

UNECE Timber Committee Statement on Forest Products Markets in 2006 and Prospects for 2007

The UNECE Timber Committee adopted the entire official text below on 6 October 2006

I. Overview of forest products markets in 2006 and 2007

Forest products markets in the UNECE region achieved record levels in 2005 and the Timber Committee forecasts continued growth in 2006 and 2007. The meteoric rise of China's forest industry and its unprecedented impact on world markets, presents challenges and opportunities to both market players and policy makers, as do other factors such as climate change, high energy prices and public concern about unsustainable forest practices. Taken together, these influences are fostering a major reshaping of the marketplace. The continuing concern about the sustainability and legality of wood has led some governments to enact public procurement policies for wood and paper products. Trade associations and even some corporations are also establishing guidelines for the responsible purchasing. High energy prices are making wood energy economically attractive and, in combination with policy drivers for renewable energy, are creating new opportunities for forest owners and energy suppliers, which includes the forest industries in some countries. One effect of this has been increased competition for raw material, which has raised prices significantly for some industries.

China's influence on UNECE region markets. China has rapidly become the world's largest exporter of forest products in value terms, and is second only to the United States (US) as an importer. China's own forests meet only a small part of its industrial roundwood appetite, with the result that China is now the world's number one importer of logs, both softwood and hardwood. Russia is the main source of softwood logs, supplying about 70% of China's needs. A small part of China's imports is of certified origin but it does seem that a significant share may be from illegal sources. According to official Russian sources, China imports 19.2 million m³ of logs from Russia, but Russian experts

estimate that in addition to that volume there is a significant supply of logs from the Far East region of Russia based on illegal logging.

Investments in Chinese mills and transportation, aided by government incentives, have led to a huge expansion in value-added processing, especially furniture, millwork and mouldings. Over the last decade China's furniture exports have grown at a rate of 34% per year and China is by far the major supplier of furniture to the US, and second only to Canada as a supplier of forest products. China's low-cost labour is balanced by rising raw material, energy and transportation costs. Competition from low-priced Chinese wood products is leading to the increasing trade disputes: complaints have been filed in the US, Canada, Germany and Italy. Although exports are escalating, domestic consumption equivalent to about 75% of production is rising with the standard of living. UNECE region forest products companies are faced with a rapidly changing marketplace: some are successful in profiting from investments in China and trading with China, while others that were not able to adapt have reduced revenues.

Certified forest products. In 2006 the forest area certified for sustainable management reached nearly 275 million hectares, about 90% of which is in the UNECE region distributed by nearly 30% in EU/EFTA and nearly 60% in North America. Russia's forests remain uncertified, but even their largest log export market, China, is beginning to import certified wood (mainly for re-export of finished products to environmentally sensitive retailers in Europe and the US). The major certification systems are actively pursuing certification of Russian forests. Government and corporate procurement policies are increasingly calling for certified forest products as assurance of sustainable forest management. Concerns were voiced about availability of information to monitor, measure and analyze certified forest products markets: inclusion of certified forest products in trade classification and reporting by certification schemes would improve the situation.

Sustainable forest products industry. Major corporations and trade associations are increasingly accepting responsibility for sustainable forest management and sustainable development of the forest sector. They are subscribing to codes of conduct including responsible procurement guidelines. Associations and organizations, such as the International Council of Forest and Paper Association and the World Business Council for Sustainable Development, are requiring member companies to report on many sustainability principles, most recently on wood and climate change. Companies and industry associations are devoting considerable time and resources to demonstrating their business practices are not only at the legal minimum standard but also satisfy more ambitious expectations in the social and environmental field. The objective of this investment is to reduce risk to corporate image, which can cause major economic damage, especially to companies with highly visible brands and corporate reputation.

II. Economic outlook

In October 2006, global economic growth remains strong, at over 5%, with a similar rate of growth expected for 2007. Developing regions' economies are growing faster than those of developed economies (over 7% compared to about 3% in 2006). Inflation remains low. Energy prices are high by historical standards and influencing all parts of the economy, although oil prices have dropped since their peak in summer 2006. Housing prices have risen globally over the past 5 years, creating concern about a possible sharp fall in prices. It appears that the US housing market peaked in 2005: housing starts in July 2006, at an annual rate of 1.8 million, were still high, but down 13% from July 2005. There is concern about the volume of unsold housing stock in the US.

III. Market sector developments

Wood raw materials including wood energy. For the fifth year in succession, roundwood removals reached record levels in 2005 for the UNECE region as a whole. Forecasts show increases in North America and Russia, but in Europe a fall in removals in 2006 followed by a modest increase in 2007, a reflection of the effects of the storm damage in Sweden, where almost all the windblown

volume has now been harvested, although some is still held in storage. China now dominates world trade in roundwood, even though its roundwood consumption is still much lower than European or North American removals. Most roundwood prices in Europe have risen, reflecting increased demand, in particular for softwood sawlogs, as well as the sharp rise in oil prices since June 2004, which has added to both production and transport costs.

The increases in energy prices, along with policies that favour sustainable development and increasingly promote renewable energy, are continuing to drive demand for wood energy upwards, sharply in some countries. Processed woodfuels, such as pellets in Europe have seen strong growth and there is now a well developed international trade in biofuels. High transport costs tend to favour processed fuels which need less volume or weight for a given energy content. Transport costs may well influence the location of new large scale investment in wood energy capacity, with coastal areas likely to be favoured, where fuel can be imported readily, as has been the experience in the Netherlands and Sweden. China's ambitious goal to increase bioenergy's share of its overall energy markets, coupled with its limited indigenous forest may result in demand for woodfuel well beyond China's boundaries.

Sawn softwood. The Timber Committee forecasts that sawn softwood markets will continue to rise, reaching new record levels in 2006 and 2007. The downturn in US housing seemingly may not severely impact the UNECE region as a whole.

In 2006 North American consumption is forecast to increase by 1.3%, and then stay near that level of 130 million m³ in 2007. Sawnwood prices have been volatile, but have been falling in 2006. In British Columbia, Canada, the mountain pine beetle continues to ravage lodgepole pine forests. The growing stock at risk is estimated at 1 billion m³, especially if warm winters continue to facilitate the insects' invasion. The Government has provided incentives to industry for processing the dead timber, so a surge in supply from western Canada over the next 5-10 years is expected. The long-standing US/Canada softwood lumber dispute was apparently resolved in September 2006 with a new 7-

year agreement which provides for Canadian companies to pay export taxes and/or operate under quotas with a set price trigger. It refunds to importers of record, in many cases Canadian companies, 80% of the \$5 billion collected in duties.

European consumption is forecast to rise by about 2% each year, reaching 102 million m³ in 2007. Sawmillers have received more logs where higher prices have persuaded private forest owners to sell timber. Conversely, some countries confirmed log shortages for multiple reasons, including prices and considerable new investments in sawmilling capacity. Sawnwood prices have risen too. Russian sawn softwood production is forecast to increase by 5% in 2006 and by 7% in 2007, reaching a record 21.8 million m³ with nearly all the increase destined for exports.

Sawn hardwood. In 2006 North American demand for sawn hardwood is forecast to fall because of declining housing starts, by 1.5% and then in 2007 to remain near that level of 27 million m³. US sawmills have rationalized capacity and forecast higher exports to offset the drop in domestic consumption, increasingly to Asian destinations. However log prices have risen partly as a consequence of China's strong imports of sawlogs. Lighter colour species, e.g., maple, are fashionable. Certified hardwood is increasingly available and public procurement programmes have been a catalyst for forest management and chain-of-custody certification as well as green building programmes. Trade associations such as the American Hardwood Export Council are developing mission statements and action plans for determining legality of source.

European consumption, however, is forecast to rise by 1.9% in 2006, and by another 0.5% in 2007, reaching 20 million m³. Market drivers include public procurement policies requiring assurance of sustainable and legal production. Imports show strength in 2006, advancing 2%, but could fall back in 2007. Exports show little change in 2006, but could rise in 2007 as forecast by two of the largest exporters, Romania and France. White oak is currently in fashion, as well as some darker species, including some tropical species. Successful promotion of natural, character-marked sawnwood is resulting in better resource utilization. Import value of secondary-processed tropical timber products

now equal primary product imports, testifying to the efficiency of policies to promote further processing of logs, sawnwood and veneer. Tropical producers and importers are expressing concern for potential non-tariff barriers in the form of public procurement policies. Many tropical timber producers are not yet prepared to meet the forthcoming EU construction regulations ("CE marking"), applicable to all structural materials. If the producers do not take steps to obtain the necessary authorisations, they risk being excluded from a major market. The international community, for instance ITTO, should consider helping tropical timber exporters to assess the situation and prepare the necessary actions.

Wood-based panels. Overall consumption of panels in Europe is expected to reach record levels in 2006 (64.7 million m³) driven by demand from end-use sectors: residential construction, furniture, cabinets, flooring and mouldings. Energy, resin and transport costs have soared due to high oil prices. However, panel prices have not risen, reducing profitability considerably. In North America, consumption of panels, influenced by the reduction of housing starts, is forecast to drop by 3.5% to 65 million m³ in 2006 and level off in 2007. The downturn of demand coincides with planned OSB mill investments so that capacity utilization drops from 99% in 2005 to 80% in 2008, with negative consequences for profits. Little change is expected for MDF, while plywood and particleboard production is expected to fall in 2006 by 3.1% and 12.6% respectively. Plywood continues to lose market share to OSB. In Russia, panel production is forecast to increase by 8.8 % in 2006 and a further 9.7% in 2007, reaching 9.3 million m³. Most of this increase will supply the domestic market rather than exports but it is dependent on a planned expansion of MDF production, which would see capacity trebled to 1.2 million m³.

Pulp and paper. Global markets for pulp, paper and paperboard were mostly firm in 2005 and the first half of 2006, with limited expansion of production capacity in the UNECE region. Markets were characterised by generally higher prices for most products, continuing the general upward price trend observed since 2003. In 2005, production and consumption of pulp and paper declined in both Canada and the United States, but European paper producers set a new record

for output. In 2006 and 2007, European consumption of paper and paperboard is expected to show little change, but production and exports will increase in 2006. Little change is foreseen in North American production and trade of paper and paperboard after the consumption decline in recent years. In 2006, Russian consumption and production are expected to continue their steady growth, by 6.2% and 3.7% respectively, and again in 2007 by 5.4% and 3.5% respectively.

Value-added wood products. There has been phenomenal growth in the level of furniture exports from China and southeast Asia into the five major importing countries, US, France, Germany, UK and Japan. The world furniture trade has opened up faster and more profoundly than anticipated and the impact on manufacturers in the US in

particular, has been severe. Chinese labour costs are low but their large-scale enterprises are highly efficient and final quality is also high. China accounts for 43% of US wood furniture imports and 33% of Europe's. China may now be the world's number one furniture exporter, unseating Italy from this long-held position. Similar impacts are being witnessed in the flooring sector. Wood has increased its share of the flooring market in Europe, but faces stiff competition from non-wood products as well as imported flooring. In terms of parquet flooring, for instance, China has increased its market share from about 10% in 2000 to over 35% in 2005. In response to these pressures, a marketing campaign to promote "real wood" flooring is being launched to raise consumer awareness and to encourage demand, in competition against other flooring materials.