



BC COAST INDUSTRY COMPETITIVENESS: GOOD NEWS AND BAD NEWS

In assessing the BC coast’s delivered log and sawmill competitiveness, the evidence is very clear on some of the longer term trends. Since 1987, about 50 sawmills have closed, where 27 of these closures occurred since 2004. BC coast lumber production has plunged from 4.7 billion board feet in 1987 to 1.4 billion board feet in 2015. With less than 30 sawmills left in operation, one may conclude that the BC coast has been a graveyard of sawmills over the last 30 years.

The good news is that all of the high cost mills have been closed. All of the remaining mills are survivors with better cost structures and increased output, where many have a reasonable chance of continuing on. Sawmills need ongoing capital spending to remain competitive and efficient and there is strong evidence of this occurring at some mills (such as in many Western Forest Products mills), but other mills still may be running on borrowed time. As a result, the future of the BC coast’s sawmilling industry will be tied to those mill owners that see a future and are able to further invest in, or innovate with, their mills. And equally important is having access to predictable supply and cost of sawlogs—this has been made more difficult with the increasing Asian (led by China) log export demand since 2009.

WOOD MARKETS has been assessing the competitiveness of BC delivered log costs, sawmill costs and margins and other elements in comparison to other competing regions since 2000. WOOD MARKETS’ most recent biennial Global Timber / Sawmill / Lumber Cost Benchmarking Report was produced late last year and covers logging and sawmilling costs in 29 countries and regions on five continents. The report focuses only on structural lumber mills and includes detailed costs for two categories of mills: “average” and “top-quartile” mills, including the BC coast.

To provide some perspective from this biennial report, various cost categories

at “average” mills in 29 countries or regions were ranked: from 1 (best) to 29 (worst). The ranking for the BC coast was documented to show the position and trend in BC coast costs since 2002 and here is a summary of the results:

BC Coast “Average” Sawmill Ranking in Global Survey

Category	2002	2008	2014	2010 to 2014 Rank Trends
Delivered Log Costs	29	11	15	FLAT
Sawmill Costs	29	12	23	FLAT to WORSENING
Lumber Revenue	7	15	22	WORSENING
Earnings (EBITDA)	19	19	16	FLAT to IMPROVING

Scale: 1 = BEST; 29 = WORST

Source: WOOD MARKETS’ Global Cost Benchmarking Report (2015)

The survey results show rankings only and many factors are in play. For example, currency exchange rate changes can increase or decrease the BC coast costs, and therefore the ranking is relative to other regions—regardless of any real cost changes. Other factors at work include changes in lumber prices in key markets, in ocean freight rates, in government policy, and other factors.

So, what conclusions or trends can be extracted about the BC coast “competitiveness ranking” in relation to other sawmill regions that produce structural lumber from the Global Benchmarking Report since 2002?

- Delivered Saw Log Costs: they are above the global average for “average” mills, but the overall trend has seen lower costs from 2002 to 2010, but they have been rising slightly (worsening) in the rankings since then.
- Whitewood Sawmill Costs: they are above the global average for “average” mills, but the overall trend has seen a steady rise (worsening) in the rankings since 2008.
- Lumber Revenue: this has been quite volatile in the rankings, but has generally been close to the global average but did rise (worsen) in 2014 to its highest rank.
- Whitewood Sawmill Margins: they have been near the global average, but

have been below average for North America and were negative in 2006 to 2010; despite this, it improved to reach its best ranking in 2014.

The rankings only provide perspective relative to other countries. For example,

with Europe’s lumber market being weak since 2012 and North America’s being better, European mills have slipped in the rankings while North American regions have improved.

What is positive in the ranking trends is that delivered log costs have been heading in the right direction. Reductions in the delivered log costs on the BC coast between 2002 and 2010 have been significant in Canadian dollars per cubic metre despite some small reductions in the rankings. This is because there will always be countries or regions with lower log costs, such as in the BC Interior and the Prairies.

While the trend in the ranking of sawmill margins at “average” BC coast mills have been improving, the actual earnings are still very low in Canadian dollars per cubic metre: the highest actual EBITDA earnings have not been higher than 5 per cent of lumber sales since 2000 in our surveys, with losses recorded in 2006 to 2010. This seems to tie into an erosion in the ranking of sawmill costs, where “average” BC coast sawmills still tend to have high costs with some mills less competitive. For the BC coast, it is important to realize that sawmill costs for processing larger old-growth timber

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a new Softwood Lumber Agreement (SLA) is a huge risk to the coast with its higher value products. When considering rates, the transactional point in time has to be considered.

As a place to start the discussion, it was agreed that the panel provided points of view that both sides of the discussion could take away and consider. However, the fact that in an audience poll conducted during the Forest Minister's presentation earlier clearly pointed to ongoing angst between contractors and the majors.

Audience Polling

Describe the nature of your relationship with your employee licensees.

- **Very good 10%**
- **Good with some, weak with others 50%**
- **Troubled 40%**

It is clear that these types of discussions need to continue and both sides need to consider the needs of the overall supply chain if we are to be mutually successful.▲

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will be much different than processing smaller second-growth logs. What is ultimately important is sawmill margins, but higher cost sawmills have a history of disappearing on the BC coast.

To maintain competitiveness or to implement innovation, capital investments are required to reduce operating costs, increase flexibility, or to consider new products or markets. No matter what the rankings are, the real question is: who is prepared to invest in the BC coast sawmills? There are always opportunities, but there is always risk, as evidenced by the steady erosion in the number of operating sawmills on the BC coast and the increase in log exports. There is no simple answer, especially when Crown timber is the base of timber supplies and government policies (both provincial and federal) are in effect and can change, not to mention the unknown details of the new Softwood Lumber Agreement that will emerge later this year.

Many of these elements, markets and competitive factors will be discussed at WOOD MARKETS' 6th Annual Global Softwood Log & Lumber Conference May 5-6, 2016 in Vancouver, including in-depth discussions on the new dynamics in China and Russia.▲

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International WOOD MARKETS Group Inc. is Canada's largest wood products consulting firm. Its consulting team has provided industry and market expertise in the solid wood products field to its clients since 1993. The company provides market research, new business development, business plan/strategy, as well as other consultative services to wood product companies in North America and around the world. The firm also publishes a number of strategic industry multi-client reports including its landmark WOOD Markets Monthly International Report (since 1996) and monthly China Bulletin. Further information is available on www.woodmarkets.com.

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