

Exports ♦ October 2002

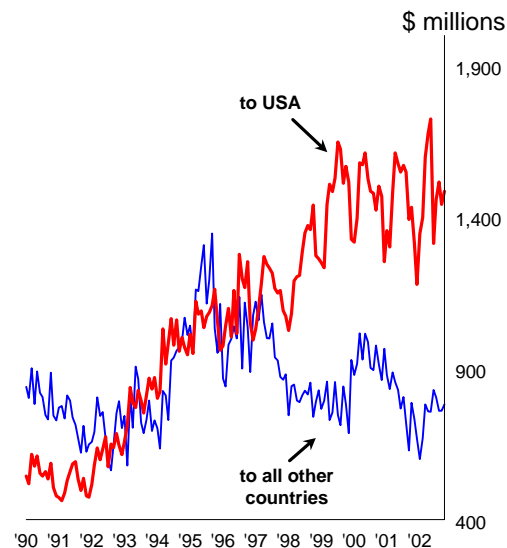
Note: Statistics Canada erred with its release of the October 2002 export data. British Columbia origin exports of natural gas and electricity were coded incorrectly and reported as zero. As a result of this error, total exports to the United States and total international exports cannot be reported. The following analysis is based on total exports *excluding* natural gas and electricity.

- Year-to-date to October, the value of BC origin exports (excluding natural gas and electricity) is 1.6% lower compared to the first 10 months of 2001. Low commodity prices in the forest sector are the main reason for the decline.
- Oversupply has resulted in reduced prices for softwood lumber as Canadian producers continue to run full out in an attempt to achieve economic efficiencies that will allow them to stay afloat despite the punishing duties averaging 27.2% on Canadian lumber exports to the United States. As a result, the value of softwood lumber shipments to the US is down 1.9% year-to-date despite the fact that volumes exported are up 8%.
- Low prices continue to plague pulp and paper as well. The value of pulp and paper exports is 9% lower year-to-date compared to the January to October period in 2001. Shipments to the

United States are 8% off last year's pace, while exports to Japan have fallen by 24% and the European Union has taken in 22% less than in the same period in 2001.

- Exports of machinery and equipment have dropped 4% year-to-date to October compared to the same period in 2001. Shipments to the United States have fallen by 3% while the European Union is taking in 30% less of BC's machinery and equipment.
- The value of BC origin exports to Japan is down 8.5% compared to the first 10 months of 2001. It is expected that the Japanese economy will improve in 2003, which will likely mean that exports to that country will pick up.

*Commodity prices in the forest sector are driving down the value of exports**



*This chart excludes exports of natural gas and electricity

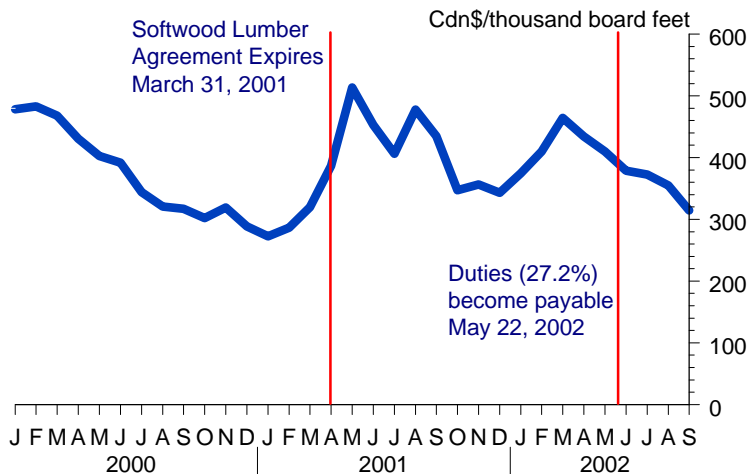
Lumber Battle Takes an Unexpected Turn

The trade dispute between Canada and the United States over softwood lumber has taken an unexpected twist that has resulted in a drop in the price of lumber to its lowest point since the expiry of the Softwood Lumber Agreement. Despite the substantial penalties imposed on shipments of Canadian lumber, Canadian companies have not reduced the quantity of wood exported to the United States. Instead, they have ramped up production, often increasing to three shifts at more efficient mills, while shutting down those mills that are not cost effective. The goal of this strategy is to minimise unit costs and enable the companies to continue to operate in the face of punishing duties while retaining their customer base in the United States.

Canadian lumber producers have taken steps to minimise costs by operating at capacity and closing inefficient mills

The result has been an oversupply of lumber on the market and consequently, a decline in price. The price of Western Spruce-Pine-Fir (SPF) has fallen to approximately Cdn\$300 per thousand board feet, its lowest level in almost two years. At this price it is likely that many lumber producers are losing money after the duties are applied.

Prices of Western SPF have been falling steadily since the implementation of American duties on Canadian lumber



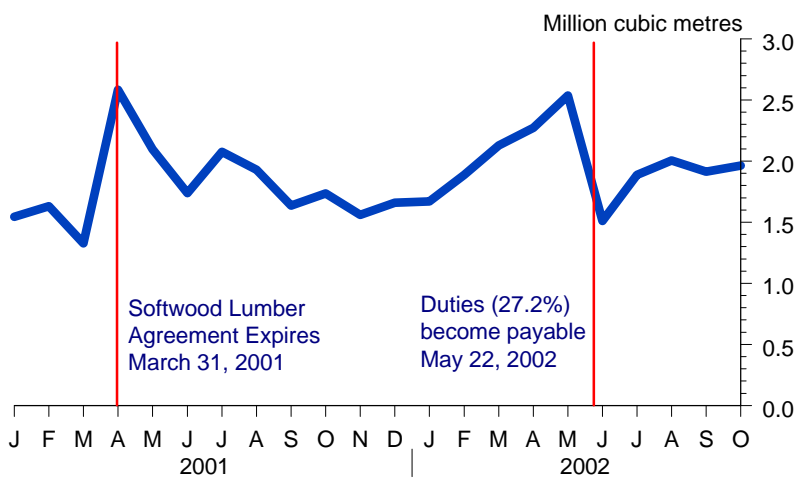
Source: Madison's Canadian Lumber Reporter

The over-supply of wood resulting from mills producing at capacity has led to falling prices for lumber

Prices fell all through 2000 and the first quarter of 2001, as supply outstripped demand. The low demand was likely due to several factors, including poor weather in the United States that delayed building, and possibly because customers were holding back, anticipating that the end of the Softwood Lumber Agreement (SLA) would bring a “wall of wood” over the border with corresponding price declines. When this influx of lumber did not materialise and the building season began in the United States, the resulting increase in demand reacted with the tight supply and drove prices

up. Prices then followed their usual seasonal pattern, falling in the winter, then increasing again in the spring. The current cycle of declining prices likely began during a duty-free gap resulting from a World Trade Organisation stipulation that provisional duties cannot be extended beyond a certain period. When this period ended, there was a short interval where Canadian lumber companies were able to ship wood to the United States duty free. Anticipating substantial duties effective May 22, the companies took advantage of the duty-free period and the wall of wood that was expected after the expiry of the SLA finally showed up a year later. Since then, prices have continued to drop as Canadian producers have kept volumes shipped to the United States at a steady level.

Shipments of softwood lumber* from B.C. to the U.S. have not declined despite the imposition of substantial duties



*Excluding siding

Quantities of softwood lumber shipped from BC to the US spiked when the SLA expired, probably because companies had been holding back shipments as their quotas were reached, and spiked again during the duty-free period prior to the imposition of combined duties of 27.2%; quantities shipped over the last few months are at or above volumes shipped through most of last year

It is difficult to predict how long Canadian manufacturers can continue to run full out with prices as low as they are. Already the smaller companies on both sides of the border are falling by the wayside. While the large operators have the option of concentrating their efforts in their most efficient mills and cranking up production to achieve economies of scale, for smaller producers this usually is not an option. Even for the larger firms, the cost of flooding the market will eventually (if it hasn't already) lead to losses as oversupply drives prices down further.

One factor helping British Columbia companies is the access to pine beetle infested timber, which is generally assessed lower stumpage rates. The lower cost of harvest means the companies can better afford to sell the wood at lower rates.

Ironically, some of the modifications made by the larger Canadian companies to lower unit costs would not have been possible if not for the threat posed by American duties. Unions were far more

Smaller forest companies can't compete with the larger firms with prices as low as they are and are going out of business



amenable to concessions with regard to shift premiums and schedule flexibility than they would have been in absence of the duties.

Prices for softwood lumber will likely fall further as the usual winter downturn in demand occurs. Fears of a slowing US economy and housing market in 2003 could also add to price declines. Already some companies are scheduling temporary shutdowns of their mills. Although this is more or less normal procedure during the winter months, the number of layoffs this year could be far in excess of usual levels. With smaller producers unable to continue operating in the face of the combination of crippling duties and low prices, and larger companies consolidating their operations by closing inefficient mills, there are already a significant number of forest sector workers in British Columbia suffering unemployment. It is likely that the low price for lumber will result in more temporary shutdowns and further temporary layoffs over the coming months.

It is not just the Canadian companies that are feeling the pinch of lower prices for wood. Lumber producers in the United States are also experiencing shutdowns and layoffs as the duties they championed are now backfiring on them. If this situation is to continue, it could mean further industry consolidation such that small operators will be pushed out of the picture. The end result could be a leaner Canadian industry with only a handful of efficient companies that will be poised to become even stronger once the duties are eventually lifted. As anticipated, the cost of this dispute to the Canadian industry will be substantial. Somewhat more surprising is that the cost to the American industry may also be significant.

The costs of the softwood lumber dispute will probably be felt on both sides of the Canada/US border

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Listed By Statistical Reference Date of Issue**

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		00-04	<i>British Columbia Shipping Smaller Portion of Canadian Forestry Products</i> (released June 2000)

NOTES

Countries Included Within World Regions:

(1) Western Europe: United Kingdom, Ireland, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Italy, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland.

(2) Eastern Europe: other Europe, including all of Russia, Georgia, Kazakhstan, Kyrgyzstan, Moldova, etc.

(3) South East Asia: Malaysia, Brunei Darussalam, Singapore, Myanmar, Kampuchea, Laos, Indonesia, Philippines, Thailand, Vietnam.

(4) Africa: continental Africa, excluding Ethiopia, Libya, Somalia, Sudan, Egypt.

(5) South America: continental South America from Colombia and Venezuela south to Chile and Argentina, including offshore islands, but not Caribbean.

(6) Central America and Caribbean: from Guatemala and Belize to Panama, plus Caribbean Islands.

(7) Pacific Rim (including Japan): Japan, Hong Kong, Malaysia, Brunei Darussalam, Singapore, Laos, Mongolia, China, Indonesia, North Korea, South Korea, Philippines, Macau, Taiwan, Thailand, Vietnam, Australia, Fiji, New Zealand.

(8) Pacific Rim: as above, but excluding Japan.

(9) Middle East: from Turkey and Iran south through the Arabian Peninsula. Excluding Afghanistan and Pakistan, but including Cyprus, Ethiopia, Egypt, Somalia, Sudan and Libya.

'Selected Value-added Wood Products' category includes prefabricated houses, doors, windows, furniture, moulding, siding, etc. It does not include panel products, shakes, shingles or any pulp and paper products.

Revisions

Statistics Canada revises trade data for the previous three data years with release of the December data. The revision number is indicated in the footer of the tables (e.g., Rev 1 is the first annual revision, etc., and Prelim indicates it is the first release of data to December for that year). In addition to annual revisions, Statistics Canada revises the data for the previous data year every quarter (indicated in the footer by Rev Q1, etc).

Service Offered for Detailed Trade Statistics

For B.C. government statistics users requiring more detailed information on exports or imports, a special report service is offered through the address below:

Dan Schrier - Trade Statistics**BC STATS****553 Superior Street,****Victoria, B.C.****V8V 1X4****(250) 387-0376**

This service is provided through the Trade Research and Inquiry Package (TRIP) computer reporting system. TRIP offers user-defined tabulations of export or import statistics for British Columbia, Canada, the United States and other countries. Tabulations can include information on commodities, countries, U.S. states, years, months, mode of transport, etc.