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## Brazil

### Solid Wood Products

### Annual Report

### 2006

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**Report Highlights:**

In 2006, exports reached approximately US\$ 3 billion, restrained by unfavorable exchange rates. Forecasts for 2007 are optimistic. However, the wood industry and federal government must eliminate bureaucratic procedures and resolve land ownership issues in order to reach the expected growth.

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## Economic Situation

Although 2006 was an election year, economic indicators presented stability in 2006. End of year inflation (IPCA) is projected at 3.11%, while the annual basic interest rate (Selic) should close 2006 at 13.25%. The forecast for 2007 is for a 3.5% increase in the GDP, and government analysts suggest that the exchange rate could reach R\$2.25/US\$.

A favorable outlook for 2007 will depend on the government's ability to complete social security and tax reforms. While 2006 was a tough year for President Lula to form alliances to promote these much-needed reforms, political analysts predict that the President's next term (2007-2011) will be smoother due to political alliances made this year.

As Brazil's presidents are limited to two terms, the country may experience significant changes in the economic situation. Interest rate reduction, tax and social security reforms and investments in infrastructure have become a priority for the upcoming year.

## Production

*Brazil remains without a reliable inventory of its forest resources, mostly in the Amazon region, which makes it difficult to estimate the exact forest area. There is no official data on solid wood production. Information provided in the Forest Area Strategic Indicator Table and on the PS&D tables are Post's best estimates, and data is derived from interviews with industry leaders and unofficial data furnished by our contacts in the sector.*

## Forest Situation Report/Outlook

Brazil is currently ranked 2<sup>d</sup> in world forest area coverage. Estimates indicate that total forest area is approximately 483 million hectares (ha) in 2006. From this total, nearly 447 million hectares are native forests and the other 6 million hectares are planted forests. The country also has 62 million hectares of federal conservation area under total protection (46%) and sustainable use (54%) regimes.

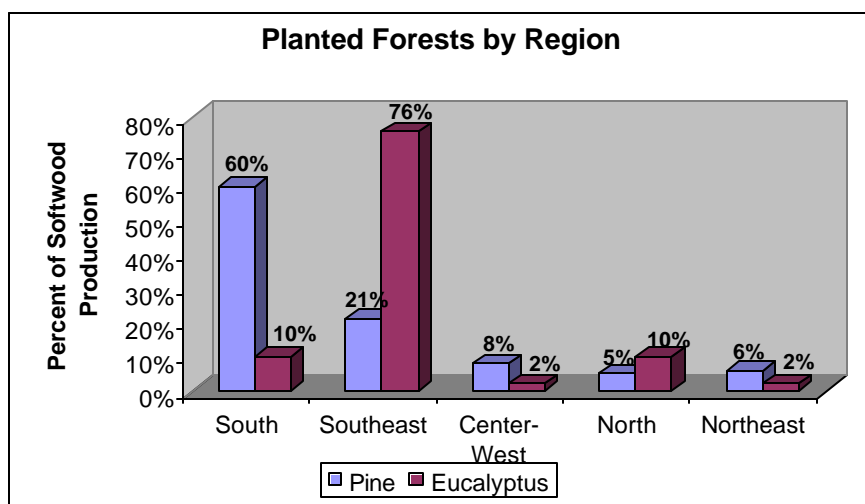
### Native Forests

Native forests in Brazil are under both private and public ownership. Production of wood products in public forest conservation areas under sustainable use regimes is minimal. However, private production areas reached 242 million hectares in 2006, corresponding to 51% of total native forest area. Private forests are the major source of tropical wood production, distributed mainly in the Northern (Amazon) region of the country. The states of Amazonas (79 million ha), Pará (71 million ha), and Mato Grosso (29 million ha) are the top resource base for wood products. The remaining inventory of native forests is destined for conservation units and indigenous lands.

### Planted Forests

Of the 6 million hectares of planted forests, 65% are eucalyptus, and the remaining 35% are pine plantations. The majority of the planted forests were established in the late 1960s, with the creation of Law 5,106/66, which created incentives for forest plantations.

The South and Southeast regions of the country are the main sources of planted forests (pine and eucalyptus). However, the pressure for increased supply of raw materials has expanded plantations to other areas of the country.

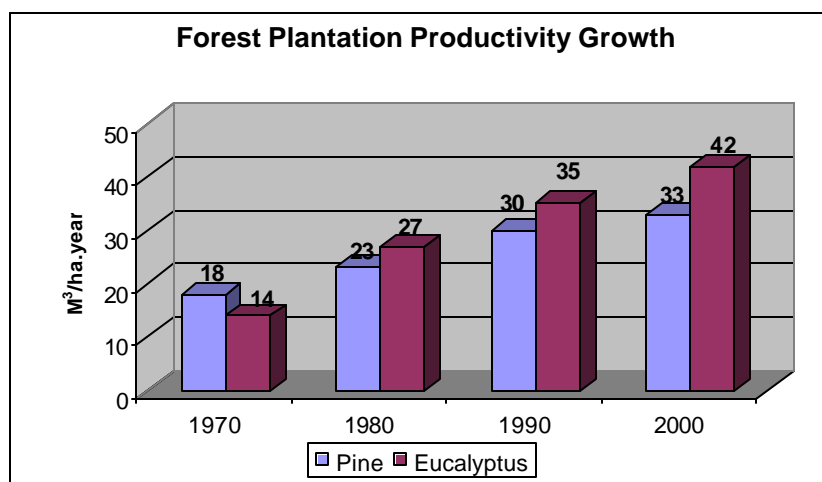


Due to the presence of large cellulose industries in southern Bahia, land prices have skyrocketed, increasing 266.6% from 2004 to R\$4,400/hectare. These industries account for approximately 500 thousand hectares of forest area. Another new frontier for forest plantations is the state of Piauí (northeast). The local government has released a forest development program that is drawing industry attention to that area. A total of 3.7 million hectares were identified as suitable for forest plantations, and land prices are among the lowest in the country.

Forecasts indicate a tendency for increasing softwood (planted forests) production between 2009 and 2022. Current social and environmental pressures, unfavorable exchange rates and increasing land and technology costs are major constraints to softwood supply, especially in relation to pine wood production. Eucalyptus projections are more favorable, due to increasing investments by cellulose industries in new plantations in the northeast region of Brazil.

Sustainable Production Capacity

The sustainable production capacity of Brazilian forests is elevated, estimated at approximately 390 million cubic meters (m<sup>3</sup>) per year. From this total, planted forests account for 179 million m<sup>3</sup> per year, of which 72% are eucalyptus wood and 38% are pine wood.



### Illegal Logging & Certification

Approximately 62% of tropical wood production comes from predatory sources, 43% of which are from illegal logging. According to the Ministry of Environment (MMA), the rate of deforestation has declined 30% since 2004.

Approximately 58% of the non-protected areas of the Amazon have ownership irregularities. In this region, 24% of the land is under private ownership. Industry sources state that land ownership issues are the second major constraint to the development of the wood industry, behind the delays in stewardship plan approvals. In fact, this delay is largely related to the ownership irregularities.

These issues are serious setbacks to the growth of certified forests in Brazil. Currently, Brazil has 5.1 million hectares (in 17 states) of certified forests under the Forest Stewardship Council (FSC) scheme. Nearly 55% of the certified forests are located in the Amazon region (2.8 million ha) and the remaining 45% are planted forests (2.3 million ha).

Another forest certification scheme used in Brazil is the Brazilian Forest Certification (CERFLOR) scheme. Recognized by the Program for the Endorsement of Forest Certification Schemes (PEFC) and regulated by the Brazilian Standards Institute (INMETRO), the CERFLOR scheme has 882,000 hectares of certified planted forests. Nearly 133,000 hectares of planted forests and 73,000 hectares of native forests are in the process of obtaining certification.

Only 2% of the tropical wood produced is derived from certified forests. Due to unsustainable forest production, wood production has an estimated deficit of approximately 200,000 hectares per year.

### Laws and Policies Affecting Logging Levels

Growth of production is limited due to inefficient regulations and time-consuming procedures. Under this context, President Lula sanctioned in March 2, 2006, the Public Forest Management Law (11,284/06), establishing a regulatory milestone for the management of public forests in Brazil. **For more information on the Public Forest Management Law, please refer to GAIN report BR6609.**

Although the Public Forest Management Law was a large step towards the prevention of illegal logging and sustainable forest stewardship, the benefits are yet to be seen by the wood industries and NGOs.

The publication of the new legislation has initiated a transition period that is significantly compromising the rate of logging. The approval and inspection of Forest Stewardship Plans (PMFs), which was previously done by the Brazilian Environment Institute (IBAMA), was transferred to State Environment Offices (OEMA), which lack appropriate infrastructure and personnel for the approval of new PMFs. In order for PMFs to be approved, the owner of the stewardship plan is required to sign a contract with the Ministry of Environment (MMA). The Ministry still has not defined the contract regulating this transition. According to industry sources, in certain regions of the Amazon region, nearly 50% of mills have closed, and over 9,000 employees have lost their jobs.

## Solid Wood Production Situation/Outlook

### Tropical Hardwood Logs

The production of Tropical Hardwood is among the main economic activities of the Northern region of Brazil. The states of Pará, Amazonas and Mato Grosso together add up to nearly 95% of the total hardwood logs production. Post estimates production at 24 million m<sup>3</sup> for 2006, showing a 4% decrease from the previous year.

**Tropical Hardwood Logs, PS&D Table**

	2005		2006		2007		UOM
	USDA Official	Post Estimate New	USDA Official	Post Estimate New	USDA Official	Post Estimate New	
Market Year Begin		01/2005		01/2006		01/2007	MM/YYYY
Production	33380	25000	0	24000	0	24000	(1000 CUBIC METERS)
Imports	450	0	0	0	0	0	(1000 CUBIC METERS)
TOTAL SUPPLY	33830	25000	0	24000	0	24000	(1000 CUBIC METERS)
Exports	40	3	0	3	0	4	(1000 CUBIC METERS)
Domestic Consumption	33790	24997	0	23997	0	23996	(1000 CUBIC METERS)
TOTAL DISTRIBUTION	33830	25000	0	24000	0	24000	(1000 CUBIC METERS)

The decrease in production may be linked to the transition in the jurisdiction of forest stewardship plan approvals, triggered by the publication of Law 11,284/06. While the impact of this transition has not been officially measured, sources state that an increase in hardwood production will depend on the macroeconomic changes in 2007, as well as investments in infrastructure and personnel by government agencies responsible for stewardship plan approvals and the resolution of land ownership issues.

Investments in machinery and technology significantly reduced the consumption of raw materials. Estimates show that a 3% increase in productivity reduced the use of hardwood logs by approximately 1.6 million m<sup>3</sup>, or 108 thousand hectares of forest. Today, yields are around 45%.

Post forecasts no changes in hardwood log production and consumption in 2007. Instructions and contracts regulating Law 11.284/06 still have not been released, and land ownership issues will continue to affect the issuance and approval of forest stewardship plans in the Amazon region.

A migration in hardwood production activities has been observed over the past 5 years. New frontiers include the southeast region of Amazonas state, western Pará and northeastern Mato Grosso, all in the Amazon region. The conclusion of BR-163 (the road connecting Santarém and Cuiabá) will likely improve profitability and production in that area.

## Sawn Wood

The Brazilian lumber industry is composed of nearly 10,000 companies, comprising mostly small-scale mills. 75% have processing capacity below 10,000 m<sup>3</sup>/year and 25% between 10,000 and 30,000 m<sup>3</sup>/year. Approximately 60% of the mills are concentrated in the Center-West and Northern regions of the country. While this area processes mainly tropical (native) wood, the Southern and Southeast regions concentrate in processing softwood.

## Tropical Hardwood Lumber

Production of hardwood lumber is estimated at 14.5 million m<sup>3</sup> for 2006, showing nearly no growth (2%) from the previous year. Approximately 10% of the tropical hardwood lumber was exported, reaching 1.5 million m<sup>3</sup> in 2006. Post forecasts an increase in production in 2007 due to an expected increase in productivity rates.

Major foreign buyers for Brazilian lumber are China (15%), Netherlands (7%), Spain (6%) and Portugal (5%). The United States remains the 3<sup>rd</sup> largest consumer of Brazilian tropical lumber, importing 152,000 m<sup>3</sup> in 2006. In 2007, exports are forecast to increase 5%, since indicators show a tendency for a devaluation of the real.

Although production has continuously increased over the past 5 years, environmental pressure has become a significant contributor to the decrease in the relative participation of tropical (native) wood in total lumber production. Other major restraints are the large distances to major consumers in the state of São Paulo, the increasing acceptance of softwood lumber, and the constraints in the acceptance of stewardship plans. 2007 calls for an increase in consumption, resulting from expected growth in productivity and production.

**Tropical Hardwood Lumber, PS&D Table**

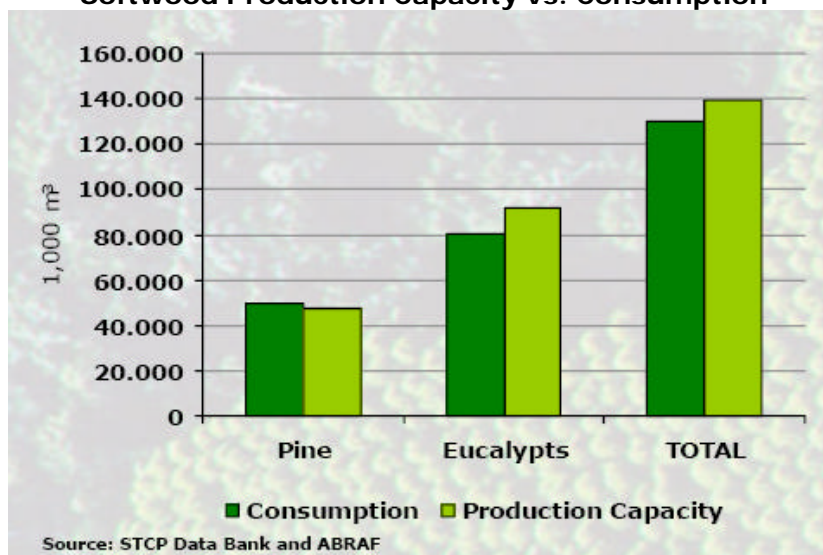
	2005	Revised	2006	Estimate	2007	Forecast	UOM
	USDA Official [Old]	Post Estimate[New]	USDA Official [Old]	Post Estimate[New]	USDA Official [Old]	Post Estimate[New]	
Market Year Begin		01/2005		01/2006		01/2007	MM/YYYY
Production	17540	14250	0	14500	0	15225	1000 CUBIC METERS
Imports	60	60	0	60	0	60	1000 CUBIC METERS
TOTAL SUPPLY	17600	14310	0	14560	0	15285	1000 CUBIC METERS
Exports	1740	1800	0	1500	0	1575	1000 CUBIC METERS
Domestic Consumption	15860	12510	0	13060	0	13710	1000 CUBIC METERS
TOTAL DISTRIBUTION	17600	14310	0	14560	0	15285	1000 CUBIC METERS

## Softwood Lumber

The production of softwood lumber continues to rise as productivity and new plantations increase. Post estimates 2006 production at 9.2 million m<sup>3</sup>, rising 5% from 2005. Consumption continued to grow, pushed by the rise of the construction sector demand. For 2006, softwood lumber exports are estimated at 1.4 million m<sup>3</sup>, reaching US\$ 260 million. Top markets for Brazilian softwood lumber are the United States (75%), Spain (3%), Morocco (4%) Mexico (3%) and Vietnam (2%).

Government incentives for the production of softwood are on the rise (see policy section below), as the industry struggles to prevent what specialist call “forest blackout”, the deficit in supply of the raw materials. Currently, estimates indicate that the production deficit is around 8%. Forecasts for 2007 production suggest that the expected increase in pine and eucalyptus plantations, as well as an increase in industry productivity will boost production and consumption of softwood lumber. Exports are also expected to increase due to more favorable exchange rates in 2007.

**Softwood Production Capacity vs. Consumption**



**Softwood Lumber, PS&D Table**

	2005	Revised	2006	Estimate	2007	Forecast	UOM
	USDA Official [Old]	Post Estimate[New]	USDA Official [Old]	Post Estimate[New]	USDA Official [Old]	Post Estimate[New]	
Market Year Begin		01/2005		01/2006		01/2007	MM/YYYY
Production	8770	8950	0	9174	0	9350	1000 CUBIC METERS
Imports	275	75	0	75	0	75	1000 CUBIC METERS
TOTAL SUPPLY	9045	9025	0	9249	0	9425	1000 CUBIC METERS
Exports	1695	1322	0	1388	0	1450	1000 CUBIC METERS
Domestic Consumption	7350	7703	0	7861	0	7975	1000 CUBIC METERS
TOTAL DISTRIBUTION	9045	9025	0	9249	0	9425	1000 CUBIC METERS



Brazilian Softwood lumber has a competitive advantage due to a faster maturing period than Northern Hemisphere producers and a favorable climate and soil conditions. Brazilian pine has a maturation period of 14 years, while eucalyptus needs only 7 years. The cost of production of softwood lumber in Brazil is R\$18 (approximately US\$ 8) for eucalyptus and R\$35 (approximately US\$ 16) for pine. Currently, the average annual productivity rates for softwood is between 30 and 40 m<sup>3</sup>/year for eucalyptus and 25 to 30 m<sup>3</sup>/year for pine trees, depending on the region.

### Softwood Plywood

Brazilian softwood plywood represents 70% of the total plywood production, supplying 2.4 million m<sup>3</sup> in 2006. Estimates for 2006 domestic consumption are 622 thousand m<sup>3</sup>. The production was primarily oriented for exports, as strong competition from Medium Density Fiberboard (MDF) and Oriented Strand Board (OSB) panels and higher prices abroad made the domestic market unattractive.

In 2006, Brazil exported 1.8 million m<sup>3</sup> of softwood plywood. The 8% U.S. import tax for Brazilian softwood plywood and the valuation of the real were the major causes for the decrease of 8% in production and 22% in exports. Major southern plywood producers are shifting sales to the domestic market and diversifying their foreign costumers. Major markets for Brazilian softwood plywood include the European Union (UK, Germany and Belgium) with 31%, and the United States, with 50% of total exports.

According to industry sources, the plywood industry is composed of approximately 500 plants, of which 62% are medium and large-scale companies, and 38% are small-scale companies. The installed production capacity of the plywood industry in Brazil is estimated at 3.8 million cubic meters, of which 45 companies account for 60 percent of this capacity. The breakdown of plywood production in Brazil is distributed as follows: furniture (45%), construction (34%), packaging (17%), and all others (4%).

**Softwood Plywood, PS&D Table**

	2005	Revised	2006	Estimate	2007	Forecast	UOM
	USDA Official [Old]	Post Estimate[New]	USDA Official [Old]	Post Estimate[New]	USDA Official [Old]	Post Estimate[New]	
Market Year Begin		01/2005		01/2006		01/2007	MM/YYYY
Production	2010	2600	0	2400	0	2400	1000 CUBIC METERS
Imports	480	0	0	0	0	0	1000 CUBIC METERS
TOTAL SUPPLY	2490	2600	0	2400	0	2400	1000 CUBIC METERS
Exports	1960	2284	0	1778	0	1900	1000 CUBIC METERS
Domestic Consumption	530	316	0	622	0	500	1000 CUBIC METERS
TOTAL DISTRIBUTION	2490	2600	0	2400	0	2400	1000 CUBIC METERS

Post forecasts no increase in production in 2007. Since softwood plywood is mainly sold abroad, the projections for a higher exchange rate will likely shift the domestic consumption to exports.

## Trade

Brazilian solid wood products (Chapter 44 of HTS) exports totaled US\$ 3 billion in 2005. For 2006, estimates indicate that Brazil reduced exports around 5%, reaching US\$ 2.9 billion. According to the Ministry of Agriculture, Livestock and Food Supply (MAPA), forest products (including paper and cellulose) ranked third in total Brazilian agricultural exports (US\$ 7.4 billion), only behind soy and meat complex.

Industry sources forecast exports to double by 2020, reaching US\$ 12 billion, as a result of the investments in the paper and cellulose (US\$14.5 billion) and solid wood (US\$5 billion) sectors.

Although solid wood production is destined primarily for the domestic market and has competitive advantages compared to foreign competitors, Brazilian wood products have shown continuous stagnation in exports over the past 3 years. The valuation of the real against the dollar, the current “forest blackout” and the problems involving the approval of forest stewardship plans remain a problem to be solved by both government and industry.

## Policy

### National Forest Program (PNF)

In 2004, the National Forest Program (PNF) launched by the Ministry of Environment had two major strategic actions to be completed by 2007:

- a) The expansion of the planted forest resource base and the regeneration of degraded areas, through:
  - Plantation of 800,000 hectares in small and medium size properties;
  - Plantation of 1.2 million hectares through industrial-size sustainable programs;
  - Recuperation of 200,000 hectares of degraded forests.
  
- b) Expansion of forest stewardship areas associated with the protection of high-value areas for conservation:
  - Add 15 million hectares of natural forests for sustainable production to supply 30% of the industrial demand;
  - Assure that 1/3 of sustainable forest production is originated from social forests, produced by local communities and family farmers;
  - Guarantee the protection of 2 million hectares with high ecological value in areas destined for forest stewardship.

### BNDES

The main source of financial resources for the forest sector is the Bank for Social and Economic Development (BNDES). In 2005, resources totaled R\$47 billion, 18% higher than the previous year. Nearly 25% of this amount was destined to micro, small and medium-sized industries. Resources for export purposes reached R\$5.9 billion in 2005.

### Credit Lines

Program for Commercial Planting and Recuperation of Forests (PROPFLORA): A credit program under the BNDES directed to pine and eucalyptus plantations, at subsidized annual interest rates of 8.75% with a loan limit per farmer of R\$150,000 (about US\$ 68,000), with a grace period of 8 years and payment in 12 years. In 2005/06, investments using the PROPFLORA reached R\$60 million, distributed to approximately 800 farmers.

PRONAF-Florestal program: Grants credit lines at a 4% annual interest rate. The grace period is also 8 years and payment in 12 years. In the 2005/06 crop year, loans totaled R\$15 million, reaching over 2,800 contracts.

The FNO-Floresta, FCO-Pronatureza and FNE-Verde are credit lines with annual rates of 6%, 8.75% and 10.75% respectively, for financing sustainable forest management projects, reforestation for energy and lumber purposes, recuperation of degraded areas, and environmental projects. Grace and payment periods vary according to each credit line, having a minimum of 6 to 20 years respectively for FNE-Verde, 9 to 16 years for FNO-Floresta, and 10 to 20 years for FCO-Pronatureza. Low credit limits and lack of information have caused little demand, and government resources remain unused. While both FNO-Floresta and FCO-Pronatureza granted a little over R\$2 million each, loans under the FNE-Verde reached R\$64 million in 2005 (no information available for 2006).

## Marketing

The Brazilian Export Promotion Agency (APEX-Brazil), created by the federal government in 1997, is responsible for coordinating and financing up to 50% of the cost of promoting Brazilian products overseas and attracting more small and medium sized companies into the export business. APEX has two programs related to the forest sector, which are similar to the FAS Market Access Program: The Brazilian Association of Furniture Industry (APEX/ABIMOVEL), and The Brazilian Association of Mechanically Processed Timber (APEX/ABIMCI).

The APEX/ABIMOVEL (Brazilian Furniture) is a cost-sharing market promotion program valued at US\$ 8.5 million (50% paid by APEX and 50% by industries from the furniture sector associated to ABIMOVEL) to promote Brazilian furniture in targeted markets, such as the United States, Europe and Mexico. The goal is to increase furniture exports by 19% per year and increase the current total export value of the sector to over US\$ 1 billion. Promotional activities include: market research, trade shows, trade missions, reverse trade missions, advertising in specialized media, and publication of catalogs. The Brazilian furniture sector is composed of more than 70,000 firms, mostly small companies, with a total gross income of US\$ 4.1 billion.

The APEX/ABIMCI is also a cost-sharing market promotion program, but has not been fully implemented. In 2006, APEX-Brazil financed 30% of Brazilian trade missions to research market opportunities for Brazilian plywood. ABIMCI is now proposing a major market promotion program valued at US\$ 8 million to double Brazilian exports of plywood within four years. According to ABIMCI, market promotion efforts are targeted at high-value products, and will include activities in the most important world trade shows, visits to importers, mostly in Europe, reverse marketing missions, specialized media teams, and catalogs.

**Tropical Hardwood Logs, Export Trade Matrix**

Export Trade Matrix Country Brazil Commodity Tropical Hardwood Logs			
Time Period	Jan-Dec	Units:	CUM
Exports for:	2005		2006
U.S.	2	U.S.	0
Others		Others	
India	1100	Sweden	1500
Spain	1000	Germany	1000
Germany	800	Spain	500
Total for Others	2900		3000
Others not Listed	100		0
Grand Total	3002		3000

**Tropical Hardwood Lumber, Export Trade Matrix**

Export Trade Matrix Country Brazil Commodity Tropical Hardwood Lumber			
Time Period	Jan-Dec	Units:	1000CUM
Exports for:	2005		2006
U.S.	190	U.S.	152
Others		Others	
China	360	China	300
France	216	France	180
Spain	135	Spain	113
Portugal	90	Portugal	75
Total for Others	801		668
Others not Listed	809		680
Grand Total	1800		1500

**Softwood Lumber, Export Trade Matrix**

Export Trade Matrix Country Brazil Commodity Softwood Lumber			
Time Period	Jan-Dec	Units:	1000CUM
Exports for:	2005		2006
U.S.	772	U.S.	656
Others		Others	
Spain	79	Spain	83
Marocco	53	Marocco	56
Mexico	40	Mexico	42
Vietnam	26	Vietnam	28
Total for Others	198		209
Others not Listed	352		523
Grand Total	1322		1388

**Softwood Plywood, Export Trade Matrix**

Export Trade Matrix Country Brazil Commodity Softwood Plywood			
Time Period	Jan-Dec	Units:	CUM
Exports for:	2005		2006
U.S.	1404	U.S.	887
Others		Others	
United Kingdom	228	United Kingdom	198
Belgium	206	Belgium	162
Germany	182	Germany	152
Italy	80	Italy	75
Ireland	24	Ireland	54
Total for Others	720		641
Others not Listed	160		250
Grand Total	2284		1778