Recent Developments in the Softwood Lumber Trade: Potential Impacts of Lumber Duties on Lumber and Timber Markets

Rajan Parajuli
Assistant Professor & Extension Specialist
North Carolina State University
Raleigh, NC
Outline

• A brief lumber dispute history
• Softwood Lumber Agreement 2006
• Recent developments
• Impacts of tariffs on lumber markets
• Impacts of tariffs on timber markets in the U.S. South
Canadian softwood lumber

- More than 95 percent of all imported lumber came from Canada last year.
- In 2017, imports of softwood lumber from Canada were valued at an estimated $6.25 billion.

1m³=423 board feet
A brief lumber dispute history

The SLA 2006 expired on October 12, 2015 after nine years in effect.

Duty thresholds under SLA 2006
### Softwood Lumber Agreement 2006

<table>
<thead>
<tr>
<th>Prevailing Monthly Price</th>
<th>Option A – Export Charge (Expressed as a % of Export Price)</th>
<th>Option B – Export Charge (Expressed as a % of Export Price) with Volume Restraint</th>
</tr>
</thead>
<tbody>
<tr>
<td>Over $US 355</td>
<td>No Export Charge</td>
<td>No Export Charge and no volume restraint</td>
</tr>
<tr>
<td>$US 336-355</td>
<td>5%</td>
<td>2.5% Export Charge + maximum volume that can be exported to the United States cannot exceed the Region’s share of 34% of Expected U.S. Consumption for the month</td>
</tr>
<tr>
<td>$US 316-335</td>
<td>10%</td>
<td>3% Export Charge + maximum volume that can be exported to the United States cannot exceed the Region’s share of 32% of Expected U.S. Consumption for the month</td>
</tr>
<tr>
<td>$US 315 or under</td>
<td>15%</td>
<td>5% Export Charge + maximum volume that can be exported to the United States cannot exceed the Region’s share of 30% of Expected U.S. Consumption for the month</td>
</tr>
</tbody>
</table>
Welfare impacts of SLA 2006

U.S. lumber producers gained $1.6 billion and U.S. consumers lost $2.3 billion in nine years under SLA 2006.

The worst one was SLA 1996


<table>
<thead>
<tr>
<th>Trade agreement (source)</th>
<th>U.S. consumer surplus (U.S. dollars, billion)</th>
<th>U.S. producer surplus (U.S. dollars, billion)</th>
<th>Annual consumer surplus (U.S. dollars, million)</th>
<th>Annual producer surplus (U.S. dollars, million)</th>
<th>Net annual U.S. welfare (U.S. dollars, million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>MOU (Wear and Lee 1993)</td>
<td>-3.8</td>
<td>2.6</td>
<td>-760</td>
<td>520</td>
<td>-240</td>
</tr>
<tr>
<td>SLA (Zhang 2006)*</td>
<td>-3.4</td>
<td>2.0</td>
<td>-674</td>
<td>392</td>
<td>-282</td>
</tr>
<tr>
<td>SLA 2006 (this paper)</td>
<td>-3.1</td>
<td>2.2</td>
<td>-344</td>
<td>244</td>
<td>-100</td>
</tr>
</tbody>
</table>

*Converted to 1982 dollars using the U.S. Producer Price Index.
SLA 2006 led to drop in lumber exports to the U.S. from QC, ON, SK and BC provinces. SLA2006 didn’t cause trade diversion.
Current Softwood Lumber Dispute – Timeline


- **Lumber V Litigation Underway** – The U.S Lumber Coalition has renewed petitions with the U.S. Department of Commerce (DOC) alleging that the Canadian government unfairly subsidizes that nation's lumber industry. Preliminary CVD determinations are expected Apr 24 and ADD June.

- **Duties Potentially Retroactive to Feb 2017** - Duties could be retroactive (up to 90d) if Critical Circumstances (e.g., rush to border) found ahead of duty implementation.

- **Companies Also Targeted This Time** - Four companies (Canfor, West Fraser, Tolko & Resolute) have been named Mandatory Respondents by the DOC on the CVD. This is different than previous investigations where only the provinces were targeted and could result in 1) a higher overall preliminary duty rate and 2) different individual duty rates. We expect Canfor and Tolko to have the lowest CVD rate with West Fraser and Resolute having the highest.

![Timeline Image]

- Expiry of Standstill Period
  - Petition filed by COALITION
  - Questionnaires issued to mandatory respondent companies
  - Preliminary CVD Determination
  - Cash deposits required
  - ADD Determination
  - Final Order for both subsidy and dumping issued by the US
  - Earliest date for Canada to file appeals under NAFTA & WTO

- Dates:
  - Oct 16
  - Nov 16
  - Dec 16
  - Jan 17
  - Feb 17
  - Mar 17
  - Apr 17
  - May 17
  - Jun 17
  - Jul 17
  - Aug 17
  - Sep 17
  - Oct 17
  - Nov 17
  - Dec 17
  - Jan 18
Recent developments

• Several bilateral meetings and talks (even at the high level) for another deal—all failed.
• Company-specific CVD and AD tariffs.—Weighted average rate of 20.83%.
• NAFTA/TPP
• A projected $500 million in tariffs by Canadian lumber companies in 2017.
What do tariffs mean to the market?

(a) Canada

U.S.
Producers’ gain: $a$
Consumers’ loss: $a + b + c + d$
Government’s gain: $c + e$
Net gain: $e - b - d$

Canada
Producers’ loss: $u + v + w$
Consumers’ gain: $u + v$
Net loss: $w$

(b) International Market

(c) United States
The trade projection model

• A 20-region global softwood lumber trade model.
  – U.S.—South, North, and West
  – Canada—BC Coast, BC Interior, Alberta, Atlantic, Rest

• The model is calibrated to the 2014 free trade data
Impacts of 20.83% tariffs

<table>
<thead>
<tr>
<th></th>
<th>Change in:</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Price $/m³</td>
<td>Consumption m³</td>
<td>Production m³</td>
</tr>
<tr>
<td><strong>Canada</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>BC Coast</td>
<td>-4.8</td>
<td>-2.5%</td>
<td>2197.6</td>
</tr>
<tr>
<td>BC Interior</td>
<td>-2.4</td>
<td>-1.3%</td>
<td>4164.0</td>
</tr>
<tr>
<td>Alberta</td>
<td>-3.9</td>
<td>-2.5%</td>
<td>8981.1</td>
</tr>
<tr>
<td>Atlantic</td>
<td>-6.4</td>
<td>-3.8%</td>
<td>8045.0</td>
</tr>
<tr>
<td>Rest of Car</td>
<td>-4.4</td>
<td>-2.7%</td>
<td>58205.7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>-4.4</td>
<td>-2.6%</td>
<td>81,593</td>
</tr>
<tr>
<td><strong>US</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>South</td>
<td>4.0</td>
<td>2.1%</td>
<td>-135371.7</td>
</tr>
<tr>
<td>North</td>
<td>5.8</td>
<td>3.2%</td>
<td>-215411.4</td>
</tr>
<tr>
<td>West</td>
<td>4.2</td>
<td>2.5%</td>
<td>-99834.1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>4.7</td>
<td>2.6%</td>
<td>(450,617)</td>
</tr>
<tr>
<td>Rest of World</td>
<td>0.0</td>
<td>0.0%</td>
<td>-2872.1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>-371895.9</td>
<td>-0.1%</td>
<td></td>
</tr>
</tbody>
</table>

1m³ = 423 board feet

Canadian lumber shipments to the U.S. are expected to fall by 3.82 million m³ (1.6 billion board feet), down about 13%. 854 million board feet
Impacts of 20.83% tariffs

Lumber Takes a Hard Hit
Canada lumber and sawmill exports fall after U.S. duties

Decline of 14% after U.S. duties

Last time they fell this much was in 2014, by 18%

Source: Statistics Canada

Bloomberg
2018 Lumber production projections

• U.S. softwood lumber consumption of about 50 BBFT in 2018.—up 3% from 2017.

• Net imports to remain stable in 2018 due to physical constraints on Canadian lumber producers.
Why low impacts of the tariffs on prices?

- 20-region global trade model—might capture some substitution effects—Other producers end up producing more.
- Lumber prices are already high.
- Other factors seem important for example U.S. domestic production, Canadian overseas exports.
- Supply constraints in Canada.
- Data limitations

Source: Madison’s Lumber Reporter
Welfare impacts of 20.83% tariffs

<table>
<thead>
<tr>
<th></th>
<th>CS</th>
<th>PS</th>
<th>QR</th>
<th>Tax</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>BC Coast</td>
<td>2,626</td>
<td>-17,652</td>
<td>-9.9%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>BC Interior</td>
<td>4,971</td>
<td>-64,081</td>
<td>-5.8%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Alberta</td>
<td>8,892</td>
<td>-29,677</td>
<td>-9.3%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Atlantic</td>
<td>8,458</td>
<td>-17,454</td>
<td>-13.8%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Rest</td>
<td>59,899</td>
<td>-72,462</td>
<td>-9.1%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Total</td>
<td>24,947</td>
<td>-128,863</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>US</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>South</td>
<td>-146,601</td>
<td>183,842</td>
<td>5.5%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>North</td>
<td>-229,321</td>
<td>29,191</td>
<td>8.1%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>West</td>
<td>-98,642</td>
<td>88,317</td>
<td>5.8%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Total</td>
<td>-474,565</td>
<td>301,949</td>
<td></td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Rest of World</td>
<td>-23,707</td>
<td>123,367</td>
<td>0.2%</td>
<td>0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Total</td>
<td>-863,046</td>
<td>395,878</td>
<td></td>
<td>0</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

The Canadian market share is expected to be shrunk by about 4%.
Tariff impacts on southern timber markets

• Sub-Regional Timber Supply Model
  – An economic model of timber supply based on FIA data, which combines timber market prices and harvest feedbacks with forest resource dynamics.

13 southern states and sub-regions
Sub-regional Timber Supply Model

- A potential 3.3% lumber demand in SRTS was increased in 2018 relative to a baseline recession recovery scenario.
Timber prices in the U.S. south are expected to go up about 7.3% over the next five years. The tariffs could raise annual sawtimber removals by 3.2%.
The slight effect on inventory indicates that the price effect continues to grow even after the tariff consumption effect stabilizes after 2021.
What’s next for Canada?

• Diversify its export markets—75% of Canadian lumber export value to the U.S. in 2017.
• Be efficient—Canadian lumber production costs are an important factor (Parajuli et al. 2016)
• Upgrade lumber quality—would be substitute to U.S. lumber (Liaqat 2018)
Conclusions

• Positive impacts on the lumber and timber markets—as expected but the effects on the price are limited.

• High rates of CVD and AD tariffs are momentary, and might go back to Canada (The U.S. returned $4 billion of tariffs in 2006).

• Uncertainty: more volatile lumber markets.

• Highly political; case with WTO
Thank you!!