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Summary

The gloomy economic conditions prevailing in the euro area will be reflected in the 2012 and 2013 figures for the Finnish forest industry’s production and exports. In the wood products industry, production and exports of sawnwood and plywood will be down in 2012 due to the impact of reduced construction activity on product demand in Europe and on the domestic market. The economic outlook in Africa and Asia is rather better than in Europe, however, and Finnish exports to these regions have been growing. Export unit prices of sawnwood and plywood will be down in 2012, due to the weaker demand in Europe.

The fall in demand on Europe’s paper market means that production and exports of Finnish paper will be down for 2012 as a whole, although export unit prices for paper will be up. This rise in paper prices has been attributable to Europe’s production capacity cuts of recent years and to the 2012 decrease in production volumes. Production, exports and export unit prices of paperboard will all be down slightly, while pulp production and exports will be up a little as a result of demand in China.

In 2013, the economy and construction activity are expected to improve in key export markets for the Finnish forest industry, and a modest recovery in demand is expected towards the end of 2013, on the domestic market as well. Production and exports of Finnish sawnwood and plywood are forecast to grow by about 2%, and export unit prices are expected to be up slightly in annual terms. The fall in demand on the paper market is expected to see a turnaround during 2013, but for the full year it will be unchanged from the 2012 level, and no change is foreseen in paper, paperboard and pulp production and export volumes. It is anticipated that export unit prices will be at the 2012 level.

The weak state of Finnish forest industry exports is also affecting the roundwood market, where commercial fellings will be down in 2012, to 51 mill. m³. The decrease in commercial fellings will continue in 2013, when roundwood imports will rise to a little over 11 mill. m³ as a result of Russia’s WTO membership. Sawlog stumpage prices for the full year 2012 will be down by 5–6% from the 2011 figures, as the faltering sawnwood market in turn affects the roundwood market. Stumpage prices of pine and birch pulpwood will be down by 3–4%. Despite the fall in stumpage prices, profitability in both the wood products industry and the pulp and paper industry will be down slightly for 2012 as a whole. In 2013, the fall in profitability will be brought to a halt as export prices rise slightly and stumpage prices remain close to their 2012 levels. In non-industrial private forestry, the fall in stumpage prices will mean reduced profitability, with the operating profit from timber production falling to less than EUR 80/ha for both 2012 and 2013.

Euro Area Problems Act as Brake on World Economy

The outlook for the world economy in the second half of 2012 is not very encouraging. Growth in the world economy weighted according to the distribution of Finnish forest industry exports will slow to about 1% for the full year 2012, and
will be only about 1.5% in 2013. On the Finnish forest industry’s key markets in the euro area no quick solution to the sovereign debt crisis is in view, and great uncertainty abounds as Spain slides into ever deeper difficulty, with the prospect that it may be joined by Italy too. Consumer and business confidence in the economy has weakened since the spring, and orders in hand are at a low level. The euro area is experiencing a downturn in the second half of 2012, and the contraction in the euro area economy for the full year is expected to be 0.5%. In 2013, led by Germany the euro area economy is forecast to grow by 0.5%, with this growth concentrated in the latter half of the year. The growth figures for the United Kingdom will largely follow the euro area trend. In Sweden, GDP growth will show a decline onto a growth track of just below 2% for both 2012 and 2013.

In the United States, the economy will see growth of about 2% for the full year 2012, and this will be repeated in 2013. As the US housing market recovers slowly and employment improves, and with the Federal Reserve’s relaxation of monetary policies, private consumption and investment have been picking up from the deep downturn of the recession. In 2013 will nevertheless be overshadowed by uncertainty due to the cessation of the fiscal policy stimulus measures at the end of 2012 and the question mark over further stimulus programmes. If no new fiscal policy solutions are formulated, there is a risk that the US economy will again enter a downturn. In Russia, the high world market price of oil will ensure that growth remains at the rate of recent years. In China, GDP growth has fallen as a result of faltering demand on export markets, but the country’s economic policy measures are sustaining growth at an annual rate of about 8%. The economies of Japan, the Middle East and North Africa – key export destinations for Finnish sawnwood – are all continuing to grow.

Demand for Wood Products Slackens Again

The decrease in residential construction in many European countries in the first half of 2012 affected the demand for sawnwood and plywood. Export volumes to Europe in the first half of 2012 were lower than in the same period a year earlier. Demand in the second half-year is expected to decrease further as construction in Europe remains slack. Although exports are slightly up to markets outside Europe, specifically Africa and Asia, production and exports of wood products are expected to show an overall decrease of 4–6% for the full year 2012, varying according to products in question. The prices of both sawnwood and plywood are expected to fall a little in comparison with the 2011 figures.

The demand for wood products in 2013 is expected to improve slightly towards the end of the year. New housing construction will begin to pick up gradually in Europe, and wood product exports to Asia and Africa will increase, while in Finland the growth in the building renovation sector will continue. Although no real recovery in construction activity in Europe is anticipated before 2014, production and exports of Finnish sawnwood and plywood are expected to be up slightly in 2013 compared with 2012. Growth in demand is expected to push up export unit prices of sawnwood and plywood by about 2%. Any more significant rise in prices would require a distinctly faster recovery in construction in Europe and the United States than that which has been forecast.

Paper Demand Declines Further, Prices Up Slightly

On the main markets in Europe, 2011 saw a decrease in the demand for paper and paperboard products and in the consumption and production of these products, due to the prevailing economic problems. This trend continued in the first half of 2012, which saw a substantial decline in Finnish paper and paperboard export volumes. As demand is forecast to remain slack in the second half of 2012, production and exports of Finnish paper are forecast to be down by 8–9% for the full year, and paperboard production and exports will also be down slightly. Pulp production and exports are forecast to be up by 1–2%, due to a growth in exports to China. Despite
the lower paper demand in Europe, export unit prices of paper and paperboard products were up in 2011. This was partially attributable to Europe’s production capacity closures of recent years. The unit prices of paper exports also rose in the first six months of 2012, due to the production limits set. The average price of paper exports for 2012 as a whole is forecast to be up by 4%, whereas the average paperboard export price will be down a little in comparison with 2011. Pulp prices are forecast to be down by 7% year-on-year.

No improvement is expected in paper and paperboard demand in 2013, but a turnaround is expected to occur in 2014. Production, exports and average export prices of Finnish paper, paperboard and pulp in 2013 are expected to be at about the level of 2012.

Forest Industry Profitability Down Slightly in 2012

Profitability in both the wood products industry and the pulp and paper industry was down slightly in 2011 compared with the previous year. In 2012, economic conditions in the key export markets have remained difficult, and the outlook for the second half-year is characterised by uncertainty and weak demand, which means that production volumes in both the wood products industry and the pulp and paper industry will be down year-on-year. Declining demand is accompanied by falling stumpage prices, however, and this is keeping in check the rise in production and transportation costs. A moderate year-on-year decrease in profitability is thus expected for 2012 in both the wood products industry and the pulp and paper industry. Despite the challenging economy and the planned production limits, companies have been investing or have announced investments in production development in the wood products and pulp and paper industries, in Finland too.

In 2013, the export outlook for Finnish forest industry products is expected to improve gradually towards the end of the year. The trend in export prices in the wood products industry is expected to be marginally positive. Export prices of pulp and paper industry products are expected to be at about the same level as in 2012. There will be no significant upward pressures on production costs, and stumpage prices in 2013 are expected to remain at about their 2012 level. Profitability in the Finnish forest industry in 2013 is expected to be at about the 2012 level.

Stumpage Prices Down on Roundwood Market

The further deterioration in the world demand outlook for forest industry products is also being felt on Finland’s roundwood market. Although roundwood sales in the early part of 2012 were brisk, the worsening economic conditions on both the sawnwood and paper markets are curtailing roundwood sales during the second half of the year. Softwood sawlog stumpage prices for the full year 2012 are forecast to be down by 5–6%, and by 8% for spruce pulpwood, year-on-year. Due to the more favourable demand situation for pulp, the prices of pine and birch pulpwood fell by a lesser amount, 3–4%. Commercial fellings are forecast to reach 51 mill. m³ for 2012, which is 3% less than in 2011. Roundwood imports will also be down year-on-year.

On the end-product markets the economy is not forecast to improve until the second half of 2013, and roundwood sales in the first six months will show a year-on-year decrease. In the second six months of 2013 sales will pick up a little as sawnwood demand improves. Average prices for the full year will be more or less unchanged from 2012. However, commercial fellings will be down by 2%, to 50 mill. m³, as imports of roundwood will be up significantly on account of the reduced price of imported Russian roundwood following the country’s WTO membership. Demand for forest chips used for energy purposes is continuing to grow, reaching 7.8 mill. m³ in 2012 and 8.3 mill. m³ in 2013. The energy plant gate price of forest chips in 2012 will remain unchanged from 2011, while in 2013 it will increase slightly.
Drop in Forestry Operating Profit

The reduction in domestic commercial fellings and the drop in stumpage prices will mean that gross stumpage earnings in non-industrial private forestry in Finland will fall to EUR 1.3 billion for the full year 2012, and the 2013 figures are not expected to show any improvement. Investment in timber production in 2012 will nevertheless be at the previous year’s level in real terms, rising in nominal terms by about EUR 5 mill. from the 2011 figure of EUR 210 mill. The proportion of this investment accounted for by work input and financing from the forest owners themselves will have risen to over 70% in 2012, while the real value of state subsidies will have fallen by 3–5%. The per-hectare operating profit from non-industrial private forestry will remain at about EUR 75/ha for both 2012 and 2013, down by a quarter from the post-2000 average. The decrease in stumpage prices will push the real investment return on timber production into the red in 2012. In 2013, real stumpage prices will fall, but the investment return will nevertheless climb back into the black (2.5%).

Assumptions and Uncertainties in Forecasting

The aim of this Economic Outlook is to provide information on the current state of the entire Finnish forest sector and the short-term outlook for the sector. The forest sector forecasts are based on publicly available statistics, world economic forecasts, forest sector market information from different sources, and research conducted by the Finnish Forest Research Institute. The forecasts presented here are based on the principle of derived demand, according to which fluctuations in GDP growth on the domestic and export markets will, via demand, be reflected in forest industry production and thus the domestic roundwood market. Changes in the forest sector’s operating environment and the effects of the Government’s economic policies are taken into account in making the forecasts. If GDP growth turns out to be below the level forecast, this would mean that export prices, production and profitability for the Finnish forest industry will be lower than indicated in the forecasts given here. With falling demand for wood, the adverse impact would spread from the forest industry to roundwood markets and would affect forestry employment and the profitability of non-industrial private forestry. Growth in the Finnish forest sector would then fall short of the forecasts presented here.

The views of GDP growth in the world economy and on export markets have been formulated on the basis of forecasts made by a number of different organisations, among them the Organisation for Economic Cooperation and Development, the International Monetary Fund, the Research Institute of the Finnish Economy, Nordea, and the Bank of Finland. The forecasts given in this publication are based mainly on forest sector information available in late September and early October 2012 and world economic forecasts for 2012 and 2013. The forest sector forecasts presented here are the views of researchers about the most likely course of events. They are point forecasts and are based on export market GDP forecasts and other background assumptions about the markets.

The most significant risk regarding materialisation of the forecasts presented here is that economic growth will be lower than forecast. Uncertainty is focused particularly on the euro area’s GDP growth in 2013 and the continuation of the fiscal policy stimulus measures being

<table>
<thead>
<tr>
<th>Forecasting variables</th>
<th>2011 % change from previous year</th>
<th>2012 % change from previous year</th>
<th>2013 % change from previous year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sawnwood production</td>
<td>3</td>
<td>–4</td>
<td>2</td>
</tr>
<tr>
<td>Sawnwood export</td>
<td>4</td>
<td>–4</td>
<td>2</td>
</tr>
<tr>
<td>Sawnwood export price</td>
<td>–4</td>
<td>–2</td>
<td>2</td>
</tr>
<tr>
<td>Paper production</td>
<td>–4</td>
<td>–9</td>
<td>0</td>
</tr>
<tr>
<td>Paper export</td>
<td>–3</td>
<td>–8</td>
<td>0</td>
</tr>
<tr>
<td>Paper export price</td>
<td>5</td>
<td>4</td>
<td>0</td>
</tr>
<tr>
<td>Commercial fellings</td>
<td>1</td>
<td>–3</td>
<td>–2</td>
</tr>
<tr>
<td>Roundwood imports</td>
<td>–9</td>
<td>–6</td>
<td>19</td>
</tr>
<tr>
<td>Sawlog prices</td>
<td>Pine</td>
<td>3</td>
<td>–5</td>
</tr>
<tr>
<td></td>
<td>Spruce</td>
<td>3</td>
<td>–6</td>
</tr>
<tr>
<td></td>
<td>Birch</td>
<td>8</td>
<td>–4</td>
</tr>
<tr>
<td>Pulpwood prices</td>
<td>Pine</td>
<td>4</td>
<td>–4</td>
</tr>
<tr>
<td></td>
<td>Spruce</td>
<td>2</td>
<td>–8</td>
</tr>
<tr>
<td></td>
<td>Birch</td>
<td>2</td>
<td>–3</td>
</tr>
</tbody>
</table>

Price changes are nominal
concluded at the end of 2012 in the United States. If the difficulty in agreeing political solutions in the euro area and the turbulent economic events of spring 2012 are repeated in 2013, the slow rise in the euro area’s economy will be delayed further into the future. This would also affect the export recovery in the Finnish wood products industry and pulp and paper industry, as the demand and price trends for sawnwood, paper and packaging materials would remain weak. On the other hand, the emerging growth in the United States could come to a standstill if there is political deadlock over the future direction of fiscal policy. This would also have a considerable impact on the entire world economy. In addition, any regional conflicts, for instance in the Middle East, or natural catastrophes like the Japanese earthquake of 2011 and subsequent destruction, could affect the course of the world economy via cost increases on energy and raw materials.