

# CORTON GLOBAL TIMBER FUND

SPECIAL REPORT – November 24, 2020

## *Softwood Lumber – Duty Deposit Rates Adjusted Downwards*

**Impact:** VERY POSITIVE for the lumber companies held in the Corton Global Timber Fund

**Event:**  
Today, after two lengthy “tolling” delays due to COVID-19, the **U.S. Department of Commerce** (“USDOC”) announced the final determination for the First Administrative Review (AR1) of its antidumping (AD) and countervailing duty (CVD) investigations of imports of softwood lumber from Canada. The preliminary determination was released on February 3, 2020. **Table 1 lists the new cash deposit rates. The big winner is Canfor where its current rate drops from 20.52% to 4.62%, while Resolute Forest’s rate actually goes up to 20.25% from 17.9%.** Once the new rates are published in the Federal Register (expected November 30), the new cash deposit rates will apply to all subsequent lumber shipments until AR2 is completed in late 2021.

**Table 1 – New Cash Deposit Rates**

COMPANY	Current CVD/AD Dut Deposit Rate	New – AR1 CVD/AD Duty Deposit Rate	Decrease /Increase In Rate	Duties Paid in 2020 (e) C\$ mils	Duties Paid in 2021 (e) C\$ mils	Y-O-Y Reduction C\$ mils
Canfor	20.52%	4.62%	-74%	\$149.3	\$38.8	\$110.5
Interfor	20.23%	8.99%	-51%	\$49.7	\$24.4	\$25.3
Resolute Forest	17.90%	20.25%	+11%	\$92.0	\$102.0	(\$10.0)
West Fraser	23.56%	8.97%	-57%	\$161.0	\$69.2	\$91.8
All Others	20.23%	8.99%	-51%	-	-	-

Source: Corton Capital estimates

Note: The Decrease/Increase Rates are based on the “entered value” formula that is used by U.S. Customs and Border Protection

### **What is an Administrative Review ?**

The current CVD and AD duties (commonly referred to as “**Lumber V**”) went into effect on January 3, 2018. Under U.S. trade law, each year (unless the trade case is settled as in Lumber II, III, and IV), an administrative review is conducted by the USDOC to recalculate the countervailing and antidumping duty rates for shipments during the period of review and to establish a new cash deposit rate for future shipments. **The Period of Review for AR1 was April 28, 2017 through December 31, 2018.** On January 2, 2020, the USDOC initiated the Second Administrative Review (AR2) based on the period of review (January 1, 2019 - December 31, 2019). The **U.S. Coalition for Fair Lumber Imports** (the U.S. plaintiffs in the lumber trade dispute) is pushing the USDOC to not delay AR2 and the review results could be released as early as September 2021. The duty deposit rates could be further adjusted.

**The U.S./Canada Lumber Trade War History:**

**Lumber I** (1982-1983) ended when the USDOC made a negative CVD determination on technical grounds. **Case ended.**

**Lumber II** (1986-1991) The USDOC found the under-pricing of Canadian government timber constitutes a subsidy and assessed a subsidy rate of 15%. **The U.S. and Canada settled by signing a Memorandum of Understanding (MOU), in which Canada imposed an export tax of 15%.**

**Lumber III** (1991-1994) Canada withdrew from the MOU in October 1991. The USDOC initiated a new CVD investigation. Under Chapter 19 of the U.S./Canada Free Trade Agreement (FTA), the FTA dispute panel ordered the USDOC to revoke the CVD order (rate was 11.54%). The U.S. Coalition for Fair Lumber Imports launched a suit. The U.S. and Canadian governments, in an effort to find a durable solution to the lumber dispute, created the first **“U.S.-Canada Softwood Lumber Agreement” (SLA 1996)** in April 1996, which set fees on over-quota shipments. **The duties on deposit were returned to the Canadian producers.**

**Lumber IV** (2001-2006) Canada declined to renew the SLA 1996 when it expired in March 2001. The Coalition re-submitted CVD and AD petitions to the USDOC. In May 2002, USDOC implemented CVD and AD orders at a combined duty rate of 27.2%. The second **Softwood Lumber Agreement (SLA 2006)** came into effect in October 2006 for an initial term of 7 years with a two-year extension. Canada imposed taxes and quantitative restrictions on lumber exports to the U.S. **The U.S. returned approximately US\$5 billion in duty deposits.**

**Lumber V** (2016 – present). The SLA 2006 expired in 2015. The Coalition launched another trade petition in November 2016. The USDOC assessed preliminary CVD/AD duties in early 2017. The final duty rates went into effect January 3, 2018. **Total lumber duties on deposit to date are an estimated US\$3 billion.** The Table below lists the lumber duty deposits for the major publicly traded companies. The deposits are being held in trust by U.S. Customs and Border Protection.

**Table 2 – Lumber Duty Deposits**  
(millions)

COMPANY	As of Sept 30, 2020	Per Share
West Fraser	US\$495.0	US\$7.20
Canfor	C\$547.5	C\$4.37
Resolute Forest	US\$214.0	US\$2.48
Interfor	US\$121.1	US\$1.80
Western Forest	C\$113.9	C\$0.30

Source: Company Filings

**Will the Lumber Trade Wars Ever End ?**

**Probably Not**, but a lot has happened since the mid 1980s, which has changed the landscape:

- Canadian companies have acquired/built dozens of sawmills in the U.S. Canadian companies own and operate 47 sawmills in the U.S. South representing 34% of total lumber capacity. <sup>1</sup>
- A total of 75 of Canadian sawmills<sup>1</sup> have closed since 2006 due to timber supply issues as a result of insect infestations and environmental policies.
- Canada’s market share in the U.S. has dropped from 35.6% in 2005 to 23.4% in 2020. <sup>1</sup>
- U.S. sawmill operating rates are forecast to reach 92% in 2021 – highest level in 20 years. <sup>1</sup>
- Lumber markets have seen two record “peak price” periods since 2015.

<sup>1</sup> Corton Capital analysis

### Will There Be a Another Softwood Lumber Agreement ?

**Probably Not.** There is no desire by the Canadians (with a few exceptions).

- The Canadian producers have had record earnings and with higher demand from North American and Asian markets, the high level of earnings will continue for the foreseeable future.
- Balance sheets are in excellent shape.
- Capacity expansion and acquisitions by Canadian companies operating in the U.S. will negate the effect of lumber duties.

### What Will Happen ?

**The USDOC will continue with its Administrative Reviews.** The Canadians are patient.

- Canadians will wait as US trade law slowly takes its course. The USDOC may eventually work the CVD/AD duty rates down to “de minimis” rates (i.e. below 1%).
- The Canadians may win future determinations by NAFTA Panels regarding injury and anti-dumping cases.
- “Outside Appeal” processes such as under WTO will continue. On August 26, 2020, the WTO dispute resolution panel ruled unanimously that the U.S. countervailing duties against Canadian softwood lumber are inconsistent with the WTO obligations of the U.S. The WTO process was temporarily derailed by the Trump Administration. The new Biden Administration is likely to re-instate the U.S. /WTO relationship.

### What Happened to Lumber Prices ?

**December 2004** – Duties on Canadian lumber lowered to 21.2% (from 27.2%). **Lumber prices rose by 15%** to US\$420 in April 2005.

**October 2006** – SLA came into effect. **Lumber prices rose by 10%** to US\$305 in June 2007.

**October 2015** – SLA expires. **Lumber prices rose by 25%** to US\$370 in August 2016.

**November 2017** – USDOC issues final CVD/AD Duty of 20.23%. **Prices rose by 30%** to a record US\$565 in August 2018.

***Based on history and considering the current tight lumber market conditions, we expect the reduced lumber duty deposit rates will not have a negative effect on lumber prices.***

For more information on how to invest in the Corton Global Timber Fund, please contact: David Jarvis – [David@cortoncapital.ca](mailto:David@cortoncapital.ca), John Duncanson - [john@cortoncapital.ca](mailto:john@cortoncapital.ca), or Jenny O’Meara – [jenny@cortoncapital.ca](mailto:jenny@cortoncapital.ca)

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