



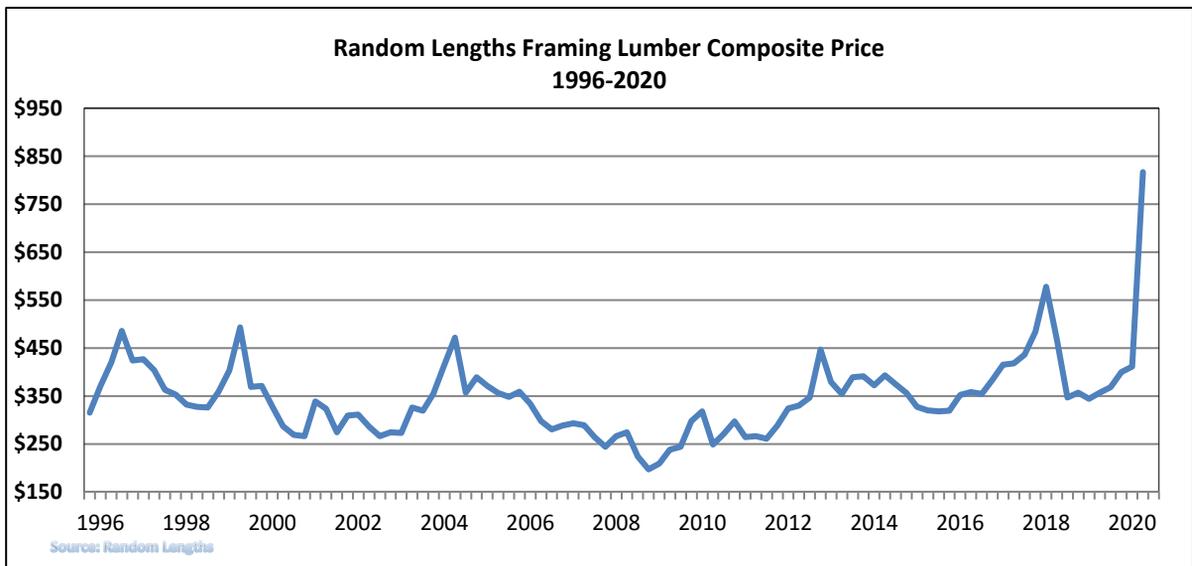
CORTON GLOBAL TIMBER FUND

Special Report – August 24, 2020

THE CASE FOR \$1,000 LUMBER

Background

- Over the past 20 weeks we have seen lumber prices (WSPF 2X4) increase by **205% to US\$860** per mfbm as of August 20 - **an all-time high**.
- This is the sixth record high we have seen in the past 25 years.
- In March 2020, when prices were trading at \$282, we were forecasting a 2020 average of \$443.
- **We have subsequently revised that forecast to \$548 and our 2021 forecast to \$675** from \$600.
- In the near-term, we could easily see **\$1,000** per mfbm.



What has driven prices so high?

- At the onset of the COVID pandemic in March, the major lumber companies started to schedule rotating sawmill closures fearing that Government mandated “stay-at-home” orders would negatively affect demand. It is estimated that **30% of North American lumber capacity was closed in April and May.**¹
- Some businesses such as hardware stores and home centres were deemed “significant” and remained open – lumber demand surged at the big box stores (**Home Depot, Lowes**).
- The sawmill closures coupled with high retail demand drove **inventories to record lows**.
- **Government stimulus had an unprecedented positive impact on real personal income.** The stay-at-home orders and the resulting drop in vacation and travel expenses lead to increased repair and renovation expenditures as the pandemic dragged into its fifth month.
- Meanwhile, **record low interest rates** and a rush to move to the suburbs lead to a rebound in new house construction in June and July – starts jumped from 924,000 in April to pre-COVID levels of 1.5 million units SAAR (seasonally adjusted annual rate) in July.

¹ RISI/Fastmarkets

Higher prices historically have lead to capacity additions and eventually “the Party” ends.

- Over the last 25 years, every one of the previous lumber price peaks ended when new lumber production hit the market. For example, in 2004/05 a total of 9 new greenfield sawmills and many sawmill rebuilds added approximately 3.8 billion board feet of new U.S. sawmill capacity. ¹
- **The 15.9% increase in B.C. sawmill output between 2003 and 2005 was largely attributed to an increase in the provincial annual allowable cut (AAC) in order to accelerate the harvesting of beetle-killed pine timber. (Note: the beetle-killed timber has now all been extracted).**

Table 1 - North American Softwood Lumber Production
(million board feet)

Region	2003	2004	2005	Change
US - West	10,877	11,982	12,815	+17.8%
US - South	16,674	17,360	18,485	+10.9%
US - Other	8,831	8,912	8,953	+1.4%
Total US	36,382	38,254	40,253	+10.6%
Canada – B.C.	14,867	16,722	17,231	+15.9%
Canada – East of Rockies	17,860	18,188	16,940	-5.2%
Total Canada	32,727	34,910	34,171	+4.4%
TOTAL	69,109	73,168	74,424	+7.7%

Sources: Western Wood Products Association, Southern Forest Products Association, Statistics Canada

- **The last peak in lumber prices, \$578, in May 2018,** ended when as a result; extreme cold weather in January/February which caused serious railcar deliveries, panic buying in April and May as dealers scrambled to replenish inventories (resulting in record high inventories), the U.S. Federal Reserve raised interest rates four times in the second half of 2018, and record rainfalls in Texas and the U.S. South in September and October. The latter two combined to slow lumber demand and force dealers to liquidate inventories. **Prices dropped 45%** from May to July 2018.
- **Prices languished in 2019,** as 7 greenfield sawmills and 6 major rebuilds in the U.S. South added an additional 1.9 billion board feet of lumber capacity. However, offsetting this increase were the permanent sawmill closures in British Columbia, which resulted in the removal of 1.9 billion board feet of lumber capacity. **Prices were largely range-bound between \$325 and \$400.** ¹

Table 2- North American Softwood Lumber Capacity
(million board feet)

Region	2018	2019	2020 (e)	2021 (e)	2022 (e)	Change
US - West	18,024	17,598	17,407	17,400	17,400	-3.5%
US - South	20,940	21,758	23,291	23,825	24,460	+16.8%
Total US	41,065	42,102	42,635	43,165	43,800	+6.7%
Canada – B.C.	14,061	13,307	12,929	11,525	11,225	-20.2%
Total Canada	31,360	30,540	29,954	28,550	28,250	-9.9%
TOTAL	72,425	72,642	72,589	71,715	72,050	-0.5%

Sources: Western Wood Products Association, Corton Capital Estimates

¹ Random Lengths

Where will the new supply come from to fill the current supply/demand gap?

- As illustrated in Table 2, despite the new capacity that came onstream in the U.S. South in 2018/19, a combination of; 3 older sawmill closures in the South, 6 permanent sawmill closures in the U.S. Pacific and Inland States, and the 15 permanent sawmill closures in B.C., **North American softwood lumber capacity is projected to remain flat over the next two years.** A planned 5% reduction in B.C.’s AAC by 2024 will result in another 4 permanent sawmill closures.
- U.S. lumber imports from Europe are up 42.8% year-to-date, however, represent less than 3% of total U.S. consumption ¹. **European countries are also experiencing a surge in retail lumber demand.**

The U.S. South is the only growth region in North America, but still not enough capacity !

- Table 3, lists the announced sawmill capacity changes in the twelve U.S Southern states. **Many of the expansions, however, have been delayed due to COVID-related reductions in capital expenditures.**

Table 3 – Sawmill Capacity Changes – U.S. South – 2020/22
(million board feet)

Company	Location	Date	Capacity	Notes
Georgia-Pacific	Rome, Ga.	Feb 2020	75	Debottlenecking
Canfor	Camden S.C.	Mar 2020	50	Debottlenecking
Klausner	Live Oak, Fl.	Mar 2020	(200)	Indefinite closure – Bankruptcy
Klausner	Enfield, N.C.	Mar 2020	(200)	Indefinite closure – Bankruptcy
Canfor	Urbana, Ark.	Apr 2020	115	Debottlenecking
Canfor	Moultrie, Ga.	June 2020	70	Debottlenecking
Georgia-Pacific	DeQuincy, La.	June 2020	(195)	Indefinite (built in 1990)
Abbeville Fibre	Abbeville, Ala.	Sept 2020	50	Greenfield – Phase II
Southeastern	Ackerman, Miss.	Sept 2020	170	Expansion - DELAYED
Canfor	Fulton, Ga.	Nov 2020	105	Rebuild
Interfor	Thomaston, Ga.	Dec 2020	30	Debottlenecking - DELAYED
Interfor	Eatonton, Ga.	Dec 2020	30	Debottlenecking - DELAYED
Interfor	Georgetown, S.C.	Dec 2020	30	Debottlenecking - DELAYED
Westervelt Lumber	Thomaston, Ga.	Dec 2020	250	Greenfield – DELAYED
West Fraser	Opelika, Ala.	Late 2020	?	Debottlenecking - DELAYED
West Fraser	Dudley, Ga.	Late 2020	?	Debottlenecking - DELAYED
TBD (Mercer ?)	Live Oak, Fl.	TBD	200	Restart - Former Klausner mill
Resolute	El Dorado, Ark.	Apr 2021	180	Restart - Former Conifex sawmill
TBD	Enfield, N.C.	TBD	200	Restart - Former Klausner mill
Canfor	Washington, Ga.	Late 2022	275	Greenfield – ON HOLD
TOTAL			1,235	1.7% of NA Capacity

Sources: Company Filings, Corton Capital

- Acquisitions are also expected to be few and far between due to unrealistic valuations, the result of the over-heated lumber markets and the age of many of the mills.**

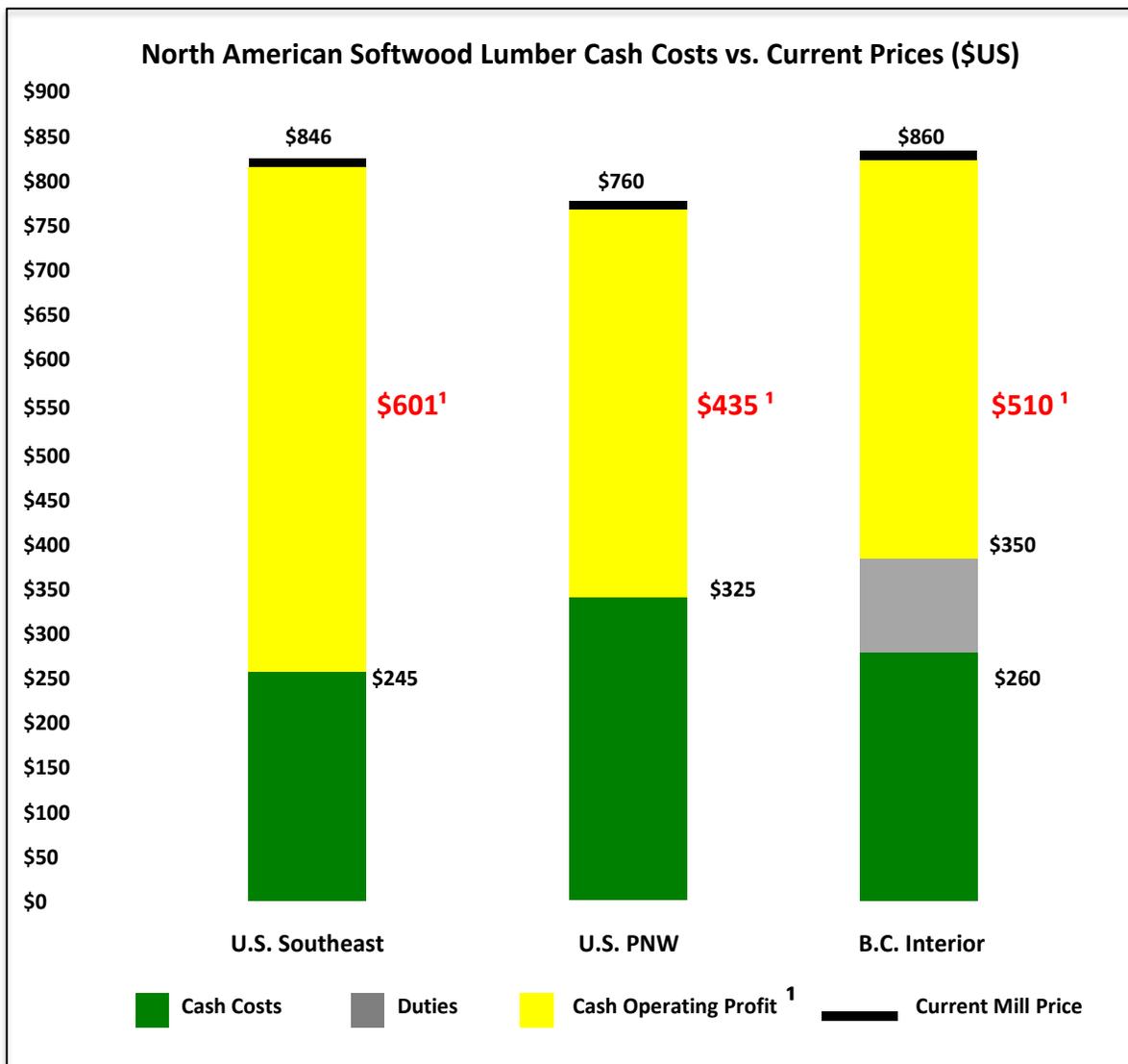
¹ U.S. Commerce Department

Other factors will affect near-term lumber supply.

- **COVID-related shift/mill reductions**, especially in the U.S. South – a virus “hotspot”
- **Delay in equipment installation** due to COVID protocols regarding outside contractors.
- In B.C., **low availability of independent logging contractors** after years of attrition.
- An industry-wide **low availability of skilled tradesmen**.

North American lumber companies prepare for RECORD PROFITS !

- **The Corton Global Timber Fund owns shares in ALL of the major publicly traded lumber cos.**



Source: Forest Economic Advisors

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