



STELLAR BC SAWMILL EARNINGS ON RECORD-HIGH LUMBER PRICES

The recent run on lumber prices has put big smiles on the faces of sawmill operators and lumber traders. Despite US import duties, lumber prices rose and held during a very uncertain period last year. Lumber prices then surged in the fourth quarter of 2017, catching many by surprise due to the sheer magnitude of the increases and strength of the run. As a result, most sawmills are achieving incredible earnings, with some BC companies (such as West Fraser) reaching 25 per cent

Interior companies (West Fraser, Canfor and Interfor) own 45 sawmills in the US (almost all in the South), high sawmilling returns are still being achieved for those with fewer US mills, e.g., Canfor (with 27 per cent of its production in the South) and Western Forest Products (with no operations in the South, but including coastal log sales).

Mill prices for all lumber species in North America have been trending higher since preliminary US import duties commenced in February 2017, and

demand in export markets, has created an almost perfect storm. As a result, record-level lumber prices have been achieved for most species (table 1 is on page 54). One of the major exceptions has been studs, which have languished in comparison to dimension lumber.

The record prices (chart 2 is on page 54) enjoyed by Canadian producers come with a caveat: sales to the US are currently subject to an “all others” 20.2 per cent import duty. These mean the high prices need to be reduced by import duties of US\$92/Mbf on US sales for W-SPF and US\$154/Mbf for western red cedar. Despite this, however, net returns are still as good as during some of the previous highs. In addition, record-high prices have been seen in markets such as Japan where W-SPF J-grade reached US\$660/Mbf in April and green hemlock squares have just cracked the US\$1,000 mark.

All of these stellar results occurred at a time of periodic log and lumber production curtailments in BC: 2017 BC Interior shipments were 5 per cent lower than in 2016; Coast lumber shipments were off by 7 per cent; and Coast log exports were down by 5 per cent. The shorter operating period in 2017 due to weather conditions, some mill closures and now railcar shortages has meant reduced output and deliveries at a time of strong market demand and most export markets. Even with US import duties creating some uncertainty for buyers, 2018 has started out as one of the best years ever in the lumber business, with US and global buyers chasing BC mills for their lumber products.

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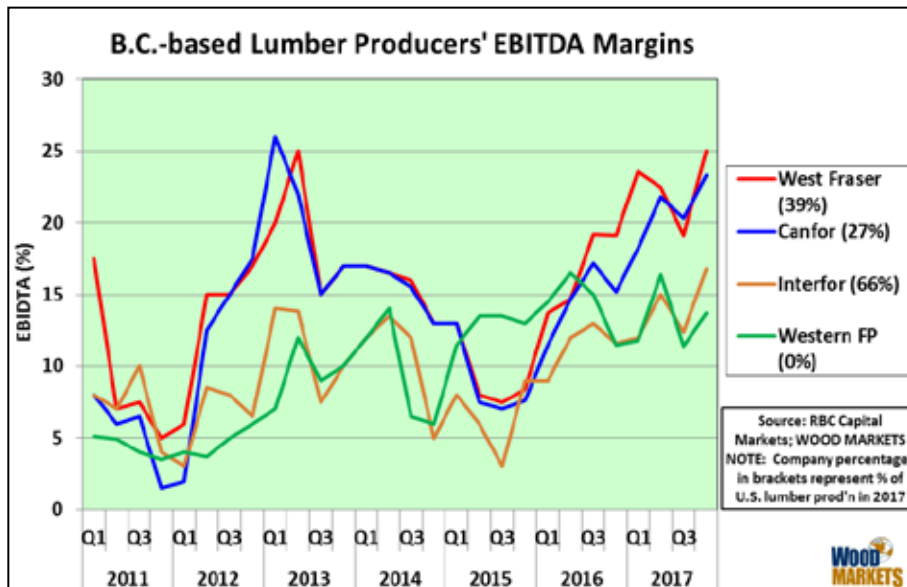


Figure 1

earnings before interest, tax and depreciation (EBITDA) on Canadian and US operations in the fourth quarter of last year (figure 1).

Global sawmill earnings are the highest in the US South, according to Forest Economic Advisors Canada/WOOD MARKETS' ongoing global sawmill cost benchmarking surveys. While three BC

especially after permanent duties averaging 20.2 per cent started in late December 2017. While the implementation of US import duties was expected to push prices somewhat higher, the interaction of several factors including the seasonal impact of summer forest fires in 2017, severe winter weather followed by railcar shortages in 2018 and continued strong

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Are we in the “supercycle” first predicted by WOOD MARKETS some eleven years ago? Maybe/probably. Certainly, the reduction in lumber output in the BC Interior and Eastern Canada

by 140 per cent in 2017 and are up 125 per cent through the first two months of 2018: European and Russian producers are attracted by high US lumber prices and can provide the incremental

All of this should translate into continued windfall of earnings for BC sawmill companies. One of the issues facing some of the larger firms will be what to do with the huge amounts of cash generated from operations.

has materialized as forecast. The wildcard has been the level of demand and US housing starts which have recovered much more slowly than almost everyone predicted but are now at a level to reveal the supply gap. This is why European lumber exports to the US grew

volumes that Canada and US sawmills cannot supply.

The outlook for lumber prices for the rest of 2018 and 2019 is for more of a wild ride. There has been so much uncertainty and so many dislocations throughout the entire supply chain

since mid-2017 that price predictions have become difficult to make. However, FEA Canada/WOOD MARKETS’ current forecast calls for record average annual prices for 2018. For 2x4 W-SPF, an average price increase of at least 25 per cent (including US import duties) is expected in 2018 versus 2017, with the average price for the year expected to exceed US\$500/Mbf. For 2019, we project strong prices in the first half of the year before a slowdown begins in the second half; the average annual price should ease, but it will still be in the high, US\$400/Mbf range. Similar strong and record-level prices are expected for BC Coast lumber.

All of this should translate into continued windfall of earnings for BC sawmill companies. One of the issues facing some of the larger firms will be what to do with the huge amounts of cash generated from operations. As has been common industry practice, some companies will be spending more on mill capital expenditures, while some will be considering more acquisitions and some will need to resort to buying back their shares. The thing companies will also need to remember is that their entire supply chain needs to be properly managed and maintained if these strong operating results are to be achieved. This means from loggers and truck drivers to logistics (rail cars, trucks and containers) from mills to customers worldwide, any part of the supply chain that is not properly managed will leave some companies unable to take full advantage of this incredible lumber market run.▲

Record 2x4 #2&Btr Dimension Lumber Prices				
	Record Date	US\$/Mbf	Previous Record	US\$/Mbf
W Red Cedar* (grn)	Jun 23 2017	915	Oct-07	815
W-SPF	Apr 13 2018	546	Dec-93	446
E-SPF (Gr. Lakes)	Mar 21 2018	625	Nov-96	529
Douglas-fir (grn)	Feb 23 2018	607	Jul-99	525
Hem-fir (Spokane)	Feb 23 2018	595	Sep-96	499
SY Pine (West)	Mar 16 2018	595	Nov-96	540
* Note: Std&Btr	Before duties	Source: Random Lengths		

Table 1

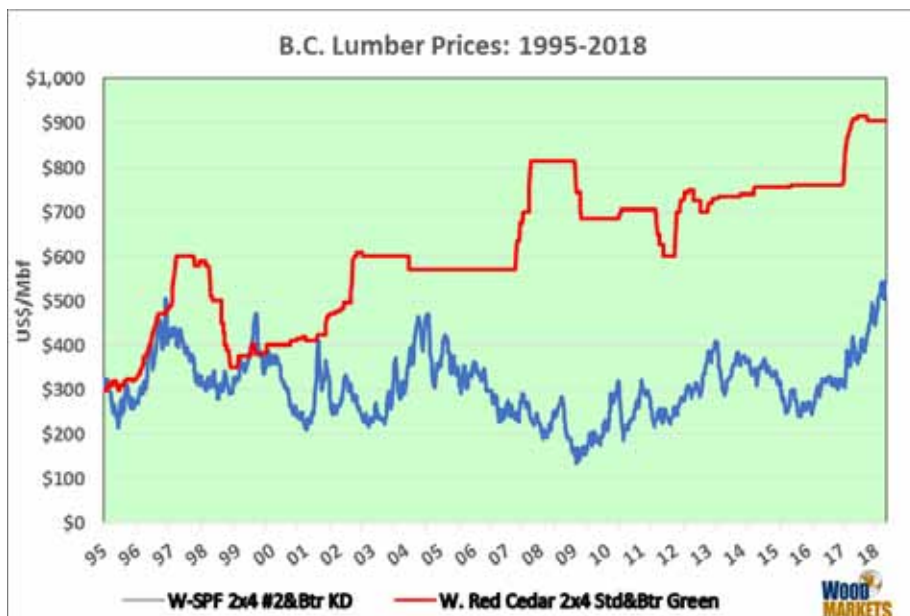


Chart 2

Russ Taylor's background in the forest industry started in 1974 and encompassed forestry, manufacturing, marketing and consulting positions. Mr. Taylor gained hands-on expertise in marketing lumber and specialty products throughout North America and overseas, holding positions in sales, marketing, custom cutting and remanufacturing.