



**Reinventing the Forest Industry:**

**A Handbook for Would-be CEO's**

*by*

**David L. Emerson  
President and Chief Executive Officer  
Canfor Corporation  
March 26, 1999**

**CHECK AGAINST DELIVERY**

Good afternoon:

It's great to be back at the University of Alberta. As a U. of A. graduate, I have many fond memories of the University, and the education I received here has given me an excellent foundation for the many twists, turns and roundabouts of my career. I am also honoured to join the roster of impressive speakers that have preceded me over the years. For this I would like to thank Dr. Woodard and the lecture series committee.

Today, I will try to help you deal with some fundamental questions that must be of concern to most of you. Perhaps most fundamental, is the forest industry a sunset industry? The corollary of which is: Are many of you wasting your time, and your hard-earned money, preparing for a career related to the forest products business? The answers are by no means self-evident.

I will argue that there is a phenomenally interesting and rewarding opportunity in the forest products business, and the timing is right to be part of it. But, and it is a very large "but", those of us now in the industry, and those who will take our place in the future, have some formidable challenges.

The first challenge is to transform an industry that has recently destroyed billions of shareholder dollars, into one which is able to deliver superior returns to shareholders for the foreseeable future. If we don't meet this challenge head on, little else matters.

The second challenge is equally critical. The forest industry must remake its image and enhance its credibility with the general public, both at home and internationally. Failure on this front will cost us dearly. It will cost us with our customers, and it will cost us with government.

Obviously, the consumer is sovereign. They can choose to buy, or not to buy our products. Governments are also sovereign but they are ultimately servants of the general public. Their policies must be an expression of public attitudes. Which brings us back to the image and credibility of the industry in the eyes of the public.

Assuming we will have a viable industry going forward, how should students of today prepare themselves to lead the forest industry in the twenty-first century? I have a few thoughts for you to mull over as you make decisions that will shape your future.

## **TGEQPEIKVICVQP"Y KJ 'UJ CTGJ QNF GT U'CPF 'ECRW'CN'OCTMGVU"**

Let's go back to the problem of "value destruction". The institutions (pension funds, mutual funds, insurance funds, etc.) and individuals that invest in forest companies do so of their own free will. However, they have choices...many choices! In the final analysis investors will select that portfolio of investments expected to deliver the most attractive combination of risk and financial return.

Based on the Standard and Poor's Paper and Forest Products index, since 1987 total returns to shareholders in the forest products sector have lagged behind the broader market (S & P 500) by more than 50 per cent. This represents a breathtaking \$66 billion U.S. destruction of value, compared to simply investing in a broad market index. It would be much worse if we were to compare forest products with the *best* performing segments of the market!

More troubling is the fact that the Canadian industry has underperformed much of the foreign competition. In B.C., we have an additional dimension of value destruction known as the "B.C. discount". Over the past three or four years forest companies with assets concentrated in B.C. have suffered *further* discounts of up to 40 per cent. This a financial market penalty for being part of an economy afflicted with the "Asian flu"-- an economy with an anti-business investment climate, and continuing uncertainties over native land claims.

The under-performance of the forest industry in Canada has occurred in spite of the cost advantage derived from the historically low value of the Canadian dollar. If the Canadian dollar were at par, or even at its purchasing power parity rate with the U.S. dollar, the effects would have been even more disastrous.

It would be wrong simply to blame governments and external factors alone for all the problems of the industry. One can argue that weak strategic management has also contributed significantly to forest industry problems. The apparent unwillingness to recognize and adapt to the new realities of technology, environmentalism, protectionism, supply chain management, marketing and public relations can all be cited.

Regardless of where you point the finger, the reality is the same. Without the ability to attract capital, the forest industry will have extreme difficulty making substantial new investments in technology, new products, plant expansions, environmental enhancements,

more intensive forest management or, for that matter, anything that requires large upfront outlays of cash. Forgone investments will, in turn, cost jobs, destabilize communities and *further* weaken the competitive viability of the industry going forward. A bit of a "Catch 22" I would say.

For those who think the problem is not that big ... think again. The forest products industry represents the largest export contributor to Canada's balance of trade. The hundreds of thousands of jobs it supports are critical to many communities, particularly smaller communities, across the country. The stakes are very high.

This may sound depressing, but it's reality. We absolutely must restore the health and the profitability of Canada's forest industry. Small incremental changes will not be enough. Government, industry and labour must come together to galvanize their efforts around a strategic plan of action for the industry. I believe that will happen.

At Canfor we're not waiting for it. We intend to regain control over our own destiny. First, we are overhauling the entire operating side of the business, to bring every strategic business unit to high levels of profitability even under very weak market and economic conditions. Second, where a business unit cannot convincingly get over the profitability hurdle, or if we feel it's a non-core business, we will establish an exit strategy. Third, we have introduced a new capital management system to ensure higher, more robust returns on capital employed. We won't even consider strategic capital expenditure requests where the return is not in excess of 30 per cent, again, under *very* conservative market and economic assumptions. And, fourth, we are committed to growing our core business by acquisition or merger.

Consolidation and rationalization are affecting virtually every major industry in the world today, whether it is telecommunications, airlines, agriculture, retailing or forest products. Consolidation in our industry has been accelerating internationally, and it will increasingly affect the industry here in western Canada.

Sharper business focus, increased specialization, and scale economies in production, distribution and fibre supply are critical factors driving this trend. However, it is also driven by consolidation at the customer end. Home Depot, for example, is growing at more than 20 per cent per year. If you want to be one of their few strategic suppliers, you must be able to grow with them. You must have the scale and sophistication to deliver advanced supply chain management, and you must demonstrate an ability to operate at a very high level of "social responsibility". Other major customers are taking a similar approach, on both the wood products side of the business and the pulp and paper side.

Adapting to new market realities has been very demanding. Job losses, mill closures and some very painful soul searching have been a part of transforming our company. However, strength is born of adversity. Canfor is turning the corner. We took some heavy financial hits in 1998, but we also saw our operating income steadily improve. 1999 will see our company return to profitability.

## TGEQPEKINICVIQP"Y K/J "VJ G'RDNE"

Let's turn to our second challenge ... reinventing the industry's relationship with the public.

Many of the problems afflicting the industry are rooted in a deeply ingrained image problem. To many, the forest industry is a lumbering dinosaur (no pun intended), that lacks the sophistication required to be a successful modern industry, that is reckless and uncaring about the environment, and that values short term profit over longer term resource stewardship. Some might say if it's an image problem, the solution is a public relations campaign. A few million on P.R. will reshape public perceptions and all will be well.

General Motors faced a similar situation when their Oldsmobile line began losing ground to the competition. Testing consumer attitudes revealed a perception that the Oldsmobile was mainly an older person's car, not a very interesting or exciting car ... a car that your father might own. To combat that image, they mounted an ad campaign, the theme of which was "this is not your father's Oldsmobile". I don't think it solved the underlying problem, any more than Richard Nixon solved his image problem when he said, "I am not a crook".

Coming back to the forest industry, our image problem has weakened our "social licence". A poor image leads to public mistrust that, in turn, encourages government to intervene with a costly, heavy hand. This image problem will also take far more than a clever advertising campaign. It will take a penetrating and substantial reconciliation of science, economics and public policy.

Let me use Canfor once more as an example.

We have a long-standing commitment to responsible environmental and resource stewardship. As good as it has been, it's not enough. We are now deeply into a process of raising the bar to new and higher levels. We have a team of people with diverse technical backgrounds, people from inside and outside the company, developing a strategy for long term forest management. We're considering the need for protected areas, and we're looking at managing the ecosystem for the very long term.

The real trick will be to apply good science and advanced technology to forest management, and do so in a way that creates value for shareholders. To accomplish this reconciliation we will need a supportive public policy environment. For example, too many forest tenures are geographically patchy, and renewal terms are far too short for a really powerful resource management framework.

Further, the method of regulating the industry is far too cumbersome and inefficient. The government should establish the public policy framework, define the desired outcomes, and establish a system of independent checks and balances to ensure standards are being

met. What we do not need are armies of bureaucrats demanding endless reports, policing every move a company makes, and driving costs to needlessly high levels.

Public policy must recognize not only that strong environmental and resource stewardship is a fundamental public policy imperative, but also that it is very expensive. Companies must have the capacity and flexibility to innovate, apply technology and develop cost-effective ways of delivering resource and management outcomes. It will not be possible to sustain substantial enhancements in resource management, while at the same time, treating industry as a cash cow.

While in British Columbia today the situation has begun to improve, we still face stratospheric stumpage rates, taxes and fees for monopoly government services (e.g. hydro). On top of that, we have been carrying the dead-weight costs of an "in-your-face" regulatory system that delivers no public policy outcomes that can not be better achieved with a cheaper, simpler, more flexible system. Ironically, in spite of massive controls and regulation, B.C. companies continue to be the target of environmental campaigns with customers.

The final piece in the puzzle will likely require that our practices and approach be validated by a credible outside body. Certification of our forest and environmental practices is desirable, and inevitable. At Canfor, we are currently seeking to expand our ISO certification from manufacturing and environmental management to include our woodlands management. We will ultimately go further, either through Forest Stewardship Council certification or CSA certification.

With these building blocks in place, a communications strategy can have more substance – going beyond clichés and spin doctoring. It can lever off of a meaningful, solid, and verifiable foundation. Thus, we come full circle. If we regain confidence and credibility, we create a climate in which companies can be given more flexibility to deliver outcomes and be accountable for the end results, rather than being policed and monitored every costly step along the way.

## **RT GRCT KPI 'HQT 'NGCF GT UJ KR"**

Heading into the new millennium the challenges will be big, complex and subject to rapid change. Going directly from high school into a good job in the forest industry is history. A successful career in the forest industry of tomorrow means you *must react* today. You must anticipate change and be prepared.

I have somewhat perverse views on education, but they are views that have grown out of 27 years of working in a multitude of very different jobs. Here's a four-point formula you might find helpful in preparing yourself:

Get a rigorous education.

Be adaptable.

Develop your communications skills.

Develop transferable skills.

Let me explain.

First, a *rigorous education* is one that demands a lot from you. It demands that you learn how to think, how to analyse, how to stretch your mental capabilities from rote learning and memorization to understanding logical paradigms. Courses in theory, mathematics and abstract thinking, that might seem totally irrelevant, often provide the most lasting benefit because they force you to think ... and thinking is far more important than committing to memory answers to questions you may never be asked.

An ability to think allows you to get outside the "envelope" of conventional wisdom and find new ways of tackling ever more complex problems. In most "real time" situations information is missing, or it's uncertain: there may be many answers or no answers. Sometimes the most you can accomplish is to create better approaches to problem solving, or better processes of change.

Second, you must be *adaptable*. The world around us is incredibly complex and it changes rapidly, usually in ways you won't predict. Be prepared to shed old paradigms, old assumptions, and old ways of doing things. I am not advocating change for the sake of change. I am arguing that you must know when and how to adapt quickly and efficiently to evolving conditions and circumstances.

I should stress that adaptability is not just a big picture strategic need – it is day to day, hour to hour. The modern workplace is far more varied and dynamic than ever before. Multi-dimensional people engaged in multiple tasks are more the rule than the exception today.

Third, *communication* is incredibly important. Writing, speaking, gesturing, listening, interacting with people – all are important. The world's complexity knows no bounds, but communication must be clear, concise and simple. Most people in leadership positions of all kinds spend as much or more time communicating than problem solving. Indeed, good communication is often central to the problem solving process. Team approaches to problem solving can typically generate more and better solutions than the "lone wolf". And the need to communicate forces greater clarity of thought, as you no doubt have discovered in writing your term paper or theses.

Fourth and finally, think about *transferability*. Think about the options you are opening up with every major decision you make. Think about what I call the "non-preclusion principle". By that I mean, make decisions that do not preclude other choices you may wish to make down the road.

Develop skills that are transferable. Mathematics is a transferable skill. It is useful in many jobs in very different sectors. Computer skills, business literacy, finance,

economics, accounting --same story. Technical specialization in areas like forestry (or economics) is an excellent core to your education, but round it out with complementary and transferable skills.

Avoid jobs and career paths from which there is no exit, limited progression and no lateral movement. Believe me when I say you will change jobs many times. You may be *forced* to change in some cases and you will *want* to change in others. You will discover that broad-based experience -- different sectors, different jobs, different regions -- enriches your knowledge and your perspectives. And, I can confirm that diversity of experience is a highly marketable asset.

So ... get a rigorous education, be adaptable, develop your communications capabilities and focus on transferable skills and you will be in a great position to participate in the forest industry of the new millennium, or any other industry for that matter.

### **REQUIREMENTS**

The forest industry is at a historic watershed. Get profitable, deliver a consistently high return to shareholders, and do it with unusually strong public approval, or face the consequences.

It's a tall order. It will require a new breed of people to cultivate change, harness science and apply technology. It's an exciting challenge and an extraordinary opportunity.

Thank you.