



13500 S.W. 72nd Avenue
Suite 250
Portland, OR 97223-8013

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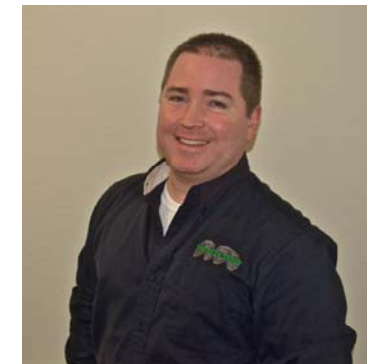
“The first rule of any technology used in a business is that automation applied to an efficient operation will magnify the efficiency. The second is that automation applied to an inefficient operation will magnify the inefficiency.” **Bill Gates**

Forest Products News The Beck Group

The Beck Group Welcomes New Staff

This past spring we wished Lindy Alexander a hearty congratulations as she retired from her career, which included 13 years with The Beck Group. Lindy was instrumental in organizing our benchmarking study reports, assisting in the coordination and delivery of our sawmill management training workshops, and providing quality control on our project reports. Thank you, Lindy, for contributing to the success of The Beck Group and best wishes for a happy retirement spending quality time with your children and grand-children!

Lindy’s retirement wasn’t the only staff change at The Beck Group. We also welcomed two new employees.



Since joining The Beck Group as a Consultant in June 2017, **Zach Rollins** has been involved in a variety of projects including a hardwood lumber benchmarking study and several due diligence research and analysis efforts. Zach also made an

immediate impact on the Beck team by developing forecasting models for costs and supply of wood fiber, analyzing long term wood products pricing and trends in end use, and evaluating economic feasibility. He has also been instrumental in helping our team plan for changes in the way we will collect and report data in our forest products industry benchmarking studies and competitive assessments.

Prior to joining The Beck Group, Zach worked as a Senior Accountant for Potlatch Corporation at their plywood plant and sawmilling facility in St. Maries, Idaho. His primary responsibilities were to ensure the accuracy of financial reporting and to support the management team with data analysis to help improve mill financial performance and efficiencies. Zach also helped develop and ensure the effectiveness, and compliance with, Sarbanes-Oxley controls for Potlatch’s Idaho Wood Products division. In his role as an accountant, he focused heavily on analyzing inventory valuation, capital project opportunities, raw materials cost, profitability of mill residuals, and a wide variety of other related activities. Welcome, Zach!

2016 Stud Mill Benchmarking Study Results



The Beck Group recently finished a benchmarking study of stud mills. The study covered calendar year 2016 and included 9 mills from 7 different companies including operations in Oregon,

Washington, Montana, Idaho, Michigan, and Colorado. The mills in the study produced and sold more than 1.4 billion board feet of lumber in 2016. (\$/MBM) was down 8 percent in 2016 compared to 2012/2013; log costs (expressed on a lumber basis) were up by 7 percent; and conversion costs were up by 11 percent. The average annual production per mill increased by 6 percent between 2012/2013 and 2016.

The study also confirmed other long-term industry trends that The Beck Group has been observing in our benchmarking studies. Lumber Recovery (log volume in relative to lumber volume out) improved by 1 percent over the prior study. Based on the results of numerous benchmarking studies of the past 20 years, we estimate that lumber recovery improves by about 1 percent per year, on average. Interestingly, this trend has been linear. At some point in time, however, the industry will reach a point when continued recovery improvements will be limited by the geometry of converting round logs into square lumber. Similarly, sawmill cut per hour improved by 2 percent compared to the prior study. This result is also consistent with long-term industry trends that show steady, long-term improvements in productivity.

Stay tuned for exciting changes to the way in which we collect and report data in our benchmarking studies.

On average, the participating mills were break-even on an EBIT basis (earnings before interest & taxes) and were profitable by about \$16/MBM on an EBITDA basis (earnings before interest taxes depreciation & amortization). The results are a significant change from a prior Beck Group stud mill benchmarking that covered the 2nd half of 2012 and the first half of 2013 in which the average mill was at \$44/MBM (EBIT basis) and \$58/MBM (EBITDA basis).

Key driver’s in the differing financial performance between the studies are that average lumber sales revenue

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Softwood Lumber Agreement

The U.S. and Canada have a long-standing trade dispute about the export of Canadian lumber into the United States with U.S. companies claiming that Canadian firms are unfairly subsidized by the Canadian government. A central argument in the dispute is the U.S. claim that Canadian firms pay lower stumpage rates (i.e., the cost of logs) than U.S. firms. In Canada, most timber is owned by either federal or provincial governments, but is managed under long-term tenure agreements held between private companies and the government. Under the tenure agreements, the tenure holder harvests timber and pays stumpage at a rate determined by the government. In the U.S., in contrast, government agencies manage forest land and sell timber to the high bidder.

The solution to this issue has been a *Softwood Lumber Agreement* (SLA), which has been in place in various forms for decades. However, in October 2015, the SLA expired. That version of the SLA had been in place since 2005 and provided for a combination of tariffs and quota restrictions on Canadian lumber shipped into the United States. Following the expiration, there was a one year “stand-still” period which ended in October 2016. After the end of the “stand-still”, the U.S. Lumber Coalition initiated trade cases against the alleged unfairly traded lumber imports. In April 2017, the U.S. Department of Commerce announced a Countervailing Duty (CVD) against Canadian softwood lumber producers averaging 19.88 percent. And, in June 2017, an Antidumping duty (AD) averaging 6.87% was also assessed against the Canadian lumber exporters. In anticipation of these CVDs and ADs, Canadian lumber producers began increasing the prices quoted on Canadian softwood lumber shipments to the U.S. to offset the duties. As a result, softwood lumber prices increased across the U.S. during second quarter 2017.

The terms of a new Softwood Lumber Agreement between the U.S. and Canada have been under discussion since the expiration of the prior agreement (i.e., before October 2015). At one point in the early summer of 2017, it appeared a deal was imminent in which Canadian lumber imports would be limited to a quota of 28 percent of total U.S. lumber market; the quota would be phased in over a five year period; and there would be certain other allowances. More recently, however, negotiations have stalled since the U.S. side called for a 28 percent quota, but only a two year phase and no ‘extra allowances’ (e.g., Atlantic Canada exclusion, free market threshold, and border mill exemption). The Canadians have apparently rejected the latest U.S. proposal.

Figure 1, shows the historic Canadian share of the U.S. lumber market. As the data shows, except for a period during and after the Great Recession, Canadian lumber exports to the U.S. have frequently comprised more than a 28 percent share of the U.S. lumber market. Thus, setting the quota level is a critical aspect of the negotiations. Perhaps more important though is the length of the

quota phase in period because there are constraints on the annual allowable cut in key Canadian timber producing regions. This means Canada has limited ability to increase lumber production, which in turn means that if U.S. demand for lumber grows over the next few years, a quota of 28 percent may have a negligible effect on Canadian lumber exports to the U.S., since their output would be relatively static and the size of the U.S. lumber market will likely increase. On the other hand, if a 28 percent quota were to go into effect in two years and U.S. housing starts (the key driver of lumber consumption) stagnate at about 1.2 million per year, CIBC World Markets, Inc. has estimated that the quota would exclude nearly 2 billion board feet of Canadian lumber from entering the U.S.

If the latter scenario were to unfold, there would also likely be impacts on the U.S. side. For example, U.S. West log prices would likely rise. This is because the estimated 2 billion board foot drop in lumber supply from Canada would increase pressure on U.S. firms to produce more. A likely result is that lumber prices would rise in the U.S. This in turn, would likely cause log costs to increase in the U.S. West as firms seeking to increase production bid log prices up in a region where there has historically been a lot of competition for logs. This is especially true if one considers the combined impact of log consumption among U.S. West sawmills and logs exported to other countries. There are obviously many factors at play and it is difficult to predict where things will end up. In any event, this is an issue that we will continue to monitor closely.

THE BECK GROUP

Phone: 503 684-3406
 Fax: 503 639-0784
www.beckgroupconsulting.com

Staff

Tom Beck — Chairman
tomb@beckgroupconsulting.com
Bryan Beck — President
bryanb@beckgroupconsulting.com
Roy Anderson — Vice President
roya@beckgroupconsulting.com
Zachary Rollins – Consultant
zachr@beckgroupconsulting.com
Hannah Hammond — Office Mgr.
hannahh@beckgroupconsulting.com

Associates

Bill Carlson
Bioenergy Technical Consultant
info@beckgroupconsulting.com

If you would like to receive our newsletter by e-mail, please contact us at info@beckgroupconsulting.com with your name, company and e-mail address. We will be happy to send you our newsletter in Acrobat Reader (.pdf) format.

BECK Projects Update

BECK staffers have been busy completing a variety of projects; a few highlights are described below.

Projects Under Development

Sawmill Management Training Workshops—The Beck Group plans to host a workshop in the Southeastern U.S in early 2018. An exact date and location are still to be determined, but we are currently considering offering this workshop in partnership with an industry vendor, in Alabama.

We are currently registering attendees for a Western U.S. sawmill management training workshop December 6-8, 2017 at the World Forestry Center in Portland, Oregon. Check our website for updated information about workshop agenda and registration information.

Western Plywood Benchmarking—BECK has recently fielded several requests for Western plywood benchmarking information. This fall we will begin recruiting for a study to be completed early in 2018, covering calendar year 2017.

California OSB Manufacturing Feasibility—By the end of the year BECK will complete a comprehensive study of the feasibility of manufacturing OSB in California in partnership with an OSB industry member.

Post and Pole Industry Survey—We are in very early stages of organizing a survey of the Western U.S. post and pole industry to gauge industry size and market value of the industry’s products. We are discussing the work in cooperation with industry associations and the U.S. Forest Service.

FiberEdge—The Beck Group is exploring options for updating the data gathering methodology, reporting frequency, and delivery of our benchmarking data. We are working with a well-established industry partner and we are very excited about the possibility of updating this service area for our clients. Stay tuned for additional details coming soon!

Recently Completed Projects

Western U.S. Mill Residual Supply and Demand—Supply, demand, and pricing of mill residuals in the Western U.S. continues to be an area of interest for a variety of clients. In response, BECK has developed a database of mill residue producers and mill residue consumers and their production and consumption of mill residues. This information is useful for those interested in utilizing these materials and those involved in selling these materials.

Manufacturing Consulting Assistance —BECK recently worked with a large scale consumer of MDF who is using the material in a unique way. Our assistance was focused on tightening the control of temperature and humidity in the manufacturing operation to prevent moisture related warp, twist, and cupping after the material had been machined to size. Additionally, we provided the customer with MDF industry statistics and market information.

Timberlands Strategic Planning - BECK assisted in a client’s strategic planning process pertaining to timberland management in the coastal region of the Pacific Northwest. In order to refine timber management targets, BECK was asked to identify trends in the regional sawmilling industry that will impact demand for logs of various kinds, with a particular focus on log scaling diameter.

Expert Witness - BECK was retained to testify as an Expert Witness to provide an opinion about the accuracy of delivered wood fuel costs at a biomass power plant.

Sawmill Acquisition Due Diligence - A client seeking to expand its portfolio of forest products businesses retained The Beck Group to assist in evaluating several sawmills in the Pacific Northwest. Our scope of work involved a comprehensive assessment of each facility’s log procurement practices, conversion practices, conversion equipment, sales realizations, management team, and overall financial performance.

Timberland Acquisition Due Diligence—A client considering the purchase of nearly 200,000 acres of timberland retained The Beck Group to assess the long-term competitiveness and survivability of sawmill and veneer mills in the region surrounding the timberlands.

Hardwood Lumber Benchmarking—The Beck Group, working in cooperation with the Hardwood Manufacturer’s Association, recently completed a hardwood lumber industry benchmarking study and wage survey. The study allows HMA members to assess their operation’s performance relative to their industry peers in a variety of key areas.

Figure 1—Canadian Share of U.S. Softwood Lumber Market (2004 to 2016)

| Year | Canadian Softwood Lumber Imports (MMBF) | Apparent U.S. Softwood Lumber Consumption (MMBF) | Canadian Softwood Lumber Import Market Share (%) |
|------|---|--|--|
| 2004 | 20,972 | 61,800 | 33.9 |
| 2005 | 21,505 | 64,334 | 33.4 |
| 2006 | 20,149 | 60,109 | 33.5 |
| 2007 | 16,672 | 52,103 | 32.0 |
| 2008 | 11,621 | 40,735 | 28.5 |
| 2009 | 8,303 | 31,873 | 26.1 |
| 2010 | 9,033 | 33,028 | 27.3 |
| 2011 | 8,848 | 34,459 | 25.7 |
| 2012 | 9,528 | 36,834 | 25.9 |
| 2013 | 10,195 | 39,616 | 25.7 |
| 2014 | 12,138 | 42,586 | 28.5 |
| 2015 | 13,259 | 44,447 | 29.8 |
| 2016 | 15,046 | 47,207 | 31.9 |

Source: Western Wood Products Association, Lumber Track (2004 to 2016)