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Mr. Chairman, I am pleased to appear before this Subcommittee to discuss the potential impact of alternative Forest Service harvest policies on the rate of inflation of wood products. In my remarks today I will address three major areas:

- o Background on the recent rates of inflation in wood prices and the potential role of the Forest Service and the Congress in reducing this **rate**.
- o The extent to which the rate of inflation in wood prices could be decreased by accelerating timber sales from the national forests.
- o The potential effects on resource depletion, regional economies, environment, and the federal budget that could accompany an acceleration of timber sales from the national forests.

BACKGROUND

Prices of wood products have escalated rapidly in recent years, contributing to the current high rate of inflation. The Producer Price Index for lumber has increased at an average annual rate of more than 13 percent since 1970—**almost** double the rate for all commodities during the same period. The price escalation of wood products affects the prices of a wide variety of industrial products because of the use of wood in many manufacturing processes. Furthermore, wood products represent about 14 percent of the costs of new housing, and therefore, this inflation has

contributed somewhat to the rapid increase in housing prices during the last several years.

Since 20 to 25 percent of the national production of timber comes from the national forests, the federal government has some direct control over the supply, and therefore the price, of timber. The recent price increases have brought pressure on the Congress to increase the timber sales from the national forests, and thereby moderate the price escalation.

The Congress can adjust the year-to-year level of timber sales by perhaps 10 percent by changing the appropriations for the Forest Service. Such funds would be used for planning, road construction, and mitigation of environmental impacts. Increases in timber sales above about 10 percent would probably require new authorizing legislation. Current law stipulates that timber production will not exceed "even flow" constraints, and that the forests are to be managed for "multiple use." Of particular importance is the provision in the National Forest Management Act of 1976 which specifies that sales or harvests of timber cannot exceed that level "which can be removed annually in perpetuity on a sustained-yield basis." More generally, the Multiple Use Act of 1960 instructs the Forest Service that no single use of the National Forests should dominate other potential uses. The decision facing the Congress is whether these laws should be modified so that more timber could be produced.

The primary benefit of an increase in timber sales is the potential restraint on future price increases of wood products. The major impediment, or cost, associated with this policy is that increased harvests might not be sustainable; that is, they would reduce the potential production of timber and other uses of the national forests for future generations. Other important potential costs include the possibility of regional economic dislocation, environmental degradation, and additional federal budget costs.

THE MAJOR BENEFIT—MODERATION OF PRICE INCREASES

Wood product prices will escalate rapidly for the next ten years regardless of public policy, because of increasing demand for wood products. Although an increase in harvests from national forests would retard price increases slightly, the effect is estimated to be small. Furthermore, the effect on prices would quickly dissipate if the increase in harvests was not maintained. There are several reasons for the small effect increased harvesting would have on prices:

- o Price increases for standing timber have been responsible for only about half of the increases in wood product prices. (Other factors are the increased costs of harvesting and of transportation.)
- o The national forests provide only 23 percent of domestic supply and they have a limited capability to expand production.

- o Domestic industries would be reluctant to expand their capacity to process timber based on what could be temporary Forest Service policies; rather they would probably substitute public timber for a portion of their own stocks.
- o The incremental production that could be supplied by the National Forests would be relatively expensive because of high harvest costs.

As a result of these factors, a continuation of the recent price escalation seems inevitable. The Producer Price Index for softwood lumber will probably increase an average of about 13 percent per year over the next decade if current levels of timber sales are continued. A moderate (14 percent) expansion in national forest timber sales could retard price escalation, but by only about half of one percent per year. A larger expansion (28 percent) could retard price escalation by 1 percent per year. Accordingly, the Producer Price Index for lumber will probably escalate at 12 to 13 percent annually throughout the next decade, with little effect from Forest Service timber sale policies. Furthermore, because the cost of wood products is only about 14 percent of total housing costs, a change in national forest harvest levels is estimated to have a very small effect on the price of new houses.

THE MAJOR COSTS OF AN INCREASE IN TIMBER SALES

The reduction in wood product prices that could be attained by accelerating forest service harvest should be compared to the various costs,

or adverse effects, that such an acceleration would generate. While the major cost is the potential reduction in our forest resources for future generations, others, such as environmental degradation and regional economic dislocation, are also important.

Resource Sustainability

The maximum sustainable harvest level cannot be definitively specified with present data. The Forest Service believes that present harvest levels are sustainable and that a margin remains for future withdrawals of land **for** other uses. The **margin** is relatively small, however, and it is composed of timber that is generally much more expensive to harvest than that now being harvested.

Some recent data are pessimistic. They indicate that the inventory which **is** available for harvest is lower than previously estimated, because of reductions through allocations of land to other uses, such as **streamside** protection, recreation, and wildlife habitat. If this information is correct, most increases in harvests could not be sustained, and even current harvest levels are called into question.

Regional Effects

The regional economic effects of an immediate increase in harvests, particularly if it is not sustained, can be adverse to the Pacific Northwest region in the long run if harvests from private lands decline. Although most analysts agree that harvests from private land **will** decline, the extent, the timing, and the effects on employment are unpredictable. Until now, the general assumption has been that, if the regional economy is greatly affected by a decline in private harvests, the national forests could compensate in part by expanding their harvests for a limited period. An increase in national forest harvests in the early 1980s, however, would reduce their ability to compensate for a decline in private harvests in the longer term. Accordingly, it might be preferable to hold whatever additional capacity is available for use at a later time when it could be more effective.

Environmental Degradation

Although CBO has not undertaken any independent analysis of the potential environmental degradation of increased harvests, other analysts expect them to have greater adverse effects per unit harvested. This will occur because they will tend to be in more ecologically fragile areas, and because they will increasingly be in areas that have high wilderness,

watershed, and other non-timber uses. Water quality, in particular, will be adversely **affected** by increased harvests.

Budgetary and Economic Effects

Any expansion of timber sales and harvests would require large federal budget increases in comparison to a continuation of current policies. The amount of increase, however, depends on the region. Generally, costs per incremental board foot are higher in the Rocky and Sierra Mountains and Alaska. They are relatively lower in the Pacific Northwest, the northwestern forests in California, and the South. The Forest Service estimates that budget costs would increase by \$300 million to \$900 million per year for expansions of 14 to 28 percent in timber sales. A large part of these costs, however, would be offset by sale receipts. On balance, the Service estimates that the **macroeconomic** benefit of harvest increases would be negative.

CONCLUSION

A modest expansion of national forest timber sales is an available option for the Congress to consider, but one which has serious drawbacks.

An expansion of harvests seems to have limited benefits and some clearly adverse effects. An expansion would not provide significant relief from the escalation of timber prices while it would contain risks with respect to depletion and the economic health of the Pacific Northwest that are not present in current harvest levels. Generally this analysis concludes that the current Forest Service timber sale policies are not obviously out of line and that expansionary policies might have adverse consequences that more than offset the beneficial price effects.

Mr. Chairman, I will be happy to answer any questions that you or other Members might have.