



Will U.S. Duties Cripple Canadian Lumber Stocks?

Description

On November 2, the United States Department of Commerce finalized its findings regarding imports of Canadian softwood lumber. It concluded that the imports are being unfairly subsidized and sold into the U.S. market at an unfair value.

Final duties on **Canfor Corporation** ([TSX:CFP](#)) will be 22%, and **West Fraser Timber Co. Ltd.** (TSX:WFT) will be subject to a 23% duty. In October, West Fraser CEO Edward Seraphim warned that the softwood lumber dispute could be a long-term and costly struggle. He stressed that the Canadian side will have to be patient and accused U.S. representatives of an unwillingness to negotiate an “effective” deal for both sides.

The tariffs will go into effect at the end of November. Meanwhile, NAFTA negotiations are ongoing and will be extended into 2018. Skepticism abounded following the most recent meetings in Washington, as the U.S. delegation laid out its demands. In the first round of negotiations in August, I [discussed the prospects for Canadian lumber stocks](#) after the U.S. made a formal demand for Chapter 19 resolutions to be scrapped.

In the fourth round, U.S. representatives called for an increase in regional automotive content from 62.5% to 85%. Another stipulation would see a clause that could trigger NAFTA renegotiations every five years. In an [October article](#), I focused on the tenuous predicament and the very real possibility of the Trump administration attempting to scuttle the trade agreement.

Leaving aside the prospects for the continuation of NAFTA, should investors be concerned about the future of Canadian lumber stocks? Investors do not have to look far back to see how tariffs can put tremendous strain on a stock. Shares of **Bombardier, Inc.** ([TSX:BBD.B](#)) threatened annual lows following duties imposed by the U.S. Department of Commerce, until the stock was resuscitated by a shock deal with European multinational Airbus SE.

In spite of the ongoing softwood lumber disputes, West Fraser Timber stock has climbed 67% in 2017 as of close on November 8 and 71% year over year. The company released its third-quarter results on October 23. West Fraser Timber posted sales of \$1.24 billion compared to \$1.15 billion in Q3 2016.

Adjusted earnings were up to \$150 million from \$115 million the previous year.

West Fraser Timber saw an expense of \$31 million in the third quarter due to the countervailing duty rate of 24.12% that was originally imposed effective April 28. The duties have resulted in expenses of \$65 million in the year to date. With the U.S. Department of Commerce now imposing a long-term duty, West Fraser Timber will be forced to prepare accordingly.

Canfor Corporation released its third-quarter results on October 20. Its net income was up to \$66.2 million from \$50.9 million in the third quarter of 2016. The company reported corporate costs of \$8.2 million in the quarter largely due to higher legal costs in relation to the expiry of the Softwood Lumber Agreement.

Canfor stock has climbed 70% in 2017 and 76% year over year.

After a tremendous 2017 for both stocks, investors should be cautious as we head closer to the beginning of 2018. NAFTA negotiations will conclude next year, and a long-term battle could shake lumber stocks for some time.

CATEGORY

1. Investing

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1. TSX:BBD.B (Bombardier)
2. TSX:CFP (Canfor Corporation)
3. TSX:WFG (West Fraser Timber Co. Ltd.)

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