Photo: Brian Dennehy Photography

THE PATH TO MUTUAL SUCCESSFUL CHANGE: CONTRACTOR SUSTAINABILITY & INDUSTRY COMPETITIVENESS

TLA Editorial

Contractor sustainability has been a focal point of the TLA advocacy effort over the past few years and the "Path to Mutual Successful Change" panel at the recent TLA convention brought together representatives from both the contractor community and the major tenure holders to discuss the issue.

In his introduction to the panel, moderator David Elstone noted the need to change the focus to a value driven supply chain in the BC forest industry, as opposed to the traditional cost driven approach that has been at the heart of contractor rate disputes for decades. He also noted that this type of venue, where participants in the supply chain get together and discuss their mutual needs is often time the best way to find mutual benefit.

Representing the contractors were Don Banasky of Western Canadian Timber Products, Mike Richardson of Tsibass Construction and Justin Rigsby of Holbrook Dyson Logging. The majors were represented by Ian Fillinger of Interfor, Mike Ward from Western Forest Products (WFP) and Brian Baarda of TimberWest.

The first question put to the panel was: What does contractor sustainability mean to you?

On the licensee side, Baarda commented that the key attributes of a good (sustainable) contractor included the fact that they run a safe operation, have a cost focus that challenges their company to eliminate waste in the supply chain and that they have an innovation focus. Words of advice for all contractors.

Ward noted that WFP harvests approximately 70 per cent of its volume using contractors today. Based on a poll they did of their contractor workforce two years ago, they define "good or healthy contractors" as having an ability to work safely, a strong management team, a strong balance sheet, a commitment to the long-term and a diverse customer base. Ward admitted WFP is not there yet with all of their contractors and there are opportunities to reconfigure contractors to meet these objectives. WFP's goal is to be a sustainable business through market cycles and Ward believes that contractors have to be able to do the same.

Fillinger noted that he is asked all the time about the sustainability of their business by customers and that the sustainability of their contractor base contributes to their overall sustainability. He believes that if Interfor can provide sufficient standing timber inventory ready to harvest, it can provide contractors with security as they know the work is ahead. He admitted, however, that there was more work to be done by Interfor here.

For the contractors, Rigsby defined sustainability as leading to a healthy retirement and he hoped, for his own sake, that his company is sustainable. However, he pointed to the fact that in a recent survey of the most profitable companies in BC, West Fraser was #12, Canfor #13, WFP #25 and Interfor was #37. As an industry, this is good because there is money in the business. However, at the same time, news reported six contractors as leaving the business due to financial difficulty and challenging relationships. Licensee rates of return are going up while contractors are going down. It is scary and clearly not sustainable. This disparity in the allocation of pie today has to change.

Audience Polling

Do you believe that the logging contractor base is sustainable?

- **No: 66%**

Is your forestry industry related business sustainable over the next five years?

- **Yes 39%**
- **At risk 36%**
- **Don't know 25%**

On the topic of what are the key things that need to change in order to support a reduction in delivered log cost, Banasky spoke to the fact that bid rates are only sustainable if the conditions don't change. The "ripples in the water" cost everybody money and they have to be a focus of the majors. Things included after the fact such as added safety requirements or more sorts are the types of changes in conditions that should support changes in agreed upon rates.

Ward noted that reductions in log costs could come with further optimization of contractors, matching of equipment complements to the harvest profile and WFP's new lean log handling process. Another key is to reduce the industry regulatory burden, fundamentally a government initiative.

Justin Rigsby and Fillinger spoke to a common issue of logging development planning. For contractors, falling, bucking and loading on the same block happens way too often and is not always safe, noted Rigsby. For Interfor, it takes up to a year to move a log to the customer as a finished product and this can tie up some $100 million annually, capital that could be used for other investments if the planning process could be sped up and optimized.

With a focus on new steep slope technology being developed globally at the convention, when asked if conditions on the coast are right to support innovation and investment, answers were mixed.

Baarda believes that there is a contractor base willing to support innovation and with manufacturers like T-Mar Industries Ltd. taking up the challenge and improving safety and productivity, he believes we are on the right track. Is the regulatory environment right? Perhaps not as WorkSafeBC is catching up and right now regulation remains a challenge on steep slopes. Ward noted on the other hand that WFP is making investments of strategic capital in manufacturing, investments that will give higher return to logs which will lead to higher free cash flow and eventually more capital for woodlands.

Speaking for his company (and contractors in general), Banasky noted that it was difficult to invest heavily as a result of trust issues with customers. Without improved trust, they cannot risk the viability of the company on erratic work programs and schedules.

Fillinger commented that there is extreme competition for capital within the company and Interfor makes investments where they see the greatest return for their shareholders. Of note, Interfor has invested in 13 mills in the United States.

Audience Polling
Are you investing in your business?
- **Yes 68%**
- **No 24%**
- **Downsizing 8%**

Are you planning to invest in new or rebuilt equipment in the next few years?
- **Yes 69%**
- **No 22%**
- **Maybe 9%**

On the topic of First Nations involvement in the industry and how First Nations fit into their corporate position, responses were focused on raw material access. Ward noted WFP engages with 45 First Nations in their operations. They have joint ventures, limited partnerships, contract logging and other types of arrangements given the exponential growth in First Nation engagement over the past 15 years. This growth is fundamentally driven by a need to access fibre which is key to WFP.

Fillinger notes that Interfor has good relationships with customers, but admitted they have more work to do to fully engage with First Nations on the fibre (raw material) side. For Interfor this is an evolving process.

Audience Polling
Have you engaged with First Nations businesses or capacity building?
- **Yes 79%**
- **No 11%**
- **I plan to 10%**

The panel participants were united on the issue of recruitment and training in their companies fundamentally driven by the "grey wave".

Ward noted that WFP has 500 employee loggers with 52 per cent older than 55. For hand fallers, the average age is more like 59, noted Richardson. It suggests the need for up to about 25 replacements annually in WFP company operations on average with an additional 75 contract employees in woodlands. WFP ran a logging fundamentals training program, but discontinued it because their graduates did not all choose to work for WFP—a challenge echoed by others.

Both Banasky and Richardson acknowledged challenges in retaining employees once an investment in their training has been made. As Richardson noted, it takes a long time to teach skills and trades people especially don't have loyalty—they tend to chase the bigger dollars in other industries.

Everyone agreed that recruitment and retention is an area where a collaborative approach is needed.

Audience Polling
Are you concerned about future employee recruitment?
- **Yes 80%**

With a focus on improved safety of the industry since 2003, when asked; within your company have you invested in safety and has it paid off, again, the answers were mixed.

Ward said WFP has a dedicated safety support team and noted that their MIR has gone from 3.5 to less than 1.0, a clear improvement. At the corporate weekly which includes the CEO, every single safety incident is reviewed. WFP is planning more investments in the area of risk acceptance internally first and then expanding to contractors.

Fillinger, however, was more philosophical and wondered why some people don't want to talk about safety. If it is a production and quality issue, they are typically dealt with immediately. But not always with a safety issue. From his perspective, the conversation about safety is not changing quickly enough.

Fillinger went on to talk about the growing need for drug and alcohol testing in the industry as a whole. It's coming to our industry because it is an issue, he noted.

Other improvements in overall safety performance were highlighted by Rigsby who noted they have invested heavily in a viable return to work program. While it is available in his company, he noted we now need the medical practitioners to buy into these types of programs to keep people working.

For Banasky, investments in a fatigue management system (changing work hours for example) in order to better address fatigue is currently being implemented. They are looking for significant results as it rolls out.

Photo: Brian Dennehy Photography

Licensees and contractors dug into the concepts on contractor sustainability and industry competitiveness—and the audience chimed in too!

Audience Polling
Have your investments in safety help to change the culture in your business for the better?
• Yes 95%

The hot button topic of rates was left to the end as Elstone asked the panel: What is the best way to ensure sustainable rates for contract work?

Rigsby said that both parties need a model or guide as an aid to negotiation. But what the industry needs is a guideline for hourly equipment rates like the Blue Book Equipment Rental Rate Guide. It is an independent guide, developed by a third party that is used in other industries extensively. He also noted that there is a need for collaboration with changing labour agreements. Currently, there are a lot of labour agreement costs being passed down to contractors with the recent pattern of agreements.

Ward countered that WFP uses rate models and benchmarks them to their own operations. He agreed, however, that what is needed is data that can be agreed to. He went on to say that log, equipment and lumber prices are all market driven so we can't have a fixed rate model. That said, we can't rely on a model alone to ensure a sustainable contractor base. It was his view that the market swings both ways and that while rates were low during the recession, today that is not the case—rates have come back.

Baarda believes that rate models based on productivity are where the discussions have to start, but then market conditions have to be considered. We also need longer-term contracts in order to allow contractors the security to invest.

Both Rigsby and Banasky agreed that the market for contractors' services is very small (due to licensee consolidation) and that this must be addressed in order to ensure contractors sustainability. As Rigsby noted, if the market rates suggest you cannot meet a minimum EBITDA, it is not sustainable.

In summary, Fillinger noted that the coastal industry is doing reasonably today given exchang e rates and lack of duties. However, he cautioned that changes in exchange rates and the potential for 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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