

BRAZILIAN AND CHILEAN COMPETITION IN THE WORLDWIDE MARKET FOR PLYWOOD AND SOFTWOOD LUMBER

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Over the past several years, worldwide markets for panel products and softwood lumber have undergone significant change. This change has been brought about by two main factors. These are the financial difficulties in Asia and Latin America and, perhaps most importantly, the emergence of Brazil and Chile as competitors. The United States has witnessed a significant erosion of market share in areas such as the European Union (EU) and Korea. At first glance, it appeared the decline in Korea was due to its economic downturn. However, a careful examination of trade statistics clearly indicate a reliance on alternate suppliers with Chile and Brazil among the most important. Statistics for the EU show a similar trend with the United Kingdom being the most notable. In addition, panel producers have recently expressed concerns that Brazilian and Chilean products are making inroads in Mexico and the Caribbean, two important markets for the United States. Statistics also indicate a growing market share for those two nations in the U.S. domestic market.

The main reason for decline in all of these markets is price. Brazilian and Chilean producers are able to produce a lower quality panel for less money. While these products are of lesser quality, the price differential is extreme. Since most buyers in these markets are only concerned with price, the United States is put at a distinct disadvantage. Further, the devaluation of

the Brazilian Real has made Brazilian exports even more affordable.

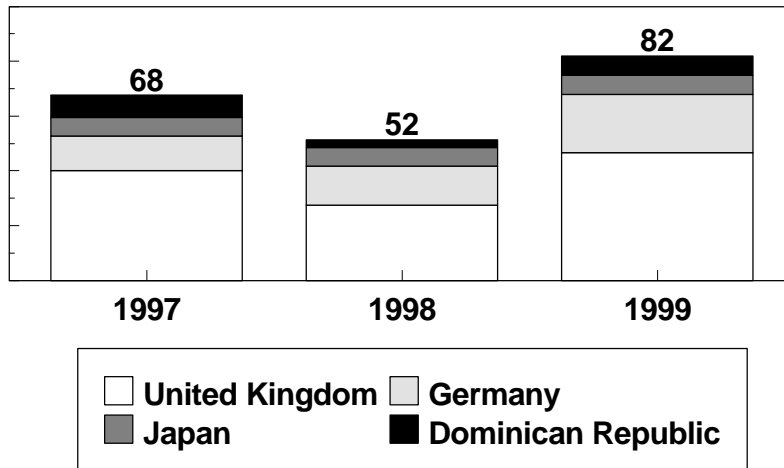
Price, while an extremely important reason for the sharp increase in Brazilian and Chilean panel exports, is not the sole reason for this surge. Both the Brazilian and Chilean governments have effectively managed their forest plantations allowing for high harvest rates which are expected to continue to increase over the next few years. Another important factor is that both countries provide incentives, such as tax breaks, beneficial credit programs, and subsidies, all of which facilitate exporting.

BRAZIL

The Government of Brazil (GOB) first took an active role in protecting and modernizing the forestry sector in 1967. This effort was aimed largely at establishing plantations that could produce wood for use in several sectors including panel and lumber production, paper and pulp production, and fuel for use in the booming Brazilian steel industry. To aid in the establishment of these plantations, the GOB with the help of several large U.S. companies imported the necessary trees. Species included eucalyptus and fast-growing species of pine such as loblolly. This program has proven most effective. Today, Brazil has approximately five million hectares under cultivation. Around 50 percent of this is planted with eucalyptus while 40 percent is planted with several species of pine. In addition to these plantations, Brazil is one of the most heavily forested countries in the world. Approximately 60 percent of the country is forest covered. This ranges from the tropical forests in the Amazon to temperate hardwoods and softwood forest in the eastern part of the country. While much of this land is legally protected from cutting, enforcement is very lax. Recent

Brazilian Plywood Exports to Selected Markets

\$ million



Source: World Trade Atlas

Lumber, both softwood and hardwood, is the leading export for Brazil in terms of the forestry sector. The primary destination for this lumber is the European Union which accounts for 40 percent of Brazilian lumber exports. Another major source of export revenue is panel products. Major markets for Brazilian panel products include the United Kingdom, Germany

and Japan. indications estimate that up to 80 percent of trees are harvested illegally. A large portion of the plantation forest is now shared between the solid wood industry and the pulp and paper industry. Plywood and other panel products are the main products produced by the Brazilian wood industry. Most of the panel industry is based in the southern part of the country. With a few exceptions, mills tend to be rather small, with recent estimates of as many as 400 currently in operation. However, new GOB incentives are helping to modernize production facilities. Brazil already accounts for 49 percent of the panel products produced in South America which translates into around 3.6 million cubic meters. This has the potential to increase to as much as 6 million cubic meters as production methods continue to modernize and harvest rates continue to increase. Additionally, this modernization is leading to a reduced reliance on traditional products such as lumber and plywood as more of an emphasis is being placed on value-added products such as particle board and medium-density fiberboard.

The GOB offers several types of tax incentives to encourage exports. These incentives include such things as tax and tariff exemptions for equipment imported for production of goods for export, an excise and sales tax exemption on exported goods, and eligibility for a rebate on the social contribution tax. In addition, the GOB has set up a drawback system designed to expand exports by allowing Brazilian companies to import raw materials and ingredients at reduced cost. A new addition to the GOB's export promotion effort is the Export Sectors Market Program. This program is used extensively by both the Brazilian panels and furniture industries. The program provides funding for a variety of activities including market research, market development, and favorable terms of credit. The 1998 budget for this program was estimated at \$17.3 million.

In 1997, the GOB created the National Export Promotion Agency to help further promote Brazilian agricultural products. Both softwood lumber and panel products are included under this agency's mandate.

The agency, known by its Portuguese name of APEX, works directly with ABIMCI, the Brazilian Plywood Industry and Exporters Association, to promote the sale of Brazilian panels to overseas markets. APEX does not directly subsidize exports, but provides tax and tariff breaks as described above. In 1997, the annual budget for APEX was \$50 million. This is allocated on an annual basis.

Since one of the leading exports for the Brazilian wood industry is panel products, ABIMCI has recently initiated a program targeted at increasing the quality of their product. While Brazilian panels are often priced well below U.S. panels, their quality is generally considered to be far below that of U.S. product. Brazil hopes that this new certification process will raise the quality of their output, but still keep the price low enough to be more attractive than U.S. panels. This program was announced during the Fourth International Tropical Plywood Congress, Belem-PA, Brazil in October of 2000. Initially developed for radiata pine plywood, this program will later include other types of panels. The program will be implemented in three stages. The initial phase calls for evaluation of panel products and producers as well as other criteria deemed important by the National Council of Plywood Quality. Later stages of the program will involve testing and any necessary adjustments before actual implementation of the program begins. The primary objective of the plywood quality program is to provide high quality products that will meet international market requirements.

CHILE

Chile has also initiated programs designed to successfully manage its forest resources. The Chilean government's management strategy began in 1974 and lasted until the early 1990's, when there were close to two million hectares under cultivation. Roughly 75 percent of this land is planted with

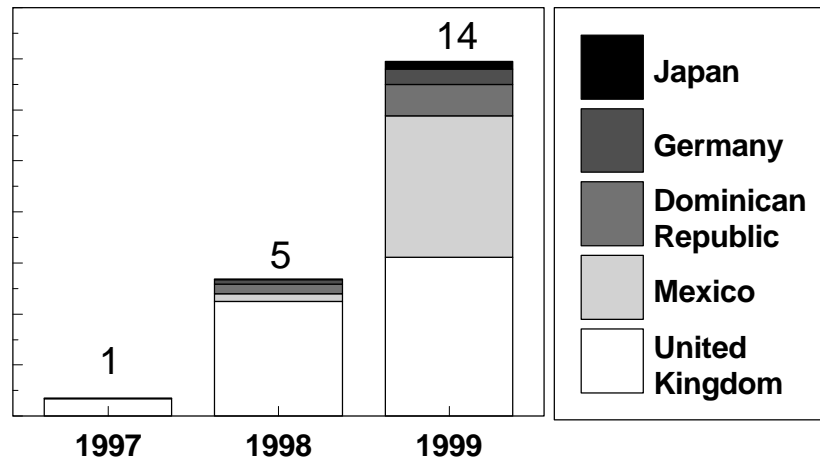
radiata pine, while 16 percent produces eucalyptus. A majority of the wood used in the Chilean wood industry comes from these large-scale, private plantations since it is illegal to harvest from public lands.

The wood processing industry in Chile is efficient, but fragmented. There are approximately 1,500 mills spread across Chile, most of which are very small and use outdated equipment. A majority of the production is carried out by 12 large international firms. The two most important products for the Chilean wood industry are panel products and softwood lumber. The panel industry produces around 1.5 million cubic meters annually with 800,000 of that total marked for export. Reliable estimates for softwood lumber could not be found. Important export markets for Chile include the United States, Japan and Middle East. Substantial growth in the panel products sector is expected to occur since both the Government and private sector are investing large sums of money into the modernization of production facilities. Present indications show that if mills continue to modernize, growth rates of 10 percent can be expected in the production of panel products. Production of softwood lumber is also expected to increase significantly over the next several years as many plantations reach maturity.

The Chilean government's efforts to promote exports began in 1974 with the creation of the Export Promotion Bureau known as ProChile. ProChile is responsible for the administration of the Agricultural Export Promotion Fund which provides funding for activities such as market development and the promotion of new products. ProChile does not accept funding requests from private companies. Instead, requests must be made by either regional or producer export associations. In 1998, ProChile contributed \$10 million for export promotion of agricultural products. This increased to \$12 million in

Chilean Panel Exports to Selected Countries

\$ Million



Source: World Trade Atlas

1999. The program will end in 2003 as Chile seeks to comply with its Uruguay Round commitments.

Chile also has number of subsidy programs in place. The first is a duty drawback system which covers specific commodities such as poles, pilings, posts, softwood lumber, temperate hardwood veneer, plywood, and particle board. Exporters receive a 3 to 10 duty percent drawback on exports based on the total value of exports of the product. No drawback is given if the total value of the exported product is over \$18 million.

Along with the export promotion efforts described above, both Chile and Brazil are taking further steps to increase their exports of wood products. Chile is also planning to invest \$3.5 billion in the wood industry between 1995 and 2001. A majority of the funding will be used to improve and modernize mills. Special emphasis will be put on improving the production of oriented-strand board and other value-added products with the goal of increasing the value of exports. Concerns

over environmental damage to Chile's forests has resulted in a domestic sustainable forest initiative. This would allow Chilean wood products to be certified as originating from a sustainably managed forest system, which has proven to be an important selling point throughout the world. It would also allow the wood industry increased access to both public and private forests.

RESULTS

The information above only partially describes why Brazil and Chile have emerged as serious competitors to the United States. Perhaps the main reason for this is the ability of these producers to supply their products at substantially lower costs than U.S. producers. While their products are often of significantly lower (albeit improving) quality, buyers in many countries base their decision solely on price. In addition, some products, especially the plywood produced in Brazil and Chile, looks much like U.S. plywood, giving the consumer the false impression that the quality is also similar. Specific

pricing data for Brazil and Chile is difficult to find. However, it is known that the Brazilian plywood industry employs a two-tiered system. One level of pricing is set for the United States and Caribbean, while a second level is set for buyers in the EU. The EU level is believed to be 15 to 20 percent less than that of the first tier. Data indicate the 9 mm Brazilian pine plywood is selling in the EU for \$210 per cubic meter (cum) and 15 mm Brazilian pine plywood is selling for \$190 per cum. No reliable data were available for Chilean prices, but they are believed to be similar. It is known that Chilean softwood lumber prices are significantly less than those charged by U.S. producers, a contributing factor to why Chilean exports of this product continue to rise.

The results of this price differential have been disastrous for U.S. panel exporters with interest in the EU. Statistics show that EU imports of softwood plywood from Brazil have increased from \$42 million in 1997 to \$123 million in 1999 making Brazil the largest supplier to Europe. This represents an increase in import market share from 10 to 35 percent. Over the same period, EU imports from the United States went from about \$200 million in 1997 to about \$30 million in 1999. U.S. market share fell from 48 to 8 percent. The United Kingdom and Germany were two of the biggest purchasers of Brazilian plywood.

Brazil and Chile have also begun to penetrate other markets traditionally dominated by the United States. These include Mexico and the Dominican Republic (DR). Between 1997 and 1999, Brazil's market share in the Mexican market has remained at a constant 19 percent. However, recent reports indicate this is likely to rise. Chile's market share in Mexico and the DR has risen substantially in the past few years. Market share has increased from 0 to 29 percent in Mexico from 1997 to 1999 and from 0 to 16

percent in the DR over that same period. Brazil and Chile are also finding a new anchor in the U.S. market. In 1997, total U.S. solid wood imports from Brazil and Chile were \$611 million, but by 1999 these had risen to a record \$901 million.

In conclusion, the significantly lower priced panel and softwood lumber products offered by Brazil and Chile have already eroded U.S. market share in several key markets. These lower prices, coupled with bilateral trade agreements with countries such as Mexico and the Caribbean, may result in further gains for Brazil and Chile. Trade statistics already show an increased presence of these products in important markets such as the Dominican Republic. The U.S. wood industry should maintain a high profile for U.S. wood products, emphasizing their superior qualities. With continued promotion and education, the United States can retain market share in these key markets.