

May Lumber Market Analysis

By Kéta Kosman

June 27, 2013

OVERVIEW

As the month of May plunged headlong into June, the great run-up of lumber prices through 1Q 2013 reversed in magnificent fashion. Not that prices returned to the lows both customers and producers became accustomed to in the past few years, far from it. However, the price drops of the past four weeks have effectively erased gains made at the beginning of this year.

A spurt of oversupply is credited for falling prices, although capacity at most US operations is still running below 85 per cent, and at around 90 per cent in Canada. Overall production levels aren't breaking any records, so it's not like a massive amount of unwanted wood is floating around the continent. The mysterious rumblings out of customers in China throughout May caused a lot of confusion: traders from that country quietly bought Canadian studs in April, from British Columbian producers, in enough volumes to drive that price right out of reach of traditional North American customers. That spike was, of course, not sustained. However benchmark WSPF KD 2x4 #2&Btr studs in the last week of May settled at US\$335 mfbm, almost exactly where they were at the start of January.

Prices are in U.S. dollars per 1,000 fbm.

Key Prices

	This Week	Last Week	Change	Month Ago	Change	Year Ago	Change
WSPF KD R/L 2x4	295	302	-7	326	-31	298	-3
WSPF KD R/L 2x6	278	294	-16	322	-44	290	-12
WSPF KD R/L 2x8	288	300	-12	312	-24	314	-26
WSPF KD R/L 2x10	324	320	+4	334	-10	368	-44
WSPF KD PET 2x4 Stud	290	316	-26	335	-45	345	-55
WSPF KD PET 2x6 Stud	285	315	-30	340	-55	355	-70
Douglas Fir Green R/L 2x4	270	255	+15	330	-60	338	+32
Douglas Fir Green R/L 2x10	350	365	-15	390	-40	268	+82
ESPF KD 2x4 8ft Stud	370	380	-10	430	-60	410	-40
OSB Ontario 7/16" (CDN\$)	290	295	-5	360	-70	255	+35
CSplywood Toronto 3/8" (CDN\$)	335	326	+9	348	-13	410	-75

The threat of a potential return of softwood lumber export taxes in August only prompted Canadian traders to rush yet more wood across the US border through June against this supposed ticking clock. Should the export tax come into play it will be at only the five per cent rate at first, while overshipping could bring commodity prices down by more than that ratio. The strategy of sending higher volumes of wood than are currently needed just to avoid taxes is questionable at best. In previous years those excessive volumes shipped to US domestic markets only further dampened demand, and kept prices depressed for even longer than they would have been had Canadian producers not tried to beat the export tax.

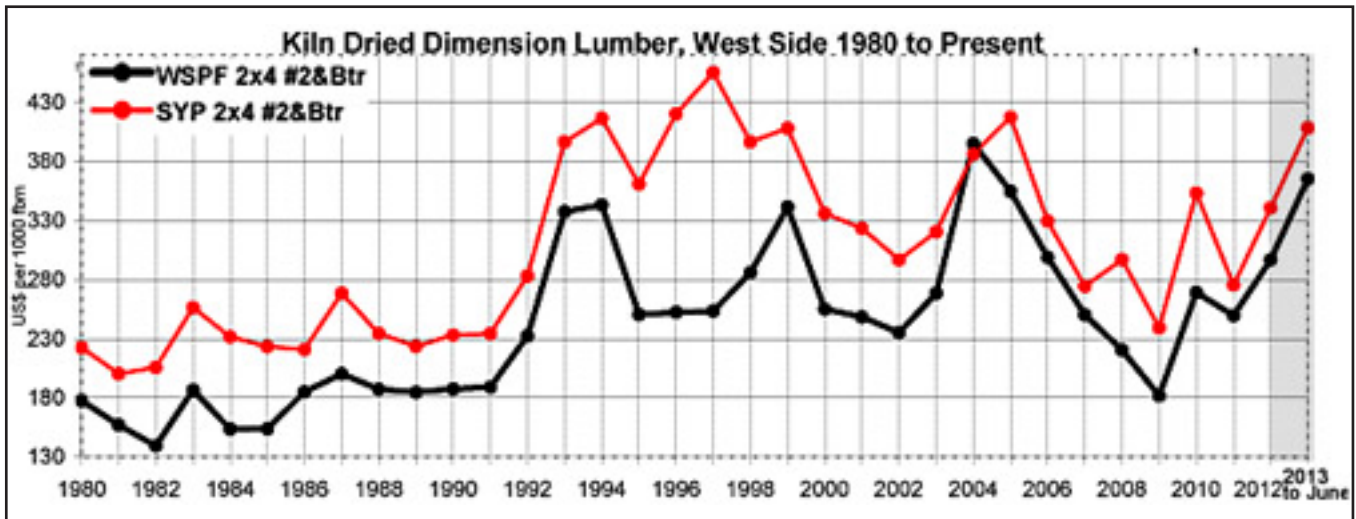
Key ideas for May 2013 lumber and panel markets:

- A bearish futures board lead commodity prices down even further; studs crashed hard.
- The pulse of commodity-trading was faint this week.
- The current tenuous supply-demand balance was still in 'price-discovery mode'.
- Sales picked up late in the week in response to up-limit lumber futures.

A bearish futures board lead commodity prices down even further; studs crashed hard.

MAY WEEK ONE RECAP

- As May dawned, American traders lamented the pervasive lack of buying momentum across almost all species and commodity groups.
- Western studs-producers pushed their asking prices down by a hefty margin in an effort to find business.
- Prices of all green Douglas-Fir commodities were sucked down along with the rest of the lumber commodities.
- Superfluous volumes of Canadian KD Douglas-fir crushed those prices in this re-tracement.



SHORT TERM ANALYSIS

The assessment of some in the industry that producers ramped up capacity too much too quickly, after the surge of sales in early 2013, does seem to have merit when looking at what immediately happened to lumber prices. But compared to historic trends the run-up of production in 1Q is barely noticeable. It seems unlikely that a small blip in increased lumber manufacturing, especially after such an extended downturn, could have such a drastic effect on prices.

In this situation it seems that perception is playing a huge role. Buyers absolutely balked at steadily rising prices in February. Once the price increases reversed and the subsequent drops became ever-steeper, it seemed like customers were out to punish mills for daring to actually make some profit.

Current lumber price levels might seem incredibly high when compared to 2010, but they are actually still quite weak compared to the long term trend.

The pulse of commodity-trading was faint this week.

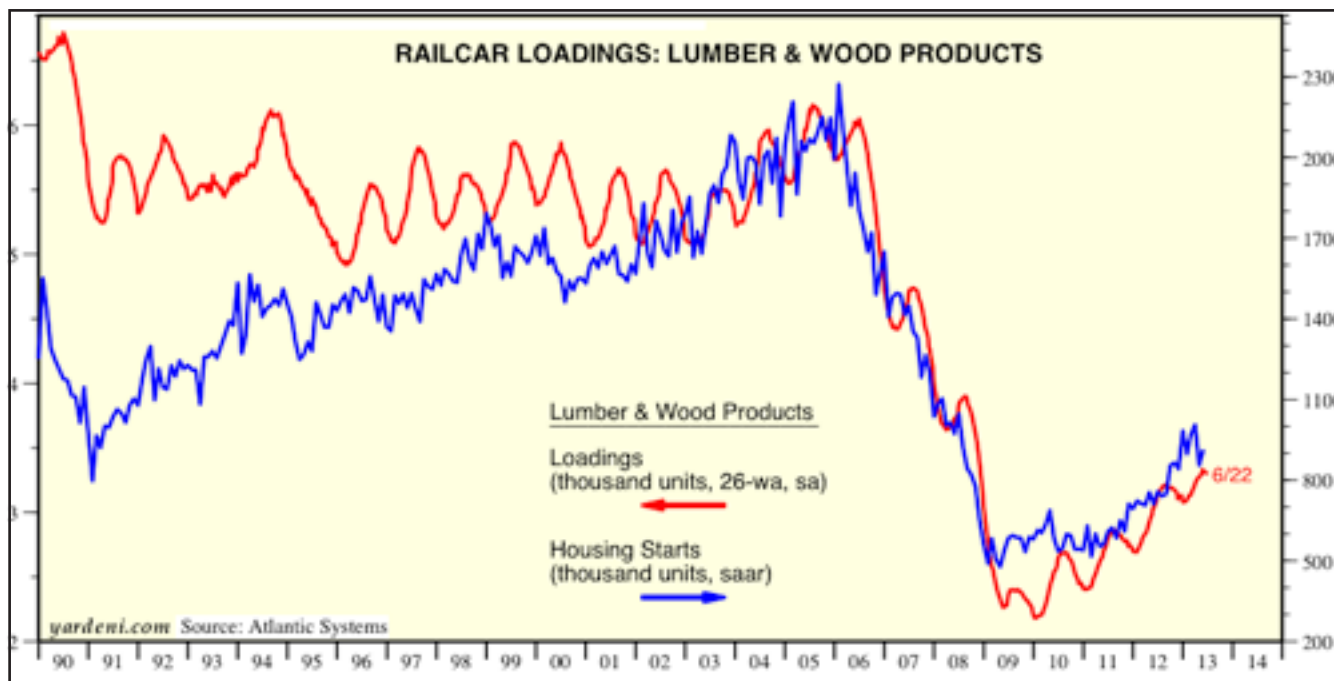
MAY WEEK TWO RECAP

- In the second week of May secondaries were content to wait even longer for lower prices even as their WSPF inventories dwindled away.
- Anything American traders did manage to sell was at a loss.
- Dangerously low field inventories, and ever-falling prices, of green Douglas fir items prompted a fierce round of buying in the second week of May.
- With OSB and plywood sales soft and prices dropping, panel traders roundly declared the month of May so far a dud.

SHORT TERM ANALYSIS

The first half of 2013 has been lopsided thus far; early in the year there was so much inquiry that producers and transportation services couldn't keep up with demand. By May - usually the busiest time of the year for harvesting timber and trading lumber - demand was curiously absent.

Wholesalers and secondary suppliers alike expressed concern at looming losses over the coming weeks if demand didn't pick up. Having bought at the absolute high, they collectively held sizable volumes of wood which they could only lose money on. The race to unload this expensive wood was afoot.

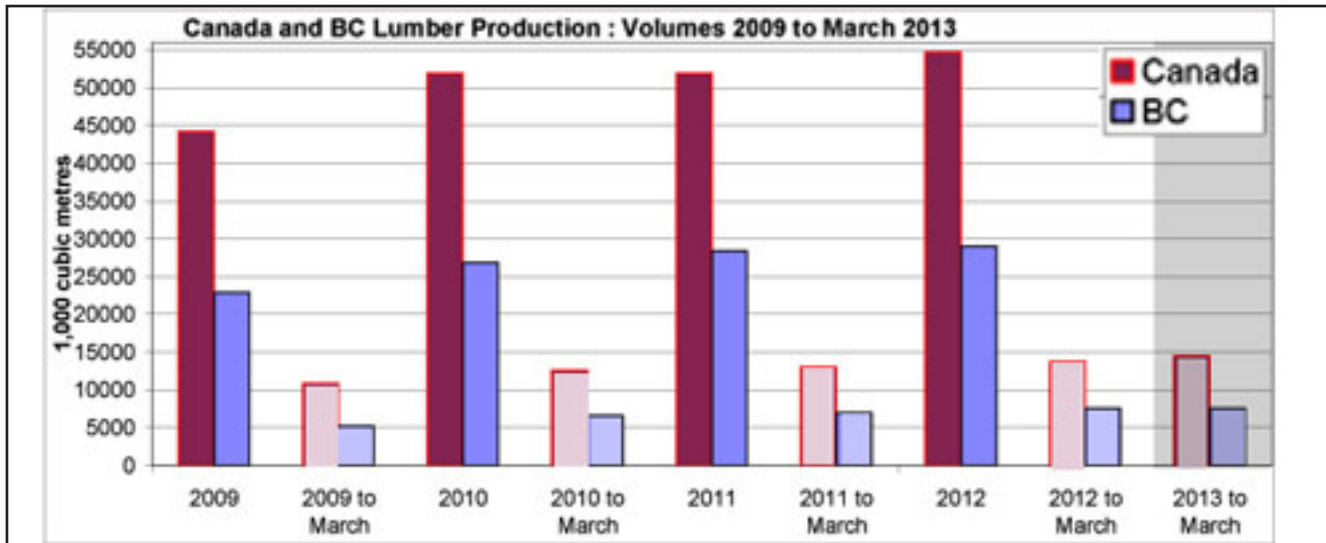


Eastern producers of OSB and plywood found they had to push their wood out through yards, as the direct loads they had gotten used to were sparse in mid-May. Mills also indicated that they had tapped out their export markets. Discounted loads flowed freely as players talked each other down in an effort to keep sheets moving. A trend seemed to be emerging in that retailers, wholesalers, distributors, and brokers in North America were content whittling down their inventories while they wait for the market to move.

The current tenuous supply-demand balance was still in 'price-discovery mode'

MAY WEEK THREE RECAP

- By mid-May producers reported concern about the lack of inquiry – and subsequent buying – from customers in China.
- WSPF traders brought low-quality wood in to the East in an attempt to conserve some sales momentum, but that wood displaced sales of ESPF in a frustrating way.
- Veteran stocking wholesalers in the US Northeast declared the lumber market over for this summer, saying there wouldn't be any more than a \$10 price movement in either direction until after Labour Day.



SHORT TERM ANALYSIS

Rumours circulated in mid-May that China had indicated it might pull out of some contract business for June and July. That populous nation apparently has enough wood to see them through their down season, which began recently. This is a worrisome potential outcome for folks in the North American lumber game; if it comes to pass, what is to be done with that extra production in the pipeline?

A recent influx of western wood into ESPF territory apparently knocked some screws loose in that market. Customers were desperate to keep lumber in their inventories, but were not willing to pay much. Trucks of this western wood represent in the range of a \$2,000 discount to the same volume of native Eastern species. In times like these, notoriously disloyal buyers are jumping on those loads.

Sales picked up late in the week in response to up-limit lumber futures.

MAY WEEK FOUR RECAP

- As the month of May wound down, no one knew what the heck tradable price bottoms would turn out to be.
- Volumes of OSB and plywood at mills and in wholesaler yards throughout the supply chain were getting noticeably low in the last week of May.
- As May waned and the futures board popped up for the first time in recent memory, many WSPF customers decided that it was time to jump in and buy.
- By the end of May, ESPF producers quoted prices fairly in line with print levels, making it clear that they were ready and willing to accept counter-offers.

SHORT TERM ANALYSIS

As a depressing month of May quietly drew to a close, the absence of North American demand – normally strong as you please at this time of year – was all too noticeable for Canadian WSPF producers. In the coming weeks, they will do everything in their power to move loads at price levels that will keep them above the softwood lumber export tax threshold.

Stocking wholesalers in the US eastern seaboard collectively blamed lumber manufacturers for the inexorable price drops, and said they won't be trusting wood makers again anytime soon. The feeling was that no one in the US Northeast made any money during the month of May, and mills are almost wholly to blame.

CONCLUSION

By June, actual price levels to the end user were well below mill asking prices. Those sawmills did anything they could to move their inventories. Just as with their cohorts in the West, ESPF producers are feeling the irritating pressure of trying to deal with recently increased capacities brought on by a bullish 1Q. Mills cannot simply turn their production on and off like a faucet; any added shifts and on-line machines are costly to idle.

At this time of year, when the US building season is traditionally at its most busy, lumber producers and resellers would normally not be shy about buying wood and about building inventories. In 2013 though, the huge run-up of prices right from the beginning of the year caused shock as players expressed a lack of confidence that the price spikes could be sustained even in the short term. Sawmills gleefully brought capacity just a little bit higher – all the while resolutely keeping prices up – sending customers into borderline panic mode.

Their fear was not entirely misplaced as a combination of atrocious service by the major Canadian railways and an abrupt turn-around in price momentum resulted in secondary suppliers holding wood on which they were consistently losing \$60 or more per thousand board feet. However the volume of sales at these losing prices is quite low compared to how much lumber would normally be changing hands at this time of year.

It seems that perception ruled June. A falsely bearish perception ruled by fear. It is almost unheard of that sawmill order files go from three or four weeks in March to barely a few days in May. The tenacity of the negative sentiment is as difficult to explain as it is to deny.