



How Low are Hardwood Lumber Prices in Real Terms?

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Prices for grade hardwood lumber have remained stubbornly low for several years. But, just how low are lumber prices? While prices reported by Hardwood Market Report for #1C lumber in most Appalachian species have increased since the summer of 2009 low point, with the exception of yellow-poplar, they are 3 to 50 percent lower than they were in the fall of 2005. The species with the largest price declines include cherry, hard maple, soft maple, and red oak.

Hardwood lumber prices are somewhat unique in that the different species do not necessarily trend with one another. During the early, 1980s #1C red and white oak prices were trending upward, while hard maple and yellow-poplar prices were fairly constant. In the early 1990s, the prices of all species were increasing. Between 2000 and 2005, the price of #1C hard maple increased by 80 percent, while red oak prices decrease by 15 percent. These diverse price trends do not occur in the markets for softwood lumber and most other commodity groups, such as grain crops, base metals, and precious metals.

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- US construction expenditures for June advanced 0.4% from May and were 7.0% above the previous year. Private residential construction increased 1.3% for the month and was 12.1% higher than June 2011. Compared to one year earlier, single-family construction was up 18.6%, and multi-family construction grew 48.8%.
- The July Manufacturing ISM Report on Business® posted a PMI reading of 49.8%, the second straight monthly decline in the manufacturing sector. The overall economy grew for the 38th consecutive month.
- According to NAR®, the Pending Home Sales Index slipped 1.4% in June from May but was 9.5% higher than one year earlier.
- The May S&P/Case-Shiller 10- and 20-City Composite Indices were up 2.2% for the month, but the 10-City Index was off 1.0% and the 20-City Index was down 0.7% from May 2011.

Canada's Raw Material Price Index fell 4.0% in June from May and was down 11.7% from one year earlier. The Industrial Product Price Index was 0.4% higher than June 2011.

Real GDP in Canada advanced 0.1% in May over April and was 2.4% higher than the previous year.

Retail sales in China rose 13.7% in June 2012 from 2011 and were 14.4% above the same period last year.

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Because lumber prices of the various hardwood species do not necessarily move together, it is hard to pick out a single species that represents the market. Instead, a time-tested way to look at prices from a broad market perspective is to use a composite price. If we develop a composite price of all reported Appalachian species weighted by sawtimber volume in the region, we find this price peaked in the fall of 2004 and declined the next 19 quarters (57 months) before hitting its low point in the summer of 2009 (Fig. 1). This was a decline of 38 percent.

The decline in the composite price of hardwood lumber between 2004 and 2009 is unprecedented in recent history in both absolute and percentage terms (Fig. 1). Another unique aspect of the 2004 to 2009 period is that prices for all major species had double-digit percentage declines. While the composite price in the spring of 2012 was higher than the summer of 2009, it has been trending downward the last two years and currently is at levels proximate to the early 1990s.

The composite price in Figure 1 trended upward between 1967 and 2004 largely as the result of inflation. Anyone who has lived for at least 30 years remembers when postage stamps were one half of today's price, and anyone in their sixties remembers when stamps were 3 cents. In fact, in the last 45 years, prices of all commodities have increased by over 400 percent, even after removing the volatile fuel and food sectors.

When we adjust the composite #1C price for inflation (real price), we see a considerably different trend (Fig. 2). Most notable is a cyclical pattern with fairly well defined peaks and valleys. The technical peak for the real composite #1C price has been around \$500 per MBF and has been approached 3 times in the last 45 years. The technical valley or low point for the real composite price was around \$350 per MBF from 1970 to the early 1990s, but shifted upward to around \$425 per MBF from 1995 to 2004. The 2004 to 2009 price decline blew through the lower of these valleys, and the small increases in price in 2010 almost approached the level of valleys of 1970 to early 1990s.

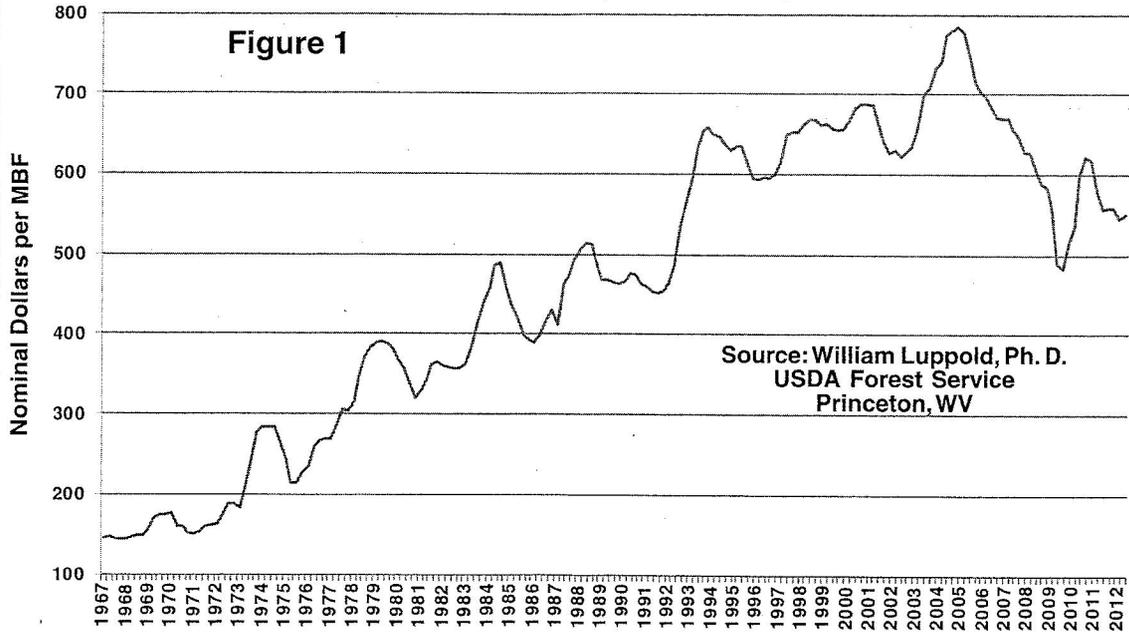
After adjusting for inflation, real composite price of #1C hit a high point in the spring of 2004 and then declined for 21 quarters (63 months) before hitting its low point in the summer of 2009 (Fig. 2). This was a decline of 47 percent. When we develop composite prices for FAS and #2A lumber, we find a 43 and 44 percent decline, respectively, during this period. Such downward movement in price of all grades and most species of hardwood lumber is indicative of structural change in the overall market, at least in the short run.

The decline in price for grade hardwood lumber after 2004 is primarily the result of reduced domestic demand for this material. Domestic demand for appearance grade lumber began to decline in 2000 after hitting a post WWII high in 1999. Initially, the decline was the result of reduced domestic production of wood household furniture, as imports from China, Vietnam, and other East Asian countries increased. This decline was partially offset by increased consumption for other appearance applications associated with home construction, including kitchen cabinet, hardwood flooring, and millwork. In 2006, new home construction started to decline, and by 2011, new single-family home construction was down 75 percent from 2005 high point. This series of events caused lumber used in appearance applications to also decline by 75 percent between 2005 and 2011. By contrast, lumber used in pallet production only declined 17 percent during this period, and crosstie production has remained constant.

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Composite Price in Nominal or Current Dollars for #1C Lumber of Appalachian Species

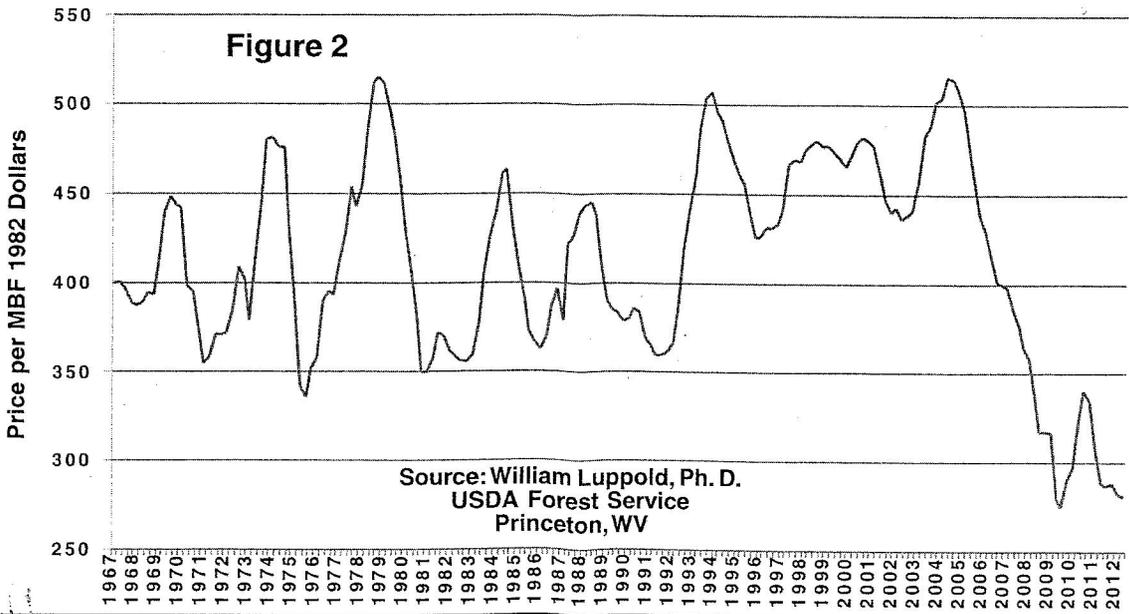
Figure 1



Source: William Luppold, Ph. D.
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Composite Price in Real or Constant Dollars for #1C Lumber of Appalachian Species

Figure 2



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The relatively high demand for pallet cants and crossties has distorted the hardwood market in terms of domestic consumption of graded appearance lumber versus industrial lumber. Between 1982 and 2005, industrial consumption accounted for between 40 and 45 percent of domestic hardwood lumber consumption. Since 2005, this percentage has been increasing, and in 2011, industrial consumption exceeded 75 percent of domestic consumption.

The short-term outlook for grade hardwood lumber consumption and price remains bleak, at least over the next year. New home construction remains low, but construction of higher priced luxury homes appears to be increasing. This bodes well for companies that supply lumber for high price cabinetry, millwork, and plank flooring, but these markets are relatively small. Construction of low- and mid-priced new homes will continued to be hampered by high down payments, increased loan requirements, and continued low rate of economic growth. Exports have been increasing in the last few years, but the potential for reduced economic growth in China and a looming recession in Euro Zone could reverse this trend.

The long-term outlook for grade hardwood lumber price is a somewhat better if the U.S. and world economies start to grow. Changes in the exchange rate for the U.S. Dollar against the Chinese Yuan could increase lumber exports for domestic consumption in China and reduce furniture imports. There also is a potential to develop new markets for semi-custom furniture based on the Amish model, and expand the use of hardwood lumber for home remodeling products. Still, it is hard to have a positive outlook on hardwood lumber markets given recent history and the current economic climate.