

MARKET STATEMENT 2013

1. GENERAL ECONOMIC TRENDS AFFECTING THE FOREST AND FOREST INDUSTRIES SECTOR

Since the end of 2009, the economic recession in Latvia has stopped and growth has resumed. Since the lowest point of the economy in the 3rd quarter of 2009, until the 1st quarter of 2013, the GDP has increased by 18%. Still, GDP is by 11% lower than during the pre-crisis period in 2007.

Stable growth of national economy of Latvia has been observed in 2012, although the overall GDP amount in the EU slightly decreased. In 2012, GDP in Latvia was by 5.6% higher than in 2011. The GDP growth was determined by the increase in both exports and domestic demand.

Despite the strained global economic situation, national economy of Latvia will continue growing also in 2013. In the 1st quarter of 2013, GDP was by 3.6% higher than in the 1st quarter of the previous year. Compared to the 4th quarter of 2012, GDP has increased by 1.4% (according to seasonally adjusted data).

Exports have become the economic driver in the recent years. Export volumes of goods and services have reached the highest level ever. In 2012, exports of Latvian goods and services increased by 8.3%, while in the 1st quarter of 2013 – by 2.9 per cent.

Further growth opportunities of exports will be affected not only by changes in external demand but also by competitiveness of Latvian producers. It should be taken into account that the improvement of Latvian competitiveness so far has occurred mainly due to the cuts in labour costs, however, further improvement of competitiveness will depend on the ability to raise productivity.

Positive tendencies are observed also in the domestic market. An increase in employment and a gradual rise in wages foster an increase in private consumption. In 2012, private consumption increased by 5.4%, while in the 1st quarter of 2013 it was by 4.7% higher than in the corresponding period a year ago. However, overall, private consumption falls behind the level of the 1st quarter of 2008 when it started to decline by nearly 15%. Faster recovery of private consumption is limited by the still high unemployment level.

In relation to the absorption of the EU structural funds, including public investments in infrastructure and enterprise investments in production equipment, in 2011 and in the first half of 2012, investments increased rapidly. The increase in investments is based to a great extent on investments in such sectors as energy, wood processing and production of metal articles.

Positive export tendencies foster the growth of manufacturing. As the domestic and external demand shrank significantly due to the crisis, production volumes of manufacturing also experienced a considerable decrease and were on average by 23% lower in 2009 than before the crisis – in 2007. Since the second half of 2009, production volumes have been growing in manufacturing. As economic growth resumed, manufacturing has been growing at a considerably faster pace than the overall national economy. Currently, manufacturing is the main driver of the national economic growth.

In 2012, turnover of manufacturing production increased steadily (an increase of 13.1%). The turnover grew mainly on the account of the increase in production volumes, while producer prices have been growing at a moderate pace. Due to the gradually growing demand in the domestic market, turnover of production sold in the domestic market in 2012 was by 5.5% higher than in 2011. Yet, turnover of exported production has increased by 18%, which is a proof of the still high demand for Latvian industrial production in foreign markets.

The rapid growth of manufacturing in the post-crisis period fosters an increase in labour demand. In 2012, compared to 2011, the number of filled jobs in manufacturing has increased by 5% or 5.5 thousand. Manufacturing has also contributed the most to creation of new jobs in national economy in general – the sector has ensured one fifth of all new jobs in 2012. At the same time it should be noted that the number of employed in manufacturing is growing considerably slower than the output, which is a proof of an increase in productivity.

Wood processing is one of the largest manufacturing sectors, and the sector constitutes 1/5 of the total output and all jobs in manufacturing. Wood processing was one of the first sectors to resume growth after the significant decrease in manufacturing. In 2012, production volumes of the sector continued increasing and were by 5.4% higher than in 2011. Production volumes of the sector already exceed the level of 2007 by 40 per cent.

About 3/4 of the total production in the sector is being exported, thus growth of wood processing is closely related to processes in foreign markets. In the first months of 2013, performance indicators of the sector have been slightly weaker than previously, mainly due to the economic situation in the EU countries that are the largest sales market of the sector. In the four months of 2013, production volumes were by 1.4% lower than a year ago.

The turnover of wood processing production is also growing steadily for both exported production and for production sold in the domestic market. The demand for wood production is increasing also in the domestic market, fostered by gradually increasing activities in construction, and in the four months of 2013, the volumes of production sold in the domestic market were by 5.2% higher than a year ago. At the same time, the turnover of exported production has increased by 2.9 per cent.

Both, the increase of demand for intermediate consumption goods in manufacturing **and improving situation in the domestic market foster an increase of imports**. In 2012, the volumes of goods and services imports exceeded the level of 2011 by 2.9%. Since imports grew at a slower pace than exports, the foreign trade deficit dropped to 3.3% of GDP. Although the volumes of imports have been growing relatively fast over the past few years, they still are far behind the pre-crisis level.

The **construction sector** keeps growing largely due to public contracts and the EU funds projects. In 2012, construction volumes increased by 14.6%, while in the 1st quarter of 2013 – by 9.8%. Although construction volumes have been growing quite fast over the past two years, currently they are considerably behind the pre-crisis level.

Further development of the economy of Latvia will still be closely related to the export possibilities, and therefore the highest risk to the growth of Latvia is related to global economic development.

2. POLICY MEASURES TAKEN IN YOUR COUNTRY OVER THE PAST 18 MONTHS

The **National Reform Programme of Latvia for the Implementation of the Europe 2020 Strategy** (the NRP of Latvia) was approved by the Cabinet of Ministers on April 26, 2011 along with the Convergence Programme of Latvia for 2011-2014. Both programmes were submitted to the European Commission on April 29, 2011.

The aim of Latvia is to foster growth and employment, thus ensuring growth of GDP in the amount of 4-5% in the medium term and a high employment rate in the amount of 73% by 2020. The NRP of Latvia reflects quantitative targets of Latvia for 2020 in the context of the Europe 2020 strategy (hereinafter – quantitative targets of Latvia). The quantitative targets have been defined based on the medium-term economic growth scenario, as well as the sustainable growth targets of Latvia set out in the Latvia 2030 strategy and reflected also in the National Development Plan of Latvia for 2014-2020 (NDP2020) approved by the Saeima on December 20, 2012.

According to the European semester process, on April 29, 2013, the Cabinet of Ministers approved the second Progress Report on the Implementation of the National Reform Programme of Latvia and the updated Convergence Programme of Latvia for 2013-2016. Both abovementioned documents have been submitted to the European Commission.

According to the Decision of the EU Council of Ministers on the EU Multi-Annual Financial Framework for the programming period of 2007-2013, Latvia has received EUR 4.53 billion or LVL 3.18 billion for implementing the cohesion policy objectives through the EU funds (the European Regional Development Fund – hereinafter the ERDF; the European Social Fund – hereinafter the ESF) and the CF.

As of October 31, 2012, projects for the amount of 92.5% of all financing of the EU funds available for Latvia within the given programming period have been approved, and contracts for a total of LVL 2945.4 million had been concluded. As of April 30, 2013, the funding beneficiaries have received LVL 2740.2 million.

National Industrial Policy (NIP) has been approved by the Cabinet of Ministers on May 28, 2013. As a cross-industry policy the NIP envisages implementation of activities in such areas as access to labour and improvement of skills, access to industrial space and territories, access to finance, promoting innovations, exports and limiting costs of energy resources.

Along with the NIP, the Cabinet of Ministers approved also the Guidelines for Export Promotion of Latvian Goods and Services and Attraction of Foreign Investment in 2013-2019 on May 28, 2013. Improvement of competitiveness of Latvian enterprises, targeted measures to attract foreign direct investments and support to enterprises for accessing foreign markets are the key strategic objectives defined in the guidelines that will ensure favourable environment for investments in Latvia and promote its international recognition and facilitate entry of Latvian enterprises in foreign markets.

3. MARKET DRIVERS

For Latvian forest industry main markets are located outside Latvia - more than 90% of production is being exported to EU, Asia and North Africa. In year 2012 Latvian forest industry has shown good performance - even experiencing decrease of log supply and turbulence on forest product markets, export turnover has set a new record level of 1,722 billion EUR, with positive forecast for year 2013.

Positive trend is possible due stable demand from Central European construction industry, further processing companies in Baltic countries, green energy projects in Northern Europe and expanding demand for softwood panels in CIS region.

Latvian local forest products market in late 2012 and beginning of 2013 has been influenced by extension of local energy consumption sector and expanding production of value added wood energy products. From year 2012 to 2014 more than 35 new DH/CHP/Industrial wood energy plants with capacity above 4 MW each will be in construction phase. According to „Forest and Wood Products Research and Development Institute” latest report, 17 of them already started operations in 2012. Wood building materials consumption in Latvia local market has been increasing with moderate pace. Local construction market during 2012 increased by 11%.

4. DEVELOPMENT IN FOREST PRODUCT MARKET SECTORS

4.1 Wood raw materials

In 2012 forest felling volume in Latvia declined by 9%. According to State Forest Service data 11,73 mill. m³ (sub) roundwood has been harvested, reaching normal historically average levels. Decrease of harvesting activity was noticed in State Forest land areas, with reason - lower cuttings in overaged forest areas.

Export of pulpwood declined by 31%, mainly due to lower demand from Nordic countries and increasing local softwood panels producer capacity. In the same time, relatively high competitiveness of Latvian saw-milling companies caused rapid increase imported sawlog volumes. In 2012 import of softwood sawlogs increased by 23%.

4.2. Wood energy

Woody biomass growing demand is one the main forest product market drivers in 2012 and 2013. Increase in woody biomass consumption now is going on both markets - internal (local consumption in Latvia) and export markets. Type of wood energy products used in local market and export markets are different.

For export markets positive trend is a pellet export. In year 2012 Latvia extended pellets deliveries by 48%, reached record level of 919 000 tones and has become on the leading EU suppliers. According to annual biomass market research, made by “Forest and Wood Products Research and Development Institute”, pellet production will continue a moderate expanding – some additional capacities are going to start operations in 2013/2014.

Local market consumption of woody biomass products continue to gain momentum, powered by fossil district heating systems (DH) alternation to wood chips and green electricity market development with new cogeneration (CHP) capacities starting operations. Local consumption of wood chips in 2012 expanded by 27% and continue to increase rapidly also in 2013/2014. After 2015 woody biomass consumption is forecasted to be stabilized, due to limited number of approved building permits, “freezing” new permit issues for CHP plants and additional taxes for CHP income.

4.3 Forest Certification

All forests managed by JSC „Latvijas valsts meži” are certified in accordance with the internationally approved FSC® Principles and Criteria. Since 2011 JSC "Latvian State Forests" are also certified according to the PEFC scheme. PEFC certificates have been granted to all 8 of LVM forest management regions. The PEFC forest management certification was performed by leading certification bodies within Latvia namely: BM Trada Latvija and SIA "SGS Latvija Ltd.". Certified areas in private forests are increasing, but with slow pace.

4.4 Value added products

Share of added and semi-finished wood product export extended in 2012. Export of planed sawn-timber increased by 8%. Intensive changes are noticed in prefabricated wood (panel) house production industry, export increased by 20%. New production capacities have started operations in this segment, focusing on growing demand in North European countries. Prefabricated house production expansion also is making positive influence for carpentry industry , including. wood door/window production.

4.5 Sawn softwood and hardwood

Export of sawn-wood in 2012 increased by minor 2.0%, volume of sawntimber exported was 2.3 mil. m³. Export to traditional markets like UK decreased, thus share of Central European, Asian and North African markets extended. Positive growth is reached despite lower availability of sawlogs from Latvian forests. To keep production rates, companies increased share imported logs. According to Statistical Bureau report, import from Baltic countries has risen from 210 to 354 th. m³.

4.6 Wood-based panels

Birch plywood production and softwood wood-panel production was keeping on high levels. Export of plywood increased by 6%, softwood panels export extended by 16%.

4.7 Innovative wood products

Latvian forest industry continues to develop activities in an innovative wood products area. Highly engineered wood panels for furniture and building blocks with trademark DendroLight have been tested to meet international standards. Ultra lightweight it is ultra-light (~ 300 kg/m³), has a capacity of carrying heavy loads and boasts good thermal and sound insulation properties. It allows replacing different kinds of construction materials, that shortens construction time lines and provides possibility to build passive house using wood natural capabilities of humidity regulation and thermal inertia. Also innovative wood treatment products, like Osiose Micropro has been used for sawntimber further processing. Installed treatment facilities are biggest in Baltic states.

4.8 Housing and construction

Housing and construction activity has been increased in Latvia. According to Central Statistical Bureau, construction industry turnover in 2012 increased by 22%. Increase of construction activity was focused in non-residential construction. New

residential housing (both single- and multi-family sectors) activities still are very limited due large amount of finished, but unsold properties. This category of dwellings exists on market since 2008 year crisis. Demand for multi family dwellings is undervaluted, in long term positive trend is forecasted.

5. TABLES

Key Economic Development Indicators in Latvia

	2008	2009	2010	2011	2012	2013f	2014f
(changes in comparison with the previous year, %)							
Gross domestic product	-3.3	-17.7	-0.9	5.5	5.6	4.5	4.5
Private consumption	-5.8	-22.6	2.4	4.8	5.4	5.0	5.0
Public consumption	1.6	-9.4	-7.9	1.1	-0.2	0.6	1.4
Gross fixed capital formation	-13.8	-37.4	-18.1	27.9	12.3	-0.5	3.6
Exports	2.5	-13.3	12.7	12.4	8.3	3.0	4.0
Imports	-10.0	-31.6	11.8	22.1	2.9	4.6	3.6
Consumer prices	15.4	3.5	-1.1	4.4	2.3	0.5	2.5
(% of GDP unless indicated otherwise)							
General government sector balance	-4.2	-9.7	-8.1	-3.6	-1.2	-1.1	-0.9
General government debt	19.8	36.9	44.4	41.9	40.7	44.5	41.0
Export-import balance	-13.6	-1.5	-1.4	-4.8	-3.3	-3.3	-3.4
Changes in the number of employed (aged 15-74 years)*	0.5	-12.2	-4.6	2.5	2.8	2.4	1.3
Unemployment rate (share of unemployed persons to the economically active population aged 15-74 years, %)*	7.5	16.9	18.7	16.2	14.7	12.0	9.6

f – forecast

* - data since 2011 has been recalculated according to the Population Census. Until then, all data after 2011 cannot be compared with the previous periods

Data source: Ministry of Economics of Latvia

Forest Products Production and Trade in 2012-2014

Product Code	Product	Unit	Historical data	Estimate	Forecast
			2012	2013	2014
1.2.1.C	SAWLOGS AND VENEER LOGS, CONIFEROUS				
	Removals	1000 m ³	3 917	3 839	3 839
	Imports	1000 m ³	335	559	587
	Exports	1000 m ³	196	257	252
	Apparent consumption	1000 m ³	4 056	4 141	4 174
1.2.1.NC	SAWLOGS AND VENEER LOGS, NON-CONIFEROUS				
	Removals	1000 m ³	3 078	3 078	3 078
	Imports	1000 m ³	33	10	10
	Exports	1000 m ³	152	120	120
	Apparent consumption	1000 m ³	2 958	2 968	2 968

1.2.1.NC.T	of which, tropical logs				
	Imports	1000 m ³	0	0	0
	Exports	1000 m ³	0	0	0
	Net Trade	1000 m ³	0	0	0
1.2.2.C	PULPWOOD (ROUND AND SPLIT), CONIFEROUS				
	Removals	1000 m ³	1 317	1 320	1 320
	Imports	1000 m ³	55	196	196
	Exports	1000 m ³	1 265	1 260	1 071
	Apparent consumption	1000 m ³	107	256	445
1.2.2.NC	PULPWOOD (ROUND AND SPLIT), NON-CONIFEROUS				
	Removals	1000 m ³	2 149	2 150	2 150
	Imports	1000 m ³	311	289	250
	Exports	1000 m ³	2 328	1 996	1 697
	Apparent consumption	1000 m ³	132	443	703
3	WOOD RESIDUES, CHIPS AND PARTICLES				
	Domestic supply	1000 m ³	3 726	4 308	4 530
	Imports	1000 m ³	95	174	120
	Exports	1000 m ³	3 087	3 732	3 919
	Apparent consumption	1000 m ³	734	750	731
1.2.3.C	OTHER INDUSTRIAL ROUNDWOOD, CONIFEROUS				
	Removals	1000 m ³	806	810	810
1.2.3.NC	OTHER INDUSTRIAL ROUNDWOOD, NON-CONIFEROUS				
	Removals	1000 m ³	90	90	90
1.1.C	WOOD FUEL, CONIFEROUS				
	Removals	1000 m ³	469	500	500
1.1.NC	WOOD FUEL, NON-CONIFEROUS				
	Removals	1000 m ³	704	710	710

Product Code	Product	Unit	Historical data	Estimate	Forecast
			2012	2013	2014
5.C	SAWNWOOD, CONIFEROUS				
	Production	1000 m ³	2 715	2 497	2 497
	Imports	1000 m ³	216	236	243
	Exports	1000 m ³	1 986	2 046	2 107

	Apparent consumption	1000 m ³	945	688	634
5.NC	SAWNWOOD, NON-CONIFEROUS				
	Production	1000 m ³	602	620	638
	Imports	1000 m ³	11	8	8
	Exports	1000 m ³	347	409	422
	Apparent consumption	1000 m ³	267	218	225
5.NC.T	of which, tropical sawnwood				
	Production	1000 m ³	0	0	0
	Imports	1000 m ³	1	0	0
	Exports	1000 m ³	0	0	0
	Apparent consumption	1000 m ³	1	0	0
6.1	VENEER SHEETS				
	Production	1000 m ³	0	0	0
	Imports	1000 m ³	89	126	126
	Exports	1000 m ³	1	2	2
	Apparent consumption	1000 m ³	88	125	125
6.1.NC.T	of which, tropical veneer sheets				
	Production	1000 m ³	0	0	0
	Imports	1000 m ³	0	0	0
	Exports	1000 m ³	0	0	0
	Apparent consumption	1000 m ³	0	0	0
6.2	PLYWOOD				
	Production	1000 m ³	278	292	301
	Imports	1000 m ³	35	30	31
	Exports	1000 m ³	247	244	251
	Apparent consumption	1000 m ³	65	79	81
6.2.NC.T	of which, tropical plywood				
	Production	1000 m ³	0	0	0
	Imports	1000 m ³	2	2	2
	Exports	1000 m ³	1	1	1
	Apparent consumption	1000 m ³	2	2	2
6.3	PARTICLE BOARD (including OSB)				
	Production	1000 m ³	734	808	872
	Imports	1000 m ³	38	36	39
	Exports	1000 m ³	675	688	743
	Apparent consumption	1000 m ³	97	156	168
6.3.1	of which, OSB				
	Production	1000 m ³	463	463	463
	Imports	1000 m ³	11	8	8
	Exports	1000 m ³	443	448	448
	Apparent consumption	1000 m ³	31	23	23
6.4	FIBREBOARD				
	Production	1000 m ³	0	0	0
	Imports	1000 m ³	28	27	27
	Exports	1000 m ³	5	5	5
	Apparent consumption	1000 m ³	23	22	22
6.4.1	Hardboard				

	Production	1000 m ³	0	0	0
	Imports	1000 m ³	6	6	6
	Exports	1000 m ³	4	4	4
	Apparent consumption	1000 m ³	3	2	2
6.4.2	MDF (Medium density)				
	Production	1000 m ³	0	0	0
	Imports	1000 m ³	15	14	14
	Exports	1000 m ³	2	1	1
	Apparent consumption	1000 m ³	13	13	13
6.4.3	Other fibreboard				
	Production	1000 m ³	0	0	0
	Imports	1000 m ³	7	7	7
	Exports	1000 m ³	0	0	0
	Apparent consumption	1000 m ³	7	7	7
7	WOOD PULP				
	Production	1000 m.t.	0	0	0
	Imports	1000 m.t.	0	0	0
	Exports	1000 m.t.	0	0	0
	Apparent consumption	1000 m.t.	0	0	0
10	PAPER & PAPERBOARD				
	Production	1000 m.t.	44	50	54
	Imports	1000 m.t.	165	181	181
	Exports	1000 m.t.	40	44	44
	Apparent consumption	1000 m.t.	169	187	191

Data source: Ministry of Agriculture of Latvia