

2x4s at US\$966! ...What Comes Next?

WELCOME! - I am pleased to present the second edition of the *View From The Stump* newsletter, a ground-level perspective of the BC forest industry.

Readers' feedback for the inaugural issue was very positive and has emboldened me to continue with this next edition.



The pandemic has changed our world in so many ways. I can guarantee that no-one could have predicted the strengthening in North American lumber demand arising out of the pandemic led-shutdowns last spring. Not surprisingly, lumber producers took a conservative stance in managing log and lumber inventories as a global recession loomed. And yet now we are amidst a lumber price super-cycle when it was least expected!

SO, WHAT COMES NEXT? A truism in the volatility of commodity lumber prices is that what goes up, must come down. SPF 2x4 lumber prices will fall. As to when will prices drop? Already, cracks in prices appear to be forming. Most importantly, how far will lumber prices fall?

To answer that last question depends on whether you believe the market is witnessing a structural change to the pricing of lumber. A major shift in lumber prices came in the early 1990s when the US government shutdown harvesting on federal lands in the Pacific Northwest in order to protect spotted owl habitat. Prior to 1992, notional prices of SPF 2x4s traded within a relatively narrow range of \$100/mbf to \$250/mbf.

The halting of federal harvest led to a lumber price rally which saw a peak north of \$400 in 1992. Aside from a cycle low of \$134 in 2009, lumber's trading range never returned to levels comparable to the pre-spotted owl era.

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The rally of 2017 to 2018 saw prices go far beyond expectations to a peak of \$658 (on a weekly, print basis) in May 2018, with prices then slipping to a low of \$298 in June 2019.

The current price rally has seen prices reach \$966, which is \$308 above the May 2018 peak.

The point is, average (and the range of) lumber prices in the 1992-2017 era were higher than the pre-1992 era, and now with the rallies of 2018 and the current one, prices appear to be stepping up to new higher averages with a new range of higher highs and higher lows above those in the 1992 to 2017 time frame.

What's In This Issue...

- 2x4s at US\$966! ...What Comes Next? ...page 1
- Analysis: Interior Harvest, North vs South...page 2
- BC Forest Industry Metrics...Page 3
- The Timber Harvesters Business Network...4
- The Radar Screen...page 5

Aside from implications to lumber demand, what do higher average lumber prices mean for BC's supply chain?

TIMBER SUPPLY: Higher prices mean greater economic latitude to access timber supply – this is particularly important for the interior where there is a balancing act between hauling distance, yield of lumber from logs (due to deterioration from beetles or fire) and the

returns on lumber. Unfortunately, I would not bet on a major uptick in harvesting as beetle-killed salvage timber is likely reaching the end of its shelf-life.

STUMPAGE: In BC, higher lumber prices brings higher stumpage. The stumpage hangover from the 2018 rally left painful memories that many lumber producers wish not to re-live. With stumpage linked to lumber prices with a three to six-month lag, it is fair to say pending increases to stumpage is a major concern when the current rally in lumber prices inevitably falters. Using **MDT's** market-based indicators model, stumpage is predicted to rise by 125% over summer rates in the next two quarters.

CONTRACTOR RATES: Higher contractor rates are not necessarily a given with higher lumber

prices. It's all about supply and demand. If sawmills want logs in the near-term, and there is only so much contractor capacity available to respond, it is plausible that we will start seeing higher contractor rates.

EQUIPMENT SALES: Like contractor rates, equipment sales will not increase just because of higher lumber prices. In fact, the general observation from our latest **Timber Harvesters Business Network** survey suggests most contractors are holding off as much as possible on purchases, rotating only what is necessary, given what many view as a repeat of 2018.

If you are a contractor running heavy equipment you should be part of the THBN.

To join the THBN, [CLICK HERE](#)

Analysis: Interior Harvest, North vs South

Conventional wisdom would view higher lumber prices as driving harvest volumes higher, yet timber harvesting in the interior has been decreasing so far this year. Covid-19 shutdowns earlier this year undoubtedly was one source for a reduced harvest. Another source has been the amount of precipitation, depending where you operate.

Harvesting in the northern interior saw activity down by 30.3% ytd through August while in the southern interior, harvesting was down by 16.8% ytd. Harvesting during the month of August made a big difference for each region, with the north down 26.8% y/y while the south increased by 52.6%.

Obviously, there is something going on here – and it comes down to rain. It has been wet, particularly in the northern interior. The Prince George weather station shows the aggregate of June, July and August as the soggiest in over a decade. Last year was wet too, but only for July and August.

Muddy haul roads have severely reduced delivery of logs to northern interior sawmills – possibly a contributing factor to the current lumber rally. It has also added to contractors' costs, who have wood decked, but still need to deliver.

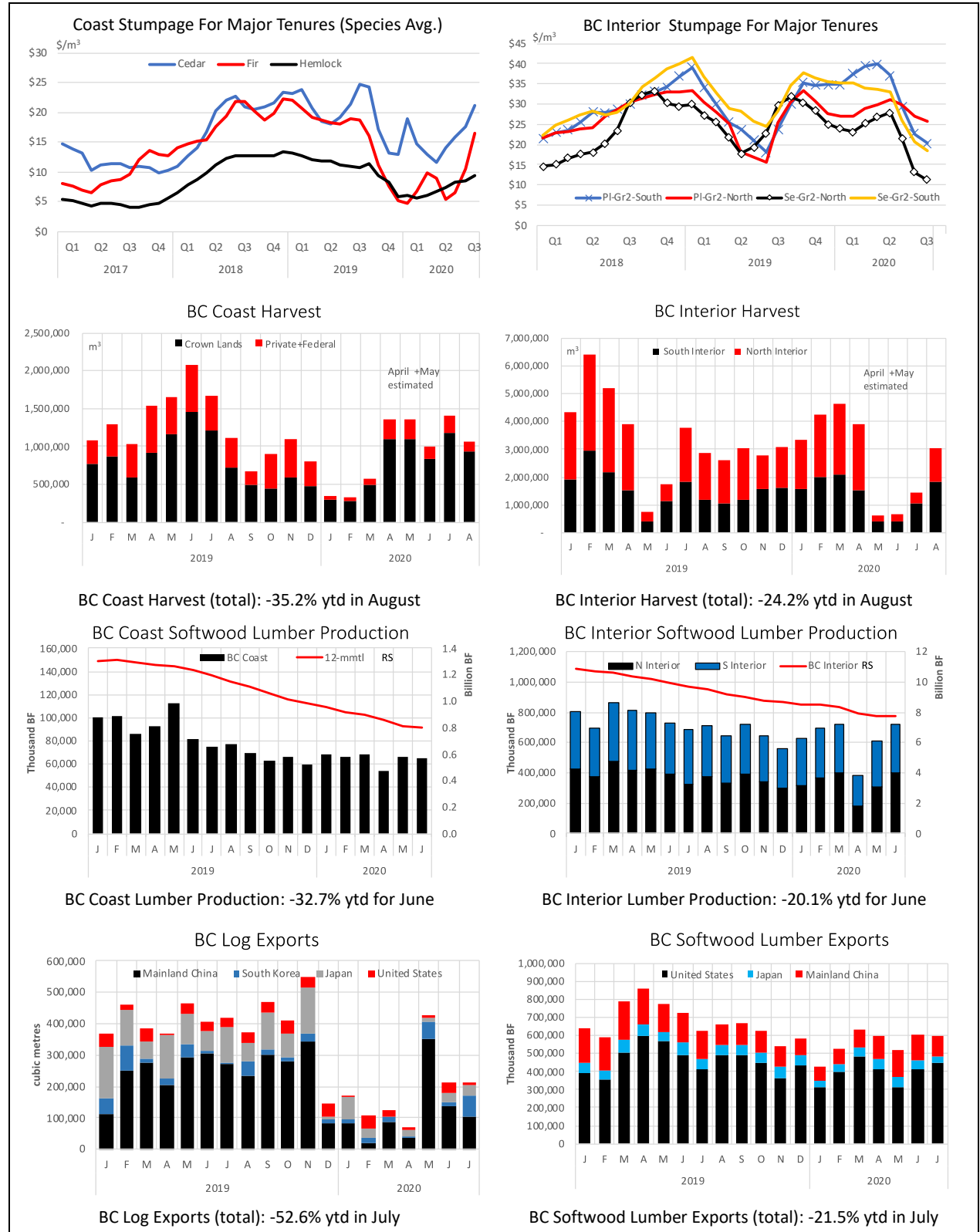
TIMBER HARVESTERS BUSINESS NETWORK:

This last summer's **THBN** survey has expanded to include input from over 6 million m³ of coastal and northern interior contracting capacity!

Northern interior contractors stated they had work lined up until next spring. That's great, although how much of that was work which should have been completed well before now – that's a question that did not get answered.

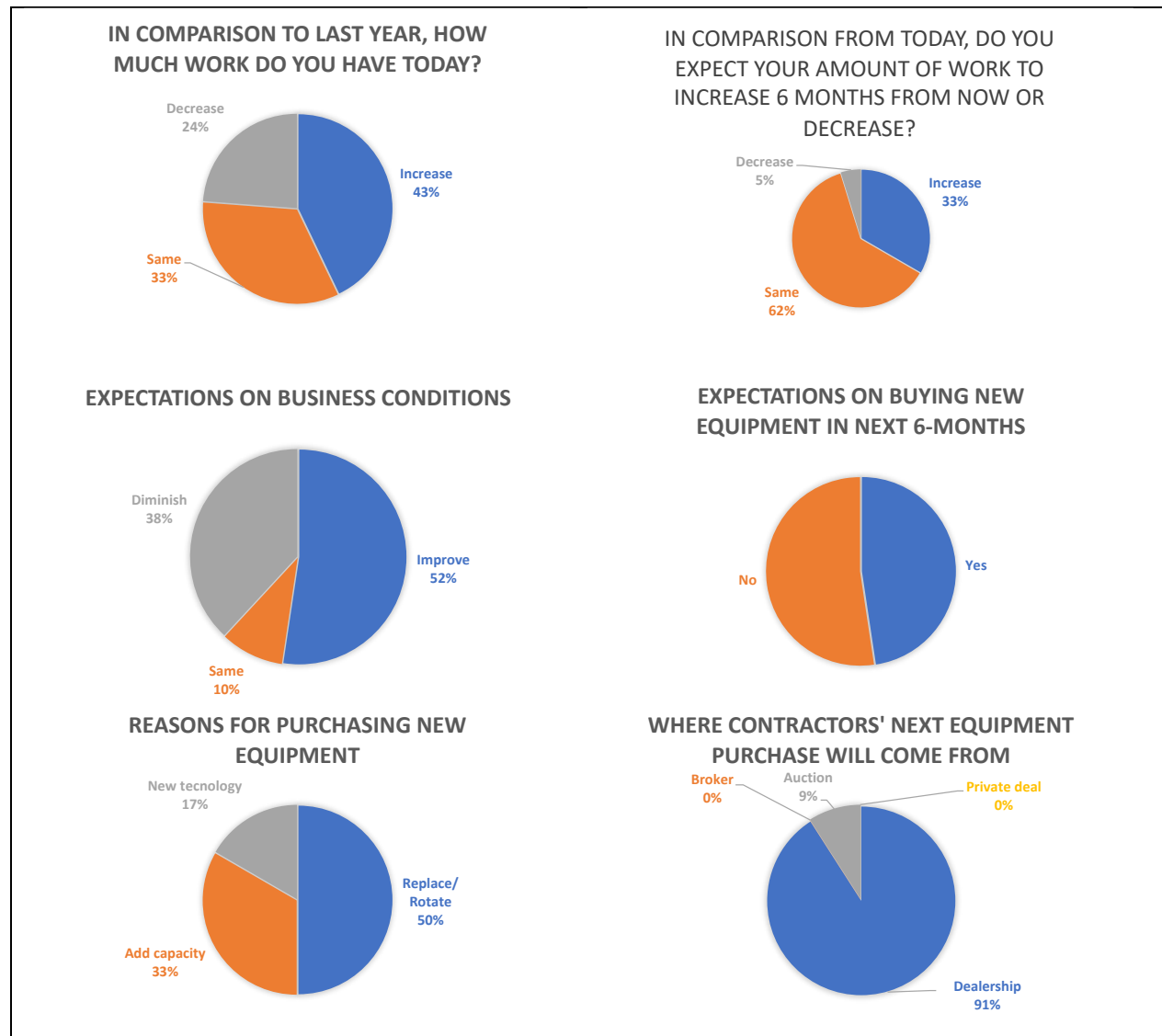
In general, the collective feedback from the interior and coast finds that contractors have not seen much evidence of this rally reflected in their position within the supply chain but are hopeful for themselves and their employers.

BC Forest Industry Metrics



The Timber Harvesters Business Network: Expectations

Data collected throughout July, August and September represents the second survey for what is becoming a unique perspective of expectations. The expectations shown in the charts below consist of coastal and northern interior timber harvesting contractors in aggregate.



Understand the BC Forest Industry from the ground-up. Our data set is growing – contact us to find out what we know about supply chain demand, that you do not...
Contact: david@spartreegroup.com
 Suppliers – for presentations on what contractors’ expectations are for their next equipment purchases and business prospects, please contact us.

The Radar Screen....a summary of announcements including new government policies that you must have on your radar screen as they will affect the BC forest sector supply chain:

BC PROVINCIAL ELECTION

October 24th, 2020 – GET OUT AND VOTE!!!!!!

Old Growth Strategic Review – the report is now public! Upon release of the report, the BC Government moved immediately to defer harvesting in 353,000 ha across nine areas around the province. *At first glance this report appears weak on the analysis of economic and social considerations.*

Interior Forest Sector Review – a public engagement process to gather input on what the industry/communities see for the future of the BC interior forest sector. A “What We Heard” report has been released. *Tenure and fibre supply topped the list of policy areas of highest importance.*

Softwood Lumber Dispute – changes to cash deposits for U.S. counter-veiling and anti-duties has been postponed until late November 2020. *This will reduce the cost burden of the Canada/U.S. trade dispute on BC lumber exporters to the U.S.*

Manufactured Forest Products Regulation – implementation of changes was delayed to September 30, 2020 - when there will be a fee-in-lieu on exports of minimally processed sawnwood on all permits as of October 30, 2020.

Contractor Sustainability Review – discussions lead by industry associations on potential changes to the Timber Harvesting & Sub-contractor Regulation (aka Bill 13). *Timing – indefinite given October 24th, 2020 provincial election.*

Short-term Work Opportunities For Interior Contractors – no indication yet what this will look like going into 2021.

Coast Logging Equipment Support Trust – offers bridge financing from a \$5 million fund for coastal contractors – the majority of funds remain unused.

Covid 19 – Provincial Tax & Revenue Changes - carbon tax increases have been postponed, staying at April 1, 2019 rates of 8.89 ¢/litre for gasoline and 10.23 ¢/litre for diesel.

Industrial Inquiry Commission – recently announced Ministry of Labour review of contract tendering in the forestry sector to assess protections for fair wages and job security when services are tendered.

BC Increased Employment Incentive – as part of the recently announced BC Economic Recovery Plan, a tax credit for businesses hiring new employees.

BC PST Rebate on Select Machinery and Equipment – as part of the recently announced BC Economic Recovery Plan, a 100% PST rebate on equipment purchases – ends Sept. 30, 2021

View From The Stump

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This newsletter represents an example of the analysis and strategic guidance and insights that I am available to provide. I hope you enjoyed this issue!

To subscribe, please contact
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