

MADISON'S LUMBER REPORTER



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News & Updates

Madison's Timber Preview

This week's issue of *Madison's Timber Preview* examines the recent upswing in share prices for several North American forest products companies. Among others, West Fraser Timber and Canfor had inexplicable rebounds on the stock market, all the more puzzling given dismal 2Q results.

Contact us any time for a subscription.

Home Sales

Pending home sales in the US, considered a leading indicator because closings typically follow a month or two later, rose 3.6 per cent in June, compared to May—the fifth consecutive monthly increase. That's the longest streak of increases in six years. Signed home-purchase agreements in the US rose in June to the highest monthly level in two years, according to the National Association of Realtors' pending home sales index that was released on August 4.

Meanwhile, the national median home price fell 16 per cent from a year earlier to \$174,100, the National Association of Realtors said Wednesday. Distressed homes, which accounted for 36 per cent of the deals in the quarter, typically sell for 15 to 20 per cent less than traditional homes, skewing the median prices.

Total existing-home sales, including single-family and condominium sales, were at a seasonally adjusted annual rate of 4.76 million units in the second quarter, down 3 per cent from last year and up 4 per cent sequentially.

In other news, Toronto-based Brookfield Asset Management is betting the real estate market has hit bottom, and announced plans Tuesday to back its contrarian wager by raising a stunning \$4.9 billion to buy homes, office towers and shopping malls around the globe.

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Canadian Housing Starts

Housing starts in Canada fell in July to a seasonally-adjusted annual rate of 132,100 from 137,800 in June, Canada Mortgage and Housing Corp. said Tuesday. In urban areas, housing starts fell 5.5 per cent in July, driven largely by the 9 per-cent drop in the "multiple starts" segment. Construction of single homes edged down 1.1 per cent.

"The slight decline in July's housing starts is mostly attributable to the volatile multiple starts segment," said Bub Dugan, chief economist of the agency's Market Analysis Centre. "Although July registered a decline, housing starts are expected to improve throughout 2009."

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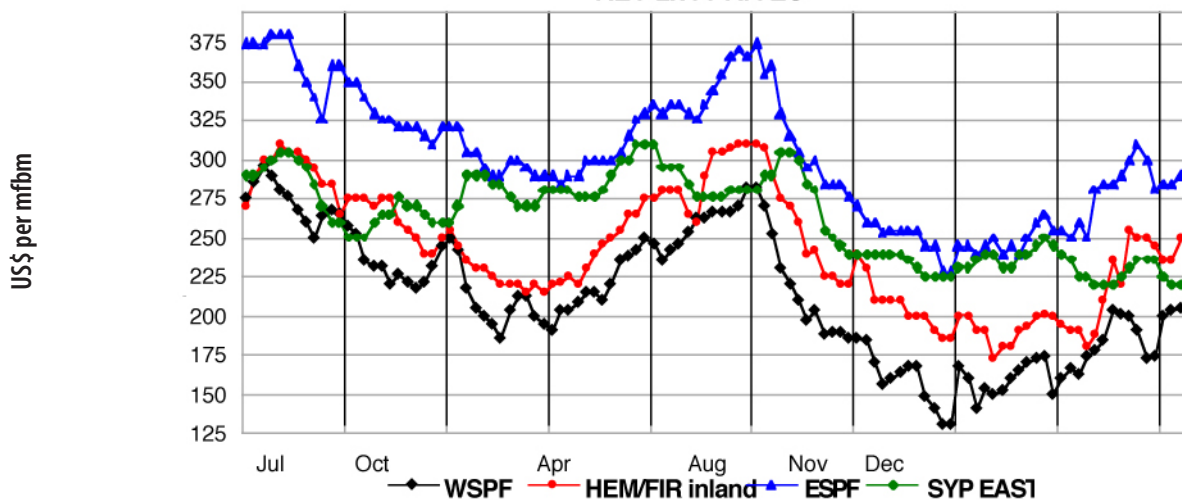
Forest Industry Globally

Once again Ontario's Sino-Forest Products has outperformed expectations on the stock market. First studied in one year ago in *Madison's*, Sino-Forest has just posted financial results significantly higher than expected.

Deltic Timber, Plum Creek and Domtar have all seen a rebound in share prices in the past two months.

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KEY 2x4 PRICES



Key Prices

	This Week	Last Week	Change	Month Ago	Change	Year Ago	Change
WSPF KD R/L 2x4	205	204	+1	173	+32	282	-77
WSPF KD R/L 2x6	201	199	+2	190	+11	300	-99
WSPF KD R/L 2x8	228	225	+3	225	+3	288	-60
WSPF KD R/L 2x10	317	320	-3	310	+7	295	+22
WSPF KD PET 2x4 Stud	210	205	+5	195	+15	220	-10
Douglas Fir Green R/L 2x4	170	168	+2	163	+7	194	-24
Douglas Fir Green R/L 2x10	260	250	+10	240	+20	240	+20
ESPF KD 2x4 8ft Stud	285	285	0	285	0	295	-10
OSB Ontario 7/16" (CDN\$)	220	220	0	220	0	215	+5

Weekly News

Brookfield's Big US Real Estate Buy

CONTINUED There are 3,200 unfinished McMansions sitting in a suburban Los Angeles neighbourhood, where developers spent more than US\$150 million to build sewers, grade lots and pave roads for an upscale development, only to see the market crash.

These homes are at the heart of the real estate meltdown and Brookfield recently bought this Riverside, CA, development out of bankruptcy – for 20 cents on the dollar.

Calling a bottom to the real estate market is not for the faint-of-heart. Brookfield is planning to buy at a time when US house prices continue to fall, and mall and office building owners are struggling to keep tenants and collect rent.

"We do know this is currently one of the worst residential markets in the US," Brookfield chief executive officer Bruce Platt said in explaining the Riverside project during a conference call last Friday.

"However, just to put it into perspective, the lots are within an hour of Los Angeles [and] were purchased for less than 10 per cent of the value attributed to land and infrastructure at the peak. ... So these are at pretty low values."

Canadian Home Building

CONTINUED "The setback in Canadian residential construction activity in July is likely a temporary bump on the road to recovery, especially when taken in combination with surging permits and home sales," said BMO Nesbitt Burns economist Robert Kavcic. "Still, housing starts will likely remain below the 175,000 rate of housing formation through 2010, a far cry from pre-recession levels that consistently ran in the 225,000 range for six years."

Housing starts are expected over the next several years to reach an annual rate of 175,000, which the CMHC said more closely matches demand.

In Quebec, which has shown surprising resilience during the recession, construction starts increased 16.6 per cent.

The prairies, Ontario, British Columbia and Atlantic Canada all registered declines.

The slump in the real estate industry, though over all now clearly on the rebound, has had a widespread ripple effect.

Meanwhile, Canadians are still in the housing market, as more homes were sold last month than any previous July on record.

The Canadian Real Estate Association said Friday that 50,270 homes traded hands on the Multiple Listing Service in July. That's 18.2 per cent more than in July, 2008.

On a seasonally adjusted basis, resales are only 1.4 per cent below the peak reached in May, 2007.

The average price rose by 7.6 per cent to \$362,800 over 12 months.

BC Labour Issues

After a brief break, the United Steelworkers were back at the negotiating table with the CONIFER employer group this week.

Bob Matters, Wood Council Chair for the Steelworkers told *Madison's* on Friday that the two sides are still talking, which he sees as a good sign. The next round of talks is scheduled for three days next week, which Matters also finds encouraging.

He did say that so far "there is only agreement on a couple of items, which were on the union agenda." Specifically these items are related to job security issues, which is high on the union's list of priorities.

Matters said that the union strategy is to "take small steps in addressing key issues of job security, and to keep attention there."

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The Continued Changing Face of the Lumber Business

A Global Industry

First highlighted in the August 14, 2008 issue of your *Madison's Reporter*, Mississauga, ON, based Sino-Forest Products

by Kéta Kosman

is once again making news for big moves forward on the stock market. As the largest forest operator in China, Sino-Forest owns and manages about 434,000 hectares of plantation trees in China and derives most of its revenue from there, selling wood products needed for infrastructure investment and the rebounding housing market. The company surpassed analysts' expectations with second quarter profit of US\$45 million, or 23 cents a share, compared with US\$43 million a year earlier. Revenue increased by more than 21 per cent to \$224 million, the company said in its earnings report Monday.

Sino-Forest's stock gained 22 cents, or 1.36 per cent, after the earnings release. In the past year, the shares have ranged from a low of \$5.25 to a high of \$20.03. The company has a market capitalization of a little over \$3 billion. At Thursday's close, Sino-Forest shares were trading at \$15.99.

While headquartered in Canada, Sino-Forest has significant operations in China and is well positioned to take advantage of recovery in the Chinese economy, expected to be in the very near future. Goldman Sachs has raised its forecast for Asian economic growth this year and next, projecting that China's gross domestic product will grow by 9.4 per cent this year and 12 per cent in 2010. China had earlier announced a 4 trillion yuan (US\$585 billion) stimulus package, aimed at providing an impetus to its domestic economy. The plan included initiatives such as construction of low-cost houses and rail projects that could boost demand for wooden logs. Sino-Forest said that while fibre prices remained steady during the quarter, it anticipates log prices will return to 2008 levels by the end of this year.

The company, which operates in nine provinces in China, expects wood log prices to rebound about 5 per cent to 10 per cent in the latter part of this year, from their low level in 2008, it said in a presentation on its website.

Sino-Forest's advantages globally include the strength of the Chinese economy, the Russian log export tax, currency exchange rates, and oceangoing freight rates. The company earns about 70 per cent of its

annual earnings in the second half of the year, mainly due to its harvesting cycle.

Two other timber companies being closely watched on the stock market, this time out of the US, are Plum Creek Timber and Deltic Timber. According to financial analysts at TheStreet.com, "Housing starts will eventually recover. Soleil's Anna Torma believes she is conservative in hoping for starts to return to 1 million or so in 2012. That would drive demand for lumber. The catalyst is that about one-third of US lumber needs have historically come from Canada, and half of that comes from British Columbia, where there is a terrible infestation of mountain pine beetles. Significant capacity has been closed in Canada, and this infestation will affect the harvest for decades. [. . .] These stocks have limited downside risk and over the next two years could show more-than-acceptable appreciation with any sort of US economic recovery," according to TheStreet.com.

A Canadian company that is finally seeing the positive results of difficult financial decisions in 2008 is paper producer Cascades Inc., which this week announced second quarter profit of \$30 million, or 30 cents a share, on Tuesday. Profit for the quarter ended June 30 rebounded from a loss of \$25 million in the second quarter of 2008. "Our results have shown significant progress since the trough experienced in the first half of 2008," Alain Lemaire, chief executive of Cascades, said. "Results improved in all our sectors as we benefited from a favourable variable cost environment." Based in Quebec, Cascades produces packaging and tissue

products mainly from recycled material. The company employs almost 13,000 people in North America and Europe.

Last week, US hardwood flooring retailer Lumber Liquidators Inc. said its profit grew 18 per cent in the second quarter as consumers snapped up the company's products and gravitated to stores in new markets. Sales for the quarter ended June 30 increased 12 per cent to US\$143 million from US\$128 million. Lumber Liquidators attributed the rise to its ability to drive increases in traffic by leveraging the appeal of its value proposition. The company opened eight new stores during the quarter and said sales at its new locations grew US\$17 million over the same period one year ago. Lumber Liquidators is the largest specialty retailer of hardwood flooring in the US.

While, for the moment, most solid wood commodity prices continue to be depressed, strict adherence to mill closure and curtailment policies by the large-volume, low-cost producers until demand comes back seems to be serving most company financial positions well.

Lumber and panel inventories, at the mill level as well as with stocking wholesalers and retail yards, are currently very low. All eyes are watching the US real estate market, which may be showing the first signs of hiccuping back into gear. Once home sale activity returns, the inventory of unsold homes, both new and existing, will disappear very quickly. Simultaneously, US new home building will resurge, demand for solid wood products will rise sharply, and North American lumber mills will start up with a vengeance.

