

Wood procurement strategies for the 1990s

David Maass

In the 1990s, the problem will be to get cost-effective, higher quality fiber.

After the high-flying 1980s, what is in store for pulp and paper mill wood procurement in the low-riding 1990s? We have already seen a downturn in the economy and a decline in demand for some paper products. This paper examines six trends that are putting an upward pressure on prices for wood and will outline two strategies for dealing with those forces. In the 1980s, the problem was to get more fiber; in the 1990s, the problem will be to get cost-effective, higher quality fiber.

Transportation costs are increasing

The days of cheap fuel are behind us. We can foresee increased fuel costs as a result of world events such as the Persian Gulf crisis and increased taxes on gasoline and diesel. In addition, many state transportation agencies are putting pressure on trucks to reduce their weight. Equipment costs are increasing, and the days of short-haul logging are over.

Loggers are harder to find

The labor pool is decreasing as loggers and contractors look for safer, more steady kinds of employment. In the past, rural workers were able to move from farming or seasonal activities into logging without much effort. Capital costs were low, and the training required was minimal. Now loggers and their contractors need to be much more sophisticated and greater training is required not only in the use of equipment, but also safety, silviculture, and business.

Associated costs for workers' compensation, health benefits, and insurance are likely to increase. Higher equipment prices will make it difficult for many loggers to move in and out of this employment easily.

As a result of these trends, the pool of skilled labor available for logging will grow smaller. However, loggers will be much more professional and more productive than in the past. Likewise, these professional loggers are going to demand full-year employment and expect higher prices for their wood.

Availability is declining

Another factor affecting the logging industry is a national decline in availability of timber from the public sector, as in

the case of planned National Forest reserves for the spotted owl. Law suits are altering many National Forest plans. Environmental groups are looking to increase wilderness protection areas and old growth timber preserves.

States are also being called upon to augment this public reserve, while cuts in state budgets will reduce timber sales from state forests throughout the country. With fewer staff, many state forest systems today are yielding far fewer trees than they could. This will increase demand and prices for wood from nonindustrial private landowners. These landowners are becoming more sophisticated and will not tolerate widespread liquidation of timber to feed the mills. A benefit of increasing prices is that it will make additional money available to the landowner for forest management. That is all to the good in the long run, but it is not clear that this group of private landowners will provide all of the wood needed for the mills.

Regulations reduce availability and increase costs

With concerns about wetlands, the environmental impact of logging, and clearcutting, states are looking to put in place stronger regulations that limit harvesting practices. In addition, the industry, particularly in the southern United States, has been emphasizing the use of best management practices for control of timber harvesting. These efforts for environmental benefit will have the effect of reducing how much wood gets cut in the short-term.

Wetland regulations, for example, may require strict compliance with road building standards for access to harvesting areas. Special permits might also be required and limits may be placed on when and for what period of time timber may be harvested. Such requirements may make some tracts of trees temporarily unavailable or may divert harvesting to cheaper sources of timber.

Best management practices and forest practice acts may also restrict or impose permitting or performance requirements for harvesting in environmentally sensitive areas. These increase costs for specific increments of wood. In the long-term, however, they minimize site degradation, which may actually increase available wood supplies.

Increased competition

Competition throughout the United States will increase as mills bid against each other for cheap wood supplies. The movement to take bids on standing timber will undoubtedly

Maass is an associate for The Ireland Group, 7 North Chestnut St., Augusta, ME 04330.

increase throughout the United States, because this means more money for the landowner.

Biomass boilers will be the new competition in the 1990s as states and utility companies turn to woods for renewable energy sources. Many projects will be sold with the idea that they enhance forest management, don't increase carbon in the atmosphere, and offer a "clean" alternative to nuclear power. The boilers will, however, place an additional burden on fiber uses.

The increased competition will decrease flexibility in fiber supply. In the past, mills had the option of switching to lower cost alternative fibers. Various technological fixes allowed them to make use of underutilized species. Demands now are being placed on those species, either making them no longer low cost or simply unavailable.

Increased internal competition

A decline in product demand naturally leads to a decline in dollars available to pay for raw materials. When products were selling at premium prices, it was necessary to pay extra dollars for the raw material of wood to keep the mills at full capacity. Mills in the 1990s will have less flexibility to pay high prices, and mill managers will not tolerate increasing prices throughout the system.

Most importantly, pulp prices are off, and when they will recover to recent levels remains uncertain. This is the major limit on wood pricing flexibility for mill managers.

Also, substitution of recycled fiber and imported pulps, such as eucalyptus, for raw fiber will decrease the need for virgin fiber in at least some mills. Assuming mandated or regulated amounts of substitutes will be used in the short-term, then regardless of price, these substitutes will reduce the ability to pay higher prices for wood. If the price of the substitutes is high, it will limit a mill's ability to buy wood. On the other hand, if their price is low, then this tends to put a ceiling on wood prices.

Use of substitutes could reduce the competition for wood, however, which is probably helpful. Still, the net effect is likely to be to reduce an individual mill's ability to bid for more wood with higher prices.

Two strategies available

In the past, managers "solved" this dilemma by throwing money at the problem. They would bid up prices of wood, truck farther, or offer short-term bonuses in another mill's woodshed. However, every mill can play that game. These approaches have not only been short-term solutions, but have led to ill will and bad reputations. There are few things worse in the wood procurement business than being an inconsistent participant.

Managers will need to develop more insightful strategic plans to meet mill requirements that minimize wood cost. They will have to be at the right place at the right time. Managers will have to adopt this philosophy and then alter their direction as the situation changes. They will need to examine continually their strengths, weaknesses, opportunities, and threats. Managers will need to develop a more precise supply analysis.

There are two solutions to increasing fiber prices. These are not without their own difficulties. First, managers may pay a premium for just the right kind of wood. If aspen from second growth stands between 18 and 35 years old is just what they need to maintain product consistency and quality, then managers may benefit from paying a premium for this kind of wood. If wood supply can provide savings in other parts of the pulping process, then it makes sense to buy fiber to a high level of specifications. Quantitative studies would need to be done in the mill to demonstrate that cost savings there can offset the higher priced wood. Wood procurement managers will also need to examine ever more closely the availability, cost, and location of fiber sources. They will have to recognize the strategic vulnerability of the mill for relying on limited sources. After identifying their needs, they will need to establish long-term supply contracts.

The second approach is to pay minimum price for fiber supply, but provide more services to suppliers so that they willingly bring wood to the mill. There are other ways to pay for wood than net 10 days with a check in the mail. Suppliers respond favorably to quick payment for wood, long gate hours, quick turnaround, and other benefits. These allow for more cash in hand and more trips in a day. This has led to a lot of hidden costs of wood procurement. Smart managers are no longer going to allow wood costs to be hidden in complicated accounting procedures and statements.

Although both of these strategies have been used in the past, in good times and bad, for strategic reasons, managers no longer have both options available. They will have to choose between one or the other.

In the northern United States, at mill after mill, obsolete woodyards are serious obstacles to mill profits, or more efficient wood procurement. Since the woodyard is not the end of the mill that brings in the money, funding improvements there have been difficult even in good times. The result is chronic, frustrating problems with size limits on wood, breakdowns, or other inefficiencies. Mills are gradually catching up, but the pace has been slow. That's not surprising, because costs are high and space is often tight.

A further approach is to be a consistent and trusted buyer. By developing an enduring relationship with the supplier, your mill becomes the "desirable customer." In this philosophy, managers need to adopt the practices of meeting the customer needs by turning this around to meeting the needs of the supplier.

The old marketing adage applies here. "If you want to make some money, give the customers what they need. If you want to make a lot of money, give the customers what they want." This will require listening closely to the suppliers, to figure out what they need and want. This requires working closely with the suppliers, getting to know them and their businesses, respecting them as individuals.

This approach does not come free or cheap with low prices for wood. However, it may benefit the mill in the long run with lower direct costs of wood and supplier loyalty.

We appreciate the review of this article by Richard Finley and Lawri Noel.