

# PALLET OUTLOOK

## MARKET TRENDS AND MANUFACTURING CONCERNS

BY HARDWOOD PUBLISHING COMPANY

**C**ompetition for hardwood lumber in the pallet industry and other industrial sectors continues to intensify. Moreover, rising raw material prices could force pallet manufacturers and end-users to consider substitute species or materials. In this article, we'll examine trends in pallet usage, the demand outlook and possible industry responses to rising raw material costs.

### Pallet Usage Trends

The Freedonia Group expects the pallet market to grow by 3.5% a year through 2017, according to a September 2013 report by Executive Editor Bob Trebilcock in *Modern Materials Handling* (MMH) magazine.

That's well ahead of expected growth in the general economy.

According to MMH's 2013 survey of 353 pallet-using companies, 56% said price was the most important factor in deciding which pallets to purchase and use. That bodes well for wood pallets. In fact, 91% of surveyed companies used wood pallets in 2013, nearly three times as many as used plastic pallets. However, some trends suggest wood pallets could lose some market share in 2014.

First, absolute price was less important in 2013 than in 2012. Price is still the leading decision factor but the number of companies citing it as a factor fell from 63% to 56%. Nearly 40% of companies said "cost per use" was also

important, which works against wood since users believe plastic pallets are longer-lasting and more re-usable than wood. In 2013, 34% of companies said they used more plastic pallets and 33% expect to increase their plastic pallet usage in 2014.

Second, a gradual shift away from the "standard" GMA stringer pallet could also precipitate a shift away from hardwood pallets. The GMA was still the most commonly used pallet in 2013, but it was far less dominant than in prior

years. Fifty percent of MMH survey respondents were shipping some loads on block pallets in 2013, even though Costco remains one of the few companies mandating their use.

While plastic, presswood and metal pallets are taking some market share, Trebilcock

concludes, "It is still a wooden pallet market. No alternative is as versatile and cost-effective as new, used or pooled wooden pallets."

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**- Bob Trebilcock,  
Modern Materials Handling (MMH)**

### Raw Material Crunch

Pallet manufacturers seem to have about as much control over lumber costs as they do pallet prices – very little. Analyst Jeff McBee with Pallet Enterprise, notes, "As raw material prices have climbed, pallet prices have adjusted slowly. It seems that every pallet price increase is a fight, and some pallet manufacturers only manage to move pallet prices when they have no other choice."

Low supplies along with rising demand and prices for

## Hardwood Lumber Market Overview

Severe weather across much of the hardwood producing region this winter will likely slow production, extend the inventory shortage, and keep lumber prices firm through spring. Domestic demand for hardwood lumber should recover at least as fast in 2014 as it did last year. Improvements in employment, the overall economy and new home construction will pull up demand for cabinets, flooring and furniture, as well as for pallets, railroad ties, industrial timbers, and crane mats and board road for the energy sector. The phasing out of quantitative easing will probably push mortgage rates higher in the long-term regardless of recent decreases, but the Fed won't let rates rise enough to derail the housing recovery. Hardwood lumber exports from the U.S. set a new record in 2013, and 2014 volumes should surpass it by 5 to 7%.

Sawmills will be working hard to increase lumber production to meet rising demand. However, long lead times for new mill equipment and dry kilns are hampering efforts to quickly increase production. Log prices will be equally troublesome. Some substitution for North American hardwoods by other species or even by non-wood products may occur in some markets and applications, but concerns about significant market share erosion are unfounded.

other industrial and low-grade lumber products began pushing pallet cant prices up rather quickly last summer, and prices are now almost 15% higher than a year ago. However, average prices climbed 49% for green 4/4 #2&3A Common Red Oak and 44% for frame stock during the same period, and crosstics prices rose faster than cants in actual dollars. Average pallet cant prices are currently 44% below 4/4 #2&3A Common Red Oak prices and \$165-190/MBF below frame stock and crosstic prices. While price differences do not directly correlate with net revenue differences, it is easy to see why many sawmills have turned their focus from cants to other products.

Pallet producers are facing the toughest hardwood procurement environment they've ever seen, according to McBee of Pallet Enterprise, who believes low-grade hardwood availability will be a challenge for much of 2014.

### Potential Pallet Sector Responses

There doesn't appear to be much raw material cost relief ahead for pallet producers. Sawmill production will increase 5-7% in 2014 but demand from competing sectors won't let up. Wooden pallet industry observers, however, see several reasons for hope in 2014 and less chance for market share erosion than we would have guessed.

First, pallet demand will grow in 2014 along with the economy. Wood pallets are 1/3 the cost of plastic pallets and are stronger, according to PNG Logistics, which will keep them a favorite of shippers who put heavy emphasis on cost, strength and durability – which is the majority according to the MMH survey.

Second, there has been a pronounced shortage of used

pallets – or “cores” – for several years. More than a quarter of respondents to the MMH study reported shrinking availability of used pallets, and Trebilcock said the prices of those poorer quality cores have risen significantly. In 2013,

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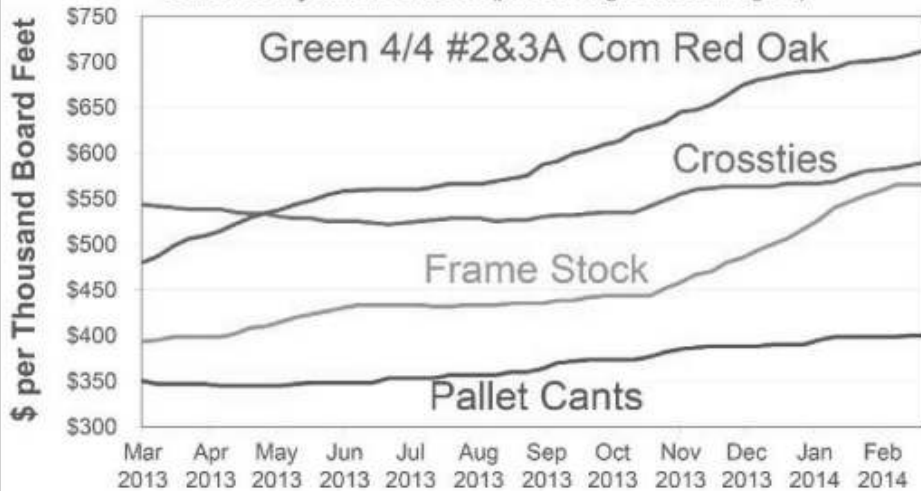
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## One-Year Price Trends for Pallet Cants vs. Other Industrial and Low-Grade Lumber Products

Source: Weekly Hardwood Review (prices averaged across all regions)



the number of companies that purchased used pallets dropped while the number that purchased new pallets rose – in part, Trebillock says, due to the shortage of used pallets.

As demand for new wood pallets grows, so too should pallet prices. Wood pallet prices are slow to move, but they are not immovable. McBee notes, “While the market may seem to be at its breaking point as far as [pallet] prices,

I believe it has some elasticity yet.” We’ll take that to mean that wooden pallets’ three-fold price advantage over plastic gives manufacturers some room to raise prices without impacting demand. “If the market were flush with raw materials,” McBee adds, “the industry has the capacity to keep pallet prices depressed and make it a buyer’s market. Tight raw material supplies, however, have flipped the leverage in the transaction and made this a seller’s market.” A quicker economy and the shortage of used pallets should give manufacturers more price leverage in 2014.

NWPCA President Brent McClendon doesn’t foresee a shift to non-wood pallets. “Our industry tracks the broader marketplace (food/beverage, construction, manufacturing, pharmaceuticals, etc.). If 2014 continues to see expansion in manufacturing, homebuilding, distribution and retail, you’ll see consistent growth in the wooden pallet sector.” **PC**

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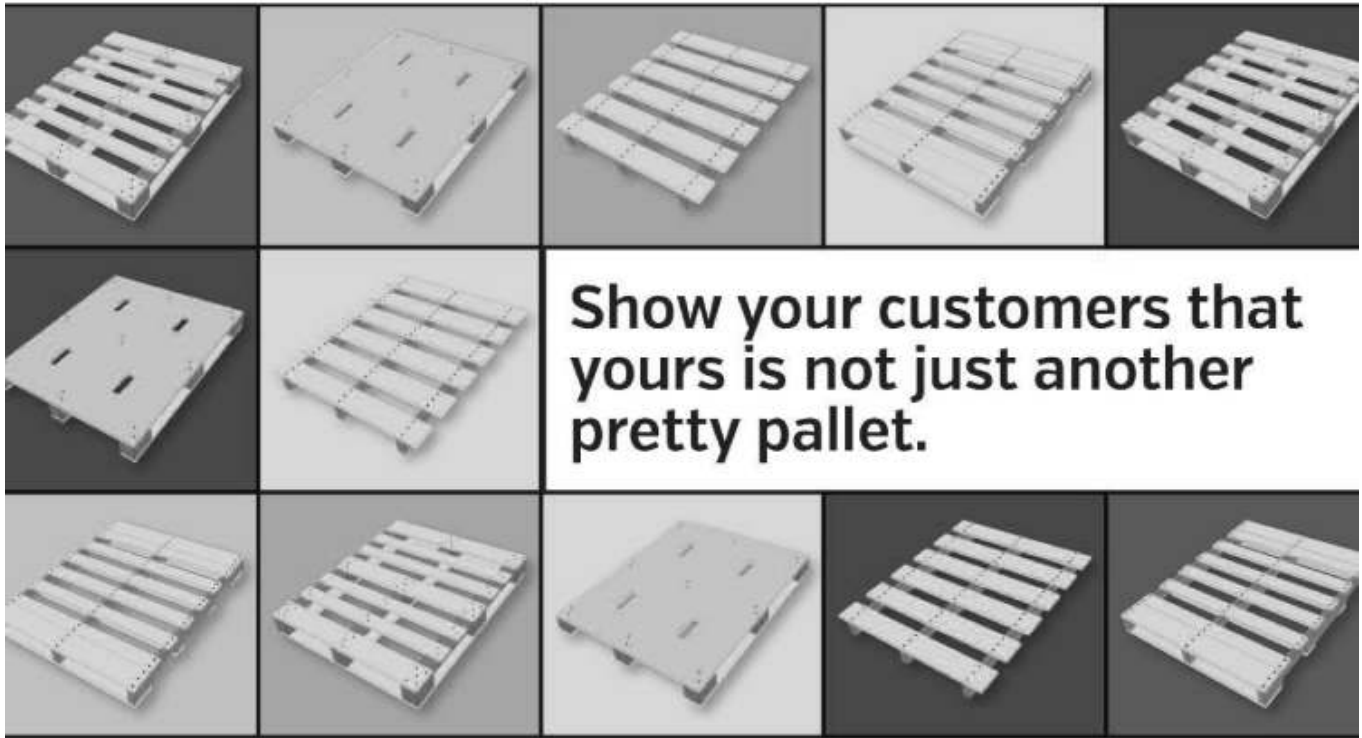


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