

## The wood product and pulp and paper industries: between tradition and innovation

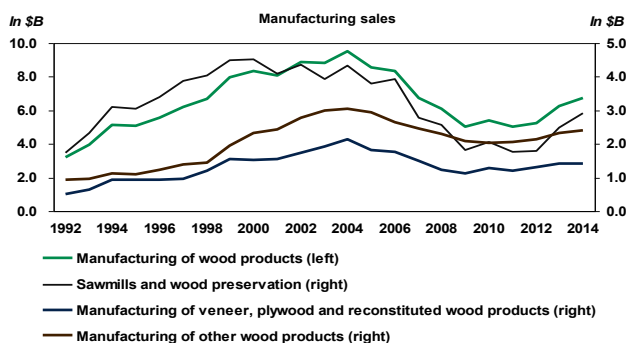
The wood and pulp and paper industries have a long history in Quebec. Sometimes, the attitude toward them is defeatist and we forget that they have a future, too. However, changes must be made if they want to remain entrenched in Quebec's economy, as industry stakeholders are well aware. This new thrust, already in the works at various levels, will come through investment in production facilities, prospecting, marketing efforts, and research and development. It will need more than good intentions to succeed, and success is not assured. Now is the time for audacity and teamwork in a sector whose actions are more in the headlines than ever before.

### POST-RECESSION RECOVERY

For the wood product industry, the last 10 years have been difficult; pulp and paper has been facing headwinds for even longer. These two manufacturing sectors have weathered demand's vagaries in their respective markets.

In the wood product sector, the collapse of the U.S. housing market, thorny trade negotiations, the strong Canadian dollar and the financial crisis, to name just a few factors, took shipments and exports down. Shipments have recently been on a post-recession upswing (graph 1), although they have not reached their 2004 peak. The industry's three main components are making a comeback, with sawmills seeing the fastest sales growth, although this should not eclipse the progress made in millwork products (such as doors and windows), and veneers and plywood.

**Graph 1 – Wood products in Quebec: an upturn is perceptible in all the major product segments**



Sources: Statistics Canada and Desjardins, Economic Studies

For wood products, the uptrend is also being seen in real GDP, which finally hit its 2007 pre-recession level. For international exports, the peak was reached in 2004 (\$4.3B), sliding to a low point in 2011 (\$1.3B). Since that year, exports have been on the rise, and 2015 follows that trend. More than 90% of shipments outside of Canada go to the United States. China is also becoming a destination for these products, but its share is slight (just over 2% of all wood products). Lastly, paid employment has not made any stellar gains in the last few years, despite growth by shipments and exports. However, the blood-letting seems to be over at last. On the other hand, replacing the current workers, who will be retiring soon, is a concern.

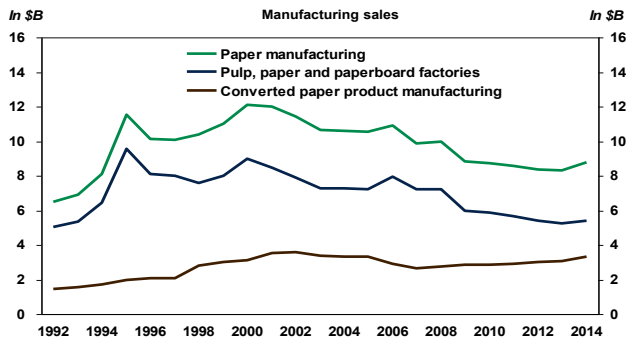
In the pulp and paper sector, a drop in demand, particularly for newsprint, printing and writing paper, has caused shipments to drop since the early 2000s (graph 2 on page 2). Despite a 2014 upswing in manufacturing sales, levels are below where they were before the recession. For converted paper products (paperboard containers, paper bags, stationery and other paper products), shipments have increased more sharply than shipments of paper, pulp, and paperboard, a rise that has also been going on longer. More specifically, shipments of paperboard containers have been on the upswing since 2009, while other converted paper products have been rising since 2008.

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**Graph 2 – Quebec – Paper products: there's a sharper increase in converted paper products**



Sources: Statistics Canada and Desjardins, Economic Studies

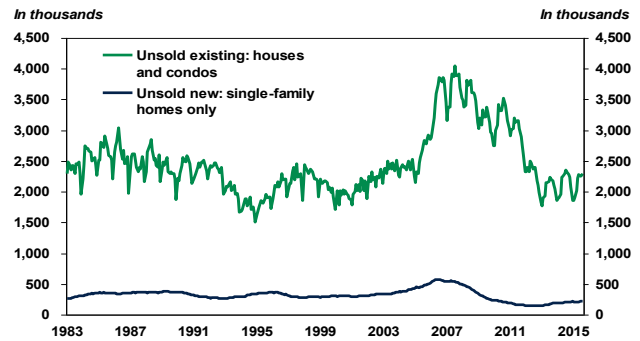
International pulp and paper exports started to grow again in 2013, and the first half of 2015 is positive. In both good years and bad, the United States accounts for 75% to 77% of Quebec shipments abroad. Despite the increase in sales and exports, paid employment continues to drop. The effort to make productivity gains is limiting employment growth.

This quick review of a few indicators shows that, for Quebec's wood product and pulp and paper industries, the value of shipments and exports has gone up recently. Production is not freefalling, but, due to major changes in demand and situational reasons, the traditional anchors (lumber and newsprint) are no longer giving these two sectors of manufacturing as much support. What can we expect? How will markets evolve by the end of the decade?

**IF THE TREND HOLDS...**

Wood products are widely associated with lumber; in fact, there is a much bigger array of goods. A few parameters provide a glimpse of what the next few years hold. In Quebec, as well as in Canada as a whole, new construction will be slower by the end of the decade (33,000 and 182,000 units a year respectively, on average, from 2015 to 2019) than it was from 2007 to 2014 (45,000 and 200,000 units a year respectively on average). However, the outlook for housing starts in the United States is good, where the volume is also much bigger. Moreover, the U.S. housing market is sounder now, as shown by graph 3, which illustrates the number of unsold units on the market. As we can see, the surplus has been absorbed and demand for new construction will be more pressing in the next few years than it has been since the end of the last decade.

**Graph 3 – Unsold units on the U.S. market: no surplus as was the case from 2006 to 2011**



Sources: Bloomberg and Desjardins, Economic Studies

The renovation market must also be considered. Resales have been high on both sides of the border in the last few years, auguring sustained demand for materials until at least 2020.<sup>1</sup>

Over a much longer horizon, the demographic projections may well be a delight to those who produce construction materials (lumber and much more). The long-term outlooks presented by various bodies suggest construction will be strong for decades to come (table 1 on page 3). In around 2060, Quebec will have 2 million more people, who will need housing. Canada as a whole will have 15.8 million additional inhabitants, while the United States will have nearly 100 million more people. However, population growth will be slower than seen in the last few decades. Keep in mind that Quebec currently only has just under 5% of the U.S. lumber market.

In the meantime, however, new living arrangements may emerge, innovative materials will have been developed, and the population's needs will have changed. The trend for large homes is already waning, giving way to homes that are more modest in size. Such changes mean the lumber product industry will have to stay alert and tailor its offer to this demand. Keep in mind that housing is one wood industry market; other sectors could get more out of all of the possibilities offered by wood fibre. The industry is already working on it.

<sup>1</sup> See Desjardins, Economic Studies, *Renovations: transitioning from a nomadic way of life to a more settled one*, Perspective, June 2014, 4 pages <https://www.desjardins.com/ressources/pdf/per0614e.pdf?resVer=1403788463000>

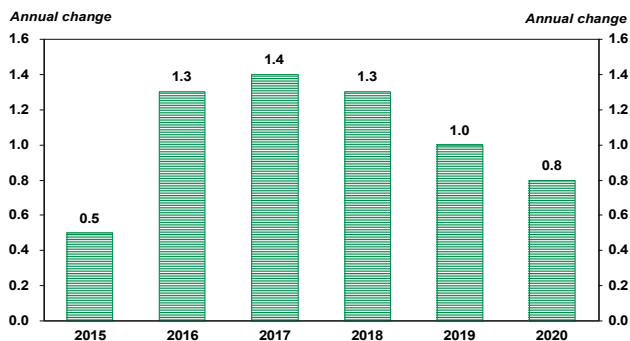
## Table 1 – Long-term demographic projections (millions)

Quebec (according to the Institut de la statistique du Québec)	In 2011: 8.0	In 2061: 10.1	Increase: 2.1
Canada (according to Statistics Canada)	In 2013: 35.2	In 2063: 51.0	Increase: 15.8
United States (according to the U.S. Census Bureau)	In 2014: 319.0	In 2060: 417.0	Increase: 98.0

Sources: Institut de la statistique du Québec (2014), Statistics Canada (2014), U.S. Census Bureau (2015)

For pulp and paper, the outlooks differ with the sector. Everyone acknowledges that demand for newsprint and printing paper will continue to wane, as it has been for decades now. Paper is not necessarily dead, because uses other than newsprint and printing are on the rise. Growth will be slight until 2020 in the U.S. market, which is currently the biggest client in North America (graph 4).

**Graph 4 – Projection of the U.S. paper end-use market output from 2015 to 2020**



Source: Statista 2015, Statista.com

### BETTING ON THE FUTURE

In recent years, every inch of the wood and pulp and paper industries has been examined. Expert groups of all stripes, engineers, university researchers and industry stakeholders all come to the same conclusions: wood has not had its last hurrah. The current uses of wood are limiting. The industries’ prospects in the coming years go well beyond lumber and newsprint. Without abandoning tradition and trying to develop new markets for our existing products, we have to work to develop all of the opportunities offered by fibre, which is where innovation comes in.

Diversification is more than science fiction in the wood product industry. Increasingly processed and ready-to-use building materials are arriving on construction sites. Saving on assembly costs and producing solutions for problems that arise in construction are among the actions being developed. However, more will have to be done to secure the industry’s future and shield it from construction cycles.

Secondary and tertiary processing are preferred avenues. Here, the Quebec government released its strategy for the 2012–2017 period. It focuses on market development, adapting factories, minimizing operating costs, workforce training and renewal, and investment in innovative products. In collaboration with the industry, it highlights the myriad applications of wood, from airbags and textiles to brake shoes for the Montreal metro, the food industry (anti-caking agent), and liquid crystal displays, to name just a few. Secondary and tertiary processing increases the wood industry’s local spinoffs, because the new products it creates are developed and manufactured in Quebec rather than abroad. The jobs and revenue generated by innovation like this increase and contribute to the vitality of municipalities.

Similarly, there is a world of possibilities beyond the newsprint production that constituted the heyday of the pulp and paper industry. This industry also produces paperboard, tissue paper and pulp used in other applications (such as fabric). Such developments point to expansion and growth of shipments to the United States and emerging markets (particularly Asia). The government’s 2012–2017 strategy allows us to see the potential, particularly in bioproducts (fuels, renewable plastic and chemical products), smart paper and paperboard (detection of bacteria, with some products even eradicating bacteria, toxin detection, etc.), highly technical paper (waterproof, washable wallpaper), with other opportunities provided by the new technologies, which help enhance the chemical properties of wood fibre.

### THE BATTLE IS NOT WON

At a time when all of these new avenues are opening up, the Quebec wood and pulp and paper industries must be ready to seize the opportunities. Following a wave that is carrying a market along (such as the recovery of the U.S. housing market) is one thing; making sure that businesses survive is another. There is no shortage of challenges. Among the obstacles to be overcome, negotiations over renewing the lumber agreement (which elapsed in October 2015) immediately come to mind because they are getting so much media attention. However, it is essential to work on making Quebec's industry more competitive. Here, as elsewhere in manufacturing, the edge provided by a weak loonie is not a viable long-range strategy.

In primary wood processing, which currently has the biggest volume of business, there is little or no product differentiation. The battle is waged over prices. Here, Quebec is facing battle-hardened competitors across the continent, with quality products in abundance at lower costs.

The difficulties facing the Quebec industry include some physical constraints: smaller wood. For example, independent firms estimate that, in British Columbia, it takes three trees to produce a cubic metre of wood, whereas it takes nine in Quebec to get the same amount. Wood has become less available in recent years. In place since April 2013, the auction model, which sells 25% of the resource, is introducing irritants, according to industry stakeholders, who would like to see some adjustments to make the model more workable. Moreover, the industry thinks that the costs of timber rights, royalties, and combating fires and insects, to name just a few, add to the burden on business and make Quebec plants less competitive. In short, the industry thinks that there are some potential savings that would make both the wood and paper segments more profitable.

Moreover, in the wake of growing concern over the environment, an increasing number of observers are keeping a close eye on the industry. On one hand, wood's ecological qualities are touted, and there is a desire to see it used more in the construction of public and private buildings. On the other, there is concern about forestry practices and forest management. The promotion of wood products has intensified in the last few years. Moreover, according to Quebec's Ministère des Forêts, de la Faune et des Parcs, "nearly 90% of the Crown's forests are now certified under one of the sustainable forest management standards,"<sup>2</sup> i.e. the CSA (Canadian Standards Association), SFI (Sustainable Forestry Initiative) and FSC (Forest Stewardship Council) systems. Such certifications do not do all of the work on their own, but this percentage attests to the actions taken in the last few years.

The wood and pulp and paper industries have many challenges to meet, including the challenge of delivering and selling products that will get more value out of wood and fibre. Decreasing their vulnerability to economic cycles is also on the agenda. To get there, changes are needed in a variety of areas. We also have to invest and work together. It's essential for actions taken at every level to be focused in the same direction. Audacity is also needed. However, those in the industry have never been afraid of hard work. They must move from tradition to innovation.

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<sup>2</sup> <http://www.mffp.gouv.qc.ca/forets/amenagement/amenagement-certification.jsp>