

COMPETITION AND INVESTMENT IN THE BC COASTAL FOREST INDUSTRY



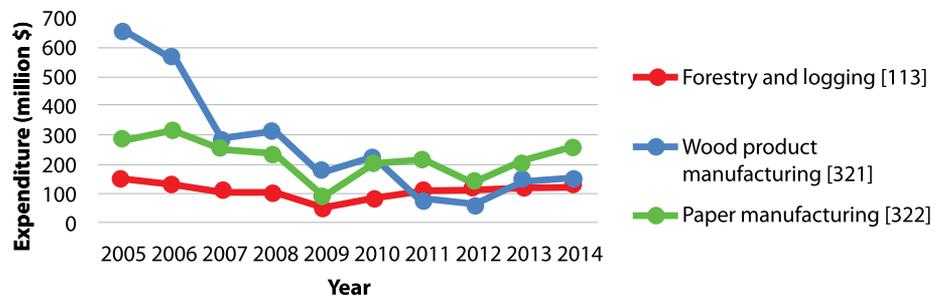
Investment in the BC forest sector has fallen sharply in recent years, most visibly in wood product manufacturing. The decline has raised concerns about the future of the industry, particularly on the BC coast where contractors are struggling to earn a competitive return and manufacturing capacity has shrunk significantly.

What is hampering investment on BC's coast? The forests remain standing on some of the most productive lands in the country, communities with a long history of forestry have not gone away and forest products are still in demand. But a successful forest industry requires more than just trees and demand for wood products: it needs competitive businesses.

From an economic perspective, the marketplace is an obvious area to begin looking for answers to the investment question. Competition, a critical element of a functioning market, works like natural selection: weaker businesses are removed from the industry while the strong ones survive. To emerge as a stronger competitor, you have three options: become more efficient and lower costs, create a higher value product and boost prices, or develop specialized markets. In the absence of competition, businesses are unmotivated to invest in these types of innovation. More effort is spent defending market power and position and less invested in continuous improvement or seeking new opportunities.

Pressures on the coast forest industry over the past decade have influenced competition in the harvesting and processing sectors in very different ways. In the wake of the US housing market

**Capital expenditures in the BC Forest Sector in \$ millions
(2005=100), 2005-2014**



Statistics Canada. Table 029-0005 - Capital and repair expenditures, by sector and province, annual (dollars) (accessed: May 10, 2016).

crash and global financial crisis, the harvesting sector has continued to experience intense competition while the processing sector was reshaped through consolidation. Both changes have important implications for investment and growth.

In addition to the pressures of the global economy, increasing mechanization and a shift from old growth to second growth timber have reduced the number of jobs in the harvesting sector and increased capital requirements. In a new reality where fewer harvesting opportunities are available, the weakest businesses go bankrupt. Competitors will continue to battle it out for contracts until a new equilibrium is reached; those that underbid will win the battle but lose the war. Businesses that are able to reinvest in capital and hang on through the tough times will have a stronger position with greater negotiating power when the dust settles.

While competition is working its painful magic in the harvesting sector, major players in the processing sector

have insulated themselves from similar pressures by becoming larger and more powerful. Current conditions enable the major players to maintain profitability through low-cost production instead of seeking opportunities to develop higher value products. From a business perspective, this strategy can prop up an existing business model in the short term and reduce the need to reinvest; over the long term, it spurs a race to the bottom that harms the industry as a whole. With a handful of processors holding the harvesting rights to a large proportion of the forest resource, other businesses are unable to access this potentially high-value fibre on the open market.

Power is not readily ceded by those that hold it. One thing that well-functioning markets can do is rebalance power by creating more options: the more buyers and sellers of logs, lumber and residual fibre, the more opportunities exist for firms to develop innovative business arrangements, processes and products. Competition is critical
(Continued to page 49)

The Market Report is brought to you by:

Stafford Lake
LOGGING LTD.



BenWest
LOGGING LTD.

Logging & Road Contractors
Campbell River

Tel: 250-287-7932 • Email: benlog@telus.net

he wants it. He loves being a skilled practitioner of a historic BC trade, one that helped build the province. "I hate breaking wood though," he says. "Some of it is more than 500 years old and I figure the least I can do is maximize its value as much as possible."

A small-town boy from Lumby, BC, Schaefer certified in 2009 and has been a production faller with Sibola Mountain Falling for the past two years. He brings to his job the professionalism of a surgeon. "Our day is full of situations you have to learn how to manage—snags, blowdown, shot rock, fog, rain and a million other things—and managing it gives me great satisfaction," he says, adding that he finds he works with applied physics every day, including monumental forces and enormous weight.

"It's kind of funny because I failed physics in high school."

A married man of 32, he says the hardest part is being away from his wife of seven years. "But she's very supportive; I couldn't imagine life without her."

He says he has no concerns about mechanical fallers putting him out of work. "I'd have to see it to believe it," he says. "We deal with sensitive areas, large amounts of rainfall, grades of up to 70 per cent, rock and bluffs, all areas where I question a machine's ability. At this point, I'm not too worried."

And that's a good thing, because working as a production faller has been, quite simply, "one of the best experiences of my life, and I plan to keep on doing it until I'm too old to pull a saw."▲

Market Report (Continued from page 15)

to promoting not only cost reduction but also investment in innovation that yields higher value.

If economists can agree on one thing, it is that the role of government is to ensure markets are functioning efficiently. To its credit, the BC Ministry of Forests, Lands and Natural Resource Operations has made some progress in this area by transferring forest tenures to communities and First Nations and creating space for innovation. However, efforts to date are insufficient to shift the balance of power from the hands of the few to the hands of many. A broader effort to redistribute harvesting rights through a fair, equitable buyback of forest tenures is one option to stimulate competition and create new opportunities for a larger number of small- and medium-sized businesses, including First Nations- and community-owned enterprises.

Current distortions in the coast forest industry are hampering investment and much-needed growth. Until major restructuring of the forest tenure system takes place, there is little place for innovation to take root, and any efforts to stimulate investment in the industry will have limited effect.▲

Harry Nelson is an Assistant Professor within UBC's Faculty of Forestry. His research interest is in analyzing natural and environmental resource policy with an emphasis on forestry and in developing new policy options that can help enhance the long run sustainability of Canadian forests and the communities and businesses that rely upon them. Harry has provided advice on forest policy and trade issues to the federal government, various provincial governments, industry associations, forest sector firms and First Nations among others. He can be reached at 604.827.3478 or harry.nelson@ubc.ca.

Ngaio Hotte is a Resource Economist & Facilitator with Resource Economics Group and a doctoral student in the Faculty of Forestry at UBC. Her current research focuses on how trust is created between First Nations, federal and/or provincial governments in the context of collaborative natural resource management. Other major projects have focused on economic impact and value analysis in the forest, fishing and tourism industries and facilitation of multi-stakeholder dialogue. She can be reached at info@resource-economics.ca.

LOG HOURS ON THE WATER

BOOK NOW FOR 2016

LEGENDARY FISHING.
BREATHTAKING WILDERNESS.

HAIDA GWAI | CENTRAL COAST



**WESTCOAST
RESORTS**

CALL 1.800.810.8933
WWW.WESTCOASTRESORTS.COM

