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Are U.S. Softwood Lumber Producers About to be "SLAin"?

As most forest-products industry watchers are aware, the nine-year-old Softwood Lumber Agreement (SLA) between the United States and Canada is slated to expire on October 12, 2015. The SLA, which imposes taxes and quotas on Canadian softwood lumber exported to the United States ("CDN lumber exports"), stipulates that when the prevailing monthly price is at or under $355/MBF, border measures of either an export charge or an export charge plus volume restraint must be placed on CDN lumber exports. Ironically, CDN exporters will face the most punitive taxes and quotas on shipments to the United States in October before the SLA expires. The four-week average of the Random Lengths Framing Lumber Composite Price (FLCP) that will determine the October tax was $313. Any time the FLCP average dips to $315 or lower, Western CDN manufacturers are assessed a 15% tax on cross-border shipments. Those in Quebec, Ontario, Manitoba, and Saskatchewan will pay a 5% tax, plus face the most restrictive quota allotments.

With the quotas and taxes going away, is the U.S. market about to be inundated by cheap CDN wood surging south? If *Business Vancouver* is to be believed, "a wall of wood, gift-wrapped in devalued Canadian mill wrap...is accumulating at sawmills, transit yards and rail points inside Canada." No doubt the hyperbole is partly true. However, WWPA's September Lumber Track pegs British Columbia (B.C.) sawmill utilization rates at 90%, suggesting only limited production upside. U.S. lumber prices continue to fall, and while the weak CDN$ lends support to CDN mills it has not rescinded the law of profitability. Also, B.C. inventories as of June (most recent data reported) are down 6% YoY. So, more CDN supply to the U.S. market in the short run? Yes. Inundated? Probably not.

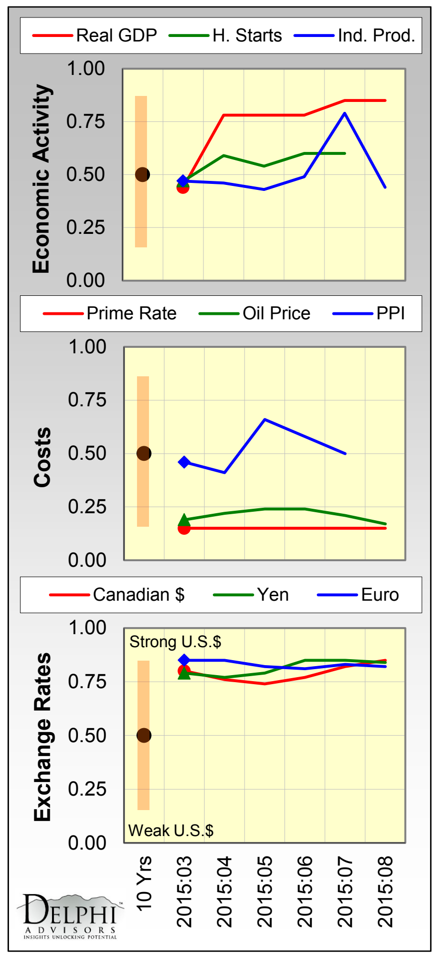
Although CDN manufacturers stand ready now to "make hay while the sun shines," the longer-term picture is less clear. As a result of the mountain pine beetle outbreak, B.C.'s annual allowable cut (AAC) is expected to be reduced in coming years by 25% below 2010's AAC. To compensate for that lost production and market share, three of B.C.'s largest timber companies have embarked on an asset buying spree and now own more U.S. than CDN sawmills. Those firms will have a clear incentive to balance their CDN production to minimize harm to their U.S. interests.

As for other trade-related developments, U.S. exports of softwood lumber decreased by 7 MMBF (5.1%) in July while imports fell by 166 MMBF (-13.9%). Mexico was the largest single-country export destination (23.8% of U.S. total) in July, whereas 96.0% of U.S. imports originated in Canada.

U.S. exports were 16 MMBF (10.9%) below year-earlier levels in July; imports were 81 MMBF (7.3%) lower. YTD through July, exports were down 13.4% relative to the same months in 2014, while imports were up 4.8%. U.S. exports to China were down over 41% YTD.

Elsewhere in the U.S. economy, total industrial production (IP) decreased 0.4% in August (-0.2% expected) after increasing 0.9% (originally +0.6%) in July; total IP in August was 0.9% above its year-earlier level. On the other hand, manufacturing output fell 0.5% in August primarily because of a large drop in motor vehicles and parts. Wood Products output edged down by 0.1% (-1.7% YoY) while Paper rose 0.1% (-1.4% YoY).

This report references articles posted on our website; those articles relate recent economic developments to the U.S. forest products sector. ■



Previous six month's behavior of macroeconomic variables indexed relative to their historical 10-year min, max and average (lower and upper ends of the orange bars, and black dots, respectively)