



Weekly economic Briefing

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Growth stalled in B.C.'s lumber production

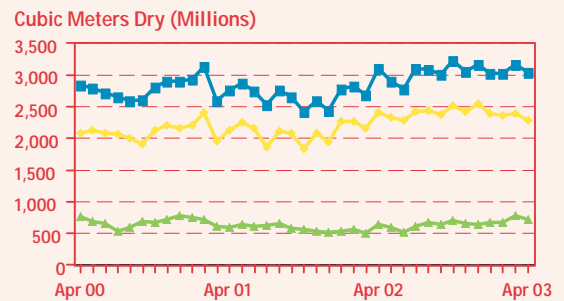
Updated and revised data from Statistics Canada indicates the quantity of lumber produced in B.C. currently remains near 10-year highs but growth in production has stalled over the past nine months. Excess timber and mill capacity worldwide and the yet unresolved US-Canada softwood lumber dispute, together with stable North American demand, have driven lumber prices down and forced B.C. producers to increase efficiency in order to remain economically viable.

Lumber production is on a short-term upward trend in B.C.'s interior versus a short-term downward trend in coastal regions. In the interior, short-term production trends are upward in the central and southern regions but are downward in the northern region. Total B.C. softwood lumber production remains below all-time highs reached in early 1988.

In May 2003 the benchmark price of softwood lumber from B.C. averaged \$318 per 1,000 cubic feet. That indicates a price decline of approximately -22% from May 2002 and -6% from April 2003. In April 2003, the quantity of lumber produced in B.C. was 3.05 billion dry cubic meters after adjusting for seasonal effects. That indicates a quantity decline of approximately -2% from April 2002 and -4% from March 2003. Total, seasonally adjusted revenue for wood shipments from B.C. mills was \$738 million in April, down approximately -25% from April 2002 and -4% from March 2003.

Lumber production remains high but growth has stalled

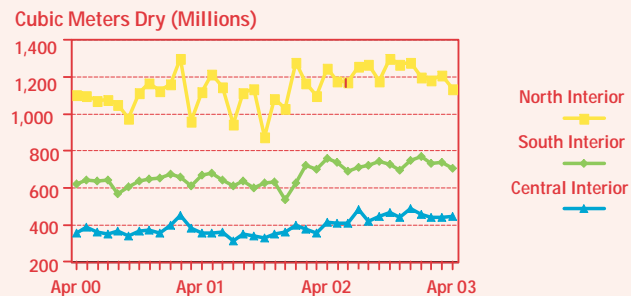
Sawn Lumber Production (Seas. Adj.)



Source: Statistics Canada.

Lumber production slowing in North Interior

Sawn Lumber Production (Seas. Adj.)



Source: Statistics Canada.

B.C.'s softwood lumber industry will continue to face difficult market conditions due to the rising U.S.-Canadian dollar exchange rate, the U.S.-Canada trade dispute and slow economic growth in our main U.S. and Japanese export markets. In May 2003, world-wide exports of softwood lumber originating in B.C. totaled \$430 million, down approximately -41% from May 2002. Softwood lumber exports to the U.S. are down approximately -50% from May 2002 while exports to Japan are down -15%.

Latest NAFTA ruling on U.S. softwood lumber tariffs a draw

Canada's latest challenge to U.S. imposed tariffs on Canadian softwood lumber has resulted in a split decision. A North American Free Trade Agreement (NAFTA) panel concluded that the U.S. followed its own laws in setting the tariff but some anti-dumping duties are miscalculated. The U.S. has 60 days to correct the miscalculation.

Although the decision is binding on both countries, the result is ambiguous and not a victory for either Canada or the United States. It is difficult to know whether the recalculation, which involves an obsolete conversion formula, will result in lower or higher anti-dumping duties. Two major issues on the lumber dispute remain under NAFTA review: What to do with the trade barriers and what to do with the duties charged since May 2002. A decision on the validity of the U.S. countervailing duties is scheduled for August 15th, while a decision on whether a U.S. coalition of lumber producers may receive softwood lumber duties charged by the U.S. Commerce Department is scheduled for September 10th.

The long-running U.S.-Canada trade dispute over softwood lumber markets boils down to somehow balancing Canada's comparative advantage in lumber production with the U.S.'s market power in softwood lumber consumption. Various agreements have come and gone over the past 100 years, the latest of which was a quota system that expired in 2001. Since then the U.S. has imposed, and Canada has disputed, anti-dumping and countervailing duties on Canadian softwood lumber. The latest slate of duties has cost thousands of jobs, millions of dollars in profits and millions of dollars of government revenues in B.C.'s lumber industry.

Monetary policy reverses direction

The Bank of Canada (BoC) surprised most forecasters with a 0.25% cut in the Bank Rate on Tuesday. The rate cut marks the first decrease since January 2002 and is a rather abrupt reversal of monetary policy. The bank rate has seen steady increases over the past 18 months.

The BoC released its monetary policy update on Thursday. It attributed the reversal in policy to a sharp slowdown in expected economic growth and inflation over the short-term. Lower expected growth and inflation were attributed to the unforeseen severity of the impact of the SARS outbreak on tourism and to lower exports caused by an isolated case of mad cow disease in Alberta, sluggish economic growth in the U.S., and a dramatic rise in the U.S.-Canadian dollar exchange rate.

Looking ahead, the BoC lowered its forecast for real Canadian GDP growth by -0.5% to 2% in 2003. The report also indicated that further cuts in the Bank Rate are more likely than rate increases. The reversal in monetary policy caused U.S.-dollar investors to sell some of their recently acquired Canadian financial assets, driving the Canadian dollar down to approximately 71 cents U.S. on Thursday.