

## **Softwood (Leads: SK, QC, ON, BC, NB)**

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### **Issue**

- Softwood Lumber Trade Dispute

### **Key Messages**

- BC is committed to working with Canada and the other provinces to find common ground in our response to the softwood lumber dispute.
- BC supports the efforts Canada has put into developing the Action Plan for Softwood Lumber we believe that funding aimed at market and product diversification is particularly critical to respond to this current dispute and to mitigate the risk of future disputes with the U.S.
- Company assistance programs must be trade-compliant; otherwise they could lead to higher future duties for all exporters.
- Trade disputes are costly to industry, the provincial and federal government, and U.S. consumers, and harm the relationship between the Canada and the U.S.
- Managed trade agreements are preferred to trade disputes due to increased stability and certainty for lumber producers and consumers on both sides of the border.
- We need to work together to ensure that Americans understand the potential consequences of trade action on their own citizens and economies. This will require us to work together to develop third party validators in the U.S. who will be willing to speak to lawmakers and appointed officials.
- While defending B.C.'s interest in litigation, B.C. continues to support Canada in negotiations with the U.S. for a managed trade agreement.
- It is important that we look for an opportunity to settle this dispute, but we must be careful not to negatively impact our litigation strategy in negotiations.
- [These are NOT speaking notes, but key messages that the Premier could draw on to articulate BC's approach to the issue.]

### **Key Facts**

- Since 1982, Canada and the U.S. have had four significant trade disputes pertaining to softwood lumber, known as Lumber I, II, III and IV.

- The central issue in these disputes is the U.S. claim that Canadian provinces subsidize timber sales to lumber manufacturers.
- The last agreement was in effect from October 12, 2006 to October 12, 2015. It provided stability and certainty for Canadian lumber producers, and allowed export tax to remain in Canada. Under the terms of the agreement, the U.S. was precluded from launching trade action against Canada for a period of one year until October 2016.
- B.C. produces about 50% of all Canadian softwood lumber, and accounts for 50% of Canada's exports to the U.S.

### Negotiations

s.13,s.16

### Lumber V

- On December 15, 2016, U.S. Commerce initiated investigation of the allegations that: Canada and certain provinces are providing countervailable subsidies to softwood lumber exporters from Canada; that Canadian lumber industry is selling at less than fair value (dumping) lumber into the U.S.; and that imports of softwood lumber products are injuring the U.S. industry.
- While the subsidy case targets government actions, the anti-dumping case is aimed at industry and is defended by industry.
- For the first time in lumber, Commerce has chosen to conduct a company-specific investigation by choosing the four largest lumber exporters, Canfor, West Fraser, Tolko and Resolute, as mandatory respondents. Except for Resolute, all companies have operations in BC.
- In January 2017, questionnaires were sent to four mandatory respondent companies, as well as to Governments of Canada, B.C., Alberta, Ontario, and Quebec to collect information for the

investigation. Responses were filed in March 2017. J.D. Irving (New Brunswick) filed a voluntary response, and the U.S. Department of Commerce chose to accept J.D. Irving as a voluntary respondent.

- On April 24, 2017, the U.S. Department of Commerce issued a preliminary determination of CVD rates. The rates for the chosen companies as well as J.D. Irving were calculated based on company-specific information. The rest of the lumber exporters in Canada received the “all others” rate, which was the average of the company specific rates.
- On June 26, Commerce announced preliminary determination on anti-dumping duties. The preliminary CVD and AD rates are summarized below.

	Preliminary CVD	Preliminary AD
	Effective April 28, 2017	Effective Jun 30, 2017 (est.)
Canfor	20.26%	7.72%
J.D. Irving	3.02%	same as "all others" rate
Tolko	19.50%	7.53%
West Fraser	24.12%	6.76%
Resolute	12.82%	4.59%
"All others"	19.88%	6.87%

- Canadian companies are subject to CVD duties in the form of cash deposits on their lumber exports to the U.S. for four months from April 28 to August 27, 2017. The AD duties are additive to the CVD duties, and will be in place for four months from June 30 to October 28, 2017. After the initial four-month period, no cash deposits for CVD or AD duties will be required until the final determination order is issued.
- Under the current timeline, the U.S. is expected to issue the final orders on CVD and AD duties as early as October 2017. However, if the timeline for investigation is extended, the final orders may not be issued until January 2018, in which case, the AD duty will remain in place for up to six months.
- On April 24, 2017, Commerce also made a preliminary finding of “critical circumstances” (significant increase in Canadian lumber exports) for J.D. Irving and the “all others” group of companies, but not to Canfor, Resolute, Tolko and West Fraser. This means that Irving and all other companies are subject to CVD duty liability on their shipments made since January 28, 2017 and AD duty liability on shipments since April 1, 2017 (90 days prior to the CVD and AD preliminary determinations being published in the U.S. Federal Register respectively). After the final orders are issued, the final

CVD/AD duties will be applied to shipments to the U.S. going forward. Canada can appeal the decisions under the WTO, and either NAFTA or the U.S. Court of International Trade. Appeals could take several years.

- Duties (cash deposit) will be held in trust by the U.S. until all appeals are finalized.
- In the preliminary anti-dumping decision announced June 26th, Commerce also announced that products being produced in the Provinces of Newfoundland and Labrador, Nova Scotia, or Prince Edward Island (the Atlantic Provinces) from logs harvested in these three provinces should be excluded. Commerce and the U.S. Petitioners preliminarily claim that the private land stumpage rates paid in the Atlantic Provinces represent fair market value and are therefore not subsidized. This determination will not be finalized until the Final Determination is issued. New Brunswick has not been excluded from the litigation.

#### Mitigation of the Impact of Duties

s.13,s.16

- As observed in the previous lumber dispute, duty impacts could be partially mitigated by high lumber prices, as experienced since February 2017.
- In February 2017, a joint Federal-Provincial Ministers Task Force was established to ensure that the federal and provincial governments are coordinated and ready to respond to the needs of workers and communities affected by U.S. trade action.
- On June 1, 2017, Canada announced \$867 million Softwood Lumber Action Plan to support the companies, workers and communities that depend on the forest industry based on recommendations from the Task Force. The Action Plan included loans and loan guarantees, market and product diversification, job loss mitigation programming and support, and worker and community support. s.13,s.16

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s.13,s.16

- [Add any additional information helpful to understanding the above. Useful information might include: recent events and actions taken by BC or others related to the topic; progress to date; positions taken by other provinces or territories or by the federal government, etc.]

**MINISTRY OF FORESTS, LANDS AND NATURAL RESOURCE OPERATIONS  
DECISION NOTE**

Date: January 19, 2017  
File: 280-20  
CLIFF: 277005

**PREPARED FOR:** Jason Fisher, Associate Deputy Minister, Ministry of Forests, Lands and Natural Resource Operations

**ISSUE:** 2017/18 Blue Book Budget Estimates Forecast

**BACKGROUND:**

The Ministry of Finance has requested that the ministry prepare a revenue forecast for the 2017/18 budget which includes the revenue estimates summary for the 2017/18 to 2021/22 fiscal years, as well as the revised forecast for the 2016/17 third quarterly report. This revised revenue forecast reflects recent changes in market conditions and prepares for a new budget.

The 2016/17 Blue Book Budget Estimates Forecast was \$740.7M and was revised upwards to \$838.5M for the October Revised forecast due to increases in both Interior and Coast timber tenure stumpage rates and stronger than expected BCTS stumpage revenue.

**DISCUSSION:**

This 2017/18 Blue Book Budget Estimates Forecast, compared to the 2016/17 Budget Forecast is summarized as follows:

<b>Crown Forest Revenue Forecast</b>						
	<b>2016/17</b>	<b>2017/18</b>	<b>2018/19</b>	<b>2019/20</b>	<b>2020/21</b>	<b>2021/22</b>
	(\$, millions)					
2017/18 Budget Forecast	794.9	790.5	813.2	816.0	812.1	815.6
2016/17 Budget Forecast	740.7	747.7	761.8	783.9	798.5	n/a
<b>DIFFERENCE</b>	<b>54.2</b>	<b>42.8</b>	<b>51.4</b>	<b>32.1</b>	<b>13.6</b>	<b>n/a</b>

For fiscal year 2016/17, total Crown Forest Revenue is forecast to be \$794.9M. This is an increase from the 2016/17 Budget forecast of \$740.7M (up \$54.2M) but a reduction from the most recent October 2016 revised forecast of \$838.5M. The decrease from the October revised forecast is predominantly attributable to weaker than expected harvest volumes in the Interior and slightly lower than expected Interior Timber Tenures stumpage rates.

Interior Timber Tenures stumpage revenues have increased year-over-year (up 9%), predominantly due to increasing stumpage rates combined with lower harvest volumes. The average year-to-date Interior Timber Tenures stumpage rate is \$10.70/m<sup>3</sup> compared to \$8.77/m<sup>3</sup> at this time last year (up 22%). In contrast, Interior BCTS stumpage revenues have decreased year-over-year (down 5%) predominantly due to a decline in harvesting activity, even though stumpage rates have increased. The average year-to date Interior BCTS rate is \$26.25/m<sup>3</sup> compared to \$23.36/m<sup>3</sup> at this time last year (up 12%).

Coast Timber Tenures stumpage revenues have increased year-over-year (up 75%), however, increases continue to be slightly mitigated as only new cutting authorities are applicable under the March 2016 Coast MPS Update. Currently, approximately 60% of the adjustable appraised volume on the Coast is on the most recent update. The average year-to-date Coast Timber Tenures stumpage rate is \$5.70/m<sup>3</sup> compared to \$3.33/m<sup>3</sup> at this time last year (up 71%). Coast BCTS stumpage revenues have also increased year-over-year (up 38%), due to historically high stumpage rates and an increase in harvest activity. The average year-to-date Coast BCTS stumpage rate is \$43.92/m<sup>3</sup> compared to \$39.19/m<sup>3</sup> at this time last year.

The Crown harvest volume forecast for 2016/17 has been reduced by 3.0 million m<sup>3</sup> (from the October revised forecast) and is now expected to be 58.5 million m<sup>3</sup>. Crown harvest volume is 8% lower compared to this time last year. More specifically, fiscal year-over-year Coast harvest volumes are 5% higher and Interior harvest volumes are 12% lower. In addition to decreasing the harvest volume forecast for 2016/17, harvest volumes have also been reduced in the outer years of the forecast.

**Key assumptions underlying this forecast are as follows:**

First, this forecast reflects the current state of the US housing market and global economy. The US housing market continues its gradual recovery, as shown by improvements in US housing starts, and in particular single family units. Lumber commodity prices, while prone to volatility, have sustained recent year over year increases. Prices are expected to remain above historic levels for 2017 and 2018 before moderating slightly for the remainder of the forecast.

Second, this forecast does not assume a US duty on BC lumber exports. Negotiations continue to occur between Canada and the US regarding a managed trade agreement. Due to these ongoing negotiations and the current subsidy investigation, it was considered prudent to not explicitly incorporate a duty into the forecast. Ministry of Finance continues to be briefed on the softwood lumber trade case and there is the potential to include a topic box in the 2017/18 Budget and Fiscal Plan to elaborate on the issue and impacts.

Third, this forecast incorporates the recent Coast and Interior MPS quarterly adjustments (Jan 1, 2017). The Interior average appraised stand rate (scale based sawlog and cruise-based) increased marginally by \$0.13/m<sup>3</sup> and is now \$15.75/m<sup>3</sup>. For the Coast, the average appraised sawlog rate has declined (7%) down to \$9.74/ m<sup>3</sup>. This forecast does not incorporate a 2017 Coast MPS Update.

Fourth, this forecast reflects lower Crown harvest volumes. If current fiscal year projections hold, the average harvest over the last 3 year fiscal years will be 59.4 million m<sup>3</sup>. For comparison, harvest volume averaged 63.5 Mm<sup>3</sup> between 2011/12 and 2013/14. The Interior harvest volume forecast has been revised downward to accommodate this recent harvest history.

Finally, this forecast reflects year-to date harvest volumes billed at minimum rates. Currently, 34.3% of Crown harvest volume is on minimums (low grade and appraised minimums); this is comparable to the previous fiscal but up from 2013/14 and 2014/15. The volume billed at minimum rate has an influence on stumpage revenue as it has a dampening impact on average stumpage rates.

**The key risks and uncertainties to the forecast are:**

## **US Protectionism and Softwood Lumber Duties:**

The US is the world's largest lumber importer and US lumber demand and consumption will continue to have material impact on this forecast. Improvement and stability has emerged in the US economy and housing market, however, the softwood trade case and increased protectionist sentiment may eliminate any potential benefits to the BC forest sector. The Softwood lumber trade case creates a significant amount of uncertainty regarding BC access to the US market. s.13,s.16

s.13,s.16

Preliminary duties are expected to be announced no later than April 24, 2017. In addition, concerns exist related to new policies and trade measures under discussion by President Donald Trump and the Republican-controlled Congress in Washington. These concerns include the potential renegotiation or termination of the North American Free Trade Agreement.

## **Chinese lumber market:**

The Chinese economy continues to experience deceleration which will have a negative impact on the global economy. BC lumber export volumes to China during 2016 are down 8.7% as compared to the same period in 2015, while associated value is down 8.9%. BC lumber exports to China peaked in 2013 and have been decreasing year over year.

## **Timber Supply:**

Concerns continue to exist regarding future timber supply in the Interior. s.13

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The emerging risk related to harvest volumes, particularly in the outer years of this forecast is of concern.

## **Stumpage Rates:**

The Interior and Coast MPS Updates continue to influence stumpage rates and the harvest volume billed at minimum rates. This forecast does not incorporate a 2017 Coast MPS Update.

## **Summary**

The revised forecast for 2016/17 Crown Forest Revenue is \$794.9M; down from the October revised forecast of \$838.5M. This decrease in revenue is due to declining Interior harvest activity and lower than expected Interior stumpage rates.

The 2017/18 Blue Book Budget Estimates Forecast for Crown Forest Revenue is \$790.5M. This Budget Forecast reflects the cautious outlook for global economic growth, softening Crown harvest volume levels and strong Timber Tenures and BCTS stumpage rates.



## RECOMMENDATION:

Please approve this 2016/17 Revised Revenue Forecast and 2017/18 Blue Book Budget Estimates Forecast by signing the attached Memorandum and Revenue Estimates Summary.

The forecast has been made with the valued assistance and advice of staff from Timber Pricing Branch, Softwood Lumber Agreement Branch, Competitive and Innovation Branch and BC Timber Sales - Ministry of Forests, Lands and Natural Resource Operations; and Fiscal Planning and Estimates Branch, Economic Forecasting and Policy Analysis Branch, and Treasury Board Staff – Ministry of Finance.



Signature

February 21/17

Date

Approved / Not Approved

Jason Fisher, Associate Deputy Minister,  
Ministry of Forests, Lands and Natural  
Resource Operations

- Attachments:**
1. Memorandum to Athana Mentzelopoulos
  2. 2017/18 Blue Book Budget Estimates Forecast Revenue Estimates Summary
  3. Appendix 1: Detailed Forecast Assumption

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Reviewed by	Initials	Date
ADM	CS	
Exec Dir.	VS	January 25, 2017
Director	SK	January 20, 2017
Author	RM	January 19, 2017

## **Appendix 1: Detailed Forecast Assumptions**

### **US Housing Starts:**

The US housing starts forecast has mildly improved but still remains below historic levels, warranting a cautious approach. US housing starts are forecast to increase to 1.16 million for 2017 and to 1.2 million for the remainder of the forecast. In 2016, BC lumber export volumes to the US are 26.9% higher year-to date as compared to last year, while lumber export value is 38.8% higher.

### **Commodity Prices:**

Expectations are for lumber prices to increase prior to the upcoming building season and remain above historic levels for 2017 and 2018, then moderate downwards in the outer years of this forecast. Lumber prices for SPF 2x4s averaged US \$281 in 2015 and US \$307 in 2016 (up 9% year over year). The price of SPF 2x4s are expected to average US \$326 in 2017, US \$318 in 2018, then tempering down to the historical long term level (US \$300) for the duration of this forecast. The price of SPF 2x10s averaged US \$329 in 2015 and US \$326 in 2016. SPF 2x10 is expected to average US \$350 in 2017, US \$344 in 2018 before moderating to US \$340 in 2019 and beyond.

Pulp prices were stable and fluctuated only minimally in 2016 and this price stability is reflected in this forecast. The price of pulp averaged US \$849 per tonne in 2015 and US \$803 per tonne in 2016. The price of pulp is expected to increase minimally to US \$806 in 2017 then to US \$800 in 2018 and for the duration of this forecast.

The average log price as reported in the Coast Log Market Reports has remained strong for the duration of 2016, averaging \$126.57/m<sup>3</sup> (ytd end of October 2016). The average log price is expected to moderate down from historic highs in 2017, down to \$118 (CAD\$) per cubic metre and decrease again down to \$110 (CAD\$) in 2018 and remain at this level for the duration of the forecast.

### **Exchange Rate:**

The Canadian dollar remains low compared to the US dollar and is reflected in this forecast. The exchange rate forecasts have decreased slightly compared to the October Revised Forecast; however, exchange rates are susceptible to fairly rapid fluctuations. In calendar 2015 and 2016 the US\$/CAD\$ exchange rate averaged \$0.7829 and \$0.7548 respectively. A further decline in the exchange rate to \$0.7369 (US\$/CAD\$) is forecast for 2017, followed by an increase to \$0.7527 in 2018 and then to \$0.7836 in 2019; to \$0.8041 in 2020 and finally to \$0.8176 in 2021 and beyond.

## Crown Harvest Volume:

The 2016/17 total Crown harvest volume has decreased significantly from the October Revised Forecast and is now forecast to be 58.5 million m<sup>3</sup>. The detailed volume assumptions are as follows:

**Crown Harvest Volume Forecast**  
(m<sup>3</sup>, millions)

Region	2016/17 Blue Book Budget Estimates Forecast	2016/17 Revised Revenue Forecast (October)	2016/17 Revised Revenue Forecast (January)	2017/18 Blue Book Budget Estimates Forecast	2018/19	2019/20	2020/21	2021/22
Coast	13.2	13.4	13.4	13.5	13.5	13.7	13.7	13.7
Interior	48.8	48.1	45.1	45.5	46.5	46.3	45.3	45.3
<b>Total</b>	<b>62.0</b>	<b>61.5</b>	<b>58.5</b>	<b>59.0</b>	<b>60.0</b>	<b>60.0</b>	<b>59.0</b>	<b>59.0</b>

For the remainder of 2016/17, Coast Crown timber volumes are projected to be 13.4 million m<sup>3</sup>. This is comprised of 11.1 million m<sup>3</sup> from Timber Tenures and 2.3 million m<sup>3</sup> from Coast BCTS harvesting. For the Interior, Crown harvest volume is forecast to decrease to 45.1 million m<sup>3</sup> (36.1 million m<sup>3</sup> from Timber Tenures and 9.0 million m<sup>3</sup> from Interior BCTS harvest).

The total Crown harvest volume for the outer years of the forecast has also been adjusted downwards. Due to prevailing harvesting trends, total Crown harvest forecast for 2017/18 has decreased to 59.0 million m<sup>3</sup>. Crown harvest volumes are forecast to be 60.0 million m<sup>3</sup> in 2018/19 and 2019/20 and 59.0 million m in 2020/21 and 2021/22. The decrease in harvest volume is occurring exclusively in the Interior and will impact both BCTS and Timber Tenures. It is expected that BCTS will achieve a harvest level of 2.3 million m<sup>3</sup> on the Coast in 2016/17 and remain at this level for the duration of the forecast. Interior BCTS harvest volumes are projected to be 9.0 million m<sup>3</sup> during 2016/17, 9.5 million m<sup>3</sup> during 2017/18 before decreasing steadily down to 8.7 million m<sup>3</sup> in 2021/22.

# 2017/18 Estimates Debate

## ADM Binder Only

### Ministry of Forests, Lands, Natural Resource Operations and Rural Development

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#### **Issue:** Softwood Lumber Background Information

s.16,s.17

#### **What has the B.C. government done to assist companies in the current trade litigation?**

- The B.C. government maintains regular communication with forestry companies and industry associations. This communication encompasses both the litigation and negotiations.
- There are also regular communication with community leaders and the First Nation Forestry Council.
- Over the course of the litigation, B.C. has jointly prepared with Canada two comprehensive submissions (January & May 2017) addressing product scope and requesting exemptions for certain wood products in BC, such as Western Red Cedar and high-value lumber products.
- In 2016, B.C. worked jointly with Canada and other provinces to develop a comprehensive 2017 company exclusions process. Unfortunately, the U.S. Department of Commerce has declined to offer a company exclusions process under the Lumber V litigation.
- In the current litigation, the B.C. government has made approximately 30 submissions to the U.S. to defend B.C.'s interest. All the submissions were made in consultation with industry and some were filed jointly with industry.
- The B.C. government worked directly with the mandatory respondents in response to the U.S. questionnaires to ensure consistent interpretation of the questionnaires across the companies, and that complete and accurate information was provided to the U.S. to minimize the risk of triggering unreasonably high duties from the U.S.

#### **What actions will the province take to help B.C. companies impacted by the high duties?**

- To date strong demand plus supply shortages have allowed exporters to pass on most of the duties to the U.S. customers.
- The B.C. government continues to work with the Federal Ministers Task Force to seek trade compliant assistance programs. These programs must be trade compliant; otherwise they could lead to higher future duties for all exporters.
- Our government is committed to supporting companies involved in the litigation and through the subsequent appeal and expedited review processes.
- Resolving the softwood lumber dispute is a priority for government. B.C. is working hard to achieve a new softwood lumber agreement that is good for B.C. industry.

# 2017/18 Estimates Debate

## ADM Binder Only

### Ministry of Forests, Lands, Natural Resource Operations and Rural Development

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#### How will the NAFTA negotiations impact the lumber case?

- The start of NAFTA negotiations does not end negotiations for a lumber agreement. These two sets of negotiations are occurring in parallel.
- Historically, softwood lumber has not been included under NAFTA. Including lumber under NAFTA does not prevent the filing of countervail litigation by the U.S. industry.
- Chapter 19 of NAFTA is a key provision that is of significant importance to the softwood lumber case. It allows for a dispute resolution process to determine if the U.S. trade laws have been applied fairly. In the previous lumber case, Canada appealed the U.S. decisions under NAFTA and WTO, and won those appeals.
- We are working hard to seek a softwood lumber agreement that would provide certainty to our lumber producers, and establish an effective dispute resolution process.

#### What are the impacts to the forest industry?

- s.13,s.16
- High degree of financial uncertainty due to potential affirmative ITC ruling on critical circumstances. No retroactive duties have been paid as of yet, s.13,s.16  
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- Currently, US consumers are bearing close to the full impact of duties on lumber products  
s.13,s.16
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- s.13,s.16
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#### What happens if an agreement is negotiated?

- If a negotiated agreement is reached prior to the release of the final determination there are two possible paths:
  - Suspension agreement – subject to the agreed upon terms, the U.S. Department of Commerce suspends the investigation. The US or petitioners could lift the suspension at any time and the investigation would continue.

## 2017/18 Estimates Debate

### ADM Binder Only

#### Ministry of Forests, Lands, Natural Resource Operations and Rural Development

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- Settlement agreement – would include the terms and conditions for terminating the investigation.
- After Final Determination
  - Settlement agreement – would outline terms and conditions for future trade s.13,s.16 s.13,s.16

#### What happens once the final determinations are published?

- Once the final determination is released, Canada will likely quickly file a notice of intent to appeal under NAFTA Chapter 19.
- Following the publication of the final determination, the ITC will allow parties to submit final comments for the ITC to consider in their vote.
- Once the ITC has published the results of their vote:
  - If affirmative on injury or threat of injury – the U.S. Department of Commerce will publish the Final CVD and AD Orders.
  - If affirmative on critical circumstances – U.S. Customs and Border will start issuing invoices for all retroactive CVD and AD duties.
  - If ITC rules no injury and no threat of injury, the U.S. Department of Commerce will end its investigation, and issue instructions to refund all deposits collected.
- s.13,s.16

**Date Prepared/Revised: October 11, 2017**

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