

MADISON'S LUMBER REPORTER



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Annual Subscription Prices
E-mail/Fax: C\$364
Discounts available for multiple
subscriptions
Published 50 times a year



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In Canada, add GST or HST
ISSN 0715-5468

Printed in Canada © 2012

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News & Updates

Madison's Timber Preview

This week's issue of *Madison's Timber Preview* examines a fundamental shift which is about to occur in the US between TIMOs, Timberland Investment Management Organizations, and REITs, Real Estate Investment Trusts, both of which are methods of investing in timber or in timberland.

Contact us any time for a subscription.

BC Logger Dies

Yet more bad news about safety issues for the Canadian forest products industry, after huge fires at two sawmills recently, came out this week with the death of a faller in British Columbia.

BC's first casualty in the woods came far too early in 2012 with the death of an experienced logger Monday while falling hemlock and fir 60 km southeast of Terrace, BC.

Arthur (Art) Loring, 56, died when a tree fell on him. Loring was performing contract work for Long Shot Holdings on the day he died and was the sole faller in a work crew of four.

China's Conifer Wood Market

Domestic demand for conifer wood in China grew rapidly during the financial crisis in 2008 despite reduced exports of manufactured wood products, according to the *Japan Lumber Journal* by way of the *China Wood Monthly Market Report*.

The demand for conifer timber rose remarkably due to the Chinese government's 4,000 billion RMB economic stimulus toward developments in infrastructure.

In the last five years, total imports of conifer logs to China reached 106 million m3, with the record high, of 24.27million m3, in 2010. Conifer log imports accounted for 70.6 per cent of the total log import volume into China in 2010, compared to 61 per cent in 2006.

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North American Timber to Japan - 2011 and 2012

At the Keihin chapter of the Japan North American Lumber Conference held January 12, Chair Mr. Enokido predicted that Japan's timber demand will increase with the full-scale reconstruction efforts in disaster-hit areas this year, according to the *Japan Lumber Journal*. He specifically expressed his expectation of the use of timber for buildings that accommodate a large number of people such as schools, community centres, and public offices.

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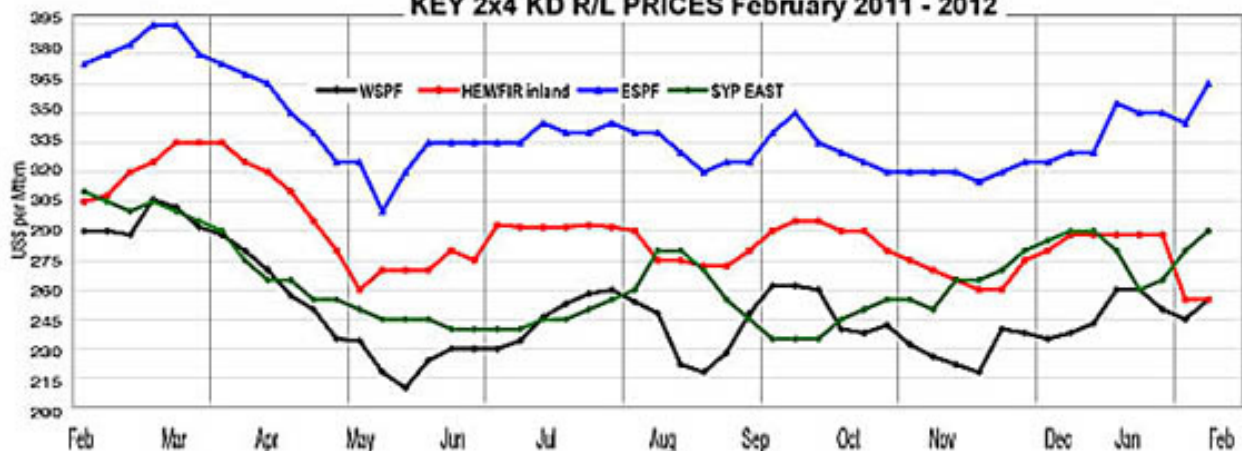
10th Timberland Investment Summit

Balmy late-January New York City temperatures and renewed financial interest in the global forest products industry following the extended economic downturn since 2006 brought a large number of attendees to the IQPC Timberland Investment Summit.

Presenters covered the knowledge base spectrum from timber appraisers to woodlot owners, financial analysts, solid wood producers, wealth funds, TIMOs, and a lumber market analyst. The Summit was attended by interested parties from around the world.

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KEY 2x4 KD R/L PRICES February 2011 - 2012



Canadian Real GDP

A new report from TD Economics released Wednesday found that Canada's economic reliance on the US in terms of share of exports and GDP has dropped steadily over the last decade.

The report said Canada's reliance on the US to import its goods is likely to continue to drop in the years ahead.

Exports to the US directly contributed an annual average of 0.5 percentage points to nominal GDP growth over the last decade. That was well below an average annual contribution of 2.3 percentage points during the 1980s and 1990s.

While exports to the US are down 14 per cent from the peak in 2002, Canadian exports to China have more than doubled and exports to Europe are up 83 per cent.

By 2020 the US will only account for about 66 per cent of direct Canadian exports, down from 85 per cent in 2002.

Direct US exports to Canadian GDP will stabilize at 20 per cent, almost half its share of 10 years ago.

Derek Burleton, deputy chief economist with TD Economics, said "Canada's competitive advantage lies in the resource sector. As such, commodities are on track to become even more important drivers of Canadian economic growth, likely at the expense of manufactured goods."

Japan's Demand for Major Imported Timber

(1,000 cubic meters; %)	2011 Results (presumption)		2012 Estimates	
		y/y		y/y
Logs				
<i>Southsea</i>	478	-14.6	435	-9.0
<i>North American</i>	3,014	6.4	3,017	0.1
<i>Russian</i>	355	-28.2	350	-1.4
<i>New Zealand-Chilean</i>	712	-4.0	745	4.6
<i>European</i>	10	-10.8	10	-
<i>Sub-total</i>	4,569	-1.5	4,557	-0.3
Lumber				
<i>Southsea</i>	637	9.8	620	-2.7
<i>North American</i>	2,728	-0.3	2,712	-0.6
<i>Russian</i>	694	9.3	700	0.9
<i>New Zealand-Chilean</i>	404	26.1	425	5.2
<i>European</i>	2,494	9.3	2,400	-3.8
<i>Sub-total</i>	6,957	6.2	6,857	-1.4
Total	11,526	3.0	11,414	-1.0

SOURCE:
Japan Lumber
Journal

Source: Japan Foreign Timber General Supply and Demand Liaison Conference

Supply/Demand of American Timber to Japan

(1,000 cubic meters)	Import			Consumption			Stocks		
	Log	Lumber	Total	Log	Lumber	Total	Log	Lumber	Total
2007	3,018	2,724	5,742	3,062	2,797	5,859	260	201	461
2008	2,638	2,931	5,559	2,644	2,909	5,583	254	223	477
2009	2,468	2,272	4,740	2,486	2,333	4,819	237	162	399
2010	2,905	2,748	5,653	2,833	2,737	5,570	309	173	482
2011									
YTD	2,845	2,537	5,383	2,865	2,496	5,361	(through Nov 2011)		



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Key Prices

	This Week	Last Week	Change	Month Ago	Change	Year Ago	Change
WSPF KD R/L 2x4	255	245	+10	260	-5	294	-39
WSPF KD R/L 2x6	255	247	+8	264	-9	270	-15
WSPF KD R/L 2x8	250	246	+4	250	0	275	-25
WSPF KD R/L 2x10	314	310	+4	314	0	338	-24
WSPF KD PET 2x4 Stud	260	265	-5	260	0	275	-15
WSPF KD PET 2x6 Stud	305	305	0	300	+5	300	+5
Douglas Fir Green R/L 2x4	230	232	-2	230	0	255	-25
Douglas Fir Green R/L 2x10	330	330	0	320	+10	302	+28
ESPF KD 2x4 8ft Stud	330	310	+20	315	+15	320	+10
OSB Ontario 7/16" (CDN\$)	203	196	+7	202	+1	200	+3
CSplywood Toronto 3/8" (CDN\$)	319	309	+10	320	-1	310	+9

Weekly News

Wood Imports, China

CONTINUED In terms of lumber, total conifer lumber imports to China in the past five years reached 24.27 million m³, with 9.37 million m³ imported in 2010, also a record high, says the *Japan Lumber Journal*. Conifer lumber imports accounted for 63.7 per cent of total lumber import volumes in 2010, compared to 34.7 per cent in 2006.

Russia was previously the main supplier of the conifer logs to China, with exports to China reaching a peak of 25.39 million m³ in 2007. Russia's log exports were seriously restricted by the 20 per cent tariff, so volumes subsequently dropped 45 per cent to 14.03 million m³ in 2010.

Meanwhile, logs imports from New Zealand, US, Canada and Australia increased substantially, says the *Journal*. Please see table on Page 5.

Japan Timber Demand

CONTINUED As for the trend for the North American lumber in 2012, Enokido predicted that the arrival and shipment would be stable compared to 2011, says the *Japan Lumber Journal*.

However, he urged participants to take precautions, saying that there is a possibility that there might be an impact from the decline in demands in China and decline in prices of European lumber.

The supply-demand balance for North American lumber products shows no signs of fluctuating, and the market remains stable.

In other news, the Japan Foreign Timber General Supply & Demand Liaison Conference, whose membership includes Japan Lumber Importers' Association, Japan North American Lumber Conference, Japan Southsea Lumber Conference, Japan Russian Wood Products Association, and

Japan New Zealand and Chilean Lumber Conference, has announced demand (shipping) forecasts for major imported timber for full-year 2012, according to the *Japan Lumber Journal*.

According to the report, demand for logs in 2012 is estimated to be 4,557,000 cubic meters, which is lower than the estimated shipping volume for 2011, of 4,569,000 cubic meters, by 0.3 per cent.

Demand for lumber was estimated to be 6,857,000 cubic meters, which is lower than the estimated shipping volume for 2011, of 6,957,000 cubic meters, by 1.4 per cent.

Total demand for imported logs and lumber in 2012 was expected to decrease 1 per cent from the previous year to 11,414,000 cubic meters. The demand was estimated to level off or slightly decrease, though the housing starts are expected to increase.

Confifex \$25 Million Financing

Confifex Timber Inc is close to raising \$25 million, the company announced Thursday.

Underwriters has agreed to purchase \$23.5 million worth of shares, with a further \$1.5 million to be raised through a non-brokered private placement.

Both transactions are expected to close on February 16 and are subject to regulatory and stock exchange approval.

The money will "fund capital expenditures and for general corporate purposes," Confifex said in a statement. The company is in the process of building a \$50-million bioenergy plant in Mackenzie, 186 kilometres north of Prince George, BC.

Hampton May Rebuild

A week after the Babine Forest Products sawmill in Burns Lake, BC, was de-

stroyed in an explosion, its owners expressed interest in rebuilding, said Pat Bell, BC's Minister of Jobs, Tourism and Innovation, to the *Prince George Citizen*.

Speaking in a telephone press conference, Bell said Oregon-based Hampton Affiliates, which has a 90 per cent stake in the mill, must first gain confidence in the timber supply before determining whether to start anew.

Hampton CEO Steve Zika has not disclosed the minimum amount of fibre that would be required, Bell said, and added the key is to avoid sacrificing one mill for another.

Babine milled mostly beetle-killed pine, but Bell expected a new mill could process other species.

"It would be the best of the best, and certainly be capable of running green wood," Bell said.

Asked what may happen if Hampton decides not to rebuild, Bell said he's "quite optimistic" that won't be a problem, and he's sure other entrepreneurs would step forward, according to the *Citizen*.

Domtar Sells Quebec Mill to Fortress Paper for \$1

Domtar Corp announced Tuesday that it has signed a definitive agreement with Fortress Global Cellulose Ltd, and with a subsidiary of the Government of Québec, for the sale of its Lebel-sur-Quévillon, QC, assets. The transaction is expected to close in the second quarter of 2012.

As per the agreement, all pulp and sawmilling assets including the buildings and equipment will be sold to Fortress for the nominal sum of \$1.00 and all lands related to the facilities will be sold to a subsidiary of the Government of Québec for the nominal sum of \$1.00.

Timberland Investment Summit

IQPC 10th

A westcoaster travelling to New York City at the end of January usually has to reach into the deep, dark recesses of their closet for that generally unused big winter coat, hat, scarf, boots etc. Not this year! Mild, balmy, spring-like weather blessed the attendees of IQPC's 10th Timberland Investment Summit. Dare it be said; the weather was beautiful.

Having grown up in Ottawa, ON, *Madison's* feels compelled to point out that there is no such thing as no winter in the east of North America. This mild winter season weather so far can only mean a slam of truly cold temperatures and snow, possibly snowstorms, before spring arrives. But, for now, all are just enjoying the warm sun while it stays around.

Conference attendees from around the US and the globe, plus a few Canadian representatives, immersed themselves deeply in topics like timberland investment return rates, log values and prices, US housing starts, timber supply and demand globally, and medium-term projections for North American lumber and panel prices. This latter insight was provided by Madison's.

Due to constraints of space, the focus today in your *Reporter* will be on the US housing market, homes-for-sale inventories, and projections for future new home building. Subscribers to the bi-weekly *Madison's Timber Preview* are updated on recent movements and short-term future expectations of US TIMOs and REITs.

As moderator of the first panel discussion, *US Housing Market Dynamics*, Jack Lutz of Forest Research Group introduced that topic by saying, "Housing is important right now because home values are dropping. A house represents a significant portion of wealth for the average US citizen. US home building consumes 20 per cent of the world's softwood lumber, and another 10 per cent goes to other US uses for wood."

Danielle DiMartino-Booth of the Dallas Federal Reserve insisted that her comments be off the record, unfortunately. Booth provided some very sobering statistics and analysis at the IQPC 9th Summit in Vancouver, BC, in June, 2011. In summary, while DiMartino's analysis this year

was somewhat less negative than last, it was by far the least encouraging of all speakers in terms of the recovery of US home building numbers and the scope of that recovery when it does occur.

The next speaker, Joseph Bench of IDB Bank, explained that the near-term forecast for new building in the US is all about multi-family units.

"Home ownership rates are at 66 per cent, and rents continue to rise. Rental rates are currently responsible for the 40 per cent increase of US CPI.

"However, iShares of the home construction industry, a leading indicator of housing starts, hit bottom last year and have since rallied significantly. They now show an improvement in home building traffic."

"The collapse in housing cost the US two million jobs, which makes the unemployment rate 8.5 per cent rather than 6.5 per cent," explained Bench. "This, keep in mind, is with a population growth of two million per year.

"The current down trend in household formation will reverse when young people start getting work," continued Bench. "Our latest figures, for August through December 2011, in our establishment survey – meaning business new hiring or intentions to hire – show new job growth of 670,000. And our household survey shows 1,340,000 people have become employed in that time frame.

"At the moment, while multi-unit starts are up and that increased demand is justified by higher rental rates, eventually there will be a substitution effect in favour of home buyers," concluded Bench.

Alvery Bartlett of the Alvery Bartlett Group had a rather gloomy outlook for US macro economics.

"In terms of risk, what sits below the surface of the US economy terrifies me," Bartlett said by way of introduction. "There is a titanic struggle between deflation and inflation, and deflation will rule. There is so much deleveraging that needs to take place, the US Federal Reserves have had the world on life support.

"Why is it so wrong to let an asset price itself?" exclaimed Bartlett.

This sentiment was echoed by analysts and economists throughout the conference, including DiMartino. Differences on the details were put aside as everyone agreed that the longer Washington tries to forestall the foreclosure process and artificially prop up

the US housing market, the longer it is going to take for the US real estate market to come back to life.

"If the US economy were indeed in recovery, the GDP should be at 5.1 per cent, not 2 per cent as it is right now. This is a pathetic recovery," continued Bartlett. "As long as there is something beneath the system, as long as the system is subject to price intervention, we really don't know what is out there. And when interest rates are at 0 per cent, the dollar is not king anymore. Right now, cash flow is king."

In terms of a forward-looking indicator, the entire panel agreed – and this is a very important point – that all anyone needs to do is, "watch US home builders move through their plots of land and start buying more. They are right now consciously working through their capital and will start buying more land. When that happens you will know the recovery is upon us."

Of all the other speeches and presentations, the most worthwhile and timely for Reporter subscribers was that of Dennis Neilson, Director of DANA. Neilson, operating out of New Zealand, spoke about *China's Timber Demand Trends*.

"In just one part of China right now they are building a new subdivision for 4 million people," Neilson started off his speech with a bang. "Since 1995 China's timber supply deficit has been more than 17 per cent, compared to GDP growth of 10 per cent. That amounts to a 160 million cubic metre shortfall in China's timber supply annually.

"China's log imports rose to more than 35 million cubic metres in 2010, from 17 million cubic metres in 2001. If the log export volumes of all the timber exporting countries were added together, the total would still leave a timber supply deficit in China starting in 2016.

"There has been a shift in the method of timber and lumber importing into China. Previously, players would use Chinese government agencies and simply act as representatives. Now, those same agencies are using existing successful private companies in China as a front, giving them unlimited funds but acting under their own names rather than the government's name.

"For example," concluded Neilson, "Through this process a large private Chinese company now holds a 19 per cent ownership stake in Conifex."