

MADISON'S LUMBER REPORTER

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News & Updates

Madison's Notice to Subscribers:

Due to entrenching economic realities, *Madison's* is forced to start charging for subscriptions and services in US dollars. Canadian subscribers are welcome to pay in US currency, otherwise the charge will be converted to US funds at the date of the invoice.

This unavoidable change will take place January 1, 2016.

The current charge for the weekly Reporter is C\$408.45. This amount will stay the same except the new charge will be itemized in US dollars.

Madison's rates last changed, by 13 per cent, in January 2011. We trust our valued subscribers will be understanding about this financial reality.

US Paper Duty and Tariff Against Canada

Canadian paper mills that produce glossy paper products will continue to pay costly duties levelled against them last summer by the US Department of Commerce, reported *CTV News* Wednesday.

In a decision released Wednesday, the department said it has determined that US imports of supercalendered paper from Canada have received countervailable subsidies ranging from 17.87 to 20.18 per cent.

The decision upholds, and in some cases increases the tariffs first put in place after a preliminary ruling in July.

Operators affected include Port Hawksbury Paper, Resolute Forest Products, and J.D. Irving — all in eastern Canada — and Catalyst Paper of British Columbia.

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Provinces Urge Canadian Government to Negotiate SLA

Cabinet ministers in both Nova Scotia and New Brunswick are expressing concern that Canada and the United States haven't started renegotiating the softwood lumber trade agreement, according to Canadian Press Wednesday.

As well, British Columbia Premier Christy Clark has called for Canadian officials to get to the negotiating table, said *Globe and Mail* October 11.

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Home Building and Selling 2015, USA

"In hot real estate markets in the US, what's happening is rental housing is being built to profit from rising rents and luxury housing is being built to meet the demand from wealthy overseas buyers," warns Adam Taggart in *Market Oracle* October 10.

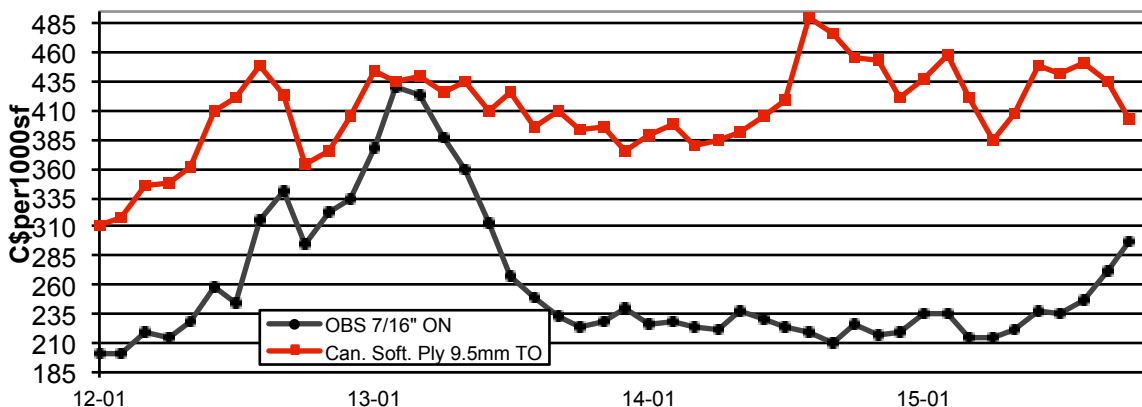
Elsewhere, in a chilling 88-page industry note, Barclays analyst Stephen Kim warns that the bullish housing tale spun by his peers is more of a fairy tale.

"And yet, over the past several months, we have become increasingly concerned about the way many analysts are portraying the industry's current weakness as a strength," Kim wrote via *Business Insider*. "To us, this seems a perilously risky oversimplification."

Further, in trading on Wednesday, shares of the iShares *US Home Construction ETF* (ITB) crossed below their 200 day moving average of \$27.20, changing hands as low as \$26.97 per share. ITB's low point in its 52 week range is \$21.22 per share, with \$29.86 as the 52 week high point.

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OSB Ontario 7/16" vs Can. Softwood Plywood 9.5mm Toronto 2012 - OCT 2015



US Housing and Real Estate Situation

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A Bifurcated US Housing Market, How Much Longer Can Unaffordable Housing Prices Last?

By: Adam Taggart

"In the normal cycle of supply and demand, new more affordable housing would be built, and prices would decline.

Eventually, prices rise to a level that is unaffordable to the majority of potential buyers, with demand coming only from the wealthy. That's the story of housing in New York City, the San Francisco Bay Area and other desirable locales that are currently magnets for global capital.

With limited land in desirable urban zones and high development fees, it's not possible to build affordable housing unless the government subsidizes the costs.

Meanwhile, the supply of existing homes for sale is limited by the owners' recognition that they won't be able to replace their own home as prices soar; it makes financial sense to stay put rather than sell and try to move up.

Some homeowners are cashing in their high-priced homes and retiring to cheaper regions. But this supply is being overwhelmed by a flood of offshore cash seeking real estate in the US.

Demographics & Housing Valuations

There are plenty of young people who'd like to buy a house and start a family new household formation), but few have the job or income to buy a house at today's nosebleed levels — a level just slightly less insane than the prices at the top of Housing Bubble of 2005-06.

Mortgage Debt & Earnings

Now that mortgage rates have hit bottom, there's not much room left to push housing valuations higher by lowering rates. No matter how solid the buyers' credit rating, mortgages remain intrinsically risky, as unexpected medical emergencies, job losses, divorces, etc, trigger defaults in the best of times. In recessions, job losses typically cause defaults and lenders' losses to rise.

All debt, including home mortgages, is based on household income and

debt levels. The higher the debt load, the more money the household must devote to debt service. That leaves less to spend on additional debt or other spending.

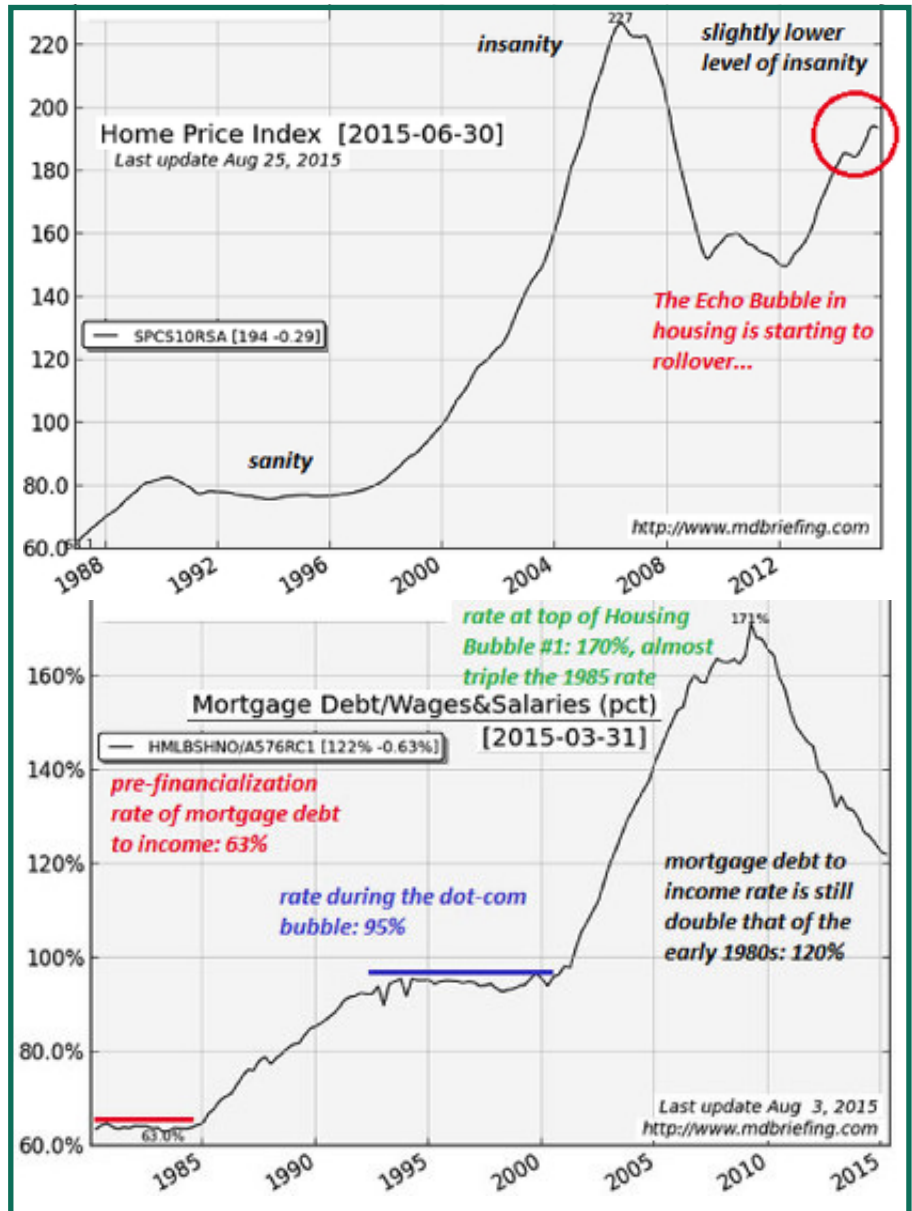
As the second chart shows, the ratio of debt-to-earned income (wages and salaries) has declined since the speculative frenzy of the Housing Bubble, but it remains almost twice the levels of the pre-bubble era.

A Bifurcated Housing Market: The New Normal?

These dynamics have created islands of strong job growth and global/domestic demand for housing in which only the wealthy can afford to buy and everyone else is a renter for life. These islands are surrounded by a sea of lower-cost housing in regions with weak job growth and stagnant wages.

Is this bifurcation the New Normal?

Right now, the general consensus is that housing prices "will never decline" in New York City, the San Francisco Bay Area, etc.—the islands of job growth and high valuations. This sentiment is due to the strong US economy and capital flows into USD-denominated assets. But if the bulk of this capital flow has already occurred, and capital controls and clawbacks become the order of the day, this prop under current nosebleed housing valuations might be kicked away far sooner than anticipated." CONT'D ON PAGE 8



Madison's Weekly Lumber Key Prices Table

www.madisonreport.com



	This Week	Last Week	Change	Month Ago	Change	Year Ago	Change
Prices are in U.S. dollars per 1,000 fbm (net FOB mill)							
WSPF KD R/L 2x4	256	250	+6	250	+6	354	-98
WSPF KD R/L 2x6	248	244	+4	250	-2	370	-122
WSPF KD R/L 2x8	278	278	0	283	-5	366	-88
WSPF KD R/L 2x10	302	302	0	325	-23	374	-72
WSPF KD PET 2x4 Stud	225	215	+10	230	-5	355	-130
WSPF KD PET 2x6 Stud	235	240	-5	250	-15	385	-150
Douglas Fir Green R/L 2x4	298	295	+3	300	-2	325	-27
Douglas Fir Green R/L 2x10	383	385	-2	385	-2	415	-32
ESPF KD 2x4 8ft Stud	310	300	+10	305	+5	430	-120
OSB Ontario 7/16" (CDN\$/msf)	302	291	+11	270	+32	228	+74
CSplywood Toronto 3/8" (CDN\$/msf)	392	404	-12	416	-24	461	-69

Madison's Weekly Lumber News

Paper Product Duties, USA

CONT'D FROM PAGE 2 The trade action is the result of a petition filed by two American producers of supercalendered paper that say the Canadian paper goods are unfairly subsidized.

Softwood Lumber Agreement Negotiation

CONT'D FROM PAGE 2 Rick Doucet, the trade minister in New Brunswick, said that it's extremely important to the industry in the province that the Canadian and US governments get back to the bargaining table.

Geoff MacLellan, Nova Scotia's acting natural resources minister, also said he's disappointed the talks are stalled and said he will work with his Maritime colleagues to protect the region's unique position in the lumber trade.

Both provinces have seen a steady increase in their lumber exports under the deal, with New Brunswick's export sales rising 40 per cent over the past four years to \$397 million, and Nova Scotia's exports reaching a value of \$85 million last year.

Out west, in 2006, BC exported US\$4.3-billion worth of wood south of the border, and that had declined to US\$3-billion in 2014.

Overall, Canada's share of the U.S. lumber market has shrunk to 29 per cent today from 33 per cent in 2006.

As well, the Alberta Forest Products Association said September 17 that Alberta's \$4-billion a year forest products

industry is concerned about the ending of the Canada-United States softwood lumber agreement.

When the trade deal expires, nine years of "relative trade peace ... could all be torn asunder," said Paul Whitaker, AFPA president and CEO.

Japan Housing Starts

Japan's Ministry of Land, Infrastructure, Transport and Tourism released Japan's housing starts for August, which were 80,255 units (up 8.8 per cent from the same month in the previous year), said *Japan Lumber Journal* Thursday.

Owner-occupied and rental houses increased for four consecutive months, and built-for-sale houses turned to an increase from a decrease in the previous month. The number of housing starts surpassed previous year's result for six months in a row.

By structure, housing starts of wooden houses were 45,140 units (up 11 per cent), marking a double digit increase on the back of the increase in housing starts of owner-occupied houses and rental houses. Non-wooden houses were 35,115 units (up 6.1 per cent). The ratio of wooden houses by the number of units increased to 56.2 per cent, said the *Journal*.

West Fraser Buys, Canfor Closes

West Fraser Timber, out of Vancouver, BC, announced Thursday it has entered into an agreement to acquire Alberta's Manning Diversified Forest Products, which has sawmill operations

located in Manning, AB, and related timber harvesting rights, to be completed before the end of October, 2015.

West Fraser plans to take the site's lumber production to 130 million board feet by adjusting current operations and expanding annual production capacity.

The timber rights acquired have a current operational annual allowable harvest of approximately 440,000 cubic metres of coniferous timber.

Also based in Vancouver, BC, Canfor Corp announced Wednesday it will stop making lumber at its Canal Flats sawmill in British Columbia on November 9, due to a lack of roundwood and dwindling demand for softwood lumber, especially from the oil and gas industry. Canfor had already switched production in Canal Flats to a single shift at the start of May for the same reasons. This production cutback halved the number of people working at the sawmill from 160 to 80.

The Canal Flats sawmill, which has a capacity of 180m bdft when running two shifts, has been owned by Canfor since March 2012.

Weyerhaeuser Breaks Ground

Site preparation for the new Weyerhaeuser sawmill complex at Dierks (Howard County), AR, is winding down as the project shifts into the next phase of it's US\$190 million construction this week, said *Arkansas Business* Monday.

The new facility will have an annual production capacity of 387 million board feet, 25 per cent more than current capabilities.

US Housing and Real Estate Situation cont'd

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The Housing-Market Bulls Could Have the Story Wrong

By: Stephen Kim, Barclays' US building products and home-building-equity analyst

"At this point, it has become hard to overlook housing's dismally slow pace of recovery.

Sure, home prices are back to historic highs and housing-market activity continues to pick up, but many important aspects of the housing market are depressed.

The housing recovery hasn't lived up to expectations so far; this is something about which housing bulls and bears can probably agree. Indeed, 10 years after the last peak, single-family starts (which matter most for public builders) are at traditional trough levels, and total starts aren't much better.

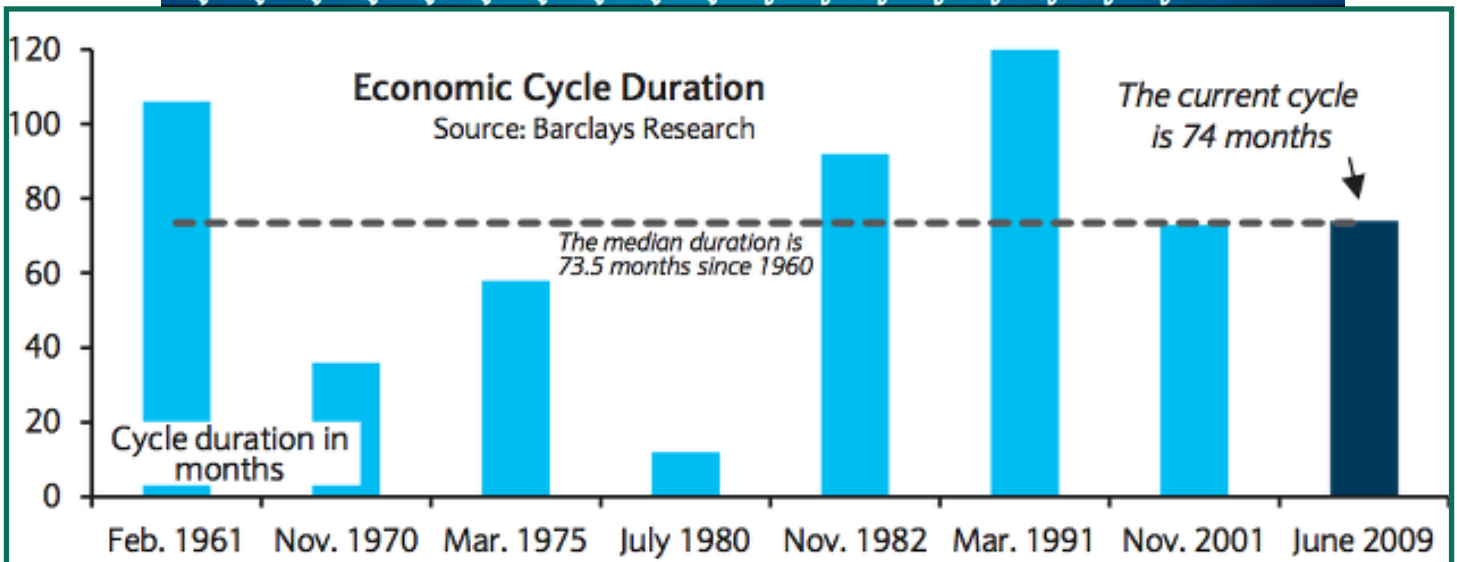
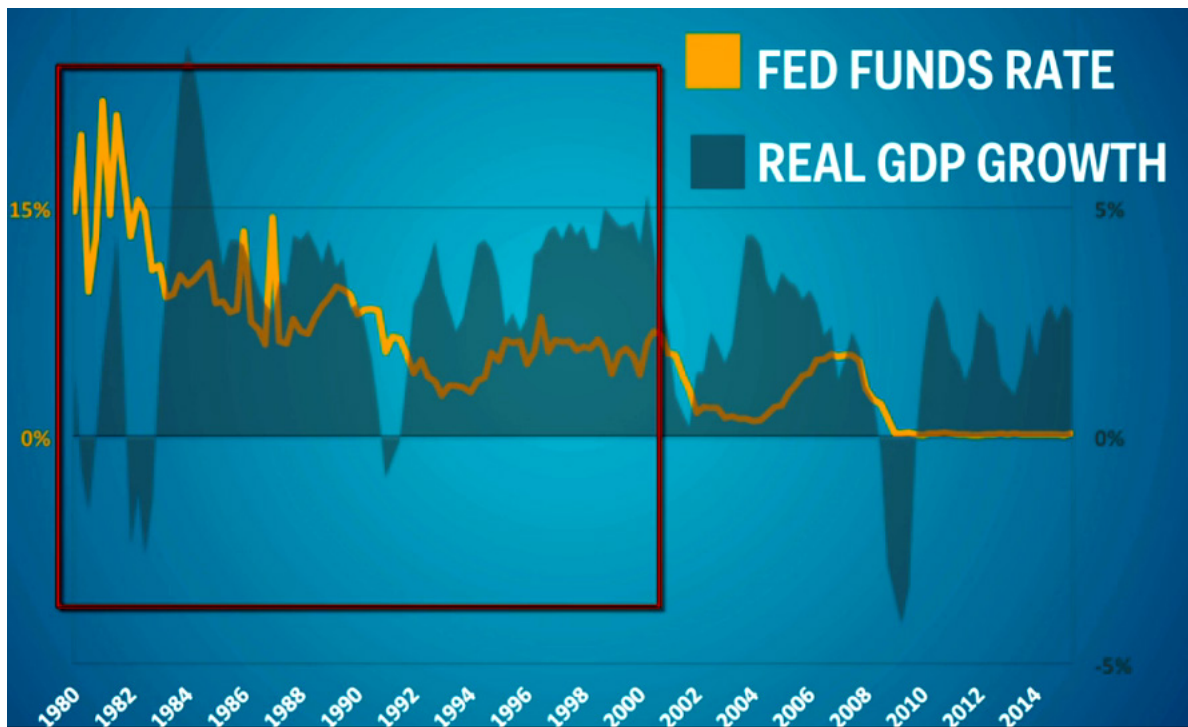
It's hard to dispute what's going on in single-family housing starts.

Particularly alarming to us is when we hear that 'housing has lagged' the economy, or that housing demand is 'slow and steady'. Call us cynical, but last we checked, housing doesn't lag anything — it's a leading indicator; and just because housing is slow doesn't make it more steady or less cyclical, it's just slow.

Two Housing Realities

There are two realities that we think investors still need to come to grips with. First, pent-up demand can stay pent up for a long time, and second, housing probably isn't early-cycle anymore.

Pent-up demand is the idea that there are buyers in the pipeline, waiting to pull the trigger, but when can you expect them to pull the trigger? CONT'D ON PAGE 9



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To be clear, we believe pent-up demand in housing is real, but we also believe this deficit may persist for many more years. Meager wage growth, crushing levels of student debt, glacial expansion of credit, negligible support for a housing stimulus in Washington, Millennials' cynicism towards home ownership, a looming Texas slowdown, and a shortage of construction labor have all been impeding a satisfying snap-back in housing demand thus far.

No Quick Fix

To our eyes, these challenges defy a quick fix, and are likely to keep the growth rate of housing demand constrained for the foreseeable future. Second, the presumption that the housing recovery is still in the early stages is worrying to Kim. He says that a common question is "What are your mid-cycle [i.e., 2017] earnings estimates?" To Kim, we may already be in mid-cycle. It seems reasonable to think that this might be a truncated cycle — cut short by an economic recession."

In this environment, Kim likes building-products companies over home builders, and he suggests staying away from companies that depend on the housing market accelerating.

Residential Construction Hiring

As if to bear out some of these sombre analyses, the US National Association of Home Builders said Friday the count of construction job openings held steady in August as hiring in the home building sector continued to slow. The average monthly employment gain for builders and remodelers is just over 5,500 over the last six months.

According to the BLS Job Openings and Labor Turnover Survey (JOLTS) and NAHB analysis, the number of open construction sector jobs was effectively unchanged at 138,000 for August. The cycle high of 168,000 was set during March.

On a three-month moving average basis, the open position rate for the construction sector ticked down to 2.1 per cent for August. The open rate has been trending upward since 2012, with the current three-month moving average slightly off the cycle high set during May (2.4 per cent).

In September, the number of jobs in home building and remodeling (seasonally adjusted) increased by only 3,900. The pace of hiring for the industry has slowed over 2015, with the average monthly employment gain standing at just over 5,500 over the last six months.

China All-Cash Purchases of US Homes

It is important to note, however, that an analysis of housing sales in the US shows that 46 per cent of Mandarin Chinese-speaking buyers who purchased homes in the 17 months ending in May 2015 paid all-cash, according to RealtyTrac Tuesday.

The analysis by the Irvine, California-based realty research company and Ethnic Technologies, a New Jersey-based multicultural marketing company, also showed that since 2005 Mandarin-speaking buyers paying all cash had an increase of 229 percent from the 14 per cent share paying all-cash in 2005.

The two companies looked at 10 million publicly recorded residential property sales deeds in 2014 and 2015 compared with 2005 by ethnicity and native language spoken. RealtyTrac quoted several US brokers in various parts of the US about sales.

Asian buyers make up more than one-third of all international real estate buyers in the US, and Chinese buyers spent US\$22 billion on US housing in the 12 months through March 2014, 72 per cent more than a year earlier, according to the National Association of Realtors, buying mostly high-end homes with a median price of more than US\$500,000.

