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PRESS RELEASE

BC Interior "Mountain Pine Beetle Attack" Report profiles how a new sawlog reality will change the BC sawmilling sector, but an improving lumber business cycle looks very good for all remaining BC mills "after the beetle"

Report's initial press release generates major North American debate but with various and opposing interpretations

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The response from the initial press release summarizing some of the highlights and projections from the recently published report, ***BC Interior – Mountain Pine Beetle Attack***, has been exceptional but with numerous interpretations. As suspected, industry response has been to accept many of the assumptions and projections presented, as they are on the front line in dealing with the realities of processing dead trees in the forest and at sawmills. Non-industry groups and the media, however, may have misinterpreted some of the report's key findings, or have taken some results partly out of perspective. For others, seeing the first and complete independent analysis that works through a variety of logical assumptions with detailed projections has provided some clarity as well as a sobering perspective that includes a number of positive and negative aspects related to the mountain pine beetle (MPB) epidemic over the short, medium and long-term.

In the first comprehensive impact analysis of the mountain pine beetle's (MPB) devastation of the BC Interior forests and the blow to its current lumber industry, the report incorporates a number of critical timber supply and economic implications in a single base case scenario that the BC Interior industry will soon be facing. Based on a number of key, forward looking assumptions, the report's base case analysis combines traditional perspectives on the annual allowable cut determinations together with critical analysis on the economics of MPB timber utilization and market demand to predict the mid to long-term impact on the BC lumber industry - <u>the bottom line being that there is a good news story for the remaining BC forest industry.</u>

To address some of the possible misinterpretations of the report's findings and to provide additional perspectives on one of the world's greatest environmental catastrophes – and in light of some of the questions that have been raised throughout British Columbia and other regions in the media <u>- the following four topics are further clarified</u>.

1. The Report indicates BC lumber production will fall significantly by the end of the decade – this is good news for all remaining mills as North America supply will be constrained.

- The report forecasts the MPB sawlog harvest to derive BC lumber production in relation to North America demand and the economics or positioning of other regional supply sources.
- With a declining supply of economic sawlogs, the base case scenario in the report predicts a peak in BC lumber production in the next 3-5 years.
- However, as stated in the report, new processing technology, higher by-product prices (from chips, wood pellets, bio-energy, etc.) or higher lumber prices could extend the shelf-life of the dead timber and lumber production incrementally during the forecast period,
- The <u>best case scenario</u> for BC lumber production at the end of the decade is near the distressed 2009 level of about nine billion bf – this compares to pre-beetle levels of about 10.5 billion bf and peak levels of almost 15 billion bf in 2005 (the report's <u>base case forecast</u> is slightly below the 2009 production levels by the end of the decade).
- With stronger US demand coupled with reduced lumber output forecast, higher prices are expected that should allow the remaining sawmills to be very profitable over the next decade!!

- **Net Outcome: the BC lumber industry will see a permanent downsizing by the end of decade but a lumber “supply gap” that should lift prices in North America will significantly benefit the remainder of the BC lumber industry.**

2. The Report forecasts that without the implementation of pro-active mitigation strategies, the sawlog timber harvest will drop by almost 20 million m3 from 2005 to 2018

- Simply put, 70+% of the pine trees in the B.C. Interior are forecast to be killed by the MPB and this will lead to reductions in both the AAC and sawlog availability.
- Sawmills and veneer plants can only use sawlogs and with the forecast 35+% decline in the available sawlog supply in the BC Interior (2005 base), or about 20 million m3 of sawlogs by 2018, mill closures are inevitable as forecast in the report.
- On a more positive note, dead trees that do not make sawlog grades could have other uses (wood chips for pulp, wood pellets, biomass energy, etc.), but these uses depend on the economics of harvesting and processing, commodity prices and government support related to green energy (e.g., as in Europe). Consequently, the total timber harvest could be higher.
- Public comments confirm that the decline projected for BC sawlogs in the authors’ report is reasonable based on the assumptions used – the wildcard is how quickly or slowly mill closures will occur.
- **Net Outcome: the base case forecast is for the BC Interior sawlog harvest to decline by approximately 35% by about 2018 from that seen in 2005. Alternatively, the harvest of biomass material could increase dramatically if new businesses can be established.**

3. Without improvements in the mid-term timber supply forecasts or higher end product prices, the Report indicates that 16 BC sawmills could eventually close

- In the Interior, there are 77 major sawmills and 13 veneer mills included in the forecast that were in operation in 2005. The average sawmill produces about 200 million bf (in the model, this varies from 15 to 600 million bf). In addition, there are a variety of smaller mills scattered throughout the Interior that also consume sawlogs that are included in the total modeled demand for sawlogs.
- Since the start of the North American market collapse in 2005, 12 BC Interior mills (lumber & plywood) have already closed and are assumed to remain so through the forecast planning horizon.
- From the report’s base case, 16 additional mills are projected to close by about 2018 (where three are currently not operating and are assumed to restart and then permanently close again) due to log shortages. This means that another 13 mills operating today could permanently close by about 2018 due to a lack of sawlogs as a result of the MPB.
- The 16 mills forecast to close represent the equivalent of 3.5 billion board feet of lumber (and veneer) production (an average of 225 million bf per mill) and a total of 11 million m3 of sawlog consumption annually.
- **Net Outcome: Based on the assumptions in the base case analysis, about 16 BC sawmills are forecast to close by about 2018. However, BC’s efficient sawmilling industry and infrastructure will remain intact and that could limit even more mill closures after 2018.**

4. The economics of MPB ‘Shelf-Life’ are a major variable to determining the future of harvesting MPB logs in BC

- In the report, specific assumptions are used to forecast the “shelf-life” of dead standing timber used in sawmills and veneer plants and to model the potential drop in sawlog availability – this is different than the overall AAC forecasts that are always higher than the sawlog forecast.
- MPB shelf-life varies by the type of growing site, tree diameter when killed and the moisture content of the site. The report assumes a different shelf life by area based on these variables, and in some cases allows for the shelf-life of dead timber to be extended beyond 20 years by assuming a 20% sawlog recovery in individual stands of trees (which normally would be uneconomic).
- The most critical variable to the longevity of MPB shelf-life is the economics of harvesting and cost of processing the logs. As a result, commodity forest product prices, including residual products, are a key variable to any harvest projections – this is identified and modeled in the report in great detail for sawlogs (the most valuable log in the forest).
- **Net Outcome: The timing or the shelf-life of dead MPB timber is tied to industry economics and commodity prices (as well as new uses for the fibre) that are unpredictable and are only indirectly related to the overall AAC projections.**

While there have been some pessimistic perceptions about the report circulated in the media, the reality of reduced sawlog harvests and lumber production was accepted long ago by the BC industry and most have a clear and well developed strategy to deal with the changes.

We are also entering a period of evolving global timber supply disruptions as the full impact of the global recession now shows a fractured forest products supply chain. These and other developments bode well for the BC lumber industry in the next decade, as those sawmills that remain are expected to do very well as a tighter supply and improved product prices in North America are forecast for much of the coming decade.

B.C Interior – Mountain Pine Beetle Attack: Impact & Outlook on B.C. Timber Availability & Wood Products Production is a strategic analysis that assesses the critical impact of the beetle attack on the key timber and wood products producing regions in B.C. The report is a result of the combined efforts of three B.C.-based consulting firms and four consultants:

- Jim Girvan (MDT Management Decision and Technology Ltd.);
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