The Forest Focus Autumn 2010

An insight to forest products industry trends and outlooks for businesses like yours in Pennsylvania.

Our world-class forest resource and innovative manufacturers hold advantages that will define the success of the U.S. forest products industry as a force in an expanding global marketplace. How will this reality impact you?

Expect Further Consolidation Opportunities

Since U.S. housing began sliding from its all-time high in 2005, North American lumber demand has contracted rapidly. Closures, retirement and slow-downs at many mills created expansion opportunities for some operations despite a smaller market. This trend is likely to continue in both the logging and the sawmilling sectors, and will favor efficient firms with strong cash positions.

Foreign Demand for Your Products

Hardwood lumber prices are up 25 percent over last year. The recent pricing strength that many firms have enjoyed results from two sources:

1. Relatively brisk foreign demand
2. Temporary effect of inventory re-building throughout the domestic hardwood supply chain

As inventory-rebuilding trends abate, watch for strong foreign demand to remain as Chinese markets increase their in-country consumption of U.S. forest products (as opposed to re-export).

Continued and Stable Demand for Lower-Grade Wood Products

U.S. economic growth, rising energy prices and continued wind and natural gas exploration activities in Pennsylvania and New York, will drive opportunities for lower-grade lumber, biomass and alternative fuels from our growing forest resource. U.S. gross domestic product (GDP) drives markets for many products derived from low-grade timber: paperboard, packaging, pallet, truck flooring, railroad ties and blocking lumber all benefit from a growing U.S. economy. Real (inflation-adjusted) GDP growth stands at a modest 2.4 percent and is likely to remain between there and 2.7 percent for the next six months. Furthermore, U.S. energy prices are expected to climb 5 percent in 2011.

Marcellus-Induced Timber Famine (or not)

Some fear landowners' newfound gas-related wealth will de-prioritize timber sales, resulting in log shortages for our recovering sawmill industry. Western Pa. is a great example of why we don't think a Marcellus-induced log famine will ever materialize. Western Pa. has enjoyed a productive oil and gas industry for 150 years, generates consistent royalty income for subsurface owners and still manages to supply a steady flow of world-class timber and forest products to global markets each year.

Here's why:

1. The average land-ownership tenure in our region is relatively short (less than 10 years).
2. Once oil/gas activity starts in an area, owners continue to sell land (surface rights), but tend to sever the surface rights from the sub-surface rights (oil and gas), and retain those rights.
3. Over a short period of time, the surface land and timber owners have no access to gas income since the gas rights are owned by another party (prior owner).
4. Over time, these same new surface owners are motivated to sell timber for reasons similar to those in the past.

However, it should be noted that gas development has become a strong competitor for skilled labor in our area, forcing some firms to consider automation in some areas.

Ash

Foreign firms now choose ash as an attractive and relatively inexpensive alternative to other higher-priced U.S. hardwoods. Many feared the Emerald Ash Borer's arrival in Pennsylvania and New York would create a glut of ash and drive prices further down. Just the opposite has happened. Ash supply is up while ash demand is up sharply. Much of the demand surge is from foreign buyers who see ash as a great value for the price.

Sure, significant challenges abound. And so, too, does American hardwood quality, service and ingenuity – key ingredients for long-term, competitive success!

Please Note: Your AgChoice Forest Products Team will sponsor the 2nd annual Forest Products Executive Development Workshop with the Pennsylvania Forest Products Association at the Ramada Inn & Conference Center in State College, Pa. on Wednesday, September 15, 2010. For a registration form call (800) 327-6878 or e-mail coudersportinfo@agchoice.com

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