

## Commodities Gather Pace in August

### Base metals lead index to four-month high; September set for another rise

The **BMO Capital Markets Commodity Price Index** notched its second consecutive advance in August, picking up 2.2% as gains in crude oil and metals countered declines in gas and agricultural prices. The BMO Base Metals Index was catapulted to a 26-month high by a variety of factors, including improved global economic activity and anticipated supply constraints. The effects of the devastating Atlantic hurricane season are already being felt in the lumber market, but are expected to be relatively limited for oil & gas, given the lower weight of the Gulf of Mexico region in total U.S. energy production since the shale boom.

The **Oil & Gas Index** rose in August, driven by a 3.1% increase in the price of crude oil, though much of the monthly average gain reflected a strong advance in the latter half of July. WTI actually weakened from its July-end peak on concerns about rising supply from Libya and Nigeria. However, it has rallied so far in September on expectations that OPEC, Russia and other exporters may continue to curtail output after their agreement ends next March. Additionally, the IEA raised its forecast for demand growth in 2017. Natural gas softened in August but has been essentially range bound between US\$2.80-\$3.10/mmbtu since February.

The **Metals & Minerals Index** surged 4.7% in August, pushing the index to its highest level since May 2015. Nickel topped the leader board with a 14.5% gain – largely retracing earlier losses – while copper, aluminum and zinc also reached multi-year peaks. After two months of steadily rising gold and silver prices fueled by relentless U.S. dollar weakness, North Korean aggression and another ratcheting down of Fed rate hike expectations, the rally now appears to be losing steam. A further modest retrenchment is likely through the fall alongside a stabilization in the U.S. dollar.

The **Forest Products Index** nudged down 0.3% in August as lumber prices softened modestly ahead of the expiring of countervailing duties on August 25<sup>th</sup> (see feature on page 2). Prices firmed by month-end.

The **Agriculture Index** plunged 10.2% in August—its largest monthly decline since the Great Recession. In the crop space, concern about the supply impact of the Northern Plains drought faded rapidly during the month, which put crop prices back under withering pressure following a short-lived rally. In the livestock space, persistent signs of herd expansion have spurred another leg down in hog and cattle prices. The index is now only modestly above last year's decade-low.

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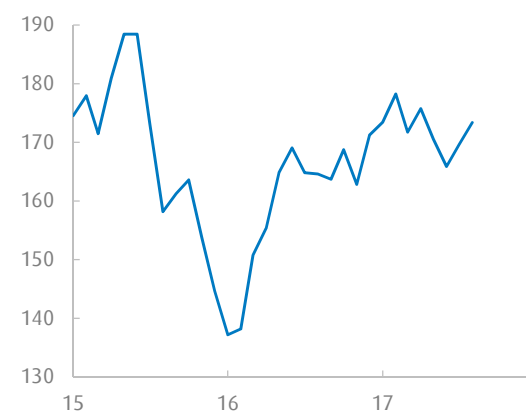
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**BMO CAPITAL MARKETS  
COMMODITY PRICE INDEX  
(2003 = 100)**

All Commodities Index



	Aug. Level (2003=100)	% Change from Mth. Ago	Yr. Ago
All Commodities	173.4	2.2	5.3
Oil & Gas	141.3	2.8	7.1
Metals & Minerals	254.6	4.7	2.3
Forest Products	147.6	-0.3	9.8
Agriculture	138.4	-10.2	7.0



## Commodity Focus: Forest Products

Cyclical Upswing Shows Few Signs of Slowing

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Although the shifting dynamics of the softwood trade dispute would normally signal that the lumber market is due for some moderation after a summer-time surge in pricing, unexpected supply- and demand-side factors will support robust prices in the medium term. Similarly, panel board prices, while quite lofty by historical standards, will be boosted by transitory factors and should generally remain strong.

Given the bombardment of NAFTA-related headlines, one could be forgiven for forgetting Canada's "other" trade deal, which is still very much in play. Re-negotiations of the expired Softwood Lumber Agreement have moved at a glacial pace after a "near deal" was seemingly on the cusp of being announced in early August. Canadian producers have since been given a bit of a reprieve as the countervailing duties (CVD) issued by the U.S. Commerce Department expired on August 25<sup>th</sup> after the mandated 120-day time limit passed. Those tariffs accounted for the bulk of the duty burden with rates averaging 20%, though they varied greatly by producer and region. Anti-dumping duties (AD) of 6.8% (on average) are still being applied.

In order for both CVD and AD tariffs to be enforced on a continuing basis, the U.S. Commerce Department must release their final CVD and AD tariffs and file their case with the International Trade Commission (ITC). The ITC then conducts a final injury determination within 45 days of the filing and sets any tariffs, if necessary, based on their findings. The ruling would be entered in the Federal Register within several days after which the tariffs, if any, would come into full effect. Key for lumber markets is when the Commerce Department's case is filed, as this determines the amount of time that Canadian producers can enjoy CVD-free access to the U.S. market (Chart 1). Originally, the process was to be very compact, with the Commerce Department targeting September 6<sup>th</sup> to file their case. This would have effectively left a small two-month window of CVD-free access. Canadian negotiators had petitioned for a fairly standard two-month extension for the case, which would have pushed the filing to December with an ultimate ruling by the ITC landing in January. Showing some rare goodwill (and quite possibly spooked by spiraling prices), the Commerce Department met in the middle and shifted its filing date to November 14<sup>th</sup>. This effectively moves the ITC's duty ruling to the end of December. It's probably no coincidence that this also corresponds with the Commerce Department's desire to wrap up NAFTA negotiations before the

CHART 1: SLA DISPUTE TIMELINE

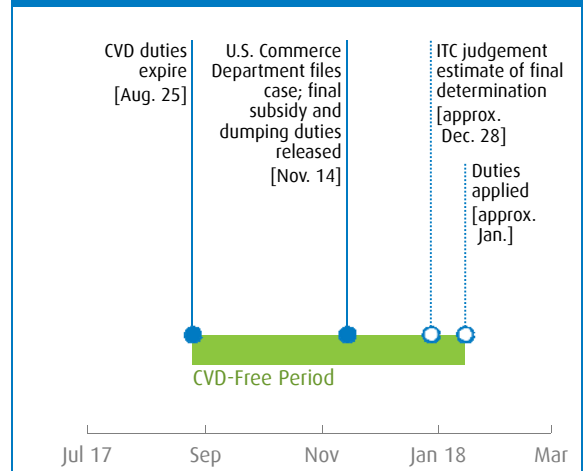


CHART 2: WOOD PRODUCT PRICES

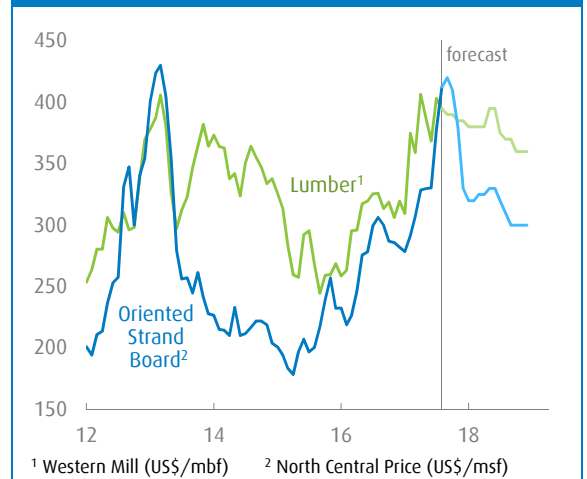
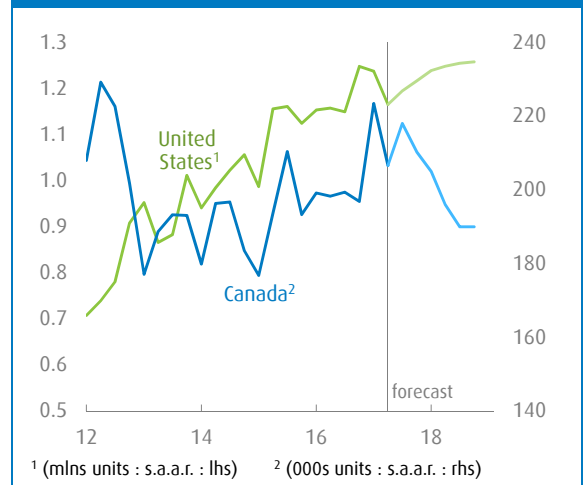


CHART 3: HOMEBUILDING



new year, as it would allow the necessary bandwidth for a new softwood lumber agreement (though this is hardly re-assuring given the U.S. Lumber Coalition's resistance and veto power). From a pricing perspective, this has extended the CVD-free period from roughly two months to four and, all else being equal, would result in a softening of prices.

However, unforeseen circumstances have upended wood product markets, giving the current rally a second wind. Unfortunately, these factors involve several tragic natural disasters: wildfires in B.C. have interrupted the supply of both lumber and oriented strand board, while the destruction caused by Hurricanes Harvey and Irma, with Maria close behind, will see a transitory boost in demand for wood products as reconstruction efforts take place.

These effects are already on display in the futures market, with Random Lengths Lumber Index Futures trending well above US\$380 for the next six months, quite high given most of this period falls under a CVD-free environment. Adjusting for inflation, this would mark the best run for lumber since the heady days of the mid-2000s housing boom. Forecasting beyond this period is confounded somewhat by the unresolved status of the softwood lumber dispute; a new agreement would see the CVD and AD tariffs nixed, but the proposed hard quotas would exert supply pressures on the U.S. market as more expensive imports would need to be relied upon (notoriously, Russian imports are up 48% year-to-date). Furthermore, there appears to be little incentive for sellers to dramatically reduce pricing given the market appears able to bear current valuations. Alternatively, a failure to reach an agreement would see the imposition of duties by the ITC in early 2018, a scenario that presents some upside risk. We believe Spruce-Pine-Fir prices should hover above US\$380/mbf through the rest of the year and average \$375 in 2018 (Chart 2). Longer-term, there appears to be little space for pricing to appreciate demonstrably as U.S. housing starts are likely to plateau at a 1.25 million-unit annualized pace, while increasing interest rates will place pressure on renovation activity (responsible for over 35% of final demand).

Somewhat lost in the shuffle is oriented strand board, which is not subject to tariffs. Prices have risen over 40% since the start of the year and that's even before accounting for the full transitory effect that hurricanes are likely to play on markets. Panel board markets in general have performed exceptionally well, so well in fact, that memories of 2013's epic rally (and fall) come to mind. While we're certainly not ones to fall into the "this time it's different" camp, there are several factors that support a more measured market re-balancing this time around. First, housing starts, at about 1.2 million units, are trending roughly 33% higher than they were then and, despite being on the softer side of industry predictions, are nevertheless showing resiliency at this level compared to the harsh false starts experienced in 2013 (Chart 3). Additionally, supply-side concerns aren't quite as acute this time around as only three idled mills are set to restart in the next few months, compared to the seven that came online during the last rally (capacity at the soon-to-be-opened mills is smaller as well). Given these factors, we are expecting prices to moderate back towards the market balance they had found in the summer (around the US\$330/msf range) before depreciating modestly to average \$315 in 2018 as capacity expansion is mostly met by a slight uptick in housing starts.

## Energy and Materials

		Crude Oil (WTI) US\$/bbl	Natural Gas (Henry Hub) US\$/mmbtu	(Alta. Express)	Lumber US\$/mbf	Pulp US\$/tonne	Newsprint
	2004	41.44	5.90	5.25	386	632	534
	2005	56.46	8.81	7.51	347	631	594
	2006	66.10	6.74	5.92	290	713	654
	2007	72.36	6.98	6.32	245	816	588
	2008	99.57	8.86	8.09	215	844	666
	2009	61.69	3.95	3.46	177	707	589
	2010	79.43	4.39	3.59	255	926	583
	2011	95.08	4.00	3.28	255	968	623
	2012	94.20	2.75	2.19	299	862	619
	2013	97.93	3.73	2.98	356	895	601
	2014	93.26	4.39	4.56	349	965	571
	2015	48.69	2.63	2.33	277	946	542
	2016	43.21	2.52	1.68	305	938	540
	y-t-d 2017	49.22	3.01	1.93	375	938	540
<b>2016</b>	September	45.20	2.99	2.07	314	938	540
	October	49.81	2.98	2.26	319	938	540
	November	45.73	2.55	1.94	306	938	540
	December	52.06	3.59	2.56	320	938	540
<b>2017</b>	January	52.56	3.30	2.17	310	938	540
	February	53.46	2.85	1.92	375	938	540
	March	49.48	2.88	1.90	359	938	540
	April	51.08	3.10	2.09	407	938	540
	May	48.51	3.15	2.14	388	938	540
	June	45.19	2.98	1.87	368	938	540
	July	46.61	2.98	2.05	403	938	540
	August	48.05	2.90	1.53	395	938	540
	m-t-d September	48.81	2.90	1.61	395	n.a.	n.a.
<b>Forecast</b>	2017 Avg.	<b>50.00</b>	<b>3.00</b>	<b>2.00</b>	<b>379</b> ↑	<b>938</b>	<b>537</b> ↑
	2018 Avg.	<b>55.00</b>	<b>3.25</b>	<b>2.55</b>	<b>375</b> ↑	<b>925</b>	<b>520</b>

Commodity price forecasts are by BMO Capital Markets Economics and are independent of those used by BMO Capital Markets Equity Research.

↑ and ↓ indicate annual forecast changes from last month.

## Base and Precious Metals

		Copper	Aluminum	Zinc	Nickel	Gold	Silver
		US\$/lb				US\$/oz	
	2004	1.30	0.78	0.48	6.27	409	6.65
	2005	1.67	0.86	0.63	6.69	445	7.31
	2006	3.05	1.17	1.48	11.00	605	11.58
	2007	3.23	1.20	1.47	16.89	697	13.40
	2008	3.15	1.17	0.85	9.57	872	15.01
	2009	2.34	0.75	0.75	6.64	973	14.67
	2010	3.42	0.99	0.98	9.89	1225	20.16
	2011	4.00	1.09	0.99	10.38	1570	35.11
	2012	3.61	0.92	0.88	7.96	1668	31.15
	2013	3.32	0.84	0.87	6.81	1411	23.83
	2014	3.11	0.85	0.98	7.65	1266	19.08
	2015	2.50	0.75	0.88	5.37	1160	15.70
	2016	2.21	0.73	0.95	4.35	1248	17.10
	y-t-d 2017	2.69	0.87	1.25	4.53	1249	17.18
<b>2016</b>	September	2.13	0.72	1.04	4.62	1327	19.28
	October	2.15	0.75	1.05	4.65	1269	17.72
	November	2.47	0.79	1.17	5.05	1240	17.48
	December	2.57	0.78	1.21	4.99	1153	16.37
<b>2017</b>	January	2.60	0.81	1.23	4.53	1193	16.85
	February	2.69	0.84	1.29	4.82	1233	17.88
	March	2.64	0.86	1.26	4.64	1231	17.61
	April	2.58	0.88	1.19	4.38	1267	18.08
	May	2.54	0.87	1.17	4.15	1245	16.76
	June	2.59	0.86	1.17	4.05	1261	16.96
	July	2.71	0.86	1.26	4.30	1235	16.16
	August	2.94	0.92	1.35	4.92	1282	16.90
	m-t-d September	3.03	0.94	1.40	5.29	1330	17.80
<b>Forecast</b>	2017 Avg.	<b>2.65</b> ↑	<b>0.87</b> ↑	<b>1.25</b> ↑	<b>4.55</b> ↑	<b>1255</b> ↑	<b>17.10</b> ↑
	2018 Avg.	<b>2.60</b>	<b>0.86</b>	<b>1.30</b>	<b>4.80</b>	<b>1280</b> ↑	<b>17.60</b> ↑

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## Agriculture

		Wheat	Canola	Cattle	Hogs
		US\$/bushel	US\$/tonne		US\$/cwt
	2004	3.46	271	n.a.	n.a.
	2005	3.19	224	87.34	68.58
	2006	4.02	257	86.23	64.08
	2007	6.38	378	93.92	65.56
	2008	7.98	527	93.60	66.05
	2009	5.30	371	83.85	58.11
	2010	5.81	429	94.95	75.60
	2011	7.10	566	114.54	90.34
	2012	7.50	601	122.65	84.93
	2013	6.84	545	126.40	89.33
	2014	5.88	400	151.50	105.83
	2015	5.08	371	146.49	69.40
	2016	4.36	366	118.61	65.60
	y-t-d 2017	4.39	391	118.45	72.71
<b>2016</b>	September	3.91	354	104.66	56.02
	October	4.09	371	100.15	46.93
	November	4.03	382	106.63	48.12
	December	3.97	386	112.09	59.81
<b>2017</b>	January	4.24	383	118.07	65.57
	February	4.37	396	118.85	70.83
	March	4.27	382	118.66	67.92
	April	4.20	377	125.99	64.21
	May	4.30	382	124.69	75.12
	June	4.54	385	124.42	84.08
	July	5.04	419	115.15	86.65
	August	4.29	398	108.94	72.50
	m-t-d September	4.25	402	106.47	61.18
<b>Forecast</b>	2017 Avg.	<b>4.50</b> ↓	<b>395</b> ↑	<b>116.00</b> ↓	<b>69.00</b> ↓
	2018 Avg.	<b>5.20</b>	<b>420</b> ↑	<b>112.00</b> ↓	<b>67.00</b> ↓

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## Commodity Indices and Forecasts

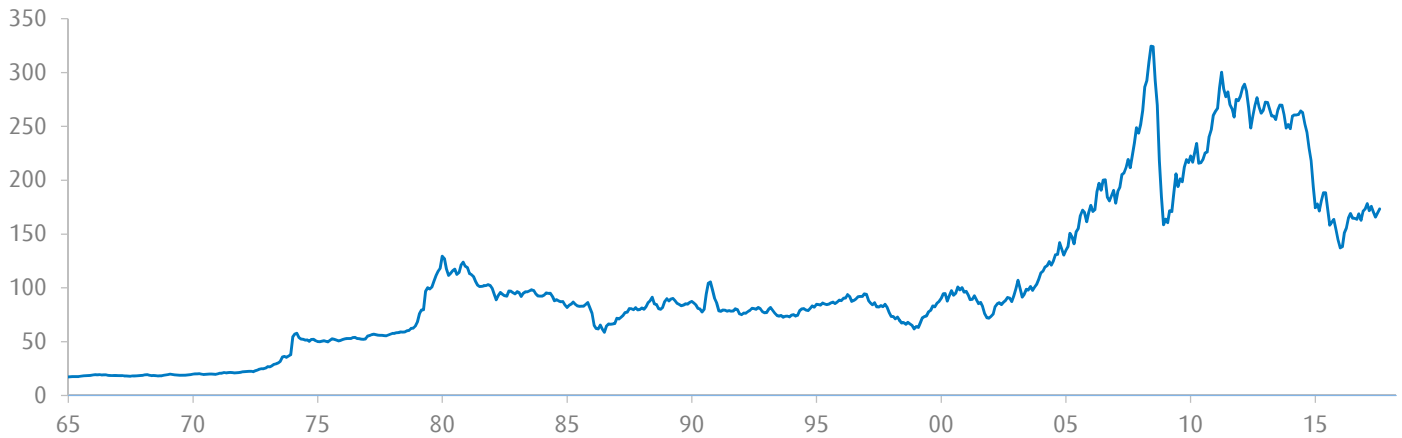
US\$-terms : 2003 = 100		All Commodities	Oil & Gas	Metals & Minerals	Forest Products	Agricultural Products	All Commodities C\$-terms
<b>Annual</b>							
	2008	264.9	299.5	287.2	113.5	208.5	198.8
	2009	191.8	182.0	267.1	97.1	145.2	155.5
	2010	229.1	232.7	291.0	122.3	163.4	168.4
	2011	275.5	275.6	364.8	125.6	205.3	194.5
	2012	271.0	270.3	353.8	128.1	216.9	193.3
	2013	262.8	283.0	300.6	139.4	200.1	193.1
	2014	246.3	271.4	272.2	138.8	170.0	193.9
	2015	169.7	142.5	245.2	125.6	151.3	154.4
	2016	159.3	126.9	239.0	130.3	135.9	150.5
Forecast	2017	<b>173.9</b>	<b>147.0</b>	<b>246.6</b>	<b>143.6</b>	<b>141.8</b>	<b>160.0</b>
	2018	<b>184.2</b>	<b>161.6</b>	<b>254.2</b>	<b>140.9</b>	<b>155.0</b>	<b>160.8</b>
<b>Quarterly</b>							
2015	Q4	154.0	122.4	228.9	123.7	143.7	146.7
2016	Q1	142.1	98.0	231.9	124.3	139.1	139.2
	Q2	163.1	132.3	239.5	131.2	145.4	150.1
	Q3	164.4	132.4	247.9	133.7	128.7	153.1
	Q4	167.6	144.9	236.7	132.2	130.5	159.7
2017	Q1	174.5	152.2	243.3	137.4	138.0	164.7
	Q2	170.7	142.3	244.4	144.4	139.2	164.0
Forecast	Q3	<b>173.1</b>	<b>140.7</b>	<b>253.1</b>	<b>147.5</b>	<b>144.0</b>	<b>154.6</b>
	Q4	<b>177.2</b>	<b>152.9</b>	<b>245.8</b>	<b>145.1</b>	<b>146.0</b>	<b>156.8</b>
2018	Q1	<b>180.1</b>	<b>159.2</b>	<b>244.7</b>	<b>141.8</b>	<b>151.3</b>	<b>159.7</b>
<b>Monthly</b>							
2016	Aug	164.6	131.9	249.0	134.4	129.4	152.6
	Sep	163.7	133.6	245.1	132.4	125.0	153.1
	Oct	168.8	146.4	238.1	132.9	128.9	159.5
	Nov	162.8	134.0	240.0	130.9	130.7	156.2
	Dec	171.3	154.2	232.0	132.9	131.8	163.3
2017	Jan	173.4	154.9	237.8	131.2	136.5	163.6
	Feb	178.3	156.4	246.6	141.4	140.7	166.7
	Mar	171.7	145.3	245.5	139.5	136.9	163.9
	Apr	175.7	150.3	247.5	147.2	136.0	168.5
	May	170.5	143.2	242.3	144.4	138.7	165.8
	Jun	165.9	133.5	243.4	141.5	143.0	157.7
	Jul	169.6	137.5	243.1	148.0	154.1	153.9
	Aug	173.4	141.3	254.6	147.6	138.4	156.2

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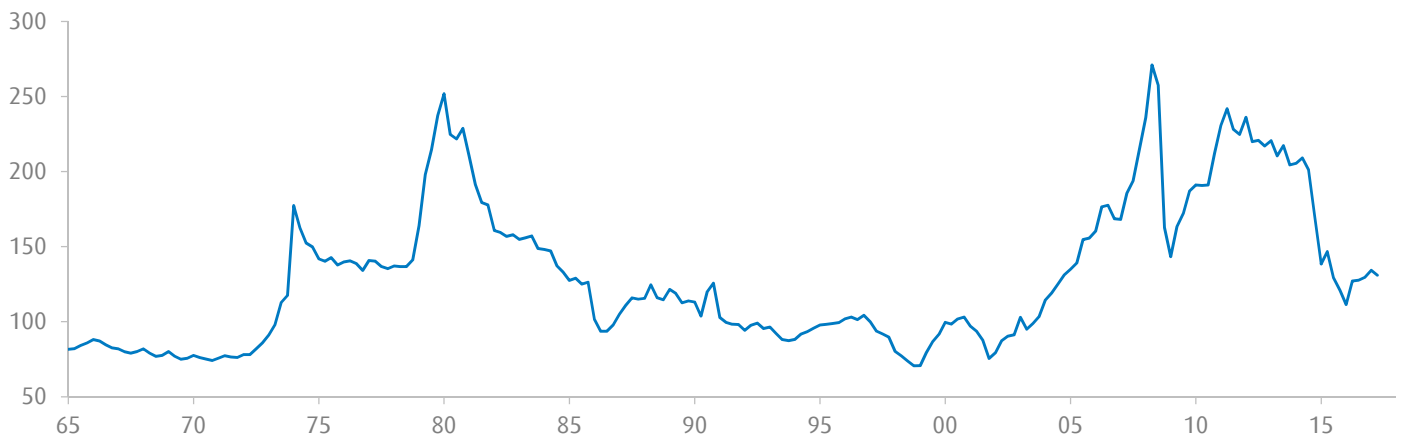


## Historical Charts: All-Commodity Index

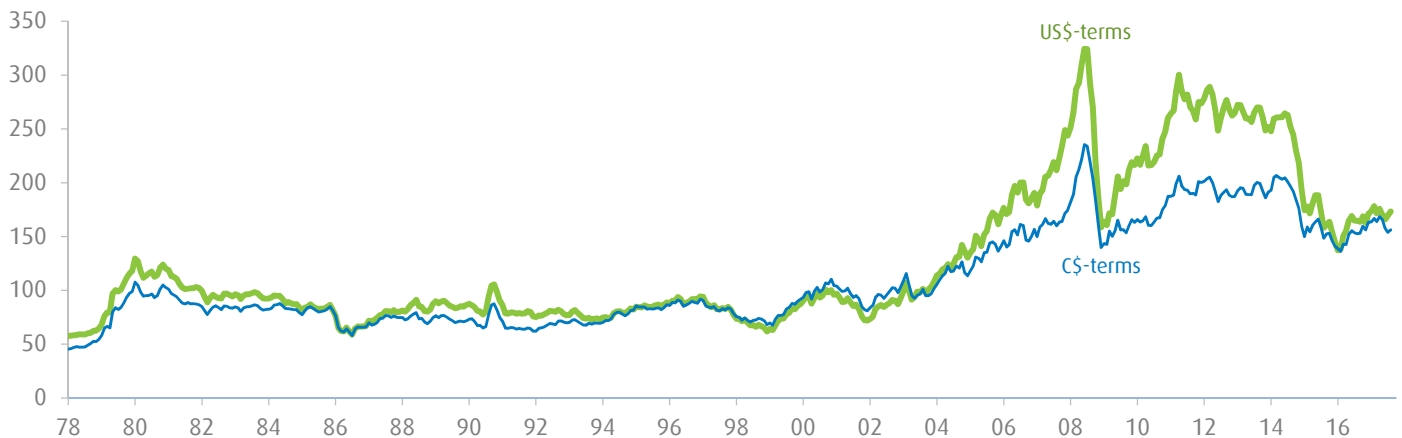
Nominal US\$-Terms (2003 = 100)



Real US\$-Terms (2003 = 100)



Nominal (2003 = 100)





## Technical Note

The BMO Capital Markets Commodity Price Index is a fixed-weight, export-based index that encompasses the price movement of 19 commodities key to Canadian exports. Weights are each commodity's average share of the total value of exports of the 19 commodities during the period 2012-16. Similarly, weights of sub-index components reflect the relative importance of commodities within their respective product group.

**The all-commodities index and sub-indices consist of the following:**

Percent	Weight in All-Commodities Index	Weight in Sub-Index		Weight in All-Commodities Index	Weight in Sub-Index
<b>Metals &amp; Minerals</b>	<b>27.8</b>	<b>100.0</b>	<b>Forest Products</b>	<b>12.6</b>	<b>100.0</b>
Gold	9.9	35.5	Newsprint	1.4	11.5
Silver	1.3	4.6	Market Pulp	3.8	30.5
Aluminum	5.9	21.4	Supercalendered Paper	1.2	9.8
Copper	2.2	7.8	Lumber	5.1	40.6
Nickel	3.0	10.8	OSB	1.0	7.6
Zinc	0.8	3.0			
Uranium	1.2	4.4	<b>Agricultural Products</b>	<b>8.5</b>	<b>100.0</b>
Potash	3.5	12.7	Wheat	4.2	49.5
			Canola	3.1	36.6
<b>Oil and Gas</b>	<b>51.1</b>	<b>100.0</b>	Hogs	0.3	3.0
Crude Oil	44.5	87.2	Beef Cattle	0.9	10.9
Canadian Natural Gas	6.5	12.8			
			<b>All Commodities</b>	<b>100.0</b>	

Unless otherwise specified, all indices reported in this publication correspond to prices in U.S. dollars.

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