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U.S. Forest Products Annual Market Review and Prospects 2001–2004

James L. Howard



Abstract

This report provides general and statistical information on forests products markets in terms of production, trade, consumption, and prices. The state of the United States economy is described as of the second quarter of 2003. Market developments are described for timber products, paper and paperboard, fuelwood, and forest products prices. Policy initiatives that address domestic markets and international trade concerns related to U.S. forest products are also discussed. Detailed information and projections are presented for the year 2004.

Keywords: production, trade, prices

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Executive Summary

Economic activity in the United States picked up during the second quarter of 2003 as noted by the 2.3% growth in gross domestic product (GDP). Thirty-five forecasters surveyed by the Federal Reserve Bank of Philadelphia predicted that the U.S. economy would likely expand at a slower rate in 2003 than that predicted. The forecasters expect year-over-year growth in real GDP to average 2.2% in 2003, down from their previous prediction of 2.5%. Measured on an annual-average basis, unemployment is expected to be 5.9% in 2003, as predicted in the first quarter of the year, although the forecasters are associating slower growth in 2003 with a higher forecast for unemployment in 2004. The forecasters see prices rising at a slightly higher rate in 2003 and at a slightly lower rate in 2004 than that predicted. With continued low mortgage rates, the expectation for continued strength in the housing sector is high. Should the value of the dollar decline and lumber prices rise, this should bolster the production and trade of U.S. lumber and paper products. Because of the importance of domestic markets in forest products trade, certain policy initiatives are also projected to add millions of dollars to the U.S. economy in 2004.

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U.S. Forest Products Annual Market Review and Prospects, 2001–2004

James L. Howard, Economist
Forest Products Laboratory, Madison, Wisconsin

General Economic and Major Market Trends

The U.S. economy will likely expand at a slower rate in 2003 than had been predicted, according to 35 forecasters surveyed by the Federal Reserve Bank of Philadelphia. The forecasters expect year-over-year growth in real gross domestic product (GDP) to average 2.2% in 2003, down from their previous prediction of 2.5%. Much of the downward revision for the year comes from a cut in the projection for growth in the second quarter, now expected to average 1.8% at an annual rate, down from 2.7% in a survey taken in the first quarter. The forecasters continue to expect a rebound over the second half of the year. Growth is expected to average 3.4% at an annual rate in each of the last two quarters of 2003. Previously, the forecasters thought growth would average 3.4% in the third quarter and 3.6% in the fourth quarter. The forecasters project growth of 3.6% in 2004, about the same rate they projected previously.

Current-dollar GDP—the market value of the nation's output of goods and services—increased 3.4%, or \$88.9 billion, in the second quarter of 2003 to a level of \$10,777.3 billion. In the first quarter, current-dollar GDP increased 3.8%, or \$99.6 billion.

Measured on an annual-average basis, unemployment is expected to be 5.9% in 2003, unchanged from the forecast of the first quarter, although the forecasters are associating slower growth in 2003 with a higher forecast for unemployment in 2004. The current estimate for 2004 stands at 5.7%, marking an upward revision from the previous 5.5%.

On the inflation front, the forecasters see prices rising at a slightly higher rate in 2003 and a slightly lower rate in 2004 than they had predicted in the first quarter. Measured on a fourth-quarter over fourth-quarter basis, CPI inflation will average 2.4% in 2003, up from 2.2% previously, and 2.3% in 2004, down from 2.4%. On a year-over-year basis, inflation in the GDP price index will average 1.8% in 2003 and 2004. The forecasters had previously thought that GDP inflation would average 1.7% in 2003 and 2.0% in 2004.

The forecasters see interest rates over the next 2 years at levels lower than that predicted in the first quarter of 2003. On the short end of the maturity spectrum, the forecasters now predict the rate on 3-month Treasury bills will average 1.2% in 2003, down from the forecast of 1.4% in the last survey. An even larger downward revision characterizes the outlook for 2004. Currently, the 3-month rate is expected to average 2.1% in 2004, down from 2.8% previously. On the long end, the rate on 10-year Treasury bonds will average 4.1% in 2003 and 4.7% in 2004, both down from the previous forecasts of 4.3% and 5.1%, respectively. An acceleration in real GDP growth in the second quarter of 2003 primarily reflected upturns in Federal defense spending and nonresidential fixed investment and an acceleration in personal consumption expenditures, which were partly offset by an upturn in imports.

The price index for gross domestic purchases, which measures prices paid by U.S. residents, increased 0.3% in the second quarter of 2003, compared with an increase of 3.4% in the first. Excluding food and energy prices, the price index for gross domestic purchases increased 0.7% in the second quarter, compared with an increase of 1.8% in the first.

Real personal consumption expenditures increased 3.3% in the second quarter of 2003, compared with an increase of 2.0% in the first. Purchase of durable goods increased 22.6% in contrast to a decrease of 2.0%, and purchase of nondurable goods increased 0.1% compared with an increase of 6.1%. Services expenditures increased 1.5%, compared with an increase of 0.9%. Real nonresidential fixed investment increased 6.9% in contrast to a decrease of 4.4%, and nonresidential structures increased 4.8% in contrast to a decrease of 2.9%. Equipment and software increased 7.5% in contrast to a decrease of 4.8%. Real residential fixed investment increased 6.0% compared with an increase of 10.1%.

Real Federal government consumption expenditures and gross investment increased 25.1% in the second quarter of 2003, compared with an increase of 0.7% in the first. National defense increased 44.1% in contrast to a decrease of 3.3%. Non-defense expenditures decreased 4.1% in contrast to an increase of 8.4%. Real State and local government consumption expenditures and gross investment decreased 1.5% in contrast to an increase of 0.2%.

The real change in private inventories subtracted 0.77 percentage point from the second-quarter change in real GDP, after subtracting 0.82 percentage point from the first-quarter change. Private businesses reduced inventories \$17.9 billion in the second quarter, following increases of \$4.8 billion in the first quarter of 2003 and \$25.8 billion in the fourth quarter of 2002.

Real final sales of domestic products—GDP less change in private inventories—increased 3.2% in the second quarter of 2003, compared with an increase of 2.3% in the first quarter. Real gross domestic purchases—purchases by U.S. residents of goods and services wherever produced—increased 3.8% in the second quarter, compared with an increase of 0.6% in the first.

Current-dollar personal income increased \$74.4 billion (3.3%) in the second quarter, compared with an increase of \$82.3 billion (3.7%) in the first. Personal tax and nontax payments increased \$8.3 billion (3.1%), in contrast to a decrease of \$12.9 billion (4.7%).

Disposable personal income increased \$66.1 billion in the second quarter, compared with an increase of \$95.1 billion in the first. Real disposable personal income increased 2.4%, compared with an increase of 2.1%.

Personal outlays increased \$85.5 billion (4.5%) in the second quarter, compared with an increase of \$86.9 billion (4.6%) in the first. Personal saving—disposable personal income less personal outlays—was \$270.6 billion in the second quarter, compared with \$290.0 billion in the first. The personal saving rate—saving as a percentage of disposable personal income—decreased from 3.6% in the first quarter to 3.3% in the second.

With a large forest resource and high production and consumption of wood products, the United States continues to play an important role in world forest product markets. The United States has the world's highest consumption of paper and paperboard (about 80 million metric tons in 2002), which is mostly supplied by domestic production and imports from Canada (American Forest & Paper Association, AF&PA). The U.S. forest products industry annually harvests more than 467 million cubic meters of softwood and hardwood timber, manufacturing about 88 million cubic meters of lumber and 25 million cubic meters of structural panel products in 2002.

New housing construction, which accounts for more than a third of U.S. annual consumption of softwood sawn wood and structural panels and for substantial volumes of other softwood and hardwood products, remained high through 2002 and into the first half of 2003. A comparison of the first half of 2003 to the first half of 2004 indicates that overall starts, seasonally adjusted, grew 5.4% to 1,803,000. All the gain between these two periods occurred in the single-family sector, where output rose to 708,100 units. Multifamily starts

in the first half of 2003 fell 2.6% when compared with multifamily starts in the first half of 2002. Total housing starts for June 2003 represent an increase of 3.7% from May. The mobile home market remained weak in the first half of 2003. The pace of shipments in 2003 as of the second quarter is less than half the volume shipped during the peak year of 1998.

Comparing the first half of 2003 to that of 2002, the greatest strength lay in the Northeast, where month-to-month output advanced 9.9% to an annual rate of 156,000. The Midwest registered the largest month-to-month decline of 0.8%, to an annual rate of 358,000. Production in the West increased by 8% in June to a second-quarter average of 486,000, while June starts in the South increased at a seasonally adjusted 803,000.

In June 2003, the real value of new residential construction remained relatively flat for the third consecutive month at a seasonally adjusted annual rate of \$446.8 billion. The second quarter averaged a seasonally adjusted \$444.3 billion, down 0.9% from the first quarter and 2.1% above the fourth quarter of 2002.

In contrast to residential construction is nonresidential activity, where the values for new construction appear to be descending slowly. The value of all nonresidential buildings was at an annual rate of \$214 billion in June 2003, down 0.8% from May and 2.1% from April. The National Association of Home Builders (NAHB) forecast calls for the housing sector to remain strong, with only a minor setback in the second half of 2003 and with starts and sales ending the year at near-2002 levels.

In 2002, investment in residential repair and remodeling, along with the strong new residential construction market, kept pace as the average expenditures for all four quarters rose 8.9% to \$173.3 billion, from \$157.8 billion in 2001. In the first quarter of 2003, expenditures for improvement and repair of residential properties were at a seasonally adjusted annual rate of \$179.7 billion, 2.2% above the fourth-quarter 2002 estimate of \$175.7 billion. Expenditures for maintenance and repair to all properties amounted to a seasonally adjusted annual rate of \$53.2 billion during the first quarter of 2003, slightly above \$52.8 billion in the fourth quarter of 2002.

Three indicators of demand for wood products—industrial production, furniture and related products, and paper products output—declined in 2003 relative to 2002:

- Industrial production—an important demand determinant for pallet lumber, containerboard, and some grades of paper—fell 0.7% in 2002 to 110.5% of its 1997 average; in 2003, production was down 0.7% at the end of the second quarter, after posting gains early in the first quarter.

- Furniture and related products—a determinant of high-grade lumber production—fell 2.1% in the first quarter of 2003 compared to that in 2002.
- Paper products output—a determinant of pulpwood and wood residue use, as well as recycled fiber availability and use—declined 0.9% over the first quarter of 2003 compared with the same period in 2002. The index (1997 = 100) of paper products output for the first half of 2003 remains below the 104.4 annual average for 2002.

In summary, housing starts are predicted to remain strong in 2003, after a very strong showing in 2002; activity in the principal markets for U.S. timber was also slightly higher in 2002 than in 2001. After a strong start during the first two quarters of 2003, growth is expected to moderate for the rest of the year. Even though the rate of growth is slowing, most analysts predict that conditions favorable to the growth of timber markets will continue. Selected U.S. economic indicators are shown in Table 1.

Timber Products Production, Trade, and Consumption

Statistics and prospects for the production, trade, and consumption of timber products for 2002 through 2004 are shown in Table 2.

Sawn Softwood

Housing and other construction markets have been strong in 2003 and are likely to finish the year only slightly below the levels recorded in 2002 for softwood lumber consumption.

According to the Western Wood Products Association (WWPA), softwood lumber consumption fell 5.2% during the first 5 months of 2003, from the record pace in 2002; shipment of softwood lumber from Western mills fell 1.1% during this period. Production in the West increased by 1.2% and production in the southern pine region declined 5.5% in the first 5 months in 2003. Apparent consumption for the first 5 months of 2002 was 46.9 million cubic meters, 5.8% above the apparent 44.2 million cubic meters for the first 5 months of 2003. The U.S. housing construction industry is predicted to remain strong into 2003. Therefore, timber production is likely to remain strong.

Sawn softwood imports fell 11.0% during the first 5 months of 2003 relative to the same period in 2002. The volume of Canadian imports decreased by 11.6% over this period. Canadian imports constituted 91% of all sawn softwood imports. However, other suppliers such as Europe continued to increase their share of the U.S. market. Total sawn softwood imports were 49.5 million cubic meters in 2002, an increase of 4.3% over 2001.

During the first 5 months of 2003, U.S. exports increased 10.0% compared with exports for the same period in 2002. Exports to Canada declined 6.3%, exports to Japan grew 13.6%, and exports to Mexico rose 175%.

Production of sawn softwood decreased 2.1% in the first 5 months of 2003 compared with the same period in 2002; 61.9 million cubic meters of sawn softwood was produced in 2002. The production of sawn softwood for 2003 is forecast to remain close to 2002 production levels.

Table 1—Selected U.S. economic indicators, 2000–2004

| Indicator | Actual | | | Estimated | |
|---|---------|---------|---------|-----------|---------|
| | 2000 | 2001 | 2002 | 2003 | 2004 |
| ^a Gross domestic product (billion (10 ⁹) 1996 dollars) | 9,191.4 | 9,214.5 | 9,439.9 | 9,647.6 | 9,970.2 |
| ^b New housing starts (million units) | 1.573 | 1.601 | 1.711 | 1.707 | 1.708 |
| ^b Mobile home shipments (thousand units) | 250 | 192 | 168 | 135 | 120 |
| ^c Nonresidential investment in structures (billion 1996 dollars) | 178.1 | 166.6 | 136.9 | 125.0 | 127.0 |
| ^d Total industrial production (Index: 1997 = 100) | 115.3 | 111.2 | 110.5 | 109.1 | 108.1 |
| ^e Furniture and fixtures (billion 1997 dollars) | 105 | 103 | 101.3 | 97.0 | 98.0 |
| ^e Paper products (Index: 1997 = 100) | 98.0 | 96.0 | 94.4 | 92.4 | 93.4 |

^aU.S. Department of Commerce 2003.

^bNAHB 2003.

^cU.S. Census Bureau 2003.

^dCouncil of Economic Advisors 2003.

^eU.S. Federal Reserve System, August 2001–2003.

Table 2—Production, imports, exports, and consumption of various products ($\times 10^3$ m³), 2002–2004

| | 2002 | 2003 | 2004 | | 2002 | 2003 | 2004 |
|------------------------------|---------|---------|---------|--|---------|---------|---------|
| Sawn softwood | | | | Oriented strandboard (OSB) | | | |
| Production | 61,914 | 62,011 | 62,001 | Production | 11,882 | 11,975 | 12,001 |
| Imports | 49,526 | 49,771 | 49,862 | Imports | 7,657 | 7,801 | 7,881 |
| Exports | 2,281 | 2,419 | 2,508 | Exports | 179 | 182 | 190 |
| Consumption | 109,159 | 109,363 | 109,355 | Consumption | 19,360 | 19,594 | 19,692 |
| Coniferous logs | | | | Particleboard | | | |
| Production | 168,628 | 167,995 | 167,563 | Production | 7,813 | 6,901 | 6,804 |
| Imports | 7,126 | 7,202 | 7,305 | Imports | 1,365 | 1,324 | 1,325 |
| Exports | 6,520 | 6,419 | 6,382 | Exports | 210 | 218 | 219 |
| Consumption | 169,234 | 168,778 | 168,486 | Consumption | 8,968 | 8,007 | 7,910 |
| Sawn hardwood | | | | Medium density fiberboard (MDF) | | | |
| Production | 26,500 | 26,109 | 25,887 | Production | 2,779 | 2,902 | 3,066 |
| Imports | 1,743 | 1,750 | 1,769 | Imports | 1,380 | 1,402 | 1,428 |
| Exports | 2,878 | 2,801 | 2,675 | Exports | 164 | 171 | 183 |
| Consumption | 25,365 | 25,058 | 24,981 | Consumption | 3,995 | 4,133 | 4,311 |
| Hardwood logs | | | | Insulation board | | | |
| Production | 60,728 | 60,026 | 59,986 | Production | 2,335 | 2,335 | 2,335 |
| Imports | 275 | 232 | 225 | Imports | 321 | 312 | 303 |
| Exports | 2,272 | 2,109 | 2,007 | Exports | 152 | 160 | 158 |
| Consumption | 58,731 | 58,149 | 58,204 | Consumption | 2,504 | 2,487 | 2,480 |
| Coniferous plywood | | | | Roundwood pulpwood | | | |
| Production | 13,452 | 13,399 | 13,475 | Production | 137,321 | 136,990 | 136,840 |
| Imports | 803 | 880 | 901 | Imports | 53 | 48 | 52 |
| Exports | 338 | 330 | 333 | Exports | 2,209 | 2,152 | 2,146 |
| Consumption | 13,917 | 13,949 | 14,043 | Consumption | 135,165 | 134,886 | 134,746 |
| Nonconiferous plywood | | | | Hardboard | | | |
| Production | 1,855 | 1,776 | 1,711 | Production | 861 | 830 | 801 |
| Imports | 2,605 | 3,054 | 3,102 | Imports | 789 | 801 | 832 |
| Exports | 159 | 155 | 146 | Exports | 197 | 180 | 177 |
| Consumption | 4,301 | 4,675 | 4,667 | Consumption | 1,453 | 1,451 | 1,456 |

Sources: APA—The Engineered Wood Association, American Forest and Paper Association, Forest Resources Association, and Composite Panel Association. Figures for 2003 and 2004 are estimates.

Sawn Hardwood

Sawn hardwood production declined by 6.5% to 26.5 million cubic meters in 2002. Imports increased by 14.3% compared with imports in the same period in 2001. During the first 4 months of 2003, the rise in imports exceeded the rise in exports: imports rose 9.6% and exports 0.2%.

Exports to European Union countries declined 13.4%, and exports to Pacific Rim nations rose 3.9%. Given the estimated growth rates for production and decreasing trade figures, and a strong housing market, apparent consumption for 2003 is forecast to increase slightly from the 2002 volume.

Softwood Log Trade

Softwood log exports to the Pacific Rim fell 2.6% in the first 4 months of 2003 compared with exports in the same period of 2002, while softwood log exports to the European Union fell 45.0%. Total softwood log exports from the United States increased 23.3% in the first 4 months of 2003 compared with 2002 exports; this level is well below export levels throughout the 1990s. During 2001, timber harvest from the National Forests continued to decline but at a lower rate than that in earlier years. The largest volume of decline has occurred in the Pacific Northwest. The U.S. South has undergone a steady increase in softwood log production, in part because of the harvest decline in the West.

Hardwood Log Trade

Hardwood log exports and imports decreased during the first 4 months of 2003. Exports declined 6.9% while imports declined 18.6%, compared with this period in 2002. For all of 2002, exports to Canada rose 7.4%. During the first 4 months of 2003, exports to the Pacific Rim fell 2.6% and exports to the European Union fell 45%.

Hardwood log imports from Canada in 2002 were relatively unchanged from those in 2001, falling only 0.9%. For the first 4 months of 2003, imports from Canada fell 19.6% compared with the same period in 2002. Canada traditionally provides about 95% of imports.

Pulpwood, Paper, and Paperboard

Combined roundwood and forest chip production for pulp and wood-based panel mills was 191 million cubic meters in 2002, down 1.4% from 2001. This includes mill residue used for pulp. The rate of decrease for roundwood pulpwood is expected to continue to decline in 2003. Pulpwood supplied from residues is decreasing relative to roundwood. The roundwood portion of pulpwood was 137 million cubic meters in 2002, a 2.5% decrease from 141 million cubic meters in 2001 (based on pulpwood receipts data from the Forest Resources Association).

Trade patterns have continued to have a significant impact on paper and paperboard production and have affected pulpwood use. Exports of paper, paperboard, and converted products increased by 0.5% in 2002. Imports of paper and paperboard also increased by 0.5% in 2002. Responding to the strong dollar and the weakened U.S. economy, paper and paperboard production increased 1.0% in 2002, following a 6.1% decline in 2001. These consecutive year declines constitute the sharpest reductions in paper and paperboard production since the mid-1970s. Most U.S. paper companies managed to remain profitable in 2002, but industry earnings remained at about half their 2000 levels.

Softwood Plywood

Softwood plywood production was 13.4 million cubic meters in 2002 according to the APA—The Engineered Wood

Association. This was relatively unchanged from 2001. The volume of softwood plywood production fell throughout the 1990s and the decline has continued into 2003. Softwood plywood production for the first two quarters of 2003 decreased by 7.2% compared with the first two quarters of 2002. The APA—The Engineered Wood Association prediction that plywood production will continue to decline in 2003 is supported by the fall in production during the first half of 2003.

Softwood plywood imports and exports varied inversely in 2002 compared with 2001 data: imports rose sharply by 26.7% and exports declined 9.4%. Softwood plywood imports increased 16.1% and exports increased 14.4% during the first two quarters of 2003. Plywood exports to Canada fell by 50% during this period and plywood imports from Canada decreased by 13%. Given these estimates, apparent consumption of plywood is estimated to increase in 2003, even as more market share for structural panels continues to be taken by oriented strandboard (OSB).

Hardwood Plywood

Hardwood plywood production was 1.8 million cubic meters in 2002, a decrease of 7,000 m³ from 2001 production. This includes core material such as softwood plywood and OSB. A decrease of about 2% in hardwood plywood is estimated for 2003, with total production decreasing to about 1.77 million cubic meters. Hardwood plywood imports increased 15.5% in the first 4 months of 2003 compared with that period in 2002. If this trend continues, hardwood plywood imports will likely exceed 3.0 million cubic meters in 2003. The amount of hardwood plywood exported in 2002 was 159,000 m³.

Oriented Strandboard

According to the APA—The Engineered Wood Association, OSB production for the first two quarters of 2003 was below (by 3.2%) production in this period in 2002. In 2002, 11.9 million cubic meters of OSB were produced, compared with 11.1 million cubic meters in 2001. The growth rate from 2001 to 2002 was 6.7%, which is higher than the 2.5% growth rate experienced between 2000 and 2001. Between 1996 and 2000, OSB capacity grew rapidly in the United States and Canada—by 25% in 1996, 5% in 1997, 5% in 1998, and 3% in 1999; it remained level in 2000 and 2001.

Prices in the first two quarters of 2003 were fueled by high demand, despite growth in capacity. The pricing trends for OSB continued through 2002 as prices ended the year lower than those at the end of 2001. Having increased through the first two quarters of 2003, OSB prices are rising toward a new high for the year. In 2002, OSB exports increased by 14.4% (24,000 m³); imports increased by 329,000 m³, a rise of 4.4% from 2001.

Structural panel consumption increased 4.3% to 33.1 million cubic meters in 2002. OSB consumption was a record 19.4 million cubic meters, 58% of the structural panel total. Only about 25% of the higher levels of housing starts can explain the increase in 2002. Because OSB now accounts for 58% of structural panel consumption (1% rise from 1999), OSB consumption is expected to continue to exceed plywood consumption.

Particleboard and Medium Density Fiberboard

Information from the Composite Panel Association indicates that particleboard and medium density fiberboard (MDF) production varied during 2002. Particleboard production was 7.8 million cubic meters, a decrease of 6.5%, and MDF production was 2.7 million cubic meters, an increase of 14.6%. During the first 4 months of 2003, particleboard imports decreased by 6% and MDF imports decreased by 12.8%, on a volume basis. Exports of particleboard decreased by 11% and MDF exports increased by 7% in this period.

Hardboard

Based on data from the American Hardboard Association, 861,000 m³ of hardboard was produced in 2002, a 13.8% drop from the 2001 level. Hardboard imports increased by 13.6% in 2002, and this trend continued during the first 4 months of 2003 as imports increased by 6.3%. Hardboard exports decreased in 2002 by 15.0% and also declined in the first 4 months of 2003, falling 30%.

Insulation Board

Available information from the AF&PA shows that 2.3 million cubic meters of insulation board was produced in 2002, unchanged from 2001. Production of insulation board has been flat for several years, which has resulted in a stable level of apparent consumption of about 3.3 million cubic meters.

Fuelwood

Using data from the most recent Department of Energy survey, adjusting for the 2002 winter weather and a declining trend in fuelwood use per household, fuelwood consumption was estimated to be 46 million cubic meters in 2002, a decrease of 1.2% from 2001. Households use most fuelwood for heating and esthetic enjoyment. Industry uses mill residues rather than roundwood for fuel. A small portion of roundwood fuelwood is used for electric power production. Use for electric power is limited by the low cost of coal and natural gas alternatives. Fuelwood consumption for 2003 is estimated to be below the level for 2002.

Forest Products Prices

Recent trends in the wholesale prices of forest products are similar across two broad categories: lumber and wood products (such as lumber, wood-based panels) and pulp and paper products (Fig. 1). Throughout the late 1990s, the producer price of lumber and wood products as reflected by the producer price index (PPI) continued to fluctuate around a level reached by the mid-1990s before peaking during the last

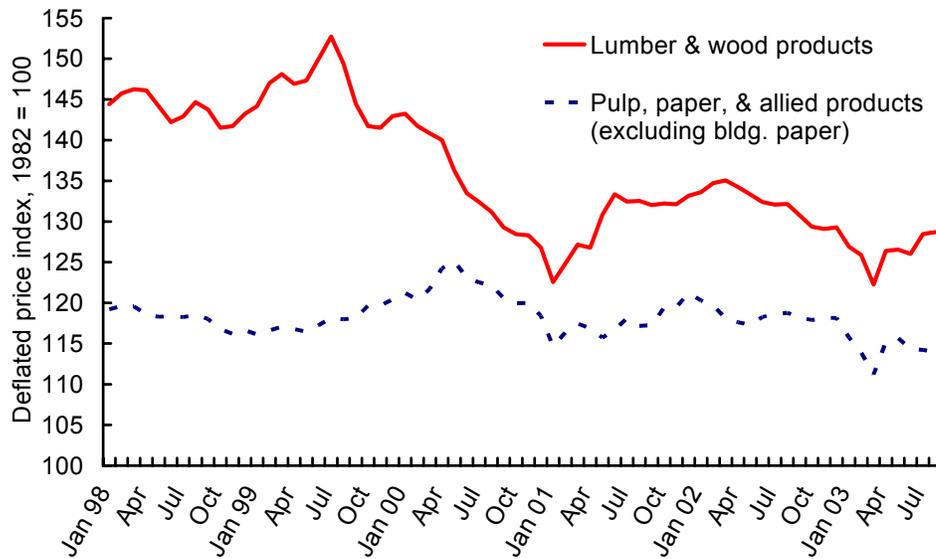


Figure 1—Recent trends in real producer prices of forest products (deflated with all-commodity PPI).

half of 1999. The PPI for lumber and wood products continued to fluctuate during the first half of 2002. Changes in the price of softwood lumber accounted for much of this change and most of the volatility in the index. Nevertheless, during the last quarter of 2002 and the first half of 2003, panel prices exceeded their record high levels. In 1999, the deflated composite price index reached an all-time high (more than 50% higher than that of the base year, 1982), followed immediately by a decline that was sustained throughout 2000 and into 2002. The PPI reached its lowest level in 5 years during this period.

Because of sustained low prices, U.S. demand for lumber and wood products in 2002 remained near record levels. In contrast, the PPI of prices in the pulp and paper sector has exhibited considerably less short-term volatility. The period of declining prices from the previous peak (1994–1995) ended in 1997, and by early 1998 the composite index had reached the level of the mid-1990s. In deflated terms, the composite index has had little volatility and a flat trend that has declined in the second quarter of 2003.

Summary

Economic activity in the United States picked up noticeably during the first half of 2002 as noted by the strong 5.6% growth in GDP, signaling an end to the economic recession that began in the United States in March 2001. Although GDP growth slowed during the second quarter of 2003, a number of factors, such as a strong housing sector and favorable monetary policy, are likely to continue to boost activity as the economy moves through the second half of 2003. With continued low mortgage rates, the expectation for continued strength in the housing sector is high. The future strength for other domestic and foreign trade sectors of the wood products industry depends on pulp and paper prices, future lumber prices (which have been volatile in 2003), and the value of the dollar. A decline in the value of the dollar should bolster U.S. wood and paper products exports.

Forestry Policy Initiatives

Presidential Initiative Against Illegal Logging

In announcing the Clear Skies Initiative on February 14, 2002, President Bush ordered the Secretary of State “to develop a new initiative to help developing countries stop illegal logging.” On July 28, 2003, Secretary of State Powell launched the President’s Initiative Against Illegal Logging.

Illegal logging not only contributes to global deforestation but also costs countries that can ill afford it billions of dollars in lost revenues annually. The World Bank estimates that countries are losing \$10 to \$15 billion annually because of illegal logging activities. Moreover, losses are not confined to countries with illegal logging. Preliminary research by the

Foreign Agricultural Service (FAS) suggests that illegal logging could be costing U.S. exporters hundreds of millions of dollars in lost sales annually.

The Initiative Against Illegal Logging is the result of an interagency effort led by the Council on Environmental Quality (CEQ) and the State Department. It focuses on the development of integrated actions in four areas—good governance, community-based actions, technology transfer, and harnessing market forces—to help countries build capacity to combat illegal logging and associated trade through public-private partnerships and incentive-based programs.

The initiative alone will not solve the issue of global deforestation. The clearing or burning of forests for farming or grazing, forest fires, urban growth, and pressure placed on natural resources by countries trying to meet the economic needs of an expanding population are also important causes of deforestation. Countries will continue to need assistance in all these areas if we are to slow down the rate of global deforestation.

Certification

Within the issue of certification, four topics remain points of discussion: where should certification take place, by whom, under what authority, and for what purpose.

It is well recognized that tropical timber producing countries have substantially less certified forest area than do temperate forest countries. This has been identified as an important issue potentially affecting future market access for tropical timber.

The reasons for the small area of certified tropical forests are varied and complex. However, one of the most important is insufficient institutional capacity for sustainable forest management (SFM) in tropical forest countries. The building of institutional capacity includes, but is not limited to, the following:

1. Proper legal frameworks and the capacity to enforce forest and environmental laws
2. Capacity for forest inventory and assessment
3. Capacity of public forest services, rural communities, and private landowners
4. Capacity to implement reduced impact logging (RIL)
5. Capacity to protect non-market values and services of forests
6. Capacity to constructively involve local communities and indigenous groups

The great bulk of the work involved in moving toward certification is in the building of the institutional capacity for SFM. Although certification schemes may vary with respect

to the relative importance placed on various aspects of institutional capacity for SFM, all certification schemes that have credibility in the marketplace have many elements in common. Those common elements have been increasing over time, and calls for mutual recognition are likely to cause even more convergence in the future.

At its 32nd Session in Bali, the International Tropical Timber Committee (ITTC) the governing body of the International Tropical Timber Organization (ITTO), adopted Decision 11(XXXII), which states: “forest certification is an important voluntary market-based tool to encourage and create incentives for sustainable forest management and improving market transparency,” and “ITTO as an international organization should not endorse, create or adopt, or be perceived to endorse, any particular certification approach or scheme, including any accompanying standards developed for the purpose of certification.”

As a member of the ITTO, the United States remains committed to that policy.

It is acknowledged that there is room for honest differences of opinion as to the appropriate role of certifying authorities and operative government and non-governmental agencies within the context of certification. A wide variety of projects are clearly appropriate for governmental and non-governmental funding. These include projects that

- help countries build their institutional capacity to achieve the sustainable management of tropical forests and that, in the process, build the capacity to become certified,
- help countries to build the capacity to measure and put into operation criteria and indicators of SFM, and to develop credible environmental auditing systems that may assist in the certification process,
- help countries develop needed legal and institutional frameworks, including best management practices and standards, law enforcement capacity, RIL, and other measures that are the foundation for SFM (and for most timber certification schemes), and
- facilitate discussions (including funding and convening workshops, conferences, and other forums, and producing publications) on timber certification, including comparison of various elements and aspects of timber certification schemes.¹

Other projects address whether it is appropriate for governments to provide funding since support could disrupt normal

marketplace interactions. The types of projects raising such questions include the following:

- Funding precertification or certification audits for particular certification schemes.
- Directly financing accreditation or standard-setting bodies or certification bodies for particular certification schemes.
- Funding public relations efforts to promote certified products under particular certification schemes (which often promote their approach at the expense of other schemes).
- Funding buyers groups that promote products certified under particular certification schemes.
- Supporting direct implementation of certification schemes that are not likely to find market acceptance.

Trade Liberalization

It is logical that a comprehensive approach to tariffs and non-tariff trade barriers be tried, although it is widely recognized that such an approach will be difficult to define. Likewise, the community should keep in mind that studies have shown that trade liberalization is unlikely to have a significant effect on forests. The use of trade-related measures to address environmental and social concerns is, and should be, widely debated, particularly as a way to encourage sustainable forest management. Trade liberalization should be supportive of environmental policies. Trade measures should not be used to address environmental problems; the effectiveness of such is unproven and may lead to unintended consequences.

In addition to providing the “world forest products economy,” domestic markets play an increasing role in forest products trade, which is not subject to international trade rules and trade negotiations. Still, market access in regional and particularly international markets is crucial for national economic development. Boycotts of tropical timber organized by consumer groups and non-governmental organizations have had a great impact on market access, particularly of tropical timber in the past. Despite its relatively short existence, the Indonesia–United Kingdom bilateral agreement on “legal timber imports” is an example of a notable shift towards less scrupulous industry conduct and increasing sensitization of markets on the issue of sustainable forest management.

Solid Wood Packing Material

On May 23, 2003, the United States notified the World Trade Organization (WTO) of a proposal to amend its regulations covering the importation of solid wood packing material (SWPM). In recent years, the United States has registered a significant increase in not only the number of pest interceptions associated with SWPM, but also in the number of species of quarantine pests being intercepted.

¹Consistent with Decision 11(XXXII), such discussions, workshops, conferences, and other forums and activities should not endorse, or be perceived to endorse, any particular certification approach or scheme.

Introductions into the United States of quarantine plant pests, such as the pine shoot beetle and the Asian longhorned beetle, have been linked to the importation of SWPM. These and other plant pests that are carried by some imported SWPM pose a serious threat to U.S. agriculture and to natural, cultivated, and urban forests.

The introduction of pests through SWPM is a worldwide problem. There is a need to develop and implement globally accepted measures that can be applied to SWPM to practically eliminate the risk for most quarantine pests and to significantly reduce the risk from other pests that may be associated with SWPM.

Development of the Integrated Plant Protection Center (IPPC) guidelines was prompted by a proliferation of national standards to address the risks associated with SWPM. In recent years, Australia, Brazil, and China have all put in place measures to address the growing risks associated with SWPM. More recently, the European Union began requiring the treatment and marking of coniferous SWPM originating in the United States, Canada, China, or Japan. Canada, Mexico, and the United States agreed to implement the IPPC guidelines by January 1, 2004.

Building Codes and Standards

Building codes and standards are influenced by a number of factors, including the diverse history of geographically based traditional approaches to design and construction in timber. Many building codes and standards go back hundreds of years and involve such simple differences as units of measure and traditionally accepted member sizes and support spacing. Global codes and standards can be used as mechanisms to facilitate or impede trade.

The WTO Agreement on Technical Barriers to Trade (TBT) aims to reduce impediments to trade resulting from differences between national regulations and standards. This agreement invites the signatory governments, including the United States, to ensure that the standardizing bodies in their countries accept and comply with a “Code of Good Practice for the Preparation, Adoption, and Application of Standards.” The WTO goal is admirable in that where international standards exist or their completion is imminent, signatory standardizing bodies shall use them, or the relevant parts of them, as basis for standards they develop. This does not mean only standards derived by the International Organization for Standards (ISO), but also those derived by standardized procedure under WTO-recognized requirements for openness and transparency, which have achieved widespread use and acceptance in the global marketplace. Inherent is the concept of mutual recognition, which should be taken not as exact replication, but rather as congruence.

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