Interior Lumber Manufacturers' Association

August, 2016

MAKING BRITISH COLUMBIA'S FOREST ECONOMIC ENGINE GREAT

This is the ILMA solution to major challenges facing our industry which will help ensure British Columbians' prosperity today and for generations to come. Our forests are a cherished renewable resource essential to both our economic future and the spirit of all British Columbians. Today, forest managers are at a crossroads with difficult choices that must be made to ensure the proud legacy is maintained.

"Men make history and not the other way around. In periods where there is no leadership, society stands still. Progress occurs when courageous, skillful leaders seize the opportunity to change things for the better."

—Harry S. Truman

Introduction

British Columbia's forest industry has been instrumental in building our province into one of the greatest places on earth. Our forest resource is the envy of many around the world. The people of B.C. trust us to ensure that this treasured resource is managed in a truly sustainable and effective manner so it continues to provide for the economic, social and spiritual well-being of our province. This trust is at the heart of the ILMA solution being presented here to address some of the challenges we have in B.C.

There have been substantial reductions in Annual Allowable Cuts (AAC) and more are expected in the next few years due to Mountain Pine Beetle, wildfire damage and increasing environmental constraints on the land base. More than 25% of the manufacturing facilities - largely in rural B.C. - have closed since 2007 due to industry consolidation. Despite governments' historical commitment to grow "Value-Added" production, this sector is shrinking; small and medium-sized independent mills of all makes are disappearing, and those who remain fear they will not be in business much longer.

The key to success in high-value wood manufacturing is getting consistent access to the right log to make specific high-value specialty products. In contrast, the production of commodity lumber can be effectively and economically achieved using a wide range of species. Both of these manufacturing sectors are equally important if B.C. is going to fully realize the wealth that can be derived from our forests. Optimizing the flow of logs to ensure we're getting the right log to the right mill to ensure maximum product value and potential business growth wherever possible is essential.

Forest policies since 2004 have encouraged industry consolidation; a few major companies control large, disproportionate shares of the fibre supply. ILMA companies believe that this near-monopoly coupled with falling AAC's and the lack of incentive to optimize the trade of logs will make it increasingly more difficult for high-value specialty producers and family-owned independents to survive.

FAST FACTS

- Policy reforms approved Nov. 4, 2003:
    - Eliminated timber processing and appurtenancy that required licensees to process timber harvested under their agreements at their own mill
    - Eliminated mill closure penalties
    - Timber harvesting agreement transfers no longer require Ministerial consent
    - Maintained restrictions on log exports to ensure vast majority is milled in B.C.

Today's Reality

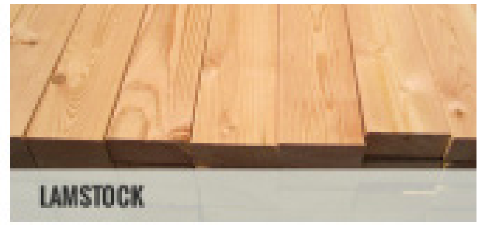
Industry consolidation continues, and the vast majority of the provincial fibre is controlled by a few major companies primarily producing standard commodity lumber products in large mills. As the provincial fibre supply is reduced, independents and specialty manufacturers will have increasing difficulties accessing enough of the right logs to remain competitive, so these sectors will continue to shrink.

Reductions in provincial timber supply are matched with a corresponding reduction in forest industry jobs, reduction in economic development primarily in rural B.C. and a reduction in government revenue. When the next downturn in the forest sector economic cycle is experienced, the lack of diversity in the forest products being produced and independent mills with the resilience to operate in poor economic cycles means an even greater impact from layoffs and closures than was experienced during the most-recent downturn.

The forest industry in B.C. is largely focused on production of standard commodity lumber making negotiations around a Softwood Lumber Agreement(SLA) with the USA increasingly more difficult.

FAST FACTS

- 2003 forest policy objectives:
  - Maximum benefits in the form of jobs and stumpage revenues
  - Significantly more timber being made available through open markets and at competitive rates
  - Every log to its highest and best use in B.C.
  - Removal of barriers to regional job creation
- Today's outcomes
  - Since 2007, more than 25% of B.C. mills closed, largely due to industry consolidation
  - Log exports went from 3.8M m^3 in 2002, to 6.4M m^3 in 2012.
  - Status quo will mean even more independent & high-value specialty mills will close



ILMA's Vision of the Future

The flow of the right log to the right mill is optimized to ensure maximum value produced and wealth generated from the public resource. Family-owned, independent mills are a priority for an equitable share of the provincial fiber supply and can compete for fiber on equal footing with large scale producers.

Large forest companies with dominant positions as a result of renewable tenures are incentivized or obligated to trade some of the high-value log profile for replacement logs suitable to their own production needs.

BC Timber Sales (BCTS) is actively targeting high-value specialty manufacturers and independent mills in their sales strategies with defined policies and target volume levels for this sector. Strict policies are put in place and strenuously enforced to ensure all Interior round-log exports are truly surplus to the province's industry needs, with the long-term objective to substantially reduce or eliminate log exports from the Interior altogether.

The reduction in provincial timber supply is offset by a corresponding growth in the level of high-value specialty manufacturing and the maintenance of small and medium-sized independent mills in rural B.C.. This ensures jobs, economic development and revenue flowing from the forest sector is maintained or grows. The forest sector has greater resilience for sustaining jobs and economic activity during future inevitable downturns because of the high degree of diversity in the products, and a reduced reliance on large, commodity lumber producers alone.

B.C.'s competitive market for logs is increased, and the volume being turned into high-value products is also increased exponentially. This creates an environment for even more independents and high-value specialty manufacturers to start, flourish and grow. SLA arguments from the USA are weakened significantly in all future negotiations.

FAST FACTS

- ILMA mills in the rural, southern interior provide 4,500 direct and indirect well-paying jobs
- ILMA mills spend more than $244M in supplies and services, most of which is local. This keeps hundreds of other small businesses going
- Independent Simon Fraser University research study 2000-2009:
  - ILMA mills created 2x more jobs/m^3 than large commodity mills
  - ILMA mills held 19% of tenure available in our local areas, but provided 43-58% of total jobs over the same area for the forest industry
  - ILMA mills operated 2-3x more days per year than large commodity mills during the last downturn, demonstrating our greater resilience for operating in below-optimal economic conditions

Call to Act Now:

Countless reviews and reports over at least the last 10 years have been undertaken to look at strategies to grow high-value specialty wood product production and the need to support small and medium-size independent mills in our province.

The value of doing this from a job-creation and wealth-generation perspective is indisputable. Our provincial government has repeatedly stated the need to focus on these objectives.

Despite all this well-meaning work and effort real tangible change has not happened. In fact, we are going in the opposite direction with a systematic shrinking of the high-value specialty product sector and the family-owned, independent mills that are at the core of many rural community economic needs.

Those remaining companies are now in survival mode. Our ILMA members can no longer accept the status quo; they want to be part of making British Columbia's forest-based economic engine great.

This is not about large commodity lumber producers versus other forest product manufacturers. It is about a strong industry on both fronts. Its essential we have a competitive commodity lumber industry because we have many logs where lumber is absolutely the best use. In fact, some of our own members also produce these products.

But when it comes to the high value log profile we must find a way to ensure that they flow to a higher end use. It is this diversity of products and manufacturers that is essential to our success in maximizing the wealth that can be generated from our cherished forest resource for future generations.

It is now time to act before today's reality becomes a future that is set in stone.

FAST FACTS

- Historical and repeated government objectives in high-value specialty manufacturing haven't been accomplished, and the sector is shrinking
- Opportunity for large growth in high-value specialty manufacturing exists, but consistent access to the right type of log is required
- ILMA mills are high-value specialty manufacturers - most are also independent, family-owned businesses - with an average of 60 years of resilient operations in rural B.C.
- Even with shrinking AAC, there is enough wood for all types of producers if we optimize and incentivize getting the right log to the right mill

Action Items:

1. Appoint a senior official in government with specific responsibility to champion growth of high-value specialty manufacturing and sustaining small and medium-sized independent mills.

   ### Outcomes:
   Consistent and deliberate attention paid to the sector at all related committees and internal discussions including support to change policy and legislation where required.

2. Ensure a non-negotiable position at the SLA negotiations that all true high-value specialty products are exempt from any trade impediments negotiated.

   ### Outcomes:
   Provides certainty to market access and relieves financial burden of extra tariffs or duties at the border required of commodity lumber products. Maintains equal competitiveness with competitors from the USA.

3. Revise BCTS mandate to include deliberate, specific objectives to support growth of high-value specialty manufacturing and support to small and medium-sized independent mills.

   ### Outcomes:
   Program and sales structure that targets and supports both the commodity lumber industry and the increase of high-value specialty products. Provides clear linkage from raw supply to production supporting the core objective of optimizing the right log to the right mill.

4. Direct BCTS to immediately establish pilot projects to test various strategies aimed at optimizing the flow of fibre with the main objective of getting the right log to the right mill and supporting small and medium-sized independent mills.

   ### Outcomes:
   Safe, justified testing environment to develop new models and sales structures that ensure the right outcomes before moving them into the mainstream Timber Sale process. Includes: how they will be incorporated into the Market Pricing System and maintain comparative revenue needs. Also ensures some immediate tangible action towards change needed to truly support growth in the high-value specialty product sector.

5. Establish a separate and new category for volume sold in BCTS (Category Y) which equates initially to 10% of the total volume sold annually in the program. This percentage is to be reviewed on an annual basis to increase it periodically until up to 25% of the total annual volume sold is in this allocation. This category is explicitly targeted to high-value, independent specialty producers and is restricted from bidders who maintain more than 200,000 m^3 in long-term tenure.

   ### Outcomes:
   Moves towards some level of equality by ensuring consistent access of the right log for high-value specialty production. Imperative, given the security and growing monopoly on the province's timber supply large commodity mills now hold.

6. Implement an incentive program for major licensees analogous with the current Grade 4 credit system. The Grade 4 program incentivizes the utilization of these low-grade logs, so the same logic can be used to incentivize the trade of high value logs to high-value specialty manufacturers.

   ### Outcomes:
   This would encourage increased trade or flow of the right logs to the right mill optimizing value and economic development opportunities. Ultimately this would help grow the high-value specialty product sector.

7. Phase-in a requirement where those with more than 200,000 m^3 and the majority of their current primary manufacturing consumption under long-term tenure are required to make available up to 15% of their products or logs for the explicit purpose of production of high-value specialty products as defined in legislation.

   ### Outcomes:
   If # 6 is effective this would be a moot issue. If there is still reluctance to support the flow of logs to optimize right log to the right mill this would make it mandatory for those not willing to voluntarily support it.

8. Ensure that any future tenure reform contains an explicit objective of incentivizing and optimizing the right log to the right mill and supporting small and medium-sized independent mills in rural B.C.

Outcomes:
This will cement this objective permanently in the future structure of our tenures and support the growth of high-value specialty product production, creating more jobs and value from our forests.

9. Increase and actively enforce a true "surplus" test for all round log export from the interior of BC. Revise the current policy for blocking export of round logs to be refined so it is species and grade-specific as apposed to the general requirement currently being imposed. Essentially allowing the block of certain species of logs from a given parcel of timber while allowing the remaining species to proceed.

Outcomes:
Decrease the volume of log export that could and should be utilized by the industry in BC. Increase the right log to the right mill for independent high-value specialty manufacturers.

LOCAL GOV'T SUPPORT

FAST FACTS
- As of Aug, 2016, this resolution has been passed by:
  - Regional District of Central Kootenay
  - Regional District of Kootenay Boundary
  - East Kootenay Regional District
  - Columbia Shuswap Regional District

"Whereas high-value forest product producers represent a critical component of local and regional economies and whose futures are seriously at risk because of unintended consequences associated with historical forest policy decisions combined with environmental outcomes resulting in dramatic reductions in provincial AAC from the Mountain Pine Beetle or other environmental constraints;

BE IT RESOLVED that the provincial government take immediate action to encourage and incentivize the distribution of provincial timber supply to optimize the right log to the right mill ensuring maximum opportunity for economic growth and the creation of jobs."

Presented to:
Honourable Steve Thomson,
Minister of Forest, Lands, & Natural Resource Operations
August 16, 2016