

MADISON'S LUMBER REPORTER



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News & Updates

Madison's Investment Rx

The May issue of *Madison's Investment Rx* has gone out to subscribers. Don't miss out on critical information on log supply, lumber production, transportation constraints, log and lumber shipments, and much more. Get in on this vital analysis for your lumber investments.

Contact us any time for a subscription.

Global Forest Industry Recovery Forecast

The global forest and paper industry is showing the first signs of a recovery, according to a report by PricewaterhouseCoopers. However, Canadian forest-product exports to the US have declined by 50 per cent since 2005 and other obstacles for local forest companies remain.

"While we are seeing some positive signs of recovery for many companies, there is hesitance to being overly optimistic," Frederic Bouchard, PwC's national deals leader for forest, paper and packaging, said in a statement.

PwC said the top 100 public companies' aggregate Return on Capital Employed (ROCE) - a key indicator of a sector's financial health - increased in 2010 although levels varied regionally. Global ROCE has been improving steadily to an estimated 4.8 per cent in 2010, up from 3.2 per cent in 2009 from 2.4 per cent in 2008. [READ MORE](#)

Japan Housing Starts

Japan's new housing starts were 63,419 units in March, down 2.4 per cent from the same month in a year earlier, which decreased for the first time in ten months, according to the Ministry of Land, Infrastructure, Transport and Tourism.

Floor area also decreased, by 0.5 per cent, after an interval of 13 months, to 5,750,121 square metres, according to the *Japan Lumber Journal*. [READ MORE](#)

Housing Starts, Canada

Canadian housing starts slipped 3.1 per cent in April, hurt by weakness in the condominium sector, the latest sign higher interest rates and new mortgage rules have cooled a recent property boom. Starts slipped to a seasonally adjusted annualized rate of 179,000 units, Canada Mortgage and Housing Corp said on Monday. [READ MORE](#)

PaperWeek and PwC Forestry and Paper Conference

The forest industry's 2011 conference season kicked off with a bang this week. Conveniently grouped in rapid succession at various locations in downtown Vancouver were: the Pulp and Paper Council's annual PaperWeek; PricewaterhouseCooper's annual Forestry and Paper Conference; and the BC Bioenergy Network conference, together running from Monday, May 9 through Thursday, May 12. Economists, analysts, industry professionals and CEOs from across North America, Europe, and parts of Asia weighed in on their estimations of the current state of the forest industry, and provided forecasts for the future.

This week *Madison's* will focus on the CEO presentations, then follow up with details of other presenters in the coming weeks. [READ MORE](#)

JAPANESE HOUSING STARTS

Month	TOTAL	Non-Wood	Wood	%Wood
Mar-11	63,419	27,994	35,425	56
Feb-11	62,252	28,720	33,532	54
Jan-11	66,709	30,969	35,740	54
Dec-10	74,517	30,917	43,600	59
Nov-10	72,838	31,384	41,454	57
Oct-10	71,930	30,939	40,991	57
Sep-10	71,998	30,857	41,141	57
Aug-10	71,972	29,899	42,073	58
Jul-10	68,785	28,740	40,045	58
Jun-10	68,688	27,940	40,748	59
May-10	59,911	24,952	34,959	58
Apr-10	66,568	32,143	34,425	52

Source: Japan Wood Products Information and Research Center

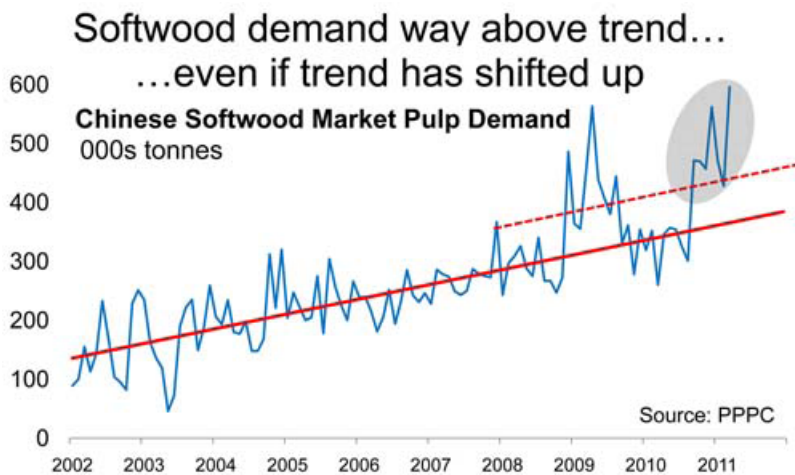
CANADIAN HOUSING STARTS

Actual and Seasonally Adjusted Annual Rates

	April 2011		March 2011	
	Actual	SAAR	Actual	SAAR
Canada, all areas	15,513	179,000	12,561	184,700
urban ctrs with >10,000	13,528	160,100	11,655	163,200
singles, urban centres	5,382	64,100	3,633	62,000
multiples, urban centres	8,146	96,000	8,022	101,200
rural areas	1,985	18,900	906	21,500
Atlantic urban centres	551	7,400	271	6,700
Quebec urban centres	3,474	96,800	3,111	40,600
Ontario urban centres	5,292	65,600	4,940	71,300
Prairie urban centres	2,283	27,700	1,897	26,300
B.C. urban centres	1,928	22,600	1,436	22,600

Source: Canada Mortgage and Housing Corporation

CHINA'S SOFTWOOD PULP DEMAND FORECAST



March 2011 saw huge growth in pulp demand, to an all time high, said Emanuele Bona of the Pulp and Paper Council at this week's PaperWeek conference in Vancouver.

Ship-to-Capacity ratios in 1Q 2011 were 93 per cent, much improved over the 1Qs of the past few years.

Softwood pulp demand grew by 9.4 per cent in 1Q 2011 to 9 million tonnes, with most of that growth in the north. The level of softwood pulp demand in China for the past six months is so high that stockpiling may explain some of the rise, as consumption is not matching demand.

For 2011 global demand for pulp is expected to grow by 4.6 per cent, with China accounting for most of this increase. Historically global growth has been 3.2 per cent. In 2012 the average expected growth will be 2.6 per cent.

GLOBAL PAPER DEMAND GROWTH FORECAST

Most of the growth will be in woodfree grades

Global demand by grade, in 000 tonnes

	2010	2013	Ch. in Tonnes	AAGR 10-13
Coated Woodfree	25 600	27 900	2300	2.9%
Uncoated Woodfree	40 300	41 900	1600	1.3%
Coated Mechanical	15 400	16 400	1000	2.2%
Uncoated Mechanical	14 200	14 600	400	1.0%
Printing and Writing	95 500	100 800	5300	1.8%

Source: PPPC



The global economy grew by 3.5 per cent in 2010, with most of that growth in the developing world, said Paul Leclair of the Pulp and Paper Council at this week's PaperWeek conference in Vancouver. In the developing world there is concern over inflation, especially regarding food.

Asian paper capacity, excluding Japan, will increase by 5 million tonnes, with China accounting for one-third of that. This rate of increase will continue for three years.

In tissue, which is fairly recession-proof, demand grew by 3.3 per cent in 2010 and will continue for the next three years. Most of that growth is in the developing world, especially Asia. 43 new tissue machines came online in 2010, with another 52 coming in 2011/2012. Most of these are in China, eastern Europe and Latin America.

Data DIGest: a weekly summary of economic news by the Associated General Contractors of America

The value of nonresidential construction starts jumped 12 per cent in April, not seasonally adjusted, above March and 14 per cent above April 2010 levels. Starts for the first four months of 2011 combined remained 1 per cent below the same period in 2010, Reed Construction Data reported on Monday.

"This reverses the weak starts reports in February and March," RCD Chief Economist Jim Haughey wrote. "Adjusting for seasonality, April starts were 7 per cent above the pace in the previous three months...Commercial starts in April jumped 37 per cent from March. Except for a surge last August, this was the highest total since January 2008. Private office starts nearly doubled...All other commercial sectors had big double-digit gains except the miscellaneous category. Both parking garages and warehouses had huge gains after very weak March totals...Institutional starts were steady in April and are now stalled...well below the 2009-10 monthly average...Heavy project starts rebounded 5.5 per cent from a weak March, but the year-to-date average is well below the average month in 2009-10."

The producer price index (PPI) for finished goods climbed 1.2 per cent in April, not seasonally adjusted (0.8 per cent, seasonally adjusted), and 6.8 per cent since April 2010, the Bureau of Labor Statistics reported on Thursday. This sharp rise intensified the ongoing cost squeeze on contractors, as the PPIs for finished buildings—which measure contractors' labor costs, overhead and expected profit as well as materials costs—rose much less.

Key Prices

	This Week	Last Week	Change	Month Ago	Change	Year Ago	Change
WSPF KD R/L 2x4	218	234	-16	257	-39	291	-73
WSPF KD R/L 2x6	226	239	-13	232	-6	293	-67
WSPF KD R/L 2x8	245	250	-5	255	-10	290	-45
WSPF KD R/L 2x10	260	277	-17	295	-35	340	-80
WSPF KD PET 2x4 Stud	220	235	-15	255	-35	320	-100
Douglas Fir Green R/L 2x4	245	245	0	265	-20	235	+10
Douglas Fir Green R/L 2x10	270	275	-5	295	-25	265	+5
ESPF KD 2x4 8ft Stud	305	310	-5	325	-20	400	-95
OSB Ontario 7/16" (CDN\$)	195	195	0	195	0	405	-210

Weekly News

PwC Forestry Forecast

CONTINUED The US and emerging economies in Asia, including China, have the highest ROCE (5.8 per cent and 5.2 per cent respectively), PwC said.

PwC also noted that North America experienced a strong revival in the number of merger and acquisition deals after a virtual collapse in 2009.

Meanwhile, PwC said the possibility to convert wood fibre for new purposes, including heat and power, biofuels and chemicals, is going to expand dramatically over the next decade.

"New biomass energy plants and bio-fuel refineries are returning to the most fundamental use of lumber for heat and power," said Bouchard. "As a result, energy will again be the baseline use for wood over the more traditional uses of paper. The energy sector's growing interest in biomass will change demand patterns, as well as industry practices."

PwC said more cross-industry partnerships will spur efforts to promote wood as a great building material, new sustainable packaging solutions, and more capital for research and development and investment in technology.

Home Building, Japan

CONTINUED Damage from the Great Eastern Japan Earthquake is already affecting the trend of housing starts, says the *Japan Lumber Journal*.

Housing starts in the three prefectures affected by the earthquake and tsunami, dropped by 19.2 per cent, according to the *Japan Lumber Reports*.

By application, housing starts of owner-occupied houses increased. However, those of rental houses continued their decrease for the sixth consecutive month. New condominiums, previously

on an uptrend, decreased for the first time in ten months.

The growth rate in single-family houses, which had been increasing by double-digit for more than one year, slowed down to 9.6 per cent.

By structure, wooden houses jumped to 35,425 units, up 4.4 per cent, owing to the growth in owner-occupied houses and built-for-sale single-family houses. The percentage of wooden houses increased 2 points from the same month in the preceding year to 55.9 per cent.

Housing starts are expected to mark year-on-year decline from April until around summer.

Canada Home Building

CONTINUED April housing starts in Canada took a big hit from multiple-unit family dwellings, which include condominiums. The segment dropped 5.1 per cent to 96,000 units. Closely watched urban single-family homes rose 3.4 per cent to 64,100 units in the month.

Regionally, urban starts were soft in Ontario and Quebec, while British Columbia, the Prairies and the Atlantic areas saw increases.

Rural starts were estimated at an annual rate of 18,900 units, down from 21,500 in March.

The housing news was not all glum. The Canadian Real Estate Association on Monday lifted its forecast for national sales activity, which it thinks will reach 441,100 units in 2011. This would still be a year-on-year decline of 1.3 per cent.

The new estimate compares with the 1.6 per cent year-on-year decline it forecast in February, which itself had been revised higher.

Much of the improvement is due to stronger-than-expected sales in British Columbia in 1Q, the industry group said.

The surge in sales of multimillion dollar homes in the area has also prompted CREA to up its national average home price forecast as well. It now expects the average price to rise 4 per cent to \$352,500, compared with February's view of a 1.3 per cent rise.

Job Action

Strikes at Finnish forest companies expanded on Friday, taking the total number of white-collar strikers to around 2,500 and prolonging disputes in one of the country's leading industries.

Stoppages at a number of mills were brought forward having initially been planned for next week, said Antti Rinne, leader of the clerical worker's union Pro.

The strikes involve white-collar workers at the Finnish sites of UPM-Kymmene, Stora Enso, Metsaliitto (which includes M-real), and South Africa-based Sappi.

Actions at some plants started last month over pay. The industry is ready to raise white-collar pay by 2.5 per cent, but the union has demanded 3.5 per cent and new salary brackets.

Strikes at UPM and Sappi are due to end on May 26 and actions at Stora Enso and Metsaliitto could last until June 9.

In Canada, following a breakdown in labour discussions between Tembec representatives and the union representatives at the Tembec high-yield pulp mill located in Matane, QC, unionized employees did not report to work Tuesday morning and went out on strike.

Consequently, all production activities have been suspended indefinitely.

Tembec is monitoring the situation very closely and is putting into place measures that will ensure uninterrupted supply to its customers.

The plant in Matane employs 143 people, of which 99 are unionized, and ships to customers in North America, Europe and Asia.

Paper and Forestry Conferences

Analyses and Forecasts

Ilkka Härmälä, CEO of Metsa Botnia, which operates four sulphate pulp mills in Finland for a total annual production of 2.5 million tonnes of bleached pulp, spoke on Monday at PaperWeek.

"There are two or three key drivers affecting the global pulp market at the moment,"

by Kéta Kosman

began Härmälä. "The scope of growth of demand from Asia is still not known, and what this will mean for producers in Scandinavia – and by extension

for fibre supply out of Russia – is uncertain. Consumption of fibre in Europe has not yet recovered from the recession, and a question remains as to whether there will be further decline in demand.

"The product mix is changing; tissue, packaging board, and viscose are the growing customers for pulp producers.

"There is a big question about the future importance of biomass. Will there be competition for raw material between pulp producers and energy producers?"

"While production of pulp and paper globally is growing, there are questions about how to manage logistics," continued Härmälä. "Distribution within Europe is good, in China it is not bad because at least there are products to ship back in containers. Elsewhere it is difficult to create a logistical network for every aspect of the industry.

"There is a growth trend developing for the production of recovered paper. Recycled rates in the developing world must improve, in order to further grow this market, the supply of materials must be stable."

BILT Paper is a subsidiary of The Ballarpur Group, India's largest manufacturer of writing and printing paper. BILT Paper is focussed on the manufacture of bulk coated and uncoated paper, and viscose grade fibre, at its three facilities in India and one in Malaysia. Company CEO Yogesh Agarwal launched his presentation with some hard figures.

"India has a US\$1.5 trillion economy and a forest base worth US\$304 billion. 10.8 million tonnes of paper is produced in India annually, using 45 per cent recycled fibres. The average mill size is quite small, especially in the non-wood based sector. Wood-based paper makes up a very small percentage of production in India," Agrawal explained. "China and India together are responsible for 70 per cent of global paper production growth, with China taking the lion's share.

"BILT produces 3 million tonnes of uncoated and 460 tonnes coated paper annually. Theoretically India is a paper exporting country, largely of coated grades, but a net importer of the lower grades especially uncoated.

"The requirements of the packaging sector are changing in India, with delivery now going directly to the customer outlet."

"Sourcing fibre is a challenge," continued Agrawal. "There might be more people in India than trees. 8 million tonnes of wood annually is used by the pulp industry, with expectation of that to grow to 12 million tonnes by 2013. At US\$122, log prices are not the worst but still not good. The average distance for wood to travel to a pulp mill in India is 2,000 km. There is no trade-off in favour of scale in this region.

"In India recycling and wastepaper collection is only about 26 per cent while in the rest of the world recovery is 40 per cent. Currently there is a fragmented market, and distribution is key," concluded Agrawal. "Previously prohibitive customs duties are now less than 10 per cent so India is poised for growth."

At Wednesday's PwC conference, Chad Wasilenkoff, CEO of Fortress Paper, spoke about that company's unique position in the paper sector. Subscribers to Madison's bi-weekly Timber Preview will be well aware of the emergence and growth of Fortress Paper.

"We started with a shift from commodity to specialty, from volume to value," said Wasilenkoff of the Fortress Paper business model. "In general we look at macro trends for the future, we consider there are a lot of distractions out there. For example, the collapse of the US housing market is just noise, although a very loud noise.

"More critical is population growth, and the transformation of that growth, which is putting pressure on land, biomass, and fibre. There is more pressure on food and energy requirements, in the long terms prices are going to be higher. There is also going to be more political conflict, especially coming from the world's poorest 2 billion people. Fibre security is going to be a critical issue," declared Wasilenkoff.

"Cotton can not keep up with the global demand for textiles, therefore dissolving pulp is the future specifically in terms of utilizing wood for rayon."

In the afternoon Rick Doman, President and CEO of Eacom Timber spoke about producing lumber in eastern Canada. "North America's lumber producers are shifting their focus from accessing fibre to using fibre more efficiently. In that regard Eacom will be improving recovery at the mill and utilization of the forest," began Doman. "The attractiveness of producing lumber in eastern Canada stems from lower energy costs. In the future transportation will be an issue, and Eacom will benefit due to our proximity to Canada's population base and also to the

large US markets. Eacom ships out of Trois Rivières and Montreal, so the European market is also easily accessible. Freight rates are attractive.

"The challenges of working wood in eastern Canada include higher logs costs, especially when taking into account the smaller log size. The additional export tax charged to Quebec and Ontario producers selling into the US should come off in July or August.

"Eacom has put capital into our mills to upgrade efficiencies and also for green energy technology, and has cut costs on the distribution side by shipping directly to customers. The company is opening a distribution centre in the UK and will be soon in northern Europe as well," explained Doman.

"Going forward freight costs may become a liability, and log costs between western and eastern Canada need to be better balanced, although both are still lower than in the southern US.

"In the next three to five years more western Canadian lumber will ship to China, which will naturally increase demand for eastern Canadian wood from North American customers," Doman concluded.

The clearest indication Doman gave in terms of a forecast is: once US housing gets to 70,000 annualized starts there will be lumber shortfalls and the price of wood is going to shoot up. This assessment was echoed by the various presenters at PwC, as well as speakers at PaperWeek. By the time US housing starts get up to 1.4 million lumber is going to be very valuable.

Joe Nemeth, President and Chief Executive Officer of the Canfor Pulp Limited Partnership, spoke next about producing pulp in western Canada.

"There is 1.2 million tonnes of Canfor capacity in Prince George. Canada still represents about 50 per cent of global northern bleached softwood kraft (NBSK) production, and Canfor will continue to invest in our asset base," began Nemeth. "The common perception that pulp and paper is a traditional product, is a sunset industry, is flawed. Our production is totally sustainable, we take waste and make something useful out of it. There is almost 100 per cent utilization at our mills, when energy cogeneration is taken into account. Canada's pulp and paper production is the single largest green power industry globally."

"The pulp and paper industry, together with the forest industry in general, needs to market itself better. We need to educate the public, especially the younger generations and the emerging markets, to tell our story proactively," charged Nemeth.

This last sentiment was also expressed by Doman, as well as other presenters throughout the three days of speeches. Madison's will delve further into this important subject of perceptions and future trends in consumption over the next few weeks.