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A Competitive Assessment of the Japanese Forestry and Forest Products Sectors

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Executive Summary

Background to the Study

The lack of competitiveness of Japan's wood producers, continued growth in imported lumber and wood products, and a growing unmanaged timber stock on Japanese national and private forests spurred the Japanese government to review lumber imports and its relation to its depressed wood products market. Although the initial Ministry of Agriculture, Forestry and Fisheries inquiry into how exports of wood products from the US and other regions of the world have proven injurious to the domestic industry never reached a pan-ministry consensus, at the time of this writing some lumber products are still on the MAFF's list of products for potential WTO safeguard protection. A Safeguard Action under WTO guidelines requires that the Japanese government: (i) identify the affected industry, be it the forestry sector or the wood-processing sector; (ii) identify the affected product and its relation to substitute import products; (iii) determine how the sharp increase in imports resulted in injury to the affected industry; and (iv) determine how Safeguard measures would improve the competitiveness of the affected industry over the 4 to 8 year period it is in effect.

Study Objectives

This study, through in-country interviews, literature review, and data analysis, sought to analyze the state of the competitiveness of the Japanese forestry and wood products industries, and, using the CINTRAFOR Global Trade Model, to determine the impact of a protectionist trade policy on the domestic industry's competitive strength and upon Japanese home-buying consumers.

Summary of Findings

During the period of the writing of this report it appeared that the threat of a WTO Safeguard Action subsided. However, as of July 2001 lumber products are still officially listed by MAFF for a potential safeguard action. Though this is not a study regarding the impact of protectionism on US or foreign exports to Japan the consequence of such a protectionist action on US and foreign wood exports to Japan is large. As the study findings suggest the benefit of trade restrictions to the domestic industry is mixed with the main burden of such an action being shouldered by the Japanese consumer. Many of the reasons for the lack of Japanese forestry and wood product sector competitiveness have more to do with internal systemic issues than with external issues traceable to exports.

Potential Impact of a Safeguard Action

Although the intended objectives of the Government of Japan forestry and forest products policies and subsidies is to realize "an era of domestic timber, a Safeguard Action may have the opposite effect by increasing log imports 44%.

- A simulated 25% increase in tariffs under a Safeguard Action, causes a 20% increase in domestic lumber production and a 7% increase in domestic log production.
- Consumers of lumber products lose approximately \$3 billion dollars annually. This is more than double the Forestry Agency subsidy monies supporting the forest and wood processing industry.
- The 16% increase in the price of lumber resulting from a Safeguard Action has the potential to increase home construction costs by ¥264,000 yen per house.

- Sawmills processing imported logs tend to have a higher level of average production, suggesting that a Safeguard Action may lead to consolidation in the industry, negatively impact the smaller mills that rely on domestic logs.

Forestry Industry: Internal Systemic Issues

- Japan has an unusually high cost of forestry compared to other regions of the world.
- Poor profitability in forestry is due in part to geography, such as steep terrain, which makes forest management challenging and increases the cost of harvest and extraction
- The low profitability is reflected in a Forestry Agency study which estimates that the internal rate of return from a *sugi* plantation has declined from 6.3% in 1965 to 4.1% in 1975 to 2.1% in 1985 to 0.9% in 1993.
- The exceedingly small size of private forests, most around 5 hectares, makes it difficult for owners to raise capital and manage efficiently.
- The depopulation and aging of the forestry and wood products workforce seriously impacts productivity and efficiency of the forestry industry. According to one survey 57% of forestry workers are over the age of 55 while less than 10% are under the age of 35.

Wood-processing Industry: Internal Systemic Issues

- Japan's harvesting and delivery costs to the mill are now nearly three times more than those costs in the US Pacific Northwest region and six times larger than those in Scandinavia and the southern hemisphere.
- Imported log prices, energy and labor costs combined with a decreasing log processing efficiency results in Japan's sawmills being high cost producers of lumber relative to their competitors.
- Electrical rates for the saw-milling sector in Japan are 3 to 4 times higher than other producers.
- The small size and scale of sawmills in Japan contribute to their lack of profitability. Production cost estimates for 1996 indicate that Japanese costs are approximately 156% higher than a sawmill in British Columbia, Canada. While labor, energy, and capital costs are less than 50% higher than BC, stumpage prices for *sugi* are 250% higher than hemlock.
- The performance based regulatory environment surrounding the housing industry (Housing Quality Assurance Act and the 10-Year Housing Warranty) is altering the product and species mix, displacing some domestic species. For example, demand for yellow cedar and treated lumber in ground sill (*dodai*) applications has also increased as a result of the 10-year Housing Warranty.

Conclusion: Protection is Not the Path to Competitiveness

Since 1955, Japan has seen its self-sufficiency in wood products decline from approximately 95% to below 20% by 2000. While there are a variety of factors that have contributed to this decline, the net effect has been that domestic forest products manufacturers have lost tremendous market share to imported wood products. Similarly, the competitiveness of the forestry sector has declined significantly relative to imported softwood logs. The dominance of the timber market by imported timber has contributed to a fundamental structural change within the forestry and forest products sector. Analysts and politicians have charged that these structural changes in the forestry and forest products sector have not only adversely affected the competitiveness of the domestic forest products sector but that they have severely restricted the ability of forest owners to actively manage forests in Japan, both private and public. In an attempt to rectify this inability to manage its forests and to bolster the competitiveness of its forestry and wood-products industries the Government of Japan has considered a Safeguard. However, the conclusion of this study is that given the burden that this trade restriction will likely cause to the Japanese consumer coupled with the probability of a significant increase in log imports, protection is not the road to profitable and well-managed forests and wood products industry. Perhaps more importantly, given the internal systemic issues described earlier, there appears to be little likelihood that a Safeguard would result in the increased competitiveness of the sawmill industry.

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