

MADISON'S LUMBER REPORTER

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News & Updates

Madison's Timber Preview

This week's issue of *Madison's Timber Preview* examines a new mountain pine beetle report out of the US Forest Service's Southern Research Station, as well as recent changes in timber management policy with US Forest Service lands.

Contact us any time to subscribe to this vital and timely information.

CN Rail and Teamsters Reach Tentative Deal

Canadian National Railway, Canada's largest rail operator, agreed to a new labour contract for some 3,300 conductors, train and yard workers, and traffic co-ordinators represented by the Teamsters union, the railway said Thursday.

The tentative three-year deal, the details of which were withheld pending ratification, comes after a week of talks with government-appointed mediators. It averts the possible disruption of a cross-country network.

BC Sawmills Face More Dust Inspections

Inspectors are heading back to 150 British Columbia sawmills over the next three months to ensure the operations are doing everything possible to reduce the buildup of potentially explosive wood dust.

WorkSafeBC said Thursday that a team of 10 officers will inspect the mills between November 1 and January 31, 2014, as part of a drive to reduce dust levels.

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Producer Price Index, Canada and US

After three consecutive monthly advances, Canada's Industrial Product Price Index (IPPI) was down 0.3 per cent in September, with 12 of the 21 major commodity groups posting declines, said Statistics Canada Tuesday. Primary metal products, down 0.9 per cent, was the largest contributor to the decline of the index, mainly as a result of lower prices for aluminum products, down 1.7 per cent, copper and copper alloy products, down 2.1 per cent, and other non-ferrous metal products, down 0.9 per cent.

The decrease in the IPPI was also attributable to petroleum and coal products, down 0.4 per cent, the first drop since April 2013. The downward movement was primarily a result of lower prices for gasoline, down 1.9 per cent. The IPPI excluding petroleum and coal products declined 0.2 per cent in September.

U.S. producer prices unexpectedly fell in September and the increase in the annual rate was the smallest in nearly four years, pointing to a benign inflation environment.

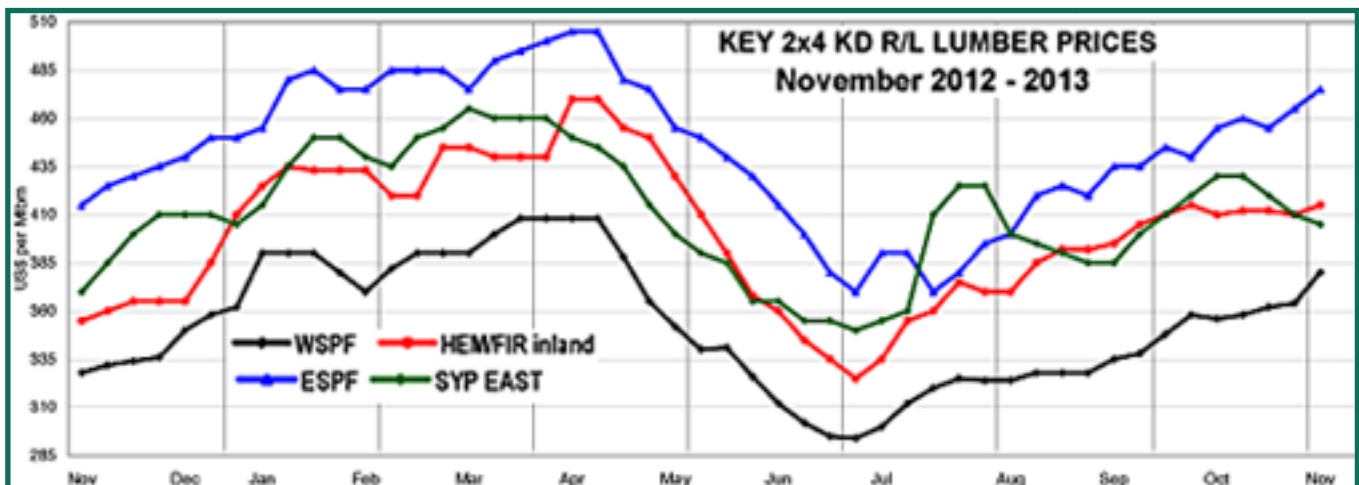
The US producer price index fell 0.1 per cent in September, following August's increase of 0.3 per cent, according to the US Labor Department also Tuesday. Year-on-year, the index continued to point to soft inflation, up by 0.3 per cent.

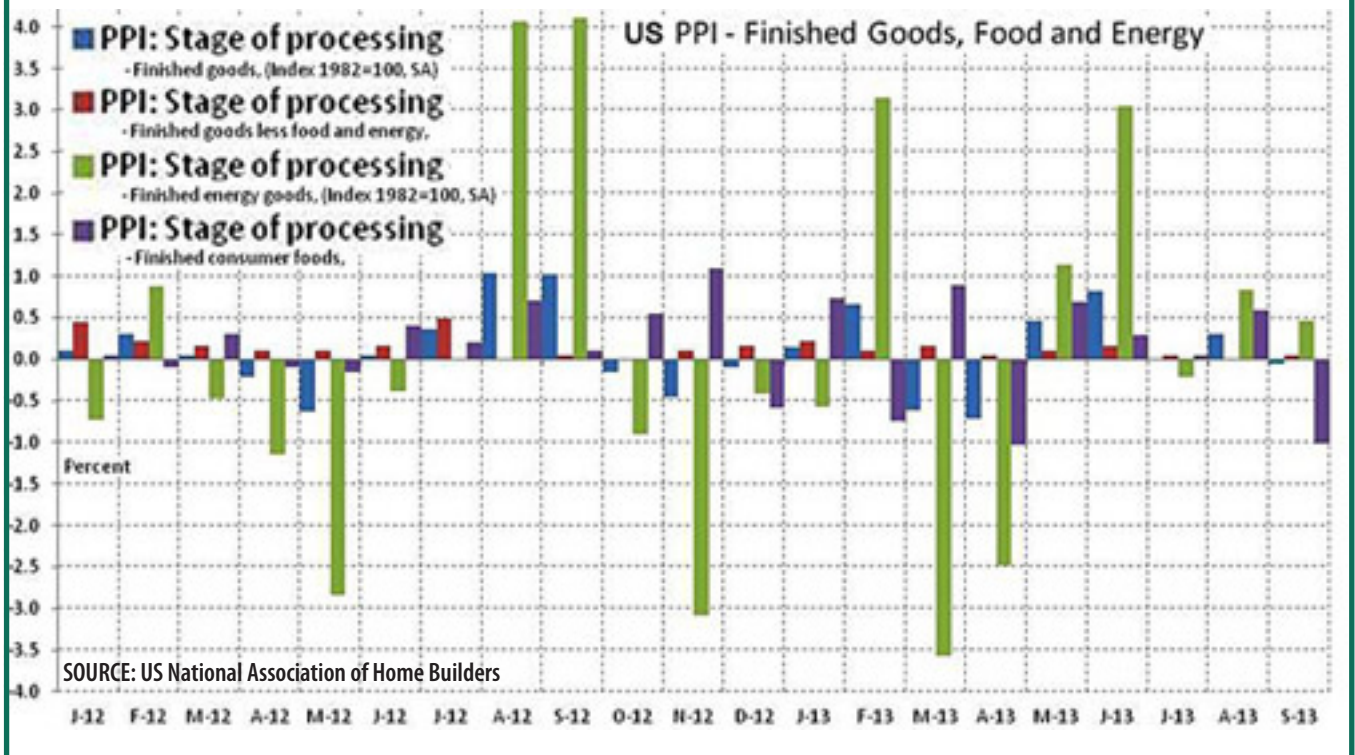
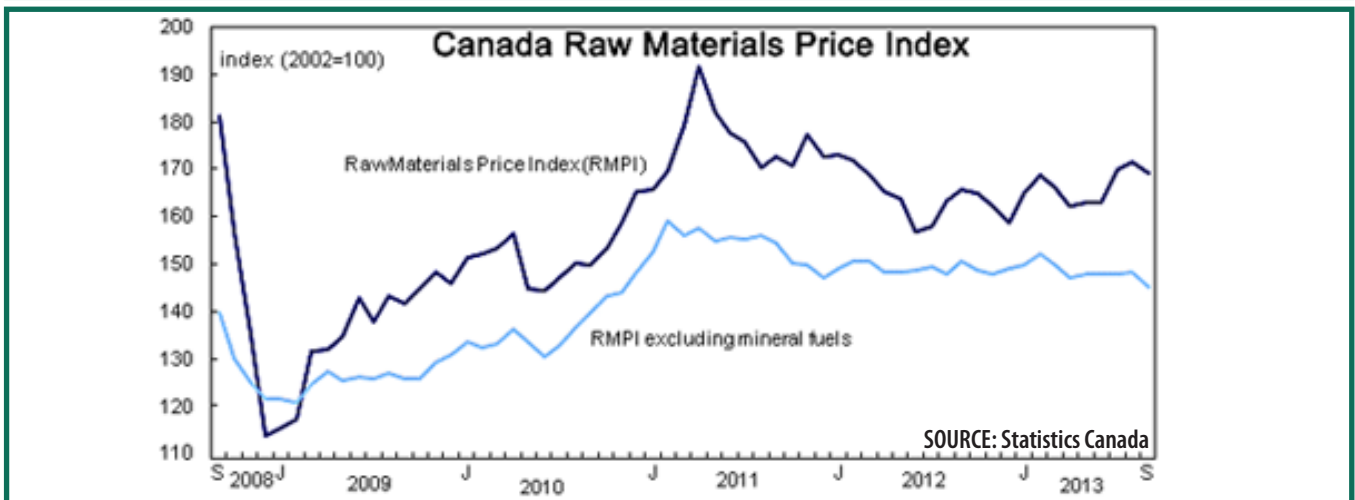
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US REO-to-Rental Properties

As interest in US real estate slowly heats up, the Blackstone Group's efforts to buy up distressed houses for the past 18 months seems to be coming to fruition as the fund attempts to create the largest single-family rental business in America.

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Key Prices

| | This Week | Last Week | Change | Month Ago | Change | Year Ago | Change |
|--------------------------------|-----------|-----------|--------|-----------|--------|----------|--------|
| WSPF KD R/L 2x4 | 380 | 364 | +16 | 356 | +24 | 328 | +52 |
| WSPF KD R/L 2x6 | 354 | 332 | +22 | 338 | +16 | 318 | +36 |
| WSPF KD R/L 2x8 | 344 | 340 | +4 | 344 | 0 | 310 | +34 |
| WSPF KD R/L 2x10 | 450 | 450 | 0 | 450 | 0 | 350 | +100 |
| WSPF KD PET 2x4 Stud | 315 | 319 | -4 | 325 | -10 | 300 | +15 |
| WSPF KD PET 2x6 Stud | 300 | 295 | +5 | 295 | +5 | 295 | +5 |
| Douglas Fir Green R/L 2x4 | 330 | 325 | +5 | 328 | +2 | 275 | +55 |
| Douglas Fir Green R/L 2x10 | 510 | 485 | +25 | 440 | +70 | 320 | +190 |
| ESPF KD 2x4 8ft Stud | 380 | 375 | +5 | 375 | +5 | 370 | +10 |
| OSB Ontario 7/16" (CDN\$) | 223 | 223 | 0 | 247 | -24 | 310 | -87 |
| CSplywood Toronto 3/8" (CDN\$) | 363 | 363 | 0 | 390 | -27 | 350 | +13 |

BC Sawmill Dust Inspections

CONTINUED This is the third white-glove inspection for the mills since dust accumulation was implicated in an explosion and fire at Hampton's Babine Forest Products operation in Burns Lake, BC, on January 20, 2012. The blast levelled the mill, killing two workers and injuring 20 others.

A second fatal mill explosion occurred in April 2012 at Sinclair's Lakeland Mills in Prince George, BC, where two workers were killed.

The cause of those disasters hasn't been revealed by investigators, as WorkSafeBC has asked the Crown to review whether the companies or any individuals could be charged for violations of the Workers Compensation Act.

The organization's officers have carried out more than 1,000 inspections of sawmills and other wood processing operations since the combustible dust safety initiative began in late April 2012.

Canada and US Industrial and Producer Prices

CONTINUED In Canada, the decline of the IPPI was moderated slightly by lumber and other wood products, up 0.8 per cent, mainly due to higher prices for softwood lumber, up 2.2 per cent, according to Statistics Canada.

The IPPI rose 1 per cent in the 12-month period ending in September, after increasing 1.7 per cent in August.

Compared with September 2012, the advance of the IPPI was mainly attributable to motor vehicles and other transportation equipment, up 3.5 per cent, specifically motor vehicles, up 4.7 per cent. The depreciation of the Canadian dollar rela-

Weekly News

tive to the US dollar on a year-over-year basis was largely responsible for the increase.

During the 12-month period ending in September, the Raw Materials Price Index (RMPI) advanced 2.1 per cent after increasing 5.1 per cent in August.

Compared with September 2012, mineral fuels, up 8.5 per cent, was the largest contributor to the increase of the RMPI, mainly as a result of higher prices for crude oil, up 8.6 per cent. The RMPI excluding mineral fuels was down 3.6 per cent on a year-over-year basis.

Among other commodity groups that contributed to the year-over-year increase in the RMPI were wood products, up 3.4 per cent, said StatsCan.

Meanwhile, in the US, one third of September's PPI increase can be put down to a 6 per cent jump in the index for home heating oil, said the US Department of Labor. Residential natural gas prices were also higher.

In the 12 months through September, wholesale prices rose 0.3 per cent, the smallest gain since 2009. That compared to a 1.4 per cent increase in August.

Financial Results

North American forest companies releasing 3Q financial results this week include Norbord Inc and Resolute Forest Products.

Norbord Friday reported EBITDA of \$45 million in 3Q 2013, compared to \$66 million in the same quarter last year, and \$102 million in 2Q 2013.

Norbord recorded \$27 million of earnings in 3Q 2013 compared to \$27 million in the same quarter last year and \$53 million in the prior quarter. Earnings this quarter include a \$9 million one-time non-recurring income tax recovery.

Company share prices jumped 5.4 per cent as the panelboard producer's earnings topped estimates.

Resolute Forest Products reported a better-than-expected profit for the fourth straight quarter Thursday as demand for its pulp products improved, sending its shares up 15 per cent in early trading.

Resolute, the largest newsprint maker in North America, said results were hurt by a \$619 million charge related to income tax.

The company's net loss was \$588 million, or \$6.22 per share, in 3Q, compared with a profit of \$37 million, or 38 cents per share, a year earlier.

Revenue fell 8 per cent to \$1.1 billion, mainly due to lower newsprint prices.

The company will continue to find more ways to save, announcing plans that it'll shed up to 170 positions at two facilities in Quebec and Ontario, the company's CEO said Thursday.

Plum Creek Acquires

Plum Creek Timber Monday announced it signed a US\$1.1 billion purchase and sale agreement to acquire approximately 501,000 acres of industrial timberlands, associated wind and mineral assets, and an interest in approximately 109,000 acres of high-value rural and development-quality lands from MeadWestvaco Corporation. The transaction is expected to close during 4Q 2013.

Boise Cascade Appoints

Boise Cascade Company announces that its Board of Directors has elected Rich Viola and Frank Elfering to new officer positions, effective October 30.

Rich has been appointed VP sales and marketing for Building Materials Distribution. Rich was the sales and marketing manager for BMD's East Region before becoming the division sales and marketing manager.

Frank has been appointed VP purchasing for Building Materials Distribution.

US Rental Rates

And a New Bond Market?

Even with the delay of September US housing starts until November 26, when the Census Bureau will put out September and October data concurrently, it is possible to get a gauge on US real estate activity. One extremely important, and often overlooked, indicator is rental rates.

In terms of macroeconomics, the US Consumer Price Index (CPI) increased 0.2 per cent in September on a seasonally adjusted basis, the US Bureau of Labor Statistics reported Wednesday. Core CPI, which excludes more volatile food and energy prices, rose by 0.1 per cent for the

by Kéta Kosman

second consecutive month. Over the past twelve months, Core CPI increased by 1.7 per cent.

The shelter index segment rose 0.2 per cent month-over-month in September for the fourth consecutive month. Over the past twelve months, the shelter index increased 2.4 per cent before seasonal adjustments.

For its part the real rent index has increased for eight consecutive months, rising by 0.1 per cent in September, while over the past year the real rental prices have risen by 1.2 per cent.

Elsewhere, the National Association of Realtors said Monday its Pending Homes Sales Index, based on contracts signed the previous month, plunged 5.6 per cent to 101.6 in September, the fourth monthly drop in a row. Mortgage rates have risen sharply since May on bets that the US Federal Reserve would soon begin winding down a stimulus program, although rates have eased slightly in recent weeks.

As well, the Standard & Poor's/Case-Shiller 20-city home price index rose 12.8 per cent over the 12 months ending in August, the agency reported Tuesday. That's up from 12.4 per cent in July from a year earlier. All 20 cities in the index showed year-over-year gains.

However, a measure of month-over month prices for the 20 cities rose just 1.3 per cent in August. That's down from a 1.8 per cent month-over-month gain in July. And 16 of the 20 cities reported more modest price increases in August than in July.

Meanwhile, according to the Conference Board Tuesday, the share of consumers planning to buy a home in the next six months was 5.8 per cent on a seasonally adjusted 3-month moving average basis. Over this same period, the share of respondents planning to purchase a "lived-in" home was 3.4 per cent, while the share of respondents planning to purchase a new

home was 0.8 per cent. These measures were all down from the prior month.

At least a fifth of all occupied single-family homes were rentals last year in 32 of the nation's top metropolitan regions, according to US Census Bureau data released October 20. That's up from seven metros in 2006.

Nationwide, 18 per cent of occupied single-family homes last year were rentals, up from nearly 15 per cent in 2006, show data from an annual Census Bureau survey.

As the selling, buying, and – most importantly – building, of homes in the US slowly sputters back to former levels, activity in the rental market is already booming.

The first-ever home rental asset-backed security (ABS), a US\$480 million bond trade from private equity giant Blackstone Group, the largest US private real estate owner, began marketing Wednesday. Some 300 potential investors were expected in New York for the Invitation Homes 2013-SFR1 transaction.

Nearly 90 per cent of the homes underpinning the ABS (or REO-to-rental) are located in and around Phoenix, AZ; Riverside, Los Angeles, and Sacramento, CA; Atlanta, GA; and Tampa, FL.

Deutsche Bank is the lead structurer on the deal, which is being jointly led by Credit Suisse and JP Morgan.

The US\$479.1 million deal will include a US\$278.7 million Triple A rated tranche that will have initial credit support of around 41.8 per cent. After New York, the roadshow for the deal will hit Boston, MA, on Thursday and Los Angeles, CA, Friday. The offering is expected to be officially announced Monday.

Investors are looking to gain exposure to the strengthening commercial real estate market in the United States. Vacancy rates are expected to decline for commercial properties and rents are expected to grow modestly, the National Association of Realtors said in a forecast released in August.

Back in January, Blackstone accelerated purchases of single-family homes as prices jumped faster than it expected. Blackstone spent more than US\$2.5 billion on 16,000 homes to manage as rentals, deploying capital from the US\$13.3 billion fund it raised last year, said Jonathan Gray, global head of real estate for the world's largest private equity firm at the time. That's up from US\$1 billion of homes owned in October 2012, when Blackstone Chair Stephen Schwarzman

said the company was spending US\$100 million a week on houses.

Please see the October 26, 2012 issue of your *Madison's Timber Preview* for details on Blackstone's plans.

Blackstone invested an estimated US\$7.5 billion in 40,000 homes, according to *Bloomberg*, and has continued buying aggressively. The homes are largely in Western states, where the foreclosure crisis hit hardest.

Overall, investors have bought close to 200,000 foreclosed homes in the last few years, sinking nearly US\$20 billion into this new asset class.

The trade will receive ratings from Kroll, Morningstar, and Moody's. At least one of those ratings will

be Triple A, a fact that shocked some investors relying on numerous rating agency reports over the past year that indicated a first-time REO-to-rental deal would never reach a rating higher than Single A.

One clue as to how the deal may get the top rating is that it will be secured by individual mortgage liens on each underlying property rather than an equity pledge in the property, said *Reuters* October 25. That will allow for the creation of a so-called real estate mortgage investment conduit (Remic) structure, according to people close to the deal. Remics, which are also used in CMBS, allow for the pooling of a diverse set of loans from different originators and offer flexibility in assembling a security.

Rating agencies had preferred that mortgages were in place as legal instruments in any potential REO-to-rental securitization structure, so that bondholders did not get shut out of payments in case competing liens were placed on any particular property.

Market watchers expect public backlash to the deal, considering that institutional purchases accounted for 14 per cent of September home sales and all-cash buyers accounted for almost half of sales, according to a RealtyTrac last week. That was the highest share since the real estate data firm began in 2011 to track transactions by that group, which it defines as buyers of 10 or more homes a year. All-cash sales rose to 49 per cent, from 40 per cent in August, and 30 per cent a year earlier.

As well, American Homes 4 Rent has purchased about 20,000 distressed properties, according to *Bloomberg* October 24.

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