



Is Now the Time to Bet on Timber Stocks?

Description

Investors who have dipped their toes in the Canadian lumber sector have certainly been a [bumpy ride](#). There are many questions as to [whether this volatility will remain](#). I'm in the camp that believes more volatility is indeed on the horizon, though not all to the downside.

The majority of products from Canadian timber manufacturers ends up in export markets, typically the United States. This has been the case ever since Canada's lumber industry was in its infancy. It will continue to be the case for at least the medium term.

Various Canadian companies have made efforts to diversify their exports to Europe and Asia, with mixed results. Shipping costs, logistics, and distribution are simply much more efficient and streamlined with U.S. partners, who have been doing this sort of trade for decades.

Canfor Corporation

This means the U.S. housing market (where the vast majority of Canadian lumber ends up) is the single biggest driver of demand for companies like **Canfor Corporation** ([TSX:CFP](#)). Therefore, a top priority for shareholders is determining which direction the U.S. housing market is headed. On this point, I've got a few thoughts that may be helpful for investors to consider.

First, interest rates are near all-time lows. With bond yields continuing to creep lower, pressure is being put on the U.S. Federal Reserve to cut rates further this year. Some estimates are now for two rate cuts in 2020. Should those rate cuts materialize, we could see interest rates drop further, adding more fuel to the fire.

Second, various metrics across the U.S. indicate that many of the hottest markets have gotten hotter of late, signalling momentum driven by a "fear of missing out".

The future of Canfor

Looking at this information alone, I'd say the outlook is broadly positive for lumber stocks right now. Of course, the same factors that may be driving this "melt up" in housing prices could also be signalling a recession is right around the corner. Lumber investors ought to remember just how bad things got last time around when deciding whether now is the right time to jump in with both feet.

Another tailwind for companies like Canfor is the new USMCA deal which is waiting to be ratified by Canada. In addition, if a new U.S. president gains power, they may remove or reduce the tariffs put in place by the Trump administration. Once settled, these factors will undoubtedly provide long-term security for investors in companies like Canfor. They may ensure profit margins and fundamentals will not be affected in the near-term or medium-term.

Bottom line

As for most commodities out there, I've been generally bearish on lumber in years past. I view a recession in 2020 as likely. I also can't see an end to tariffs and disputes over the land rights/upfront costs Canadian producers pay for their softwood lumber. However, with my concerns somewhat appeased due to the factors I've mentioned (improving housing market, decreasing interest rates, the new USMCA deal, and a potential new president), there is certainly a bull case to be made to invest in timber in 2020.

Stay Foolish my friends.

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1. canada
2. risk
3. timber

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