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Safeguarding the natural world

# TIMBER AND WOOD PRODUCTS

For the World Forum on Enterprise and the Environment

## Introduction

The global trade in forest products has been estimated at \$354 billion per annum, just under 1% of global gross domestic product (GDP). In 2006 (FAO figures), around 1.5 billion m<sup>3</sup> of industrial roundwood was harvested. This is generally converted into sawnwood and wood based panel production, as well as pulp and paper, high value added products. The EU is a significant consumer of timber and wood products. UK consumption was approximately 13 million m<sup>3</sup> (RWE) in 2006.

The implications of globalisation, as a major driving force in recent years, for the forestry sector, has been the reduction in transport costs, leading to increased exports of forest products and the creation of a truly global market for forest products. The overall outlook for the forest industry is one of continued growth, with some major changes expected in terms of its structure and location.

While globalisation has undoubtedly had widespread benefits (consumers have benefitted from better access to good quality, lower priced goods and services), it has also led to some negative effects. Increased competition has undoubtedly resulted in pressures to lower costs, often at the expense of adequate forest management, environmental and labour standards in certain countries, as well as the rule of law. These in turn have resulted in the undervaluing of timber as a commodity in some key developing countries, leading to unfair competition from other land uses. The challenge facing the industry today is how to remain profitable and competitive, while delivering the wider social and environmental benefits that can arise when forests are managed responsibly. At its best,

sustainable forest management can, in theory, ensure that wood has the potential to be a renewable resource. Before it can attain this state of “Nirvana” however, there are some key challenges that the global industry must overcome.

### Illegal logging and the trade in illegal timber and wood products

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Illegal logging occurs when timber is harvested, transported, processed, bought or sold in violation or circumvention of national or local laws. Illegal logging therefore describes a variety of illegal practices ranging from theft of standing timber and logs through to corrupt business practices, such as under-declaring volumes processed, or tax avoidance. Illegal logging exists because enormous profits can be made. These profits are most easily realised in countries with endemic corruption, lax law enforcement and poor social conditions, where there is little incentive to change forestry practice. It is driven by massive, indiscriminating demand for timber and wood products in developed and emerging economies in Europe, North America and Asia but it is important to note that it is also driven by demand in domestic and regional markets in the developing world. Illegal logging is a key driver of forest loss and degradation. It also hinders the development of many poor countries.

The nature of illegal logging means that there are no accurate figures on the extent of the problem, but the latest Illegal Logging and Related Trade report from the think tank Chatham House (2010), highlighted that despite reductions in recent years, illegal logging remains a major problem in producer countries. Worldwide, more than 100 million cubic metres of timber are still being cut illegally each year, leading to the degradation and possible eventual destruction of five million hectares of forest. The trade in illegally harvested timber is worth some €23 billion a year and it is estimated that illegal logging costs governments up to \$15 billion annually through lost revenues, lost assets and unpaid taxes, as well as undercutting legitimate business. The illegal logs still being cut each year, laid end to end, would stretch ten times around the Earth.

### Destructive logging

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With the current political focus on tackling the trade in illegal timber and wood products, it must also not be forgotten that legal logging does not mean sustainable logging. Much legal logging is highly destructive, so it is not enough to focus legislative processes on securing legal timber. National governments, in addition to securing adequate law enforcement relating to forests, need to implement the various commitments made under global conventions and international agreements such as the Convention on Biological Diversity (the CBD), the various international Human Rights Conventions, the United Nations Forum on Forests and the World Summit on Sustainable Development, among others. This is in addition to the agreements that exist at a regional and national level.

### Deforestation and Degradation

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Global deforestation rates are worryingly high and few developing countries are bucking the deforestation trend. The OECD State of the Environment Report 2008 cites tropical forest degradation and loss and illegal logging as a “red light” issue requiring urgent attention. Reforestation with plantations contributes towards these few positive

trends and may therefore also give rise to an underestimation of the rate at which natural forest is disappearing in other countries. The causes of deforestation are many, including logging (legal and illegal), agricultural conversion (including palm oil & ranching) and fire. The FAO expects croplands to expand by 3.8 million ha a year, exacerbating rates of forest conversion. Logging and forest conversion often provide short-term gains, but in the longer term they tend to make the poor poorer and more vulnerable, reduce biodiversity and contribute significantly to climate change.

Although forest cover has reduced from a half to 31% of the Earth's surface, forests remain home to 80% of the world's remaining terrestrial biodiversity and play a key role in balancing the global climate through carbon storage and climate adaptation. The OECD argues that without new policies and approaches the area of mature forests will further decrease by 68% in South Asia, by 26% in China and 24% in Africa by 2013. It estimates that during this period more than 1.2 million km<sup>2</sup> will be lost in Africa. Whilst reforestation and use of plantations may contribute to reversing forest loss trends, they would not prevent the risk of irreversible biodiversity loss and species extinction which will occur if deforestation continues apace.

### Valuing Ecosystem Services

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Forests are critical to the global economy. An EC commissioned study from 2008 estimated that the annual cost of forest loss (around 13 million hectares per annum) lies between \$2 trillion and \$5 trillion. This includes the impact that the loss of the various goods and services that forests provide, such as timber, secure water catchments, flood control, food, etc. This means that the global economy is losing more money from the disappearance of forests than was lost through the 2008 banking crisis.

Ecosystems provide a range of services such as fresh water, food, energy and protection from floods upon which humanity depends. Forests play a key role in providing a range of provisioning, regulating, supporting and cultural services. This explains why some 1.6 billion people are dependent directly or indirectly upon forests for their livelihoods. The Millennium Ecosystem Assessment reviewed 24 ecosystem services and found that only four were in a healthy state and that most were in decline. Forests and the services that they provide are at high risk in most, if not all, developing countries. A critical problem for improving and making more sustainable the management of the world's forests is that the services that they provide e.g. stabilisation of soils and prevention of floods are poorly recognised and under-valued by decision-makers thus allowing their degradation and loss. The degradation of forest services in Ghana has been estimated at 3.5% of GDP – a significant loss to the country's development potential and a reflection that the majority of forest services are not valued in Government economic planning and the only one that is – timber - is very much under-valued.

Decisions are often based on the value and utility of only one or a few ecosystem services (e.g. wood provision for a forest) and on what can be done with the land later on (e.g. after deforestation). There is rarely any assessment of the value of wider ecosystem services – not only carbon sequestration and storage that now has such a high profile, but also soil erosion control, water purification, maintenance of genetic diversity (for

crops and medicines) and air pollution control. The reality is that such services can have high value.

There is an urgent need to better understand and value forest ecosystem services in order to strengthen the case for sustainable (and poverty reducing) forest management. It is likely that interest in the carbon dimensions of forests will renew interest in ecosystem services but this will need to be balanced against a need to ensure that biodiversity and equity (in relation to good forest governance) issues are integrated into carbon financing arrangements.

There are other mechanisms which may also assist. These include good management planning, which takes account of and makes provision for the goods and services a particular forest provides; independent forest monitoring, which can have benefits for ecosystem services by improving forest management; timber and wood product certification, which also improves forest management and incorporates elements such as the set aside of high conservation value areas within a forest concession, watershed and water course protection, improved harvesting techniques to reduce issues such as soil erosion and soil compaction and the width of forest roads. The ongoing voluntary partnership agreements being negotiated by the EC are looking at the reform, strengthening and effective enforcement of forest governance, which could build in the valuation of ecosystem services in national forest legislation.

The finance sector at a local, national, regional and international level also still needs to step up to the challenge of ensuring that the financing of commercial forestry projects have been through adequate due diligence and environmental impact processes and that these processes do follow the rule of law in the countries concerned. Valuing ecosystem services (VES) through formal international economic structures, accepted by the WTO, must become part of the VES process.

Investors and shareholders have become increasingly important in influencing practices in a range of industries such as timber, palm oil, beef and soy. However, for investors, environmental impacts are considered irrelevant and largely ignored, unless they can be quantified and related to the companies' performance. The incorporation of adequate due diligence processes and environmental impact assessments should be standard practice, as should the inclusion of sustainability criteria in lending policies, tying loans with the adoption of best practices to avoid environmental impacts and increase productivity. This would help reduce the conversion or degradation of forests rich in biodiversity.

VES will also need to overcome the willingness to pay barrier. Customers in the supply chain are resistant to paying higher prices for certified timber and wood products, when cheaper, untraceable products are lined up alongside them. Unless businesses can capture the value of the ecosystem services in their operations, there is no business case for internalising the cost of a premium. The value of ecosystem services needs to be translated into the cost of failure to protect these services, so that businesses can factor it in as a material risk. The same applies to investors, who should address the risks around deforestation and environmental degradation associated with timber and agricultural commodities, if they are themselves convinced of the materiality of the risks to the performance of the company.

The TEEB report from 2009 highlighted that from the economic perspective, the most important gaps to be filled relate to the measurement of ecosystem services and of the ecological conditions of the ecosystems that provide them. The report considered that establishing a standardised system to measure ecosystem condition would be time consuming and that one possible solution would be to establish a global framework identifying a set of key attributes, and then monitor these, building on national indicators. The report noted that a possible way forward would be to develop simplified natural capital accounts, annually updated to assess losses and gains in the ecological potential of ecosystems, and estimate the economic costs of maintaining or restoring this capital. These accounts could then be integrated with conventional national accounts. It will be interesting to see how some of these ideas get taken forward in the coming years and what impact they will have.

