

NORWEGIAN MARKET STATEMENT 2007

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General economic trends in Norway

Source: Revised National Budget 2007, Ministry of Finance

The growth of the Norwegian economy has been strong for the past three years, with Mainland-GDP growth averaging 4½ %. Domestic demand has been fuelled by low interest rates, high income growth and strong growth in petroleum investments. Investments in the mainland business sector have also provided growth impetus to the Norwegian economy. The continued strong economic growth has led to a tight labour market and clear signs of pressure in the Norwegian economy.

Growth in Mainland Norway GDP is now estimated at 3.7 % in 2007, indicating the fourth year running with growth well above trend and, with that, further intensifying the strong economic expansion.

The labour market has tightened significantly over the last couple of years. The unemployment rate is now the lowest in nearly 20 years and employment growth is strong. The unemployment rate is expected to decline from an average of 3.4 % in 2006 to 2.5 % in 2007. Employment is expected to grow by 2.1 % in 2007. Inflow of workers from other countries has so far in this upturn helped to ease labour market pressures. However, demand for labour is still high and many companies are having difficulties in finding qualified labour.

The tightening of the labour market contributes to higher wage growth. Based on the wage negotiations concluded so far, wage growth is estimated at 4¾ % in 2007.

Higher wage growth is expected to lead to higher underlying consumer price inflation in 2007. The consumer price index adjusted for changes in excise duties and excluding energy (CPI-ATE) is expected to increase from 0.8 % in 2006 to 1½ % in 2007. Consumer price inflation (CPI) is expected to increase by ¾ % in 2007.

According to Statistics Norway, 33,314 new dwellings were started in 2006, a growth of 5.4 % from 2005 and the highest number of housing starts registered since 1982. 48 % are in apartment blocks, which also have the highest growth compared to 2005. A total of 17.1 % more started dwellings in apartment blocks were registered in 2006 than the previous year. Semi-detached houses have also had an increase of 9.6 %. Start of terraced houses was at the same level as in 2005, while there were started 7.4 % less detached houses in 2006. 4,980,000 m² of non-housing area was started, of which 3,612,000 m² industrial buildings, an increase of 10.5 % compared to the previous year. In addition, 1,368,200 m² were started for leisure properties and garages in 2006, a growth of 2.6 % from 2005. The pressure in the cottage/leisure building market has increased throughout the year.

Policy measures taken over the past 18 months, which might have a bearing on trade and markets of forest products or forest management

The new forestry act came into force on January 1st 2006. The new act represents a simplification compared to the previous forestry act of 1965, which it replaced. The forest legislation focuses on the role of the local authorities in forest management. Further, the responsibility of the forest owner is made more explicit. A regulation for sustainable forestry was introduced under the Forestry act in 2006. The regulation gives specific requirements for regeneration, environmental considerations to be taken when planning and carrying out forest operations. The environmental requirements are close to the performance level standards used in forestry certification in Norway.

In 2005 the Parliament expressed concern over what seems to be a low activity in the forest sector, and therefore requested the Government to propose national strategies for increasing the annual harvesting. As a follow-up on this request, and as a result of the shift in forest policy after the election for parliament in 2005, the Government has introduced several measures in order to achieve higher activity and profitability in the forest sector. Economic support for reforestation was reintroduced, and support for silviculture and bio energy purposes was increased with effect from 2006. In 2007, additional measures aimed at increasing the forestry activity was taken by the Government, including:

- Increased tax relief for forest owners when investing in forest infrastructure, forest production and small scale bio energy production
- Increased governmental support for forest infrastructure and long term investments in forest production
- Increased support for bio energy production through the Bio energy Programme
- Prolonged support for the Wood-based Innovation Scheme, supporting the sound use of wood
- Provisional regulations for road transportation allowing for heavier timber transports

A regulation under the Forestry act requires forest owners to set aside 4-40% of the revenues from harvested timber into a government administrated fund, The Forest Trust Fund. This fund is established for securing means for long term investments in sustainable forestry. The Forest Trust Fund is the property of the forest owners, but the use of the fund is regulated allowing only for specific purposes, such as planting, road building, management planning, non-commercial thinnings and other activities. When used, the money is treated as income for the forest owner, a part of it is however exempted for taxation. In 2007 the part of the Forest Trust Fund exempted from taxation was increased from 60 to 85% and the range of activities qualifying for this tax relief was expanded. One of the changes was to allow for investments in bio energy production under this scheme.

In addition to the tax relief granted through the Forest Trust Fund, economic support is given for a range of activities with the aim of increasing the availability of wood as an important and environmental raw material for all purposes, within the frame of sustainable forestry safeguarding the long term production and environmental values of forests. The economic support, which is locally administrated, was increased in 2007. Special attention is directed to areas with relatively

low utilization of forest resources due to sparsely developed forestry infrastructure, including coastal areas in western, mid- and northern parts of Norway.

In order to stimulate farmers and forest owners to produce, use and supply the market with bio energy, both as solid fuel and heating solutions, the Bio energy Programme was established in 2003. With increasing attention on the climate challenges and the role of forests as a supplier of carbon neutral energy, the budget of the programme was increased in 2007. The aim is to reduce the use of fossil fuels and to provide a basis for economic development in rural areas. It is a goal to establish activity in all parts of the country. The most important measures under the programme are investment support, pilot-projects and competence measures and capacity building

The Wood-based Innovation Scheme aims to increase the awareness and use of wood by stimulating innovation and market orientation in the wood industries. The main goal for the programme is to increase use of wood and profitability for the forest sector. The Wood based Innovation Scheme supports the forest sector industries in their goal of increasing the annual average consumption of wood per capita from 0.55 m³ to 0.75 m³ by 2010. The programme puts special effort on three areas: Industrial building, Wood products and Innovation systems. A part of the programme is jointly coordinated with the Research Council of Norway through the research and development programme WOOD.

In Norway, transportation is estimated to represent 25% of the total costs for the forest industries when buying roundwood. As a provisional arrangement from 2007, timber trucks weighing up to 56 tons will be allowed to drive on public roads identified to handle this kind of loads. This is expected to reduce the cost of transportation with as much as 15% on the selected roads.

Climate change policy

Forests contribute significantly in reducing the net emissions of greenhouse gases in Norway. Carbon sequestration in forests as a result of growing stock increment equals to 50% of the total human induced greenhouse gas emissions annually.

As a follow up of UNFCCC and the Kyoto protocol, The Government presented a parliament paper on climate change policy in June 2007. This paper forms the basis for the Government's selection and decision of sector specific targets, including targets for the forest and agricultural sectors, and measures to be implemented in the national climate change policy. A long term goal in the parliament paper is for Norway to reduce greenhouse gas emissions by 30% compared to 1990 level by 2020. The goal is further that Norway shall be carbon neutral by 2050, by reducing global greenhouse gas emissions at a level corresponding to national emissions.

The paper recognizes the important role of forests in combating climate change, and among the actions to be taken are facilitating for increased planting and forest management aiming to increase forest production.

Increased production of bio energy is another important goal presented in the parliament paper from the Government. The Government aims at an increase in bio energy production of 14 TWh by 2020 by creating favourable conditions for bio energy through focused and coordinated policy

means. This will be important as the conditions for production and use of bio energy is influenced by the politics under several ministries of the Government.

The Government is now preparing a new strategy for increased production and use of bio energy. As a first step, the Ministry of Oil and Energy has initiated a study that will examine the possibilities and challenges related to the establishment and further development of bio energy solutions. Preliminary results from the study are expected in November 2007.

The importance of wood for energy purposes is expected to increase in the future. As a result some parts of the forest industry are already experiencing harder competition for the raw materials.

Developments in forest products market sectors

Sources: Statistics Norway, Norwegian Forest Owners Federation, The Norwegian Sawmill Industries Association, Norwegian Pulp and Paper Association

Wood raw materials

There is a positive development in the forestry sector. This is explained by improvement of governmental support for forestry, increased public awareness of the economic and environmental benefits of sustainable forestry and last but not least increased market demand for wood raw materials, expressed in higher prices.

Total fellings, including wood for fuel is expected to reach 11.7 million m³ in 2007, an increase by 2% compared to the revised figures for 2006. The demand for wood raw materials is high; making the availability of machinery and operators combined with uncertainty related to weather conditions in the fall the main limitations for further increase of forest operations.

There is a significant decrease in the imports from the Baltic States and Russia. Most of the imports origins from Sweden, and large proportion of the imports from Sweden is coming from the border areas close to Norway, which is a part of the forest industries local markets.

Wood energy

Based on consumption studies the total amount of wood fuel consumption in households and recreational houses is estimated to 3.25 million m³. This is wood burnt as firewood in stoves and fireplaces. With imports only covering 0.2 million m³, the wood fuel represents a substantial part of the total fellings in Norway. The figures represents a dramatic increase when comparing to wood fuel statistics for previous years, but although the amount of wood fuel is expected to increase, most of the changes are related to change in statistical methods. A component of the total consumption of wood energy not covered in this figures on wood fuel is the energy produced and used by the wood industries, utilising the residues and waste from timber processing and timber sold or used by forest owners for small heating plants. Further increase in the use of wood for energy purposes is expected as a result of the Governments policy on increased production and use of bio energy.

Certified forest products

More than 95% of the Norwegian forestry is certified under the national certification scheme. The major imports of wood come from Sweden, where certification rates are similar for commercial

forestry. Norwegian forest certification is endorsed by the PEFC, while a large proportion of the imported wood is FSC certified. The major buyer of pulpwood in Norway, Norske Skog, requires forest certification of all their suppliers of Norwegian roundwood.

Value-added wood products

There is an increasing demand for value-added wood products in Norway. The increase can mainly be explained by the general growth of the economy, and high building and refurbishing activity. In addition the increase should probably also be explained by an increasing competitiveness of wood due to product development and marketing efforts.

Sawn softwood

Sawn softwood production in 2006 was 2.39 mill. m³, a slight increase compared to the last two years and almost equal to the last ten years' average. In most parts of the country there has been a good supply of sawlogs, especially during the 1st semester. Outgoing log stock was 415.000 m³, a reduction of 170.000 m³ compared to the beginning of the year.

Norway exported 0.47 million m³ of sawn and planed softwood, an increase of 7% compared to 2005. Denmark, Germany, Netherlands and Belgium are the four main importing countries. Export to Germany represents the highest increase in 2006. There have been very good market conditions in Europe and the trend has been increasing prices throughout the year. The reason for the moderate increase in exports is probably the good domestic market.

The import of sawn and planed softwood was 1.04 million m³ in 2006, almost identical as for 2005. More than 90% was imported from Sweden, which is similar to 2005.

Wood based panels

There have been only minor changes concerning the production of wood based panels. There are plans for restarting production in one fibre board factory that recently have been shut down, thus increasing production capacity. Due to high activity in the building industry domestic consumption is expected to increase in 2007 compared to 2006. The increased consumption will mostly be based on increased import. As for the years to come, the industry expects a stabilisation of the market. The fibre board industry has special attention drawn to the increased focus on bio energy as an increased demand for wood energy in some areas is expected to compete with the industries need for raw materials. Such competition will lead to higher prices, and thus challenge the profitability of the industry.

Pulp and paper

Production of wood pulp and paper is expected to decrease by approximately 5% each in 2007 compared to 2006. The apparent consumption is expected to remain stable, due to reductions of the export corresponding to the lower production. In the last two years there has been a reduction of production capacity by shutting down plants, but there is still considered to be a surplus of capacity in the industry on the international level. The price on paper has therefore had a weaker development than other raw materials in the last years. As a consequence, major industries are considering actions to further adapt the production level to the market situation.

Tables

A. Economic indicators

Key projections for the Norwegian economy. Volume changes from previous year. %

| | 2005 NOK billion | 2006 | 2007 | 2008 |
|--|---------------------|-------|-------|-------|
| Consumption in households etc. | 795.7 | 4.4 | 6.3 | 3.7 |
| General government consumption | 387.5 | 3.3 | 2.7 | 3.2 |
| Gross fixed investments | 356.3 | 7.4 | 7.8 | 6.6 |
| Extraction and transport via pipelines | 88.2 | 4.4 | 6.3 | 9.9 |
| Mainland Norway | 252.0 | 8.0 | 7.6 | 6.0 |
| Exports | 862.2 | 1.6 | 2.9 | 4.6 |
| Crude oil and natural gas | 427.9 | -6.5 | -2.5 | 7.4 |
| Traditional goods | 229.6 | 5.9 | 7.8 | 3.9 |
| Imports | 534.2 | 8.2 | 8.7 | 6.1 |
| Traditional goods | 351.1 | 9.7 | 8.8 | 5.8 |
| Gross domestic product | 1 903.8 | 2.8 | 3.5 | 3.7 |
| Mainland Norway | 1 410.3 | 4.6 | 5.1 | 3.1 |
| Memorandum items: | | | | |
| Consumer price index (CPI) | .. | 2.3 | 0.8 | 2.7 |
| CPI adjusted for tax changes and excluding energy products | .. | 0.8 | 1.4 | 1.8 |
| Wage growth | .. | 4.3 | 5.6 | 5.9 |
| Employment growth | .. | 3.1 | 3.1 | 1.3 |
| Unemployment rate | .. | 3.4 | 2.6 | 2.5 |
| Household saving rate. % of net disposable income | .. | 1.3 | 0.0 | 2.0 |
| Current account balance, NOK billion | | 353.5 | 335.9 | 359.3 |

Source: Statistics Norway 2007

B. Forest products production and trade in 2006, forecasts for 2007 and 2008

| | | | Unit 1000 | 2006 | 2007 | 2008 | |
|-----------------------|------------|---------------------|----------------------------|----------------|-------|-------|-------|
| Industrial roundwood | Removals | Saw and veneer logs | m ³ | 4 204 | 4 355 | 4 505 | |
| | | Production | Pulpwood | m ³ | 4 160 | 4 260 | 4 460 |
| | | | Other industrial roundwood | m ³ | 0 | 0 | 0 |
| | | | Total | m ³ | 8 364 | 8 615 | 8 965 |
| | Imports | Saw and veneer logs | m ³ | 247 | 256 | 256 | |
| | | Pulpwood | m ³ | 2 036 | 1 723 | 1 723 | |
| | | Total | m ³ | 2 283 | 1 979 | 1 979 | |
| | Exports | Saw and veneer logs | m ³ | 255 | 201 | 201 | |
| | | Pulpwood | m ³ | 471 | 401 | 401 | |
| | | Total | m ³ | 726 | 602 | 602 | |
| Sawnwood | Production | m ³ | 2 389 | 2 429 | 2 430 | | |
| | Imports | m ³ | 1 035 | 954 | 954 | | |
| | Exports | m ³ | 474 | 277 | 302 | | |
| Wood pulp | Production | Mt | 2 303 | 2 245 | 2 250 | | |
| | Imports | Mt | 59 | 47 | 50 | | |
| | Exports | Mt | 675 | 629 | 650 | | |
| Paper and paper board | Production | Mt | 2 109 | 2 020 | 2 050 | | |
| | Imports | Mt | 608 | 592 | 600 | | |
| | Exports | Mt | 1 832 | 1 755 | 1 800 | | |

Sources: Statistics Norway, Norwegian Forest Owners Federation, The Norwegian Sawmill Industries Association, Norwegian Pulp and Paper Association