

Quick Hit – It’s back! A Canada-US softwood lumber dispute that is

As widely expected, the US government has announced its intention to retroactively levy preliminary duties (ranging from 3% to 24%) on imports of Canadian softwood lumber, thrusting lumber once more to the top of the heap when it comes to trade irritants between two countries sharing the largest bilateral trade relationship in the world. From the sound of things though, the Americans have a few other bones to pick with us, whether supply-managed dairy products, energy or NAFTA overall.

We put out a *Hot Chart* this morning looking at the importance of lumber to the Canadian economy, and here we provide a bit of provincial colour. When it comes to the affected share of GDP or employment, British Columbia and New Brunswick are most directly exposed, and it was BC’s credit spread that came under a bit of pressure following the US announcement. Now, we don’t want to trivialize the potential fallout on these or other provinces. The forestry industry is an important regional employer after all, and some will recall the painful job losses that accumulated the last time duties were imposed. The application of duties will, as in the past, crimp the merchandise trade balance and current account, which explains why the Canadian dollar has been put on its back foot. And as the BC budget recently noted: US trade actions on softwood lumber pose a “key risk” to fiscal projections too.

Still, we’d note that the relative significance of the forestry industry has waned over time. In other words, there’s less relative economic or fiscal exposure to forestry in BC, New Brunswick or most provinces today than was the case back in the early 2000s. For instance, forestry revenue today comprises 1.7% of BC’s total revenue pie, just one third of the revenue share back in 2001-02. It should be noted that BC’s prudent budgeting, including conservative economic assumptions, reserves and spending contingencies provide an important degree of protection against such adverse events. Moreover, BC in particular has succeeded in developing overseas markets for its lumber and an orientation toward non-US markets (or even the domestic market) could blunt the impact.

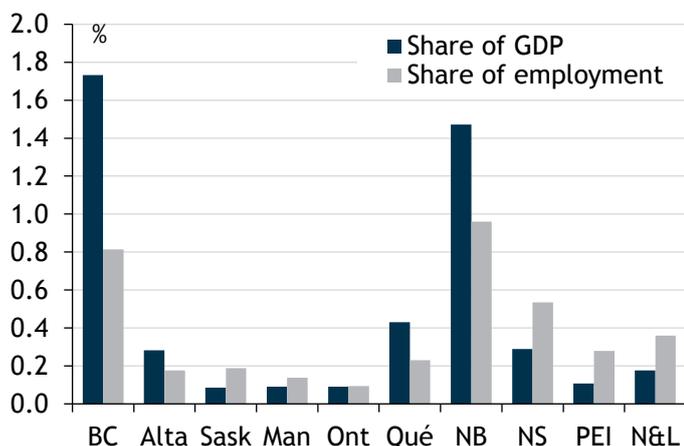
Overall, writing another chapter in a long-running softwood lumber trade dispute is hardly good news for Canada. While not exactly spoiling for a fight, one could expect Canada to mount a forceful and coordinated federal-provincial defense to what Ottawa views as “baseless and unfounded” accusations of unfair subsidization. Some may take comfort in the fact that international trade tribunals have sided with Canada in the past, and a negotiated settlement could still be reached. Still, resolving trade disputes takes time... perhaps years. The US government could be collecting duties from us all the while, displacing our exports and causing harm to a still-important industry. Ultimately, the extent of the damage to our softwood lumber industry will inform the amount of aid Canadian governments opt to provide, although the federal government has indicated its willingness to provide financial support. So while BC and some other provinces are understandably nervous, they’re hardly standing alone. There will be plenty to watch on this in the weeks and months ahead, and as we’ve previously argued, softwood lumber might well be viewed as a litmus test when it comes to Canada-US trade relations. Ultimately, there’s a lot more than ~US\$6 billion of lumber exports and 50,000 forestry jobs at stake.

Finally, note that the US move to slap on countervailing duties comes in the midst of BC’s provincial election campaign. Based on public opinion polls, the May 9 vote looks to be a close one. More than softwood lumber, it’s a prospective change in BC’s political leadership and fiscal philosophy that could be the more material driver of the province’s credit spreads from here.

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Chart 1: Relative provincial exposure

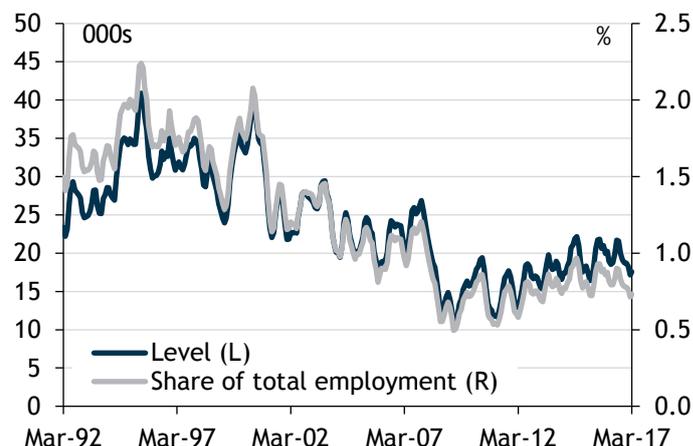
Forestry/logging share of provincial GDP and employment*



Source: NBF, StatCan | * GDP share for 2015, jobs share for 2016

Chart 2: Forestry less important to BC today

Forestry/logging employment in BC: Level & share

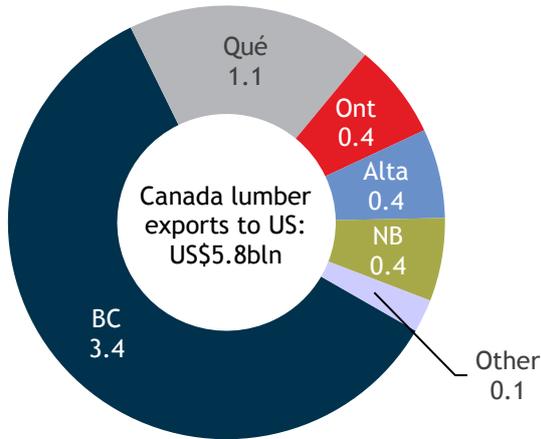


Source: NBF, StatCan

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Chart 3: BC ships most lumber to US...

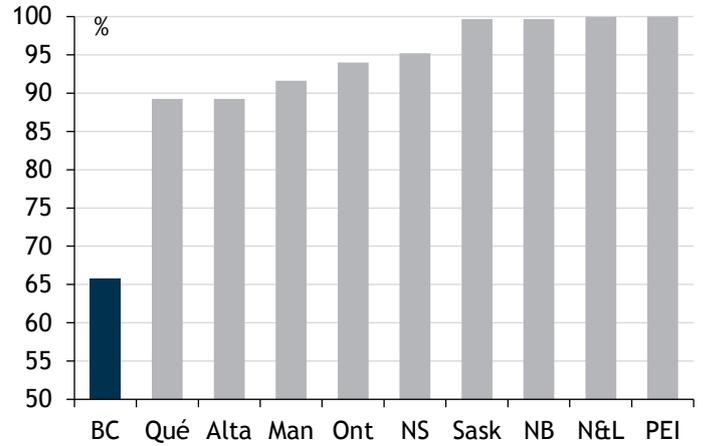
Canadian lumber exports to US by province (2016)



Source: NBF, Industry Canada | Note: Figures in chart are in US\$bln

Chart 4: ...but has diversified more than others

US share of international lumber exports by province (2016)



Source: NBF, Industry Canada

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