PM 41048506 $3.00 + HST
The Working FOREST
Summer #2 2016 • Vol. 20 #5

BC Fears the Worst

Roadblocks hamper a timely settlement to the SLA dispute

BY JOHN THOMSON

In a word, it's not going to happen. That's the view west of the Rockies when it comes to agreeing on a new Softwood Lumber Agreement before the grace period expires October 12. There are just too many significant differences to overcome. Given the political mood in the States and strong lobbying from the U.S. Coalition for Fair Lumber Imports, Kevin Mason, Managing Director of ERA Forest Products Research, a Vancouver firm which advises investors on forestry issues, believes the Americans are in no hurry to hammer out a new Agreement, and that, he says, will lead to a new round of tariffs in the immediate future.

"There's definitely a sense of protectionism," says Mason. "What's the incentive for the U.S? Why not just penalize the Canadians with high duties and bleed them dry for awhile and then when [Canada] starts winning in the courts, then maybe we've got an incentive to get the deal struck."

Paul Quinn, a paper and forest products analyst at RBC Capital Markets, echoes that sentiment. "We believe the US Coalition will petition the Department of Commerce for duties on October 12th," he says. "We think it'll take the Department of Commerce five or six months to come up with a finding and the countervailing and anti-dumping rate will be attached to that."

He expects an initial CVD / ADD duty of 25 percent will be imposed mid 2017. "Really, at the end of the day they can make the number anything they want," says Quinn. After that, it's back to the courts for a compromise.

"I think the Canadian legal position is quite a good one," he continues, referring to Canada's history of winning three out of four previous disputes before NAFTA and WTO panels. "Unfortunately in the U.S. system, the trade laws are all in their industry's favour and it's quite a difficult one to tackle. But you can win it. It's just going to take awhile." The outgoing SLA, Quinn reminds us, took five years to settle.

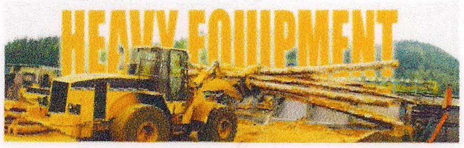
Why the pessimism? Market share is the major stumbling block. Under the previous Agreement, access to the American market was controlled through a system of tariffs in B.C. and Alberta and a quota system, coupled with a sliding scale of small tariffs, in the east. The outgoing SLA capped market share at 34 percent when in fact it hovered around 29 percent. Canadian producers liked the flexibility, quota or duties, depending upon their location but the Americans are having none of it.

"BC has been adamant they will not accept quotas and the U.S. has been equally adamant, as far as the last Agreement is concerned, scrap it, forget it. We're not about to sign a warmed over Agreement even with a few changes and we are fully looking for some kind of market share or quota limitations," says Mason of the American position. To date, the U.S. has offered 28 percent market share working down to 22 percent in four years. "Frankly, those are ridiculous starting points," he says...

"The U.S. would like a harder quota on everybody, certainly B.C., and anything above that would be subject to a penalty," says Henry Spelter, a partner in Forest Economics Advisors, a Massachusetts - based aggregator which collects data from the U.S. government, producers and private landowners and tabulates its findings in weekly, monthly and annual status reports. B.C. attracts particular attention because the bulk of Canadian softwood exports to the States (over 50 percent) come from British Columbia and the Americans are afraid unfettered access to their market will pump up the B.C. forestry industry at the expense of their own.

"In B.C. production capacity has been essentially flat with at least four mills shuttered since the beetle kill and recovery from the 2008 recession so there's no growth

Continued on **page 2**



Lumber agreement

Continued from **page 1**

in capacity," says Spelter. "There's growth in production as mills try to reach the limit of their capacity."

Regional divisions compound the problem. With BC favouring an export tax and eastern Canada preferring a quota system, it's difficult for Canada to present a united front.

"It's the old adage of divide and conquer," says Mason. "So if the U.S. just says you know what? Quota. Take it or leave it. Well, you've got BC that's saying absolutely no quota and a lot of the other parts are saying sure we'd be fine with it. You've already got us divided."

"The Americans say they want quota but what they really want is higher lumber prices and quota is one way to achieve that," continues Quinn. Pricing is another stumbling block.

Lumber prices, as determined by the Random Lengths Framing Lumber Composite, drive the triggers. At the moment, anything over the prevailing monthly price of $355 per thousand board feet is exempt from duty in B.C. and Alberta and free of volume restrictions in the east. Anything below $355/MBF triggers a tier of duties, five, 10 or 15 percent in the west and a lower rate plus volume restrictions elsewhere. It worked well when the Canadian dollar had parity with, or came close to, the American greenback, not so fine, from the U.S. perspective, when the Canadian dollar plummeted. The Americans would like to see the trigger in Canadian dollars.

"We had taxes coming in at 355. Maybe it comes up to 375. And maybe a 15 percent tax on the maximum is not high enough and it's got to go to 20," says Quinn.

"That would be the tweak that would satisfy a lot of concerns," says American analyst Spelter. "Having the trigger levels in Canadian dollars is probably the easiest way to take the exchange rate fluctuation into account so that if it moved up or down, the amount of tariff it triggers would be adjusted to offset changes in the exchange rate."

For the moment, a number of companies are waiting to see what happens with the negotiations.

"I think duties will trigger a number of decisions by companies to say 'okay, no, this mill is not viable in the long run,'" says Quinn, adding he expects a number of B.C. mills to close down. Ironically, Canadian companies which have bought mills in the southern states such as Interfor, Canfor and West Fraser will actually benefit from limitations on Canadian wood; it's the domestic mills that will suffer. "We don't have enough fibre to handle the number of mills we have now," says Quinn.

Mason believes it's the added value sector which ships out trusses, joists and any kind of custom work, that will suffer the most.

"It all comes down to market share and giving Canada the flexibility to increase exports when the market is hot and then give the U.S. the chance to break exports when the market is weak, says analyst Spelter. "So you want flexibility in both directions." The outgoing Agreement accommodated that freedom, he says, adding that he's of two minds about a new deal.

"Looking at it logically from my perspective, I would say yes, but looking at it from another point of view with the increased protectionist mood on the political front and the way things are going in that realm, it may embolden people to try to go for the home run and then it would be litigation again. It I had to put my money on it, I'd have to say we will start litigating again in October."