

Steve Ehle, Editor-in-Chief, Wood Digest  
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In early May of this year, I received an E-Mail from Steve Lawser, Executive Director of WCMA to make a presentation at this meeting. I was delighted to accept the invitation of Steven and the Board of Directors of WCMA and was indeed disappointed to learn later that it would not be possible to attend in person. As a result, Steve Ehle has kindly agreed to make this presentation. Be assured that I am with you and your organization in spirit and wish all the very best at this informative meeting and in the years ahead.

Having said that, the topics that are being discussed in this presentation are different but very much linked. The first area for discussion is 'Globalization' and how it affects our woodworking industries and what 'Globalization' means today and in the future. The second area that we will touch on is 'Trends' that I see now in progress or on the horizon.

As we all know, the world has been existence for eons and has gone through change for all those many years. However, in our lifetimes, the greatest changes that have taken place in the world are not just natural changes but the persistent metamorphosis wrought by technology.

Technological advances are generated by the needs of a growing number of people in the world who want to accomplish tasks more rapidly and with greater convenience and accuracy. Technological progress is also the result of mankind's curiosity about naturally occurring events and substances, such as trees and one of their valuable components; wood products.

Globalization is really a word that conjures up visions of world trade. However, Globalization also refers to international travel as well as political and social interchange among individuals, groups and nations. For our purposes here, we will discuss Globalization in the category of world trade; exchange of products and services between nations.

In order to consider world trade in perspective, let's take a look at the events that have brought international trade to the level that it is at today. The World Trade Organization (WTO) began operations on January 1, 1995 and was an outgrowth of the General Agreement on Tariffs and Trade (GATT) that was created in 1948. While GATT was involved with trade in goods, the WTO agreements cover trade in services and intellectual property in addition to raw materials, components and finished goods.

About 151 nations are members of the WTO, with about 1/3 of that number considered 'developed countries'. Of the 2/3 of the countries considered 'developing', about 30 countries are considered 'least-developed'. Efforts are made by the WTO to assist these least-developed and developing countries to receive greater access to the products and services offered by other member nations.

Why has global trade increased so rapidly over the past several decades? We have all heard the expression; ***Necessity is the mother of invention!*** It is necessary to feed, clothe and provide a wide array of products and services to an increasingly populous world. In 1977 for example, about 4.3 billion people inhabited the world. In 2007, The US Census Bureau and other record keepers (such as Princeton University) estimate the world population at nearly 6.6 billion people and increasing at the rate of about 6.5 million per month. This amounts to an increase of more than 50% in just 30 years. This means that nearly three new human beings are added to the world's inventory of people every second.

Because the birth rates of developing nations are higher than industrialized countries, increased demand for products and services is increasing rapidly in areas where poverty and unemployment are highest. Nigeria, for example, is the 9<sup>th</sup> most populous country in the world with about 131 million citizens and a birth rate that is about triple that of the United States. Combining birth and death rates, the natural (population) increase is more than five times greater than here in the US.

Great advances in transportation and communication and have taken place in the last 30 years. In order to serve the needs of nations around the world, container ships have largely replaced bulk carriers. Ships began carrying containers between Seattle and Alaska in 1951 on vessels that had been built in Denmark that same year. The first intermodal service consisted of 600 containers shipped from British Columbia, Canada to Alaska where the containers were transferred to trucks and rail cars in 1955. Standardized intermodal containers were developed and went into general use during the 1970's and 1980's. Today, 90% of non-bulk cargo moves by container ships; more than 25% of all containers originate in China.

To develop a general perspective of the trend toward intermodal container shipping, the Maersk Danish shipping line recently launched the largest cargo ship ever built, the Emma Maersk. With a length of 1,303 feet, it is longer than any aircraft carrier. It can carry the equivalent of 14,000 20' containers of which 2,000 can be reefer containers. The ship travels at an amazing speed of 27 knots (31 MPH) with a crew of just 13. With this increased freight capacity, freight rates fell by 8% in 2006 from their peak in the fall of 2005. Freight rates for 20' containers have decreased over \$120 since then. The result is that it probably costs more to move the container to its final destination by truck than it did to transport it from China to the United States or Europe.

Remember that trains and trucks will be required to haul the millions of these containers from their intermodal ports to inland destinations in nearly every country of the world.

In the case of emergency shipments of sensitive items or delivery of such products as flowers with a short shelf life, there are giant cargo airplanes. While there are many cargo planes in use, the largest one developed to date is the AN-225, developed in Russia. This mighty giant of the skies has 6 engines that can carry a 275-ton payload at 460 MPH.

Consider the changes that have taken place in communications. Cell phones in the US in 1995 were being used by about 13% of the population. Today, nearly 70% of our population of more than 300 million have and use cell phones. Throughout the world, there are now more than 2 billion cell phones, meaning that cell phones are in use by about 1/3 of the people on the planet.

By 2002, more than one billion personal computers had been made and shipped in the preceding 27 years. This includes PC's and laptops of all manufacturers. By 1994, three million people, mostly in the US, were making use of the Internet. By the end of 2005, more than one billion users were using the Internet. The Internet has grown exponentially. By comparison, it took 38 years after the invention of the radio before 50 million people tuned in.

It took 13 years for 50 million people to buy and start wasting their time watching 'the tube'. Sixteen years went by after the introduction of the first computer 'kit' before 50 million people were using one. However, after only four years, 50 million people were sending and receiving messages via the Internet.

Computers, telephones and other electronic devices are constantly shrinking in size and cost while increasing in speed and functionality. This exponential change is due to changing digital technology. Gordon E. Moore, the co-founder of Intel, predicted these technological changes. Moore's philosophy led to the informal creation of Moore's Law that states that the number of transistors that

can be placed on a circuit will double every two years. The result of course is that digital electronic devices get smaller, more functional and less expensive.

In an interview from his home in Hawaii just last month, a Wall Street Journal reporter interviewed Gordon Moore. He commented that the cell phones of today are a 'miracle' with more features than he can use. Moore also mentioned that he was 'continually surprised by what people can do with these things'.

As in all business enterprises, our woodworking industries are affected by economic conditions that are constantly changing for better or for worse. The rate of inflation, also known as the Consumer Price Index or the Rate of Expansion was 3.3% in 2006. That index is predicted to end up in the 2.2% range in 2007. As we all painfully know, the downward trend is being led by the rapidly slowing housing industry.

It is important for us to remember that the dollars of revenue that we received last year are automatically diminished in value by 3.3% by the CPI or Rate of Expansion. That means that in order to have your company remain the same relative size (also called trading water), your revenue must increase by that 3.3%. That is a little oversimplified, however. In addition to the inflation incurred in the previous year, we probably had other increased costs that were not budgeted. Environmental costs (pollution abatement), corporate taxes, tort costs, compliance (with constantly increasing government rules), increased fuel costs (especially natural gas) and increased employee benefits are some of these peripheral expenses.

From a competitive standpoint, manufacturers in America paid 22.4% more in peripheral costs than our nine leading trading countries just three years ago. Since that time, these costs have increased by 40% to 31.7%. These same countries are also competitors in nearly all product and service areas.

These special 'penalty' costs add several percentage points each year for our manufacturers to struggle with methods to offset the increased cost of doing business. Actions that can be taken include increasing margins, cutting material costs, improving productivity and/or increasing prices. Attempting to solve the problem by one of these solutions is challenging and implementing all of the changes mentioned is bordering on the impossible. When budgeting for next year, you had better plan for a minimum increase of 10% to 11% in your top line if you want to simply stabilize your bottom line.

In addition to a reduction of 50% economic growth during 2007, the US dollar has slipped in value. As of October 5 of this year, it took two of our dollars to exchange for one UK (British) pound and our dollars were dead even with the Canadian dollar (sometimes called the Loonie after the bird on the face of the bill).

The weak US currency tends to increase the cost-of-living due to the increased cost of foreign goods, especially from China. On the other hand, capital markets here in the US become more attractive for investment. As you probably know, China has pegged its currency to float with US currency. Treasury Secretary Henry Paulson has been working tirelessly to influence the Chinese to allow their currency to float on the open market with little success. However, over the past couple years, there have been minor movements in the yuan, allowing a slightly more competitive climate to exist between the two countries.

China began letting its currency gradually rise against the dollar in 2005. This was in response to complaints by the US and other trading partners that blamed a weak Yuan for China's soaring trade surpluses. The Chinese Yuan was pegged at 8.2 in 2005 and is now at 7.51 to a dollar, an 8.4% increase in the value of the Yuan. This is a small change but the exchange rate could make

Chinese markets more attractive for US goods and services while increasing the cost of Chinese shipments to the US. The higher prices for Chinese and other imports is bad news for consumers but is welcome news for US producers and exporters.

Despite the rise in the value of the Yuan, the US trade gap with China has continued to soar to its highest level ever and is expected to reach another record in 2007. US officials are still pushing China to raise the Yuan's value in hope that it will cut the multi-billion dollar US trade deficit with China by making Chinese goods more expensive and US exports cheaper and more competitive in China.

Of our top 15 trading partner nations, China is second in size of our imports and fourth largest in exports (Canada is #1). The total imbalance of trade in 2006 with China was \$232.6 billion. In fact, the US is such a consuming nation that among the top 15 trading partners, only the Netherlands and Singapore receive more exports from the United States than we import from them.

China is one of the fastest growing economies in the world. From 1994 to 2005, the GDP has grown from \$2.61 trillion to \$8.9 trillion. Per capita GDP has increased 270% from \$2.5 thousand to \$6.8 thousand during the same period. Commercial vehicles have increased in number from five million to more than eight million.

China has been a sleeping giant in manufacturing, world trade and internal consumer spending. A vast population of employable workers has stimulated their growth. The 1.3 billion people of China represent about 20% of the world's inhabitants. Although schooling is compulsory between the ages of 6 and 14, literacy in China is almost 91%, assuring a highly trainable pool of workers. While the natural population increase in China has been modest, employment in agriculture has fallen from 60% to 49% of the workforce while employment in commerce and industry has grown considerably.

As the Chinese manufacturing juggernaut continues to roll, some chinks in their cost structure are beginning to develop. Chinese workers are involved in a public debate with government regarding wages and benefits. New labor rules and regulations are being developed and will almost certainly cause an increase in wages, and perhaps a modest increase in productivity. Recently we have all heard about the unsafe products, such as children's toys and pet food products that have been shipped to the US. Reluctantly accepting the blame for unsafe products, 180 Chinese factories have been shuttered recently.

Pollution is a big problem in China and will cost a lot to clean up. Eventually the billions of dollars of added cost for abatement will find its way into the costs of products and services originating in China. It is estimated that \$100 billion must be invested to create a refrigerated food distribution system that insures the safe handling and shipment of vegetables and meat throughout the country. These costs of modernization will also be reflected in higher costs for products and services from China.

The Chinese people want more affordable consumer goods. An example is automobiles. The number of passenger cars on the roads and highways of China have quadrupled during the past 11-years from 2.6 million to over 12 million. The people of China also are interested in more travel. Chinese airlines are growing at double-digit annual rates and although their past dismal safety record was responsible for the deaths of 550 people over three years, they are now the world leader in air safety.

If you did not read the two-part series of articles in Wood Digest in June and July of this year by your own Steve Lawser and Al Schuler of the USFS, you have missed some MUST reading. In their articles, Steve and Al quote the ugly statistics that typify the changes taking place in our wood industries.

Here are some highlights of those articles that the authors have given permission for me to repeat here:

- The furniture industries, exclusive of kitchen cabinets, have lost 108,000 jobs or 21% of their workforce between 1997 and 2005.
- The wood HH furniture sector employment has dropped by 36% while consumer demand in the US has increased by 27%.
- Wood HH furniture is now 55% imported as of 2005 and probably higher today.
- Total furniture imports now represent 28% of furniture sales, exclusive of kitchen cabinets, compared with 9% - 13 years ago.
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Perhaps the most critical of all furniture sectors that have suffered loss of market share are those that seemed least vulnerable to imports:

- Four percent of kitchen cabinets were imports as of 2005. This rate will probably grow as importers and their Chinese suppliers solve the distribution riddle.
- Upholstered furniture is 19% imported, as of 2005.\*
- Of office furniture sold in the US, 21% was foreign made as of 2005.\*

***\*Both upholstered furniture and office furniture are probably increasing in import percentage, however 2006 and 2007 statistics are not available at this time.***

These are all critical numbers in the movement of many of the woodworking manufacturing segments to foreign countries. While efforts have been made to 'level the playing field', any major changes in tariffs and trade regulations are probably unlikely. When the current administration took office, the US had three free trade accords in place. Since then, 10 more free trade agreements have been created and are operative; several other pacts are in the works in Congress at this time.

There has been tremendous pressure to expand 'free trade' throughout the world. A full-page ad featuring anti-protectionism was published in the Wednesday, August 1, 2007 edition of the Wall Street Journal. The page listed the names of 1,028 of America's top economists who advocated opposition to protectionist policies. In my humble opinion, probably less than 1% of these 'well-respected' economists ever had to meet a payroll.

Now, it's time to take a look at some trends. The absolute winner in the NUMBER ONE trend contest is GO GREEN. That happens to be the cry of my alma mater, Michigan State University, but in this case we are talking about the ecological evolution, not college sports. In some cases, this trend may have risen to be a revolution. Although the US is currently the largest CO<sub>2</sub> emitter, China is expected to eclipse the US in greenhouse gas emissions soon.

In May of this year, Citigroup, the world's largest bank by market capitalization, announced a \$50 billion dollar investment in climate-change over the next 10 years. Wal-Mart is installing solar panels in 22 stores in California and Hawaii. The Bank of America is pledging \$20 billion to help themselves and customers finance and install new technology and products.

In September of this year, leaders of the largest developed and developing countries gathered in Washington to discuss ways to cut down on pollution. Automobile manufacturers and parts suppliers are spending money to reduce emissions. Jeffrey Immelt of GE has developed a campaign dubbed 'ecoimagination' and the company is on track to sell \$14 billion of its environmentally friendly products this year. The Marriott and Starwood Hotel chains are trumpeting 'Environmentally Friendly Lodging'. They talk about organic foods, recyclable salt and pepper shakers, environmentally friendly light bulbs and heating systems.

If you are a company that employs a dozen or more people, you should start promoting environmental friendliness. The key here is to tell your customers, suppliers and employees about it.

Discuss the costs and benefits. Put reasonable expenditures in your annual budget and keep records of the results. This issue is not going away and I urge you to get on the bandwagon.

TREND # 2 is the increasing competition domestically and from foreign sources. The good news is that I see foreign products and services becoming a little more expensive. Because of the peripheral costs of doing business in their native countries, the increase will be slow and steady. Domestic producers (that's you folks) must be creative in taking advantage of some of the changes that will be taking place regarding foreign imports. Al and Steve in their June and July articles offer some good advice on actions that can be taken. Perhaps one of the most important steps you can take is to build your brand image.

Everything you produce, every action you take, and every person in your company should be focused on enhancing your BRAND IMAGE. It may be as simple as providing your sales people with shirts with the company logo on them. It may be as complex as developing a PR campaign that features the small but important features of your products that reflect increased value. Make sure that your prospects and customers always associate your company and product names with high value. Remember, products and services are purchased on the basis of perception, not just facts.

TREND # 3 is training. Steve Ehle who is reading this presentation is an expert on training. Among the companies that I deal with and have dealt with over the years, perhaps the greatest flaw that I have observed is a lack of training. Untrained people are more expensive than the cost of training. The mistakes made by partially-trained workers are incredibly expensive. When training is incomplete or inadequate, you pay the price in lost productivity. Keep in mind that the technology of operating your business efficiently requires new and growing knowledge.

TREND # 4 is the persistent, never-ending squeeze going on with the shrinking gap between costs/expenses and sales revenue. In these economic times, be sure to cut costs before you spend money that you may not have to increase sales. It may lead to serious consequences if you anticipate increased revenue next month when your markets are trending down. Cuts in costs and expenses are tough to make, but we may have another year or so of downward trends in the economic cycle, especially in our woodworking industries. And don't be tempted to increase sales by loosening your credit policies. A weak credit policy has got a lot of companies in trouble at this time.

In closing, I want you to know how important you are to your communities and to the overall economy of this great nation of ours. You are the risk-takers that make jobs, produce quality products and services and expect only a reasonable reward for taking on that risk everyday. Your customers, your suppliers and your employees in total may benefit more than you do, but they will experience nobility and pride in their work and you will triumph in showing them the way.

Thank you.

Questions? My E-Mail address is [rbaynton@rbnet.com](mailto:rbaynton@rbnet.com) Include your name, title and name and address of your company