

European buying remains slow

Trade contacts report continuing low levels of tropical hardwood forward buying in the EU at the end of the third quarter of 2009. Earlier predictions of significant price rises in the face of widespread shortages after a long period of slow buying have yet to be realised. CIF Europe price trends for tropical hardwood logs and sawn lumber seem now to be trending upwards, but at present this seems more due to increases in freight rate and exchange rate fluctuations than to any sharp shift in the balance of supply and demand. There is some evidence of gaps opening up in stocks of certain special assortments, but generally there still seems to be enough material on the ground in Europe to satisfy current low levels of consumption. There continues to be a lot of cross-trading between European companies to fill gaps in stocks as they arise, with little interest in speculative forward purchases. This applies both to products destined for the joinery sector and for the garden decking sector. The 2009 season for decking products in Europe is now over and considerable uncertainty over prospects for the 2010 season has led to considerable reluctance on the part of importers to build stocks.

Against this background, tropical hardwood shippers continue to maintain very low levels of production so that lead times on forward orders remain extended for many products. Lead times of over 4 months can be expected for orders of African sawn lumber. Imports of tropical hardwood from Brazil are these days also subject to very significant delay. As is typical, Asian hardwoods are generally more readily for prompt shipment – although production in this region is also reported to be very low. In addition to long-term issues of log supply and mill closures during the recession, business in South East Asia slowed considerably at the end of September during the Hari Raya festival.

Impact of new regulations to remove illegal wood from trade

Insights into the impact of laws in the EU and US designed to remove illegal wood from trade emerged during two recent meetings in Geneva. The International Timber Trade Federation (ITTF) meeting, hosted by The Forest Trust on 8-9 October and attended by representatives of trade associations from around the world, was convened with the aim of discussing the trade response to these measures. These issues also generated a lot of interest during the opening session of the Annual UNECE Timber Committee Market Discussions on 13 October.

A commentary on the trade impact of the May 2008 amendment to the US Lacey Act was provided at the ITTF meeting by Jameson French on behalf of the US Hardwood Federation and American Hardwood Export Council. The amendment makes it illegal in the United States to trade in wood products in violation of the laws of any other country or international laws. The amendment effectively provides the legal authority to take action when products stemming from the practice of illegal logging enter the United States.

The Act also requires an import declaration for wood products that includes the scientific name of the tree species, a description of the value, quantity, and the name of the country from where the wood was taken. If a tree species or country of origin cannot be determined, the declaration must include a list of possible species found in

the product or a list of possible countries from which the product originated. The declaration requirements are being phased in, beginning with minimally processed products (for example logs, sawn lumber and veneers) from April 2009, to include more processed and complex products such as wood pulp and particle board from 1 October 2009, and highly processed products such as paper and furniture from 1 April 2010.

French emphasised that this phase-in period applies only to the importer declaration requirements. The legal sanctions associated with Lacey have been in place since May 2008 and since that date it has been possible to bring prosecutions against US purchasers of any product containing illegal wood.

French noted that “there has been a strong and immediate reaction amongst U.S. retailers” that fear the severe legal sanctions associated with the Lacey Act amendment. Even if purchased in good faith and efforts have been made to ensure legality, a buyer in the U.S. would have to forfeit any goods that are subsequently found to be from an illegal source. This sanction alone is a huge incentive to U.S. buyers to clean up their supply lines. It is not unusual for US wood and furniture importers to take delivery of individual shipments worth several million dollars and their loss could quickly lead to bankruptcy. Even more severe penalties – including imprisonment – may be imposed if the buyer is unable to demonstrate due care to minimise the risk of sourcing illegal wood products. French suggested that concerted efforts are already being made by the U.S. authorities and other interests to identify and investigate cases with potential for prosecution and that it is only a matter of time before a successful case is brought.

Against this background, many U.S. wood and furniture importing companies are now very actively promoting the measures they are taking to ensure their compliance with the Lacey Act. They are also now putting considerable pressure on their overseas suppliers to ensure that there is a low risk of any wood raw material being illegally sourced.

However French also commented that the Lacey Act amendment has caused considerable confusion amongst overseas suppliers to the US. For example, many wood product manufacturers in China and South East Asia have the impression that the law amounts to a mandatory requirement to source only FSC certified wood. This is not the case. The law makes no assumptions and provides no guidance on the measures that importers must take to show due care that wood is from a legal source. The new declaration requirement does not require the importer to have all of the information necessary to be certain of the legal origin of the wood. Instead it requires the importer to collect information that, depending on what it suggests about the origin of the wood, should prompt further inquiry by the importer to assure its legality. The sanctions that may be imposed in the event of a prosecution vary widely depending on the level of knowledge and the extent of “due care” exercised by the defendant. It is also important to emphasise that the law implies no reversal of the burden of proof. Successful prosecution is dependent on the U.S. authorities proving that a particular forest product derives from an illegal source.

While the impact of the Lacey Act has already been significant, French noted that its effects have been muted by the economic downturn in the US. This has led Chinese

wood product exporters, for example, to concentrate more on domestic markets and less on the US market. French believed the full effects of the Act outside the US will not be felt until after the US economy recovers.

The ITTF and UNECE Timber Committee meetings in Geneva also provided details of the current status of EU proposals to impose “due diligence” requirements on operators that “first place” timber on the European market. This legislation was proposed by the European Commission in October 2008 and is now being considered for adoption by the European Council of Ministers and European Parliament. There is much discussion over the exact details of this law, particularly with respect to the companies within the EU that should be subject to the due diligence requirements and the scope and content of the corporate risk management procedures required. Some EU Member States, supported by members of the EU Parliament and some wood trade associations, also advocate that the requirements for due diligence systems should be combined with a Lacey-style prohibition on trade in illegal wood within the EU. This is seen as a necessary measure to reinforce corporate commitment to due diligence (further details of these complex issues are explored in a new series of papers prepared by the NGO Client Earth – see: http://www.illegal-logging.info/approach.php?a_id=120).

Expectations are high that the European Council will reach a final position on the due diligence legislation by mid December with a view to introduction sometime during 2010. Linkage of the regulation to other measures targeting deforestation within the climate change regime has provided powerful impetus to these negotiations within the EU.

UN Timber Committee highlights contrasting construction outlook in the U.S. and EU

One piece of good news relating to the U.S. wood market emerged early on in the UNECE Timber Committee Market Discussions held in Geneva in mid October. Dr Eric Hansen of Oregon State University, quoting data provided by APA (the American panel products association) suggested that U.S. housing starts, which fell from over 900,000 in 2008 to a forecast 560,000 in 2009, are expected to rebound strongly to again reach close to 1 million by 2011.

However Hansen’s comments did not reflect so well on the European Union where, he said, “the housing bubble has been far greater [than in the U.S.]”. This gloomy conclusion with respect to European construction activity accords with the conclusions of the Euroconstruct conference held over the summer in the EU. This conference suggested that construction output across the 19 countries in the Euroconstruct network is projected to fall by 7.5% this year following a 3.1% decline in 2008. Construction sector output is projected to fall by a further 1% in 2010 (-1%). After three years of decline, a very slight recovery is only expected in 2011 (+1.6%). The worst performers over the next two years (2009-2010) are expected to be Ireland, where the industry is projected to reduce in size by 51%, Spain (-25%), Finland (-21%) and Portugal (-18%). Only Switzerland (+2.3%), Germany (+1.1%) and Sweden (+0.5%) are expected to record growth over this period. Euroconstruct forecasts for the market as a whole were revised downwards in the summer compared with the forecasts made last December due to the worsening global economic environment and

continuing uncertainty regarding the approaches being taken by banks and governments to deal with improperly functioning credit markets.

UNECE Timber Committee report on sawn hardwood markets

The UNECE Timber Committee meeting also provided an update of the sawn hardwood market situation across the UNECE region (which covers Europe, the CIS and North America). It was reported that sawn hardwood production in 2008 across all three UNECE subregions amounted to a total of 42.8 million m³, which marks a decrease of 8.2% over the previous year. In line with production, total consumption of sawn hardwood across the UNECE region reached 44.2 million m³ during 2008, falling by 6.1% from the previous year. According to the UNECE Timber Committee report, oak continues to dominate the global sawn hardwood market. For example, European and American white oak together accounted for nearly 60% of all European hardwood flooring production.

In Europe, production of sawn hardwood fell by 6.8% to a total of 14.3 million m³ in 2008. Hardwood flooring production and consumption in Europe decreased significantly last year, marking the first downturn in this sector for 18 years, due mainly to the slowdown in the housing sector. No recovery in demand is expected over the next 12 months due to the weak economic situation in Europe.

In North America, production of sawn hardwood reached a total volume of 24.6 million m³ in 2008, having fallen by 9.1% from the previous year, due to weak demand in both the US domestic and export markets. A significant recovery in North American sawn lumber production and consumption is not expected until at least 2010, although tighter supplies could lead to price increases in the near future.

During 2008, the CIS region recorded its first drop in sawn hardwood production in 15 years. Government efforts to boost the sawn hardwood sector in Russia are now being undermined by the global economic situation. While Russian hardwood log and lumber production seems well below long-term potential, the uncertain economic and political environment means Russia's future role as a potentially significant producer and exporter of hardwood sawn lumber is still unclear. Export tariffs on Russian logs have been raised to 50% but plans to further increase these to 80% have been delayed. The existing tariff has significantly reduced Russian log exports, although Chinese importers are reported to be side-stepping the measure through the simple expedient of importing squares/cants rather than raw logs. In the West, Finnish wood processing companies – that have been heavily dependent on Russian logs in the past - have so far been reluctant to commit to new investment in Russian processing capacity despite the high tariffs and Russian prompting. At present, most Finnish companies seem more interested in seeking to increase utilisation of Finland's domestic forests to offset declining log availability from Russia.