Market Trends and Prospects

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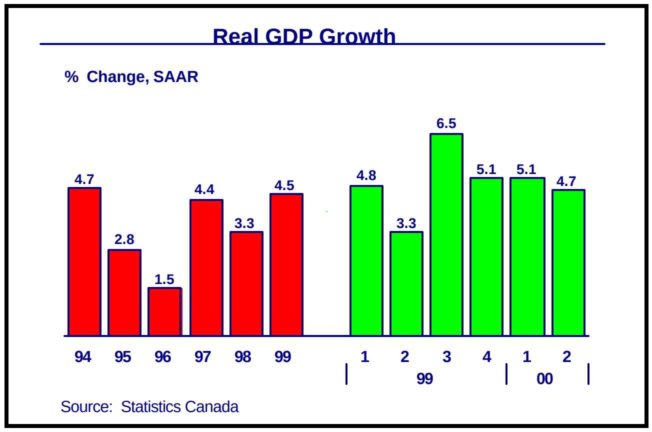
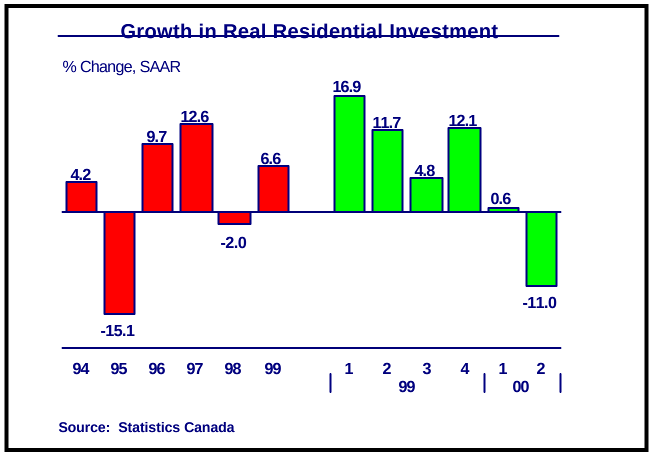
An Economic Overview

General Economic Conditions

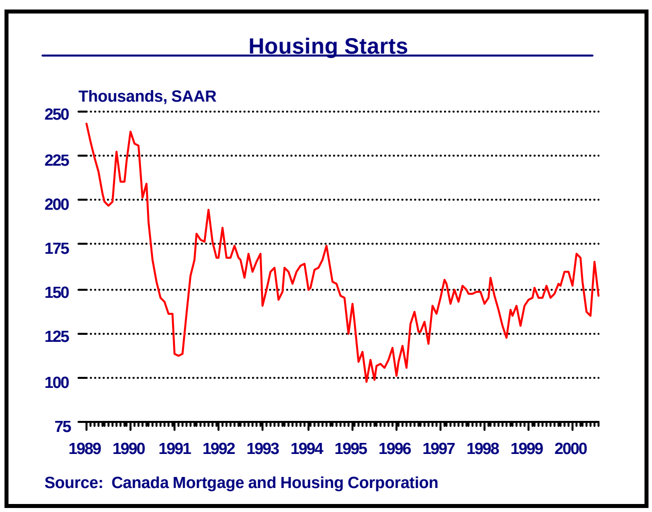
The Canadian economy expanded by 4.5% in 1999, and has carried this strength into 2000, with growth averaging 4.9% in the first two quarters. While business investment has risen so far this year, consumer spending is also expanding at a healthy pace, and export growth remains strong. The high-tech sector was a major source of strength in the second quarter of this year.



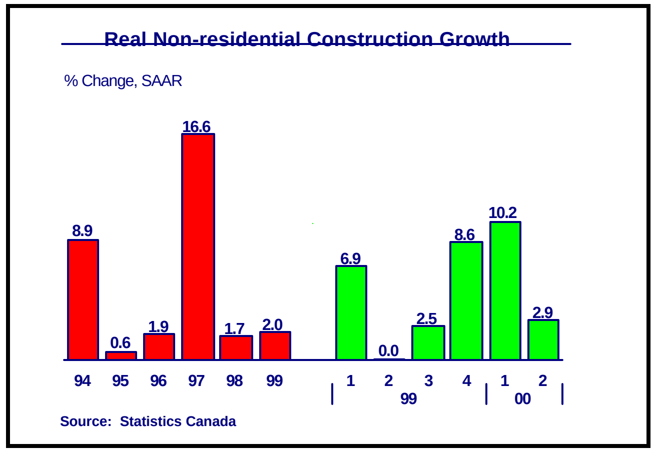
Activity in the housing sector has weakened in the first half of 2000 after posting gains in 1999. While this was partially due to strikes in Ontario and skilled labour shortages, this weakening was not concentrated solely in Ontario. Following a strong 1999, investment in residential construction rose 0.6% (annual rate) in the first quarter of 2000, and posted a decrease of 11.0% in the second quarter. New housing, renovations, and resale activity have all registered a slow-down so far this year. Housing affordability and consumer confidence, however, are expected to remain positive despite recent upward movements in mortgage rates.



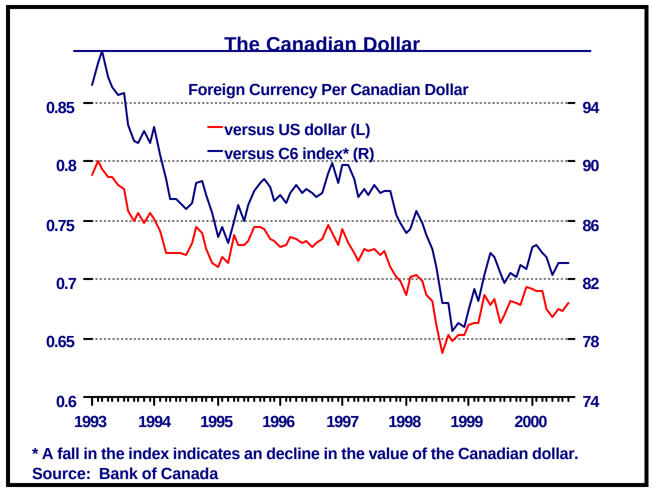
Despite weakness early in the year, the momentum appears to point to a resumption of the growth trend: municipalities issued $21.5 billion in residential building permits over the first seven months of 2000, the best performance for that period since 1989. Most of the increase in permits, has been for single-family dwellings, as the value of multi-family dwellings remained virtually unchanged from 1999 levels. On a provincial basis, the largest increases were recorded in Ontario, Quebec and Alberta, while permits in British Columbia and New Brunswick were lower than in 1999.



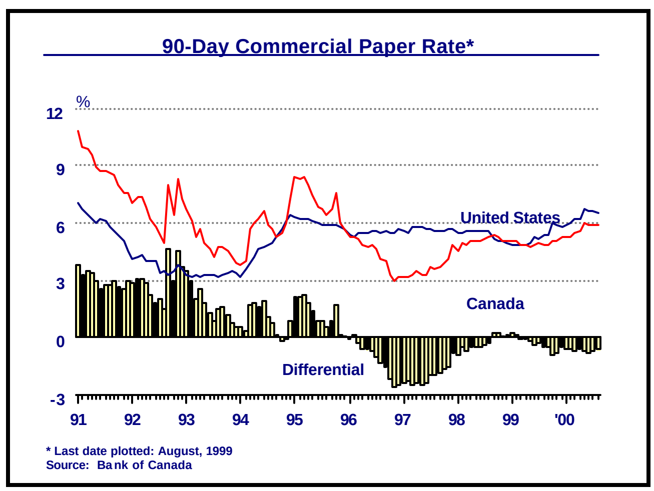
Investment in non-residential construction has picked up so far in 2000, as activity in the oil patch was much higher. Over the first seven months of 2000, non-residential building permits were up 6.6% compared to the same period in 1999. Commercial building projects spearheaded the overall growth, but industrial and institutional projects also contributed.



The Canadian dollar has drifted lower in the first half of 2000, after gaining roughly four cents over the course of last year. Although concerns of higher U.S. rates still pose a downside risk to the Canadian dollar, the strong economy, firm commodity prices and a solid fiscal situation could provide support for the Canadian dollar in coming months. It is noteworthy that the dollar is faring better against other international currencies, such as the Euro and the yen.



This year, the Bank of Canada raised its trend-setting rate in February, March and May for a total of one full percentage point from the end of 1999. The outlook for further interest rate increases is uncertain. While the Canadian and U.S. economies are both relatively strong, some signs of a moderate slowdown have emerged and there is little evidence pointing to a general pick-up in inflation. Canadian short-term interest rates still remain below comparable U.S. rates.



LUMBER and LOGS

Sawn Softwood

Situation in 1999

Canadian output of sawn softwood reached 68.2 million cubic metres in 1999, an increase of 6.5 percent over 1998's production of 64.1 million cubic metres. Sawn softwood stocks rose moderately by 4.5 percent to 8 million cubic metres.

Domestic demand for sawn softwood was robust in 1999, soaring 19 percent to 20.3 million cubic metres. Strong growth in the Canadian economy and a healthy residential construction sector contributed to higher domestic demand for sawn softwood. Increased industrial and repair and remodelling activity created additional demand. Housing starts were 150 thousand units in 1999, an increase of 9 percent from 1998 levels.

Canadian exports of sawn softwood rose 2.5 percent to 48.4 million cubic metres. Exports to the United States (US), which represent 88 percent of sawn softwood exports, increased by 1.2 percent to 42.7 million cubic metres. Housing construction activity in the US, which reached 1.64 million new units, remained robust throughout the year and pushed demand for sawn softwood higher.

Exports to Japan began to recover in 1999. While the Japanese economy continued to produce mixed results, Canadian sawn softwood exports jumped 14 percent to 4.5 million cubic metres. The positive export performance in Japan was a result of improved residential construction activity, as housing starts in Japan reached 1.2 million units, up 3 percent from 1998. Sawn softwood shipments to Japan represent 9 percent of Canadian exports.

Exports to Europe were 524 thousand cubic metres in 1999, an increase of 6.1 percent. However, exports to Europe are only a fraction of the historical high of sawn softwood exports to the region.

Prospects for 2000-2001

Canada’s economy continues to grow but sawn softwood production has not shown the same growth. Production of sawn softwood fell 3 percent to 35.5 million cubic metres in the first six month of the year. The three week sawmill workers strike in British Columbia negatively impacted Canadian production in the first half of the year. An oversupply of sawn softwood in the North American market is also causing many mills across the country to extend downtime, further cutting Canadian production levels for 2000.

Residential construction in Canada, which represents the single largest share of sawn softwood demand, is expected to finish the year below 1999 levels. Housing starts are expected to be approximately 147 thousand in 2000 and, with an expected downturn in the housing market, to fall to 140 thousand in 2001. Domestic consumption of sawn softwood was extremely high in 1999 and is not expected to achieve the same level in

2000. Domestic demand for sawn softwood is forecast to fall from their 1999 levels to 18.6 million cubic metres in 2000 and to 17.8 million cubic metres in 2001 as the Canadian economy begins to slow.

Interest rates increase in the fall of 1999 and the spring of 2000 by the US Federal Reserve are beginning to be felt in parts of the US economy, especially the residential construction sector. Lower demand for sawn softwood has caused prices to tumble. Despite this, Canadian sawn softwood exports to the US are up 4 percent in the first half of 2000, reaching 21.8 million cubic metres. Exports are expected to fall in the second half of 2000, finishing the year below 1999 levels at 42 million cubic metres. In 2001, exports to the US are forecast to remain near 2000 levels as economic growth in the US weakens slightly.

Exports to Japan were up 3.5 percent to 2.3 million cubic metres in the first six months of 2000. The Japanese economy remains fragile, shrinking in the second half of 1999, but surging in the first quarter of 2000. Should the economy stabilize, Japanese demand for Canadian sawn softwood should rise, surpassing 1999 levels this year, and increasing again in 2001.

Coniferous Logs

After increasing to 1.05 million cubic metres in 1998, exports of coniferous logs jumped a further 79 percent to 1.9 million cubic metres in 1999. Exports to Japan and the United were both up 79 percent, reaching 758 thousand and 1.1 million cubic metres respectively. Export of coniferous logs are expected to fall in 2000 and again in 2001, as the US economy begins to slow.

Imports of coniferous logs dropped 26 percent to 1.7 million cubic metres. In 2000 and 2001, imports are expected to remain stable at 1999 levels.

Sawn Hardwood

Production of sawn hardwood was 1.1 million cubic metres in 1999, an increase of 2.3 percent. Stocks increased 14 percent to 143 thousand cubic metres. Export demand was strong, up 15 percent to 1.34 million cubic metres for 1999. Exports to the US reached 1.1 million cubic metres, motivated by the strong US economy. Domestic consumption dropped 3.5 percent to 748 thousand cubic metres. Imports of sawn hardwood into Canada rose 10 percent to 1.05 million cubic metres. In the past few years, significant quantities of imported sawn hardwood appear to have been re-exported after further processing at Canadian mills, resulting in higher Canadian exports than production.

As the Canadian and US economies continue to grow, hardwood production in 2000 is expected to remain near or finish slightly higher than 1999. Imports of sawn hardwoods, in demand by Canada's growing furniture industry, are expected to increase again in 2000 and 2001.

Hardwood Logs

Canada exported 274 thousand cubic metres of hardwood logs in 1999, an increase of 19 percent from 231 thousand cubic metres in 1998. The US remains the largest market for Canadian hardwood logs. Log exports are expected to increase slightly in 2000 and fall in 2001 as the US economy begins to slow. Imports of hardwood logs increased 19 percent to 1.5 million cubic metres in 1999.

WOOD BASED PANELS

Coniferous Plywood

Production of Canadian coniferous plywood in 1999 totalled 1.93 million cubic metres up almost 10 percent from the volume produced in 1998. The increase in output reflected the strong domestic market and an increase in export sales. Domestic consumption in 1999 remained unchanged from the previous year at 1.4 million cubic metres as both the industrial and residential housing markets remained strong. Imports, which represented relatively small volumes of low grade sheathing products and certain specialty products not manufactured by the industry, increased 22 percent in 1998. Exports in 1999 increased by 40 percent with most of the increase going to the US and Japan, offsetting reduced volumes of exports to Europe. Exports to Europe in 1999 totalled only 80 thousand cubic metres down from the 169 thousand cubic metres achieved in 1998.

Production in 2000 is projected to total 1.8 million cubic metres, slightly below 1999 output. During the first 6 months of 2000, mills have generally operated at normal, near capacity, levels. However a second quarter softening of North American demand for plywood and other structural panels has resulted in traditional summer shut downs being expanded, leading to the current improved balance in the supply demand situation.

Despite the decline in European demand for Canadian coniferous plywood over the past decade, Canadian producers continue to view the market as important and they remain committed to serving it with their traditional high quality and value-added products. Through their industry association, the Canadian Plywood Association (CanPly), an increase in market service in Europe is being formulated. Overall export shipments are projected to increase in 2000 to approximately 610 thousand cubic metres, with exports to the US increasing significantly, based on statistics for the first half of 2000. Exports to Europe and Japan in 2000 are expected to reach about 110 and 225 thousand cubic metres respectively, a small decrease from the previous year’s volumes.

Particleboard

In 1999, the Canadian particleboard industry operated at near capacity and achieved an output of more than 2.4 million cubic metres, an increase of about 4 percent compared to the volume produced in 1998. Domestic consumption of 1.6 million cubic metres also increased by 8 percent compared to 1998 in response to continued strength in both the domestic furniture and residential building sectors. Exports in 1999, which represented about 43 percent of production and were predominately to US, decreased about 2 percent over the previous year in response to strong demand in the domestic market. Imports in 1999, including specialty and overlaid products, some of which are not generally available from domestic producers, also increased by almost 7 percent due to the strong domestic market.

In the first six months of 2000, the output of the Canadian particleboard industry increased marginally to about 1.3 million. So far in 2000, several major modernization projects in the sector have been completed which, when operated at full capacity, will add nearly 1 million cubic metres in new capacity. In addition, some melamine overlaying capacity has been added. A straw-based particleboard mill, which started production in 1998, has recently ceased production as a result of financial and technical difficulties .

Statistics in the first six months of 2000 indicate that particleboard exports, which are almost entirely to the US, should equal the volumes achieved in the previous year and are projected to total about 1.25 million cubic metres. Imports in the first half of 2000, which are mostly from the US, are expected to increase in 2000 in response to the strong demand in the domestic furniture sector.

Oriented Strandboard (OSB)

In 1999, Canadian oriented strandboard (OSB) production increased by 1.4 million cubic metres to 7.7 million cubic metres, an increase of approximately 22 percent. This dramatic increase in output continues a recent trend which has witnessed the output of OSB triple over the past six years. The increase in Canadian capacity reflects the strength of the North American building sector, the start-up of many new mills and the expansion of existing mills during this time period.

Consistent with the strong residential building activity experienced in Canada during 1999, domestic consumption more than doubled to about 1.0 million cubic metres. Exports in 1999, which remained highly dependent on the housing market in the US and a favourable currency exchange rate, continued to demonstrate strong growth by increasing 775 thousand cubic metres (13 percent) over the previous year’s levels. Imports of OSB represent small volumes and are largely supplied by mills in the US which are close to markets in Canada.

Despite the oversupply of structural wood based panels, OSB production during 2000 is expected to increase marginally and achieve a new record output of about 7.7 million cubic metres as new mills, which started production during the past several years, move towards design capacity. Exports, during the first half of 2000 were 4 percent above those recorded in the same period of the previous year and are expected to reach an estimated 6.8 million cubic metres for the year as a whole. In the second half of 2000, a weakening demand in the North American market and increased capacity, have caused prices to decline to the point where some producers have taken extended summer holidays and other short term shutdowns. At least three new OSB mills in Canada are currently being built with startup dates in late 2000. In addition, many mills have undertaken some capacity expansion or efficiency improvement projects in the past 12 months.

Hardboard - Medium Density Fibreboard (MDF)

The output of hardboard/MDF in 1999 totalled 1.0 million cubic metres, an increase of about 25 percent when compared to the previous year. Although no new plants entered production in 1999, several MDF plants, which had began production in previous years, achieved major gains in output as they began producing near design levels. Although hardboard is included in this category of wood based panel, the majority of output of this product grouping is represented by MDF which has expanded rapidly in the past five years. Exports in 1999, which are mostly MDF, increased by more than 30 percent from the levels achieved in the previous year. Imports in 1999, which included some raw hardboard and certain MDF and hardboard products not generally manufactured in Canada, showed a minor increase in volume terms from 1998.

Based on statistics available for the first 6 months of 2000, production of hardboard/MDF is expected to increase by about 7 percent in 2000. Some additional MDF capacity which was added during early 2000 will increase output. Exports in 2000 as a whole, also based on the statistics from the first six months, are expected to increase by about 3 percent above the level as achieved during 1999, due to the favourable US /Canada currency exchange rate and strong demand in the US furniture market. No new capacity expansions have been announced and industry sources suggest that MDF may be in short supply if additional capacity is not built in the short term.

Non-Compressed Fibreboard

Statistics for the non-compressed fibreboard, or rigid insulation board as it is known in Canada, are no longer maintained by Statistics Canada. However, based on consultations with the industry, it is estimated that production in 1999 remained essentially unchanged from the 1999 level of approximately 460 thousand cubic metres. Domestic consumption in 1999 is estimated to have increased by almost 3 percent to about 392 thousand cubic metres as it replaced some wood based panels in residential and commercial construction applications. Exports, supported by a favourable currency exchange rate increased marginally. Imports in 1999, which totalled 61 thousand cubic metres in 1999, reflected the strong domestic housing market, were up substantially from the previous year.

For 2000 as a whole, production and domestic consumption are expected to increase marginally from the levels achieved in 1999. Imports and exports are also projected to demonstrate some growth in volume terms from the previous year.

MARKETS FOR CERTIFIED WOOD PRODUCTS

Statistics on the production, consumption or trade in certified wood products in Canada are not differentiated from the standard product categories. As a consequence, the output and trade in these products cannot be traced by national statistics. Despite the rapid growth in international demand for certified wood products, until recently only relatively small areas of forest lands in Canada have been certified as being sustainably managed forest lands. As a result, only very limited quantities of certified wood products have been produced and marketed.

The demand for certified products has been driven largely in the export markets, particularly in parts of Europe and more recently in the US where there is increased interest by retailers for certified products. Several major

North American retailers, which together represent about 25 percent of lumber sold in North America, have recently announced that they will give preference to certified wood products.

During the past year, forest product companies in all regions of Canada have been actively implementing one of the four certification systems used in Canada. The Canadian Standards Association (CSA) reports that as of September 2000, over 21.5 million hectares of forest land have been certified following independent third-party audits. This land area represents almost 33 million cubic metres, or nearly one-fifth of Canada's annual forest harvest.

The Canadian Sustainable Forestry Certification Coalition anticipates that by the end of 2003 some 92 million hectares of forest land will be certified in Canada . While nearly all of this 95 million hectares of forest land will be certified through the ISO 14001 Environmental Management System Standard, an estimated 36.5 million hectares of the total will also will certified under the CSA Sustainable Forest Management Standard, 9.5 million hectares will be certified under the Sustainable Forestry Initiative standard and 5.5 million hectares under the Forest Stewardship Council. Canadian industry is also actively promoting the mutual recognition of different systems which use third party certification as a means of verifying compliance with one or more of the available standards.

Appendix

Statistics and Prospects

Figures for 2000 and 2001 are estimates

Sawn Softwood (000 Cubic Metres)

	1998	1999	2000	2001
Production	64,082	68,235	*65,500*	*64,000*
Stocks	7,669	8,015	*7,500*	*8,000*
Consumption	16,997	20,255	*18,615*	*17,750*
Imports	618	742	*750*	*700*
Exports to Europe	494	524	*550*	*550*
Export Total	47,176	48,376	*48,150*	*46,450*

Coniferous Logs (000 Cubic Metres)

	1998	1999	2000	2001
Imports	2,364	1,740	*2,500*	*2,000*
Export Total	1,045	1,874	*2,000*	*1,800*

Sawn Hardwood (000 Cubic Metres)

	1998	1999	2000	2001
Production	1,027	1,051	*1,000*	*1,000*
Stocks	125	143	*108*	*113*
Consumption	775	748	*2,010*	*1,910*
Imports	955	1,054	*1,150*	*1,100*
Exports to Europe	176	179	*175*	*185*
Export Total	1,178	1,339	*175*	*185*

Hardwood Logs (000 Cubic Metres)

	1998	1999	2000	2001
Imports	1,216	1,449	*1,500*	*1,450*
Export Total	231	274	*230*	*225*

Coniferous Plywood (000 Cubic Metres)

	1998	1999	2000	2001
Production	1,760	1,928	*1,800*	*1,800*
Stocks	73	68	*70*	*70*
Consumption	1,420	1,426	*1,313*	*1,225*
Imports	108	132	*125*	*125*
Exports to Europe	169	80	*110*	*130*

Export Total	456	639	*610*	*630*

Oriented Strandboard (OSB) (000 Cubic Metres)

	1998	1999	2000	2001
Production	6,304	7,694	*7,700*	*8,000*
Imports	59	84	*80*	*60*
Export Total	5,952	6,727	*6,800*	*7,000*

Particleboard (000 Cubic Metres)

	1998	1999	2000	2001
Production	2,347	2,436	*2,800*	*3,000*
Imports	242	258	*550*	*250*
Export Total	1,073	1,055	*1,250*	*1,200*

Fibreboard

Hardboard and Medium Density Fibreboard (000 Cubic Metres)

	1998	1999	2000	2001
Production	824	1,029	*1,100*	*1,150*
Consumption	178	143	*185*	*175*
Imports	127	132	*135*	*125*
Export Total	773	1,018	*1,050*	*1,100*

Non-Compressed Fibreboard (000 Cubic Metres)

	1998	1999	2000	2001
Production	450	460	*460*	*460*
Consumption	382	392.4	*380*	*380*
Imports	42	61.4	*50*	*50*
Export Total	110	129	*130*	*130*

Pulpwood Exports (000 Cubic Metres)

	1998	1999	2000	2001
Total Exports	182	43	*50*	*50*

Pulp Chip Exports (000 Cubic Metres)

	1998	1999	2000	2001
US	1,035	735	*740*	*600*
Japan	557	522	*775*	*750*

Export Total	1,590	1,259	*1,515*	*1,350*

Source: Industry Canada based on Statistics Canada data, 2000