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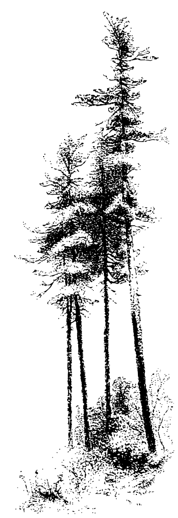
Washington's Forest Products Industry: Current Conditions and Forecast, 2007

Produced by
The Inland Northwest Forest Products Research Consortium, a research cooperative centered at the Forest Products Department at the University of Idaho, the Bureau of Business and Economic Research at The University of Montana-Missoula, and the Wood Materials and Engineering Laboratory at Washington State University.



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Overview

Forests cover over half of Washington's land area. Of the 23 million acres of forestland in the Evergreen State, 16.2 million acres are classified as commercial forests. Washington's $253.1 billion gross state product in 2005 included $1.6 billion from lumber and wood products. Paper and allied products contributed another $1.5 billion in the same year.

Washington State remained the second largest softwood lumber producer in the United States by a comfortable margin. Lumber production during 2006 appears to have increased slightly relative to 2005 levels. However, weak markets during the latter part of 2006 led to increased inventories of unsold, sawn wood products in the distribution channel, and some mill closures. Additional mill closures appear likely during 2007, with older milling capacity at the greatest risk. The production of structural plywood panels remained strong in 2006 (Figure 1), with a small increase in production levels over the previous year. However, panel production appears to have declined in 2006 due to weaker markets and mill closures. Markets for sawn wood products and structural panels appear likely to remain weak during 2007 as a result of the cooling off of the housing market.

Nearly two-thirds (64%) of all forestlands in Washington are owned or managed by federal, state, local, and tribal governments. The U.S. Forest Service is the largest land manager in Washington State, overseeing 9.2 million acres of National Forest land; however, federal timber harvests in Washington State currently account for a very small percentage of the state's annual harvest. National Forest harvests in the state have not exceeded 100 million board feet in the past decade. The volume of sold timber on federal lands in the state increased to 85.5 million board feet in 2004, up dramatically from the previous year. The increased volume of sold material is, at least partially, a reflection of the implementation of the Healthy Forest Initiative. Although, data for 2005 or 2006 are not available at this time, it appears likely that federal timber harvest levels may increase modestly, but will remain a very small proportion of the total volume harvested in the state.

The Washington State Department of Natural Resources (DNR) is the second largest government manager of forestlands in the state, overseeing 2.1 million acres of forested trust lands. Harvest levels on state trust lands are an important source of logs for the state's mills. Harvest from DNR lands is currently projected at 528 million board feet (Scribner scale) in 2006, rising to 621 during 2007. Harvest levels on DNR lands are expected to gradually increase over the next few years reaching a projected harvest level of 755 million feet in 2011.

Approximately 36 percent of Washington's forests are privately owned. Slightly more than half of these lands are managed by the forest products industry. Industrial forestlands are managed primarily for timber production.

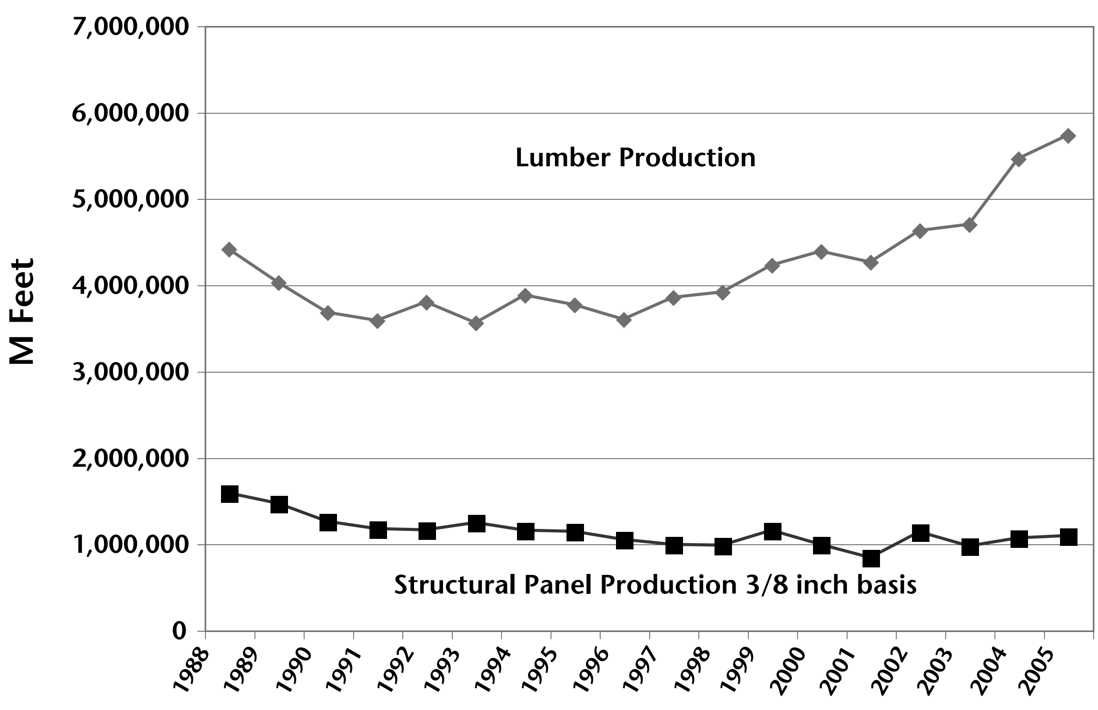

Figure 1.
Lumber and softwood structural panel board production.

Nonindustrial landowners and other private business entities own the remainder of Washington's privately owned forest lands. In recent years these ownerships combined have accounted for over 75 percent of the state's annual harvest of over 3.5 billion board feet, a trend that appears likely to continue in 2007. Harvest levels from all private lands are estimated at 2.56 billion board feet (Scribner scale) for 2006, based on data compiled by the State of Washington, Department of Revenue (Figure 2). Continued weak markets may result in a modest reduction in harvest levels on private lands during 2007.

Tribal lands are also an important source of timber harvests in the state. Current harvest volumes from tribal lands in the state are not available at this time. Available annual harvest volume data for the period 1994 through 2003 ranged from a low of 161 million board feet to a high of 334 million board feet, with an average of 267 million board feet (Scribner scale) for the period. Given current market conditions, it appears unlikely that harvest levels on tribal lands will exceed the average for the 1994 to 2003 period and may be even lower during 2007.

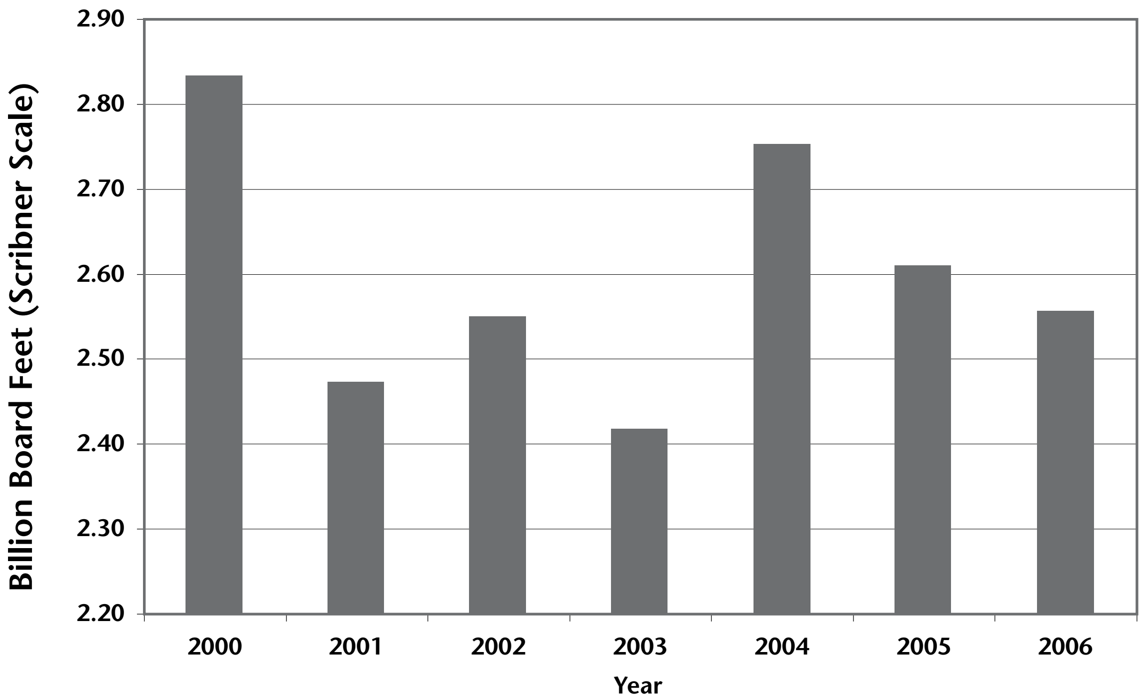

Figure 2.
Timber harvest on private lands in the State of Washington.

National and International Factors

During 2006 we saw a slowing of growth in the national economy, but the creation of new jobs remained relatively strong. The national unemployment rate dropped to 4.5 percent by the end of the year—the lowest level in several years. The sharp run-up in oil prices during the spring and summer of 2006 tended to limit consumer spending and increased concerns over inflation. Declining energy prices during the latter part of the year reduced these concerns, but industry and consumers remain wary about what will happen to energy prices during 2007.

GDP—the output of goods and services produced by labor and property located in the United States—has been projected to average 3.3 percent growth nationally during 2006. Economic growth is projected to drop to 2.4 percent during 2007 with employment increasing at an annual rate of 1.4 percent. Overall GDP growth is expected to slow over the next two years. Current forecasts call for growth rates of 2.6 percent in 2007 and 2.7 percent in 2008.

The Federal Reserve held to its "target funds rate" of 5.25 percent throughout the last half of 2006 after several years of steady increases. Although the Federal Reserve continues to express concern over inflation, current forecasts indicate that the economy will gradually slow to allow the Federal Reserve to begin cutting the target rate in 2007. These forecasts suggest that the economy will likely achieve the hoped for "soft landing" in 2007.

The growing federal deficit contributed significantly to the decline of the U.S. dollar relative to other major currencies in 2006. The dollar is expected to continue its decline in 2007, which, in turn, will increase the attractiveness of wood product exports from the State of Washington.

Outlook

The lumber and wood product sectors provided an estimated 20,300 jobs during 2006, an increase of 300 jobs over 2005 levels. The pulp and paper sectors employed an additional 12,100 citizens of the state of Washington (Figure 3), down slightly from 2005 levels. Employment in the pulp and paper sector is projected to be relatively stable through 2009; however, the sawn wood product sector is projected to lose 2,400 jobs by 2009.

During 2006, the United States and Canada signed the Softwood Lumber Agreement ending years of negotiation. Canadian shippers now face a 15 percent duty at the border instead of the previous 10.8 percent duty. (Note: The actual duty will vary from zero to 15 percent based on the Random Lengths Framing Lumber Composite Price over the previous six months.) The signing of this historic agreement initiated the refunding of approximately US $4.3 billion paid since May of 2002 to Canadian mills. An additional US $1.0 billion will stay in the United States.

A key question is: "What will the Canadian mills do with this windfall of cash?" One potential option would be for the Canadian operators to invest at least a portion of this money in improved milling efficiency as well as new capacity. Both of these investments appear likely as the Canadians attempt to salvage as much beetle-damaged timber as possible over the next 10 to 15 years.

U.S. housing starts are projected to remain at or below the 1.7 million mark for 2007. The housing market appears saturated at this time, with home ownership at almost 70 percent of adult families, up three percent over the course of the recent housing boom. Home vacancy rates have also increased over the past year and rent-to-value ratio of multi-family homes has declined. Similarly, the affordability of housing has fallen sharply due to the run-up in home prices and rising mortgage rates. As a result of these and other factors, prices for lumber and other wood products appear unlikely to improve in 2007.

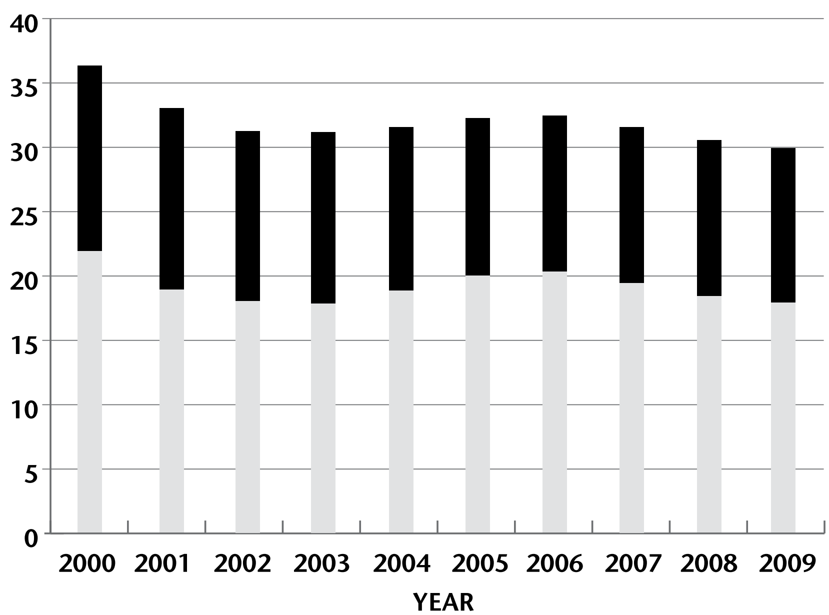

Figure 3.
Estimated employment in Washington's forest products industry by sector.

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