** in the Baltic Sea region in January 2005, and the hurricanes in the Gulf region of the United States in September 2005, caused extensive forest damage with subsequent effects on roundwood and residue production. The ramifications are affecting primary wood products production in North America and Europe and have altered trade patterns.

The widespread and significant consequences for the forest sector in the UNECE region of the expansion of the **Chinese forest products industry** were discussed. Chinese industries are buying wood raw material and primary products (logs, sawnwood, recovered paper) from the UNECE region, as well as from other regions, and exporting manufactured products, notably plywood and furniture. As a consequence of the large scale of the operations and the low Chinese labour costs, prices have fallen all along the supply chain, reducing the economic viability of the European forest and timber sector. China is now the largest plywood exporter in the world and the second furniture exporter. As a response to trading practices which they consider unfair, the EU has put anti-dumping measures in place for plywood, and the US has set punitive tariffs on some Chinese furniture. At the joint EU-China summit in September 2005, the leaders of the two sides pledged to work together to tackle the problem of illegal logging in the Asian region. Meanwhile some North American and European companies are moving woodworking operations to China while maintaining their domestic marketing operations.

Certified forest products

Certification policies are influencing all forest products markets sectors in the UNECE region. About 50% of the forests in western Europe and North America are now certified for sustainable forest management according to independent, internationally recognized certification programmes. Certified forests in North America and Europe account for over 96% of the world's certified forests. Demand for certified forest products is growing, driven by concern for the sustainability of supply, either by companies up and down the wood chain, or by purchasers of wood and paper products, especially business-to-business and governments. Considerably less tropical forests are certified (approximately 1% of certified forests). It is now difficult to export products from uncertified tropical forests to environmentally sensitive markets in the UNECE region, for example to the Netherlands and United Kingdom. Conversely, tropical timber from certified forests in some tropical countries, e.g. Malaysia, is finding improved export opportunities and strong market growth. Many tropical countries are not able to achieve certification in the short term and are advocating a phased approach towards certification of sustainable forest management, to enable market access during the necessary transition period and to maintain revenues to pay certification development costs. In Russia, certification of sustainable forest management is starting, and according to forecasts it will be further developed. In Europe and North America so far the great majority of forest owners have not received any premium from sales of certified wood.

Corporate responsibility

Faced with concerns about illegal logging and other issues, companies in the sector, either alone or through their trade associations, are establishing corporate responsibility programmes to protect and even gain market share in environmentally sensitive markets. Many forest products companies are striving to develop the environmental and social values of forests while maintaining their own economic viability. Companies are aiming to minimize the risk of using controversial sources, by buying sustainably, or at least legally, produced wood. Some firms are benefiting from growing markets by local and national government procurement policies specifying sustainably and legally sourced timber. Trade associations stated that the multiplying public procurement programmes, with their wide variation in requirements, which

sometimes specify only certain certification schemes, are making it more complex and expensive to meet requirements of public purchasing officers. Associations call for harmonisation between the requirements of different government procurement policies. Better understanding and communication is needed on public and private (corporate) procurement policies.

Overall Economic Outlook

World economic growth is expected to remain robust, although the rate of expansion will decline slightly, from 3.8% in 2004, to about 3% in 2005 and 2006. The major engines of growth have been China and the USA, but there has also been solid growth in central and eastern Europe, south east Europe and the CIS. The euro zone however has shown relatively modest growth (less than 2% in 2004) and a slowdown to about 1¼ per cent is expected for 2005. Record high and rising oil prices are dampening global economic activity. House prices have shown unprecedented growth in recent years in some countries, notably the USA. Downside risks to the short-term outlook include a further significant rise in oil prices, the widening of global external imbalances (countries expressed concern about the large US current account deficit), a sharp rise in long-term interest rates and a sudden sharp reversal of the rise in house prices.

Market Sector Developments

Wood raw material including wood energy

Following record removals in 2004, roundwood removals are forecast to grow slightly in 2005 with further modest growth in 2006. The storm damage in Slovakia in late 2004 (7 million m³ affected), and the Baltic region in early 2005 (85 million m³ affected, of which 75 million m³, mostly spruce, in Sweden) influence these trends. In Sweden, almost half the windblown volume has been harvested, although much is still at roadside or being stocked, and the work is expected to be complete by the first half of 2006. Fellings have risen in the affected area of South Sweden and fallen elsewhere. Exports of spruce have risen, and imports fallen. Pre-storm market conditions are expected to return in 2007-2008. The hurricanes that battered the Gulf region of the US in late 2005 will also bring large volumes of roundwood to the market, at the same time as creating a huge demand for housing repair and reconstruction. Global competition has forced down roundwood prices on many markets, although the rising demand for wood energy may

cause more positive price signals. There is evidence that consumption of energy wood is growing in many regions under the influence of a high oil price and official policies to reach renewable energy goals and Kyoto Protocol commitments.

Sawn softwood

Consumption of sawn softwood was at record high levels in 2004 in the UNECE region, and is forecast to increase by approximately 2% in 2005 and 2006 in Europe and North America, and by even more in Russia. Production and trade are similarly forecast to rise to new records in all subregions in 2005, although in 2006, exports are expected to drop slightly in Europe and North America. For the first time since 1998, exports of Russian sawn softwood are not forecast to increase in 2006, in line with an anticipated rise in domestic consumption. Russia's exports to its important UK market have fallen because of lack of certification of sustainable forest management, although other environmentally sensitive European markets have been maintained. In order to achieve better cooperation between the woodworking industries the European Confederation of Woodworking Industries (CEI-Bois) has launched the Roadmap 2010 action plan for public recognition of wood products as the leading material. The windstorms in the Baltic Sea region in January 2005 led to an oversupply of roundwood, mainly in Sweden: this will raise Swedish sawnwood production by an estimated 6% in 2005, or by 1 million m³. North America became a net importer for the first time in 2004, and this situation is forecast to continue in 2005 and 2006, despite increases in production in both Canada and the United States. The September 2005 hurricanes in the Gulf region destroyed up to a 400 000 (wood-based) homes, and damaged a similar number, and will create an additional demand for sawnwood and other wood products for their reconstruction and repair.

Sawn hardwood

The Committee's forecasts for sawn hardwood markets are optimistic for 2005 and 2006, with rises in Europe and North America for consumption, production and trade. Demand for sawn hardwood is forecast to rise in 2005 by 5% in Europe, and 4% in North America, and by lesser amounts in 2006. European exports are forecast to continue falling in 2005, with a slight rise in 2006, while exports are expected to end a 4-year drop and begin rising. The US forecasts large import increases in 2005 and again in 2006,

presumably from offshore, while it also forecasts large increases in exports in 2005, up by 5%, and in 2006, up by 9%, with some of the increase going to Europe. Exports to the Pacific Rim will slow from the record levels in 2004. One reason for the optimistic forecasts for 2006 are new hardwood promotion efforts in the US by the Hardwood Federation, and in Europe by the European Hardwood Export Council. Hardwood producers and traders are turning increasingly to certification for assurance of the sustainability and evidence of legality of the timber. Despite the positive nature of the forecasts in Europe, hardwood trade associations drew attention to poor economic viability of the sector. Severe price erosion has been experienced for beech sawnwood in Germany, falling by 60% over the last 7 years. Beech sawlogs have dropped more, by 87%, down to a price in 2004 of Euro 52/m³. Meanwhile over the past 5 years, a few large-scale hardwood sawmills have been built in western Europe, while a number of smaller mills have gone bankrupt. Sawn hardwood producers in both North America and Europe are losing domestic markets for furniture manufacturing as capacity for these sawnwood-consuming industries moves to eastern Europe, CIS and Asia.

Wood-based panels

Consumption of wood-based panels (plywood, particle board, OSB and fibreboard) in Europe in 2004 attained a new record level of 59.2 million m³. The Committee's forecasts confirm continuation of this trend. In 2005 consumption will increase by 2.7% to 60.8 million m³ and marginally in 2006, with MDF and OSB continuing their strong growth. However, production costs are expected to increase as a result of record oil prices which are raising production energy, resin/glue and transport costs. Industries in Europe and North America expect higher competition for wood raw material notably residues and small diameter wood as a consequence of policies to develop the wood-energy sector. The increase of panel consumption is expected to be stronger in the CIS countries than in Europe, 6.3% in 2005 and 2006 attaining 10.2 million m³ in 2006. Plywood exports from the Russian Federation, which exceed domestic consumption, will further increase in 2005 by 4.3% to 1.5 million m³. In North America overall consumption of panels is forecast to increase marginally in 2005 to 69.7 million m³ and by a further 1.6 % in 2006. Demand for OSB continues to be strong. Imports from China of plywood and wooden furniture have increased sharply.

Paper, paperboard and wood pulp

Consumption of paper and paperboard is expected to continue to expand steadily in all parts of the region in 2005, and 2006, by 1-2% in 2005 in Europe and North America and around 3% in Russia. Production and exports in Europe will drop slightly in 2005, chiefly because of a lockout in Finland which stopped production for several weeks. Competition is global and intense, leading

to consolidation measures to correct possible over supply. Profitability is generally rather low, and strongly influenced by exchange rate movements. Fibre supply is a concern for the industry due to the competition for wood supplies from renewable energy. Certification is considered essential to maintaining the good image of paper and paperboard with consumers.

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