

C I N T R A F O R

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Overview of the Indian Market for US Wood Products

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Executive Summary

The economic liberalization policies initiated in 1991 have led India along the path of increased economic growth and greater macroeconomic stability. Real GDP growth averaged 6% over the period 1997-2001, exceeded 8% from 2002-2005 and is projected to be about 9.2% in 2006. This rapid economic growth has been supported by a loosening of trade restrictions which have contributed to a rapid increase in both imports and exports. Between 2000 and 2005, imports increased from \$US50 billion to \$US149 billion while exports increased from \$US36 billion to \$US103 billion. Future economic growth may be tempered by rising inflation, which is projected to be almost 7% in 2006, and rapidly increasing wage rates for skilled labor. For example, food price inflation rose by 10% in 2006. In addition, poor infrastructure (especially roads, ports and electrical power distribution), restrictive labor laws and poor quality public services (especially in education and health) also pose serious challenges to continued high levels of economic growth in India. It is estimated that almost 40% of India's fruit and vegetable harvest rots before reaching market due to inadequacies in the transportation and electrical distribution infrastructure. India will continue the process of opening its economy due to the fact that it must create on the order of 15 million new jobs every year simply to provide employment for young people entering the job market. However, future economic growth is dependent on reducing (and eventually eliminating) subsidies and providing improvements in the road and electrical distribution infrastructure, particularly in the rural areas of India.

The forest cover in India is estimated to be 637,293 km²; 19.4% of the total land area. India's forests are mostly state owned; only 10% of the forests are classified as community or private forests. A recent survey by domestic and international organizations revealed a moderate increase in India's forest cover. Forest plantations play a very important role as a source of raw material to the domestic wood-based industry. Since adopting the National Forest Policy of 1988 (NFP), there has been a ban on the felling of trees in all forests located above an altitude of 1,000 meters. In addition, high priority has been given for planting fuelwood and deciduous fodder producing trees in government forests. Finally, industrial wood production was restricted to farms and wastelands. As a result, there was a drastic reduction in timber harvest volumes as a number of states stopped timber harvesting and a ban was announced on all harvest operations in the national parks and protected sanctuaries.

The NFP emphasized meeting the fuelwood, fodder and small timber needs of local communities rather than the raw material requirements of the wood-based industry. It should be noted that even before the NFP was implemented in 1988, the existing forest policy was more conservation oriented than industry oriented. The raw material crisis for the wood-based industries became more acute following the adoption of the NFP. As a result, the forest-based industries have had to increase their dependence on private forests and bamboo from natural forests (bamboo harvesting from natural forests is permitted) for their raw material supply. Though large reforestation programs were proposed in conjunction with the NFP budget, constraints prevented the forestry department from meeting the reforestation targets. To meet the community demand for fuelwood, small timber plantations were designed which provided timber products that were less useful for industry. In order to improve the availability of raw materials, the NFP proposed the liberalization of log, chips and pulp imports.

The Indian forest products industry, both the wood products sector and the paper and paperboard sector, have been constrained by severe raw materials shortages. This raw material shortage for the forest products industry has been further accentuated as a result of a Supreme Court ruling limiting the felling and movement of timber within the country. In an effort to alleviate the raw material shortage, the forest products industry is increasingly relying on imported logs, chips, wood pulp and waste paper. Hence, for the wood-based industries, imports have become a very important component of their raw material mix.

The graduated structure of tariffs applied on wood product imports clearly indicates that the Indian government encourages the import of unprocessed lumber that can be used by the wood-based industries as raw material inputs. Higher tariff rates are imposed on imported finished and value added products to protect the less efficient domestic manufacturers from international competition. In addition to the basic import tariffs, India also imposes duties such as surcharges, additional customs duties and special additional duties. Other additional levies can be imposed on imported wood products depending on the nature of the product. These additional levies include countervailing duties, anti-dumping duties and safeguard duties. Other non-tariff barriers include state taxes, which can be as high as 18% of the value of imports and various port of entry restrictions which might add up to a large mark-up on imported items. Such tariff and non-tariff barriers by the government make imported products less competitive in India . Over the past decade the tariff rates and the non tariff barriers have been reduced dramatically and India has started importing large volumes of forest products.

Indian trade in forest products has increased tremendously over the period 1999-2005. This is in response to both the decline in the domestic timber harvest as well as the increased demand for wood products within the domestic wood processing industry. Over the period 2000-2005 Indian exports of wood products jumped from \$US30 million to \$US99 million, a 230% increase. In contrast, imports of wood products went from \$US528 million to \$US957 million, an 82% increase over the same period. As a result, India saw its balance of trade in wood products worsen from \$US498 million in 2000 to \$US858 million in 2005. It is important to note that over 88% of India 's wood imports were logs, primarily from Malaysia and Myanmar .

Housing has long been neglected in India 's national 5-year plans. The unfulfilled demand for housing was estimated to be approximately 50 million units in 2001 and was projected to be increasing at a steady rate. This housing shortage stems from a lack of government funding and the inadequacy of financial institutions, coupled with an increase in building material, labor and land costs. In the tenth five-year plan, from 2002 – 2007 special emphasis has been given to the housing sector and some state governments have announced a target of achieving “shelter for all” by 2012. Efforts have also been made to reform the allied institutions in an attempt to provide support to the housing sector. The government is beginning to view the housing sector as a very important driver of economic expansion and increased employment. These new initiatives by the government and the huge latent demand for housing, coupled with an expanding economy, should result in higher housing starts in the country over the next decade.

The middle class population in India , which is almost the size of the US population, is becoming more exposed to the western life-style and is showing an interest in western style doors, windows and kitchen cabinets. India has a centuries old tradition of wood use, particularly for interior design and furniture. Although structural wood is rarely used for construction, outside observers have noted that India uses more interior wood than Japan . Recent estimates suggest that the market for high end imported value-added wood products is increasing steadily as a result of continuing economic prosperity in India . This represents one of the largest emerging markets for value-added wood products in the world. New residential construction, primarily multifamily units, are increasingly going to standardized sizes for doors, windows, and interior fittings. This has led to an increased demand for imported doors, windows and cabinets. The total annual demand for furniture in India is estimated to be \$US1.25 billion of which 90% is for wooden furniture. The market for branded (higher quality) wooden furniture is estimated to be \$US37 million and growing at an annual rate of 15%.

Imports of wood products into India have been growing rapidly, although the demand for wood products is heavily skewed towards raw materials such as logs, chips and pulp. While the middle class in India is growing and becoming more open towards using imported value-added wood products, much work needs to be done to take advantage of this demand. For example, India must accelerate their rationalization of import tariffs and remove those non-tariff barriers designed to protect inefficient domestic manufacturers from international competition. This will not only ensure compliance with their WTO obligations but will also force the domestic processing industry to invest in more efficient processing technologies. In addition, there remain long-term opportunities to introduce North-American wood frame construction technology in India . The combination of a severe housing shortage and interest in developing energy efficient housing both provide impetus for working to gain acceptance for wood frame construction. However, in order to achieve the successful introduction and adoption of wood frame construction it is important that the US government and industry associations work with the Indian government to develop and adopt wood frame building codes. Finally, acceptance of wood frame construction technology is dependent on increasing the familiarity and understanding of this construction

technology within the architect and construction communities. A key element to gaining this acceptance could be in educating architects and residential builders on the superior environmental performance and energy efficiency of North-American wood frame construction technology.

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