

India: An Emerging Market for U.S. Forest Products

By Rajat Panwar and Eric Hansen, Summer 2007

After independence in 1947, much of India's economic system was built around the erstwhile Soviet model of a planned economy. The government took the role of being the major driver of economic development with some room for private entrepreneurship, subject to heavy government scrutiny. Imports and exports were highly controlled through licenses. Realizing the changes in the global marketplace, the government of India started opening up the Indian economy in the early 1990s, and since then trade barriers are being gradually eliminated.

In recent years, the media has cluttered the news regarding India's potential role in the global economy. U.S. attention to the topic peaked last year when President Bush visited India. The population of India is growing fast (1.38 percent annually, 2006 estimates) as is its economy (with a GDP real growth rate of 7.6 percent, 2005 estimates). A growing middle class with significant disposable income is resulting in lifestyle changes and consumption patterns leading many people to see India as a major world market, surpassing the much-known reputation as a hub of information technology. All these positive signs are fueling investor confidence. However, much of the development is occurring in services or selected manufacturing sectors, and the boom has not necessarily spread to sectors such as the forest industry. Despite initial resistance from thousands of small shopkeepers in all parts of the country, large-scale retail stores and shopping malls are sprouting up in urban areas. Wal-mart is set to begin operations later this year.

The forest products industry in India consists of a huge number of small players. During the past two decades, the plywood industry has undergone technological improvements and an increase in production volumes, but as a whole, production is still very fragmented. Raw material scarcity and price fluctuations are major constraints facing the industry. Further, feeling the need for forest conservation, the government of India has placed a ban on natural forest felling, so the limited volume of timber originating from natural forests is through government auctions of those trees the forest department decides to cut. Despite the harvesting ban, demand has continued to grow, leading the industry to look for other sources of raw material.

Agroforestry provides sizeable volumes to the industry, especially the hardwood plywood sector. Imports have increased dramatically in recent years. According to a recent report from the University of Washington's Center for International Trade in Forest Products, total imports of wood products into India increased 75 percent between 2000 and 2004. Hardwoods are purchased from across Southeast Asia and some softwood comes from New Zealand. Thus, a

combination of imports, limited government supplies and agroforestry-based plantations are meeting India's present market demand. Currently, a proposal regarding development of special forestry economic zones is being considered by government that would aim at enhancing domestic raw material availability for the forest products industry.

The growing middle class in India represents over 250 million people. This middle class is a broad segment and is different from the U.S. notion of middle class. The majority of these 250 million people is on the "lower" end and would typically be comprised of junior executives with an annual income of approximately \$6,000. In terms of living style and economic status, this segment could be comparable with around \$50,000 annual income in the U.S. For the more affluent segments of society, price is often a secondary consideration to the desire for products that match their psychological notion of a Western lifestyle.

Retail outlets in many bigger cities are selling products positioned with an image of being "imported." European and American brands are especially sought after. With respect to wood products, furniture and interior doors are the biggest market opportunities for manufacturers that do not have a low cost advantage. Further, "American" brands provide a psychologically based premium in the middle-class population segment, reflected by success stories in products such as fruits (e.g., Washington apples), fast food and automobiles. Given this pattern, there is reason to expect this consumer segment to be willing to pay for well-positioned and promoted wood products. Some European companies have already established retail outlets for furniture and doors in bigger cities and are doing well.

Positive development in the housing sector creates significant opportunity for wood products in interior applications. The primary building materials in India are brick and concrete, with only a few hilly hamlets where wooden houses are built. These geographical locations may present an opportunity to educate and collaborate with architects and builders toward western-style wood houses, though architects in India have much less say regarding wood use than their U.S. counterparts. Such a shift would create opportunity for Pacific Northwest wood products. Although the Indian culture does not generally perceive wood-based housing positively, recent increases in steel prices and resulting price increases in traditional housing may make wood a more attractive building material

A huge market exists for windows and interior doors in the many houses being constructed in all the major cities of the country. According to Integrated Database India Limited web report, with an urbanization rate of 28 percent per the 2001 census, an estimated housing shortage of 22.4 million, and increasing population, India will need 80-90 million new housing units during the next two decades.

Housing developments by builders, as is typical in the United States, are just beginning in India. Builders, therefore, represent a market segment for direct collaboration. These builders typically promote the salient features of houses through advertisements, and U.S. companies should seek to have Pacific Northwest wood products included as a salient feature. This development could lead to making other Indian market segments aware of Northwest wood quality and availability.

Despite the many positive macro economic indicators, the Indian market presents many challenges for potential exporters. Understanding cultural norms and the resulting unique business behavior of traders is critical to developing long-term trade relationships. Although developing quickly, India has many infrastructure bottlenecks and challenges.

Transport times are often two to three times what might be expected in the United States. The forest products sector presents special challenges and complications based on inventory storage availability and a highly fragmented value chain. Development funding agencies in India have realized that sustained economic growth can only be realized by infrastructure development and this is on the priority agenda of the government. Nonetheless, change takes time and foreign business partners must incorporate this fact in their decision making.

India's forest products industry is dominated by small family business units. In most cases, trading activities and timber production units are passed from one generation to the next, and trade relations are based on trust and goodwill. Trade is predominantly credit based and established trust directs business terms more often than written documents. Distributors at the top end of channels usually guide the market for species selection and other attributes. These distributors tend to exploit their financial leverage and credit to influence decisions by the next actors in the value-chain. For any potential export of lumber to India, the best strategy would be to focus on these higher level distributors rather than spending time and effort in understanding market behavior that is very confusing due to cultural contrasts from the U.S.

International freight prices have been soaring in recent years and many knowledgeable persons in the forest products business in India feel that these prices will ultimately determine the inflow of forest products from the U.S. Interested exporters must find innovative ways to match neighboring international destinations with Indian ports. At the same time, high-end, niche products, especially those from species such as western redcedar could find a small, yet price insensitive market.

United States wood products exports to India have not been significant in the past. Given the need for developing new markets for U.S. wood products, India's promising economic indicators and raw material shortage, and the lowering of the tariffs by the government of India, there is

strong reason to believe that India could be a potential wood sector partner for U.S.-based manufacturers. A democratic political system in the country and English being understood by most people engaged in trade and production bolster this proposition.

Efforts from academia and government are already exploring such potential and it is expected that exports will increase in the near term. This brings opportunities for Pacific Northwest manufacturers to cater to a new market. Export market development by Pacific Northwest manufacturers is positive for woodland owners as it serves to increase overall log demand. In addition, the issue of illegal logging in Southeast Asia could dramatically alter existing trade flows into India and potentially create a competitive advantage for places such as western North America that can depend on a sound forest management reputation.

Rajat Panwar is a graduate research assistant and a member of the Forest Business Solutions Team at Oregon State University in Corvallis, Ore. He can be reached at 541-737-4343 or rajat.panwar@oregonstate.edu. Eric Hansen is professor, Forest Products Marketing, Department of Wood Science and Engineering, at Oregon State University in Corvallis. He can be reached at 541-737-4240 or eric.hansen2@oregonstate.edu.