



# MADISON'S TIMBER PREVIEW

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There are a lot of questions being asked about the recent storm in the US northeast, and what effect the rebuilding and reconstruction will have on solid wood prices in the next few months. Some industry watchers look to the devastation caused by Hurricane Katrina, which hit the US gulf coast in August 2005, for an example of how the lumber market will react. Katrina is not a fair comparison. Hurricane Andrew, making landfall in Florida in late August 1992, was a more similar situation. At that time retailers raised plywood prices in advance of the storm by US\$100 in one day, as people rushed to buy materials to board up their houses. This ruthless act led to charges of antitrust and price fixing, and prompted Florida to pass anti "price-gouging" laws.

A parallel can be drawn, however, between Sandy and the series of tornadoes which hit the US mid-west in spring 2011. The rebuilding from that disaster was served entirely by lumber produced locally, as determined by a study undertaken by BC Forest Innovation Investment (BCFii). At that time, demand for wood products in North America was so low that there were no ripple effects of higher lumber prices during and after the rebuilding.

The supply-demand balance for solid wood in North America is completely different now than it was in spring 2011. It is likely that the 30,000 to 40,000 homes which were destroyed last week -- if they will indeed be rebuilt in the same style on the same location -- will again source materials from local operators. However, wood supplies currently are so tight, and inventories are so low, that this time the spate of ordering -- when it eventually does happen -- will absolutely have an effect on prices in other species and regions.

There are several reasons for this.

The latest figures on North American sawmill capacity, released Monday by the Western Wood Products Association (WWPA), show increased production compared to recent years but also room for improvement.

The WWPA pegs US softwood lumber production for January to August 2012 at 19.2 billion board feet, a 7.2 per cent increase over 17.4 billion board feet in the same time period one year ago. The largest improvement, of 9.4 per cent, was in the west, which produced 8.6 billion board feet in the first eight months of 2012, compared to 7.9 billion board feet in 2011.

Canadian producers also experienced recovery of lumber demand this year. Canadian lumber production January to August 2012 was 15.5 billion board feet, a 4.7 per cent increase over 14.8 billion board feet one year ago. In Canada it was companies east of the Rockies, assuredly led to a large degree by Alberta, which had the greatest improvement, of 6.1 per cent, from 6.7 billion board feet in 2011 to 7.0 billion board feet for the first eight months of this year.

Using the previous year as a comparison, US softwood lumber production for that time frame increased by 8.8 per cent from 2010 to 2011, while in Canada it increased by 2.3 per cent.

For its part, sawmill capacity in the US went from 69 per cent in the first eight months of 2010 to 73 per cent in 2011 and 78 per cent this year. In Canada the rates improved to a similar degree, with sawmill capacity going from 74 per cent in 2010 to 79 per cent in 2011 and 83 per cent this year.

Inventories, meanwhile, are severely depleted. *Madison's* has been warning for the better part of this year that a supply crunch is coming, and it seems to be upon us now. When 1Q 2013 dawns, companies are sure to announce the restart and reopening of operations. In the US, softwood lumber inventories have grown at a relatively stable rate, of 5.2 per cent from 2010 to 2011, and by 4.1 per cent from last year to this. In Canada the numbers tell a completely different story. Two years ago inventories of softwood lumber in Canada grew by 8.7 per cent, from 2.5 billion board feet in the first eight months of 2010 to 2.7 billion board feet the following year. The trend completely reversed this year however, with inventories in Canada for January to August 2012 dropping by 9.4 per cent compared to 2011, from 2.7 billion board feet to 2.5 billion board feet.

US				Inventories (million board feet)				Canada			
	Aug-11	Aug-10	% Chg		Aug-11	Aug-10	% Chg		Aug-11	Aug-10	% Chg
West	1,181	1,225	1,156	5.9	British Columbia	1,077	1,139	1,026	11.1		
South	1,297	1,359	1,297	4.8	East of the Rockies	1,548	1,576	1,471	7.1		
Other	158	161	156	2.8	Total	2,625	2,715	2,497	8.7		
Total	2,636	2,745	2,610	5.2							
				Inventories							
	Aug-12	Aug-11			Aug-12	Aug-11			Aug-12	Aug-11	
West	1,213	1,291	1,295	-0.4	British Columbia	1,100	1,057	1,174	-9.2		
South	1,359	1,482	1,359	9.1	East of the Rockies	1,410	1,383	1,529	-9.5		
Other	154	158	190	-1.5	Total	2,510	2,449	2,703	-9.4		
Total	2,726	2,930	2,815	4.1							

**SOURCE:  
WWPA**

Taken together with steadily increasing demand from the US through this year and the latest spurt of buying from China in the past few weeks, these August numbers indicate that in 4Q 2012 lumber supply will be even more restricted. Prices will move upward accordingly.

Going forward, the data of previous years will become only less reliable in making projections. This is because a lot of companies have changed their business model. The scope of effort British Columbia, and Canada, have made to foster a new customer in China for wood is by now well known. Elsewhere, forest products' producers are also widening their market base and their product mix. This new business is not necessarily just going to shut down and go back to making framing lumber for US home building, that sole focus was what got everyone into trouble when the housing market crashed in 2006.

For example, in response to the US housing downturn, Idaho lumber exports grew by 200 per cent between 2009 and 2011. Idaho Forest Group, with five mills in North Idaho, said to the *Idaho Statesman* this week that one-eighth of its production went to China, Vietnam, Japan, and elsewhere in Asia. A company spokesperson said this new business can continue as long as the US dollar stays cheap. The latest data shows that Idaho lumber exports appear to be slowing. Second-quarter exports this year were down about 15 per cent. Idaho Commerce officials cite two reasons: an improving US home-building market is keeping more timber in this country, and Asia's building boom is softening, says the Statesman.

North of the border, meanwhile, total softwood lumber exports from BC have grown 6.5 per cent so far this year. Last year, forestry exports to Asia surpassed \$3 billion, eclipsing US exports for the first time. As a result, Vancouver-based West Fraser Timber exported roughly 30 per cent of its Canadian lumber shipments to Asia in 3Q 2012, up from virtually nothing just five years ago, said company CEO Hank Ketcham to *Surrey Now* this week.

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