



IS THE FOREST INDUSTRY WOOD SUPPLY CHAIN READY FOR RECOVERY?

Surveys/Studies: logging

November 2013

INTRODUCTION: This project, commissioned by the Wood Supply Research Institute (WSRI), is an assessment of the capability of the wood supply chain for the U.S. forest industry's primary manufacturing. Because of the long decline in wood consumption associated with the economic recession, we have determined that there was a significant net divestment in harvesting capacity infrastructure in the 2007-2010 period. The focus of this study was to evaluate the current regional harvesting capacity and to quantify supply chain capabilities to meet future roundwood consumption. The focus question is, ***“Does the wood supply system have sufficient capacity to meet the anticipated growth in harvest demand over the next five years?”***

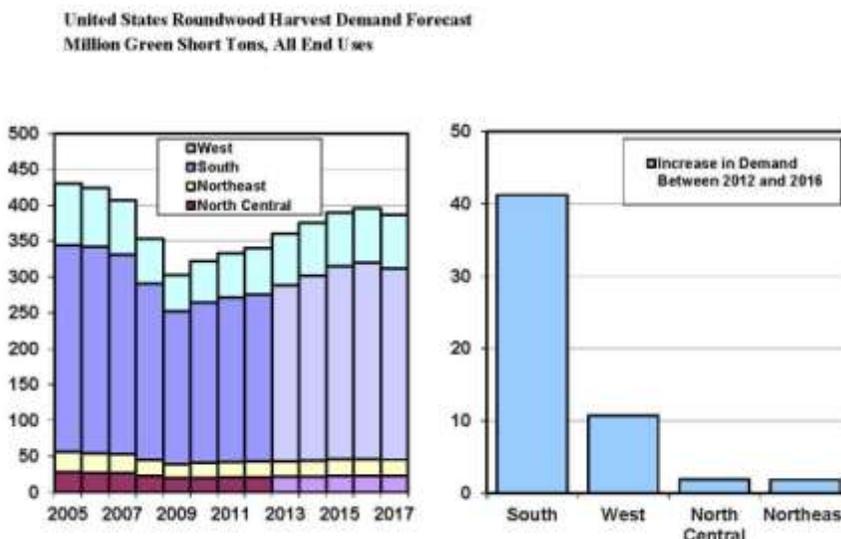


Fig. 1: RISI's forecast demand for roundwood harvest for the U.S. forested regions.

The primary metric used to quantify required harvesting and trucking capacity is investment capital in harvesting and trucking equipment. The first step was to determine the various logging systems throughout the United States and their average productivity related to capital deployed. To contend with the problematic aspects of estimating industry capital stock, we performed a number of risk simulations. The projected roundwood harvest demand is based on the latest RISI forecast, prepared in May 2013.

The value of this information is to understand that wood suppliers will need to have a reasonable investment environment to be willing to spend capital to expand operations on a timely basis. Based on our findings, we recommend that the end-user community evaluate the magnitude of change in demand within its respective procurement basins. If appropriate actions are implemented, the industry can take full advantage of the favorable business cycle.

STUDY FINDINGS: The results show that a significant infusion of capital will be required to meet forecast demand. We see the level of invested capital within the wood supply chain needing to increase from a low of \$5.9 billion in 2010 to \$7.75 billion by 2017 (*Fig. 2*). WSRI also recognizes a critical need to improve the working relationships between suppliers and wood-consuming mills in order to improve the investment environment and the overall capacity.

Below is a list of the most important points underlying this analysis:

1) The last four years of severe recession in primary markets have significantly weakened the supplier businesses, depleting savings and worsening debt.

2) Equipment is aged and in need of replacement. The availability of labor is another important consideration, but outside of the scope of this analysis.

3) Supplier-consumer relations are strained, and a sense of trust and recognition of suppliers' importance to the industry needs to be improved.

4) The markets are in the beginning stages of a robust recovery. Wood procurement organizations will need to accommodate an accelerated rise in log demand.

5) Reinvestment in harvesting equipment has begun, but in every U.S. region investment levels are still below the levels required to maintain the capital stock.

6) Massive logging and trucking capital investments will be required to meet the projected harvest demand.

7) Due to restrictive logging equipment financing, and poor returns within this sector, new entries into the wood supply business will be spotty at best. The existing supplier businesses are the most likely to expand the capacity.

8) There is a recognized need to rebuild business relationships to minimize disruptions in the flow of wood. If business relations can be improved, suppliers and consumers of wood fiber and harvesting capacity will be more able to accommodate future harvest demand and support cost control for both suppliers and consumers.

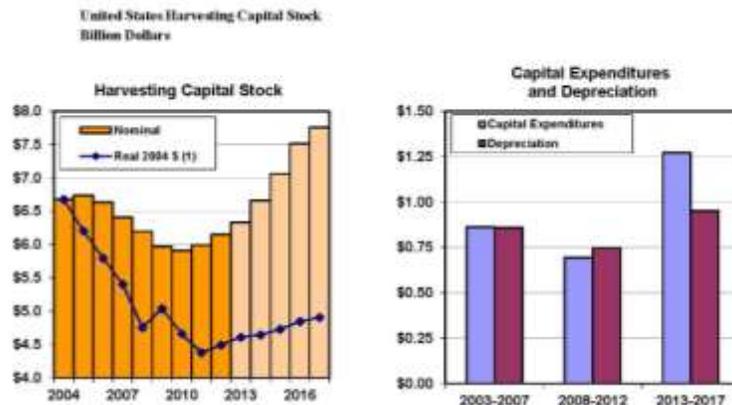


Fig. 1: U.S. harvesting capital expenditures and projections.

RECOMMENDATIONS: Each company has to make its own strategy based on the local conditions. It is certain that there is a looming challenge ahead for a recovering industry. It is time for procurement organizations to examine and rethink all procurement policies and strategies. A favorable business environment must be cultivated if the necessary capital investments both to hold and expand harvesting capacity are to be realized.

The recommendations include:

- 1) *For procurement managers:* It is time to assess your wood supply system to determine the magnitude of increased demand in your procurement basin and if harvesting capacity is adequate. We think it is fair to say that the industry (whether large public or private companies) tend to think of the independent wood supply system as having the ability to react quickly to market demands. The results of this study indicate that this perception presents operational risk for the next market cycle. An assessment that indicates a deficit in logging capacity should be communicated and understood by the top levels of the consumer companies. As part of planning, the age-old "arm's length" restrictions need to be reexamined in the light of well-developed supply chain management techniques that maintain supplier independence and use tested strategies that lead to success for both suppliers and consuming mills.
- 2) *For procurement managers:* It is time to learn as much as you can about your key suppliers, their current equipment configurations, ability to expand, purchased stumpage backlog, and financial

capability to obtain capital. For those willing and capable, it may be time to ask what they need to provide to a business environment to begin planning for expansion. Capital investment will require solid contracts, documented (“take-to-the-bank”) volume commitments, and steady wood orders. This is also a good time to assess the quality of the business relationship with key suppliers and address factors that may hinder productivity.

- 3) *For wood suppliers:* It is time to assess your business strategy and examine the relationship with your customer mills. This assessment may include attention to business relationships with the mills that are core to your business and focus on organizations that demonstrate they care about building strong relationships.

CONCLUSION: the forest industry is working through a unique and unprecedented industry market cycle. A new and innovative approach is required to meet the challenges associated with capacity for harvesting and delivering wood. It is a manageable situation if the issues are intelligently approached with clear backing from the most senior levels within the company organizations. The major objective is for both suppliers and consumers to come together to make sure that the US forest industry can take full advantage of the coming economic upswing.

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FRA STAFF COMMENT: This Technical Release is a very brief summary of the comprehensive *Wood Supply Chain Analysis Report* that is posted in the “Research Findings” section of the WSRI web site (www.wsri.org).

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