Pulp and paper industry forecast for the next five years

JOHN C. EDWARDS

U.S. pulp and paper executives assess the industry's future in a global market.

The pulp and paper industry of the 1990s has witnessed considerable changes from the industry we knew a decade ago. Although hindsight is usually clear, our industry operated in a "business as usual" mode in the 1980s. Many companies were profitable, demand was reasonable, and environmental regulations were minimal. Today most companies fight to be profitable, and few can say the road ahead is smooth. Although most paper companies are optimistic about the future, each knows its optimism rests considerably on its creativity and its effectiveness in what is now a global market.

To get a firsthand glimpse at what lies ahead for the pulp and paper industry, *Tappi Journal* interviewed seven paper company executives: **Samuel Benedict**, president and COO, Mead Corp., Dayton, OH; **Patrick F. Brennan**, president, CEO, and COO, Consolidated Papers, Inc., Wisconsin Rapids, WI; **Bill Claypool**, VP, Paperboard Division, Sonoco Products Co., Hartsville, SC; **George J. Harad**, president and COO, Boise Cascade Corp., Boise, ID; **John R. Kennedy**, president and CEO, Federal Paper Board Co., Inc., Montvale, NJ; **Arnold M. Nemirow**, president and CEO, Wausau Paper Mills Co., Wausau, WI; and **Wesley Smith**, executive VP, Printing Papers, International Paper Co., Purchase, NY. We present their views knowing that many responses will be specific to each individual's company. However, it is these very responses that form a broader picture of what the industry can expect over the next several years.

Samuel Benedict
President and COO
Mead Corp.
Dayton, OH

With few exceptions, several trends are universal. Most respondents agree that a stronger U.S. and world economy is needed to turn around today's pulp and paper marketplace. All agree that we are now truly part of a global industry, subject to currency fluctuations and economic policies of countries outside our own. Finally, most of the executives we interviewed feel that government and political groups have overstepped their bounds in attempting to protect the environment. Most agree that air and water cleanup was necessary based on our status a decade ago. However, these same respondents fear that if stricter, and perhaps unnecessary, regulations continue to be enforced, our ability to compete on a global basis may be jeopardized.

The executives interviewed represent a wide range of the pulp and paper industry. It is their range of opinions that will help us forecast the industry as a whole over the next several years. We sincerely appreciate the time these individuals spent preparing for and participating in the interviews.

TJ: *Economic conditions have been tough for the industry as a whole during the past several years. What do you think is needed to improve that situation?*

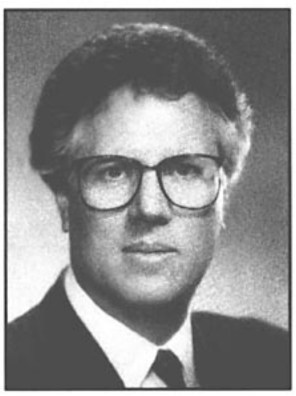
HARAD: In general, we need an economic growth accelerating faster than the 1–2% pace currently seen in the United States. In particular, this growth needs to affect job formation, especially in the grades we produce, e.g., office papers and newsprint.

NEMIROW: Global economic softness has hurt our industry, particularly because it has created overcapacity in many grades. This overcapacity can be helped by more focused use of capital as opposed to continuously building more and better machinery and mills.

SMITH: The worldwide economic picture must improve. Although we have seen some U.S. improvement, the European and Japanese markets have remained soft. We must strive for a balance

Patrick F. Brennan
President, CEO, and COO
Consolidated Papers, Inc.
Wisconsin Rapids, WI

Bill Claypool
VP, Paperboard Division
Sonoco Products Co.
Hartsville, SC



George J. Harad
President and COO
Boise Cascade Corp.
Boise, ID

John R. Kennedy
President and CEO
Federal Paper Board Co., Inc.
Montvale, NJ

of supply and demand on a global basis.

TJ: *How have recent economic conditions affected your capital investments and research efforts?*

BENEDICT: We have "stayed our course," keeping our capital investments in line with past years but focusing them more on improving product quality and cost-effective issues. Similarly, our research spending has remained relatively constant but again, we are focusing our research dollars on efficiency gains and quality improvements.

BRENNAN: Our capital investments have remained high. We just completed the heaviest capital investment program in our history, purchasing two new paper machines and making other investments totaling US$1 billion. Our research spending has remained constant throughout the recent past.

CLAYPOOL: We have slowed our capital investments and evaluated a corporate "affordability level" based on returns from these investments. In cutting some programs and delaying others, our capital spending is down about 20%. Our research efforts have been reduced by 40%.

NEMIROW: The state of our industry has had little impact on our capital spending. In part because of our strong cash flow, we have invested heavily in plants and equipment. For example, we recently purchased James River's Groveton, NH, mill to increase our capacity. We have also increased research spending, investing in new laboratories at our Rhinelander, WI, facility.

TJ: *What do you consider the greatest opportunity open to the industry in the next few years? What would be its greatest threat or challenge?*

BENEDICT: Although we currently are active in the European and Pacific Rim markets, we see new opportunities becoming available in Latin America. Our greatest threat is twofold: a slowdown in the world economy and how we handle environmental issues. It is important that environmental regulations and spending be done in a rational way without wasting capital on projects whose results are not measurable or those that do not have results.

BRENNAN: Our greatest opportunity would be the approval of a North American free trade zone, equalizing or eliminating tariffs between the United States, Canada, and Mexico. Our biggest threat may come from the evolution of the "electronic highway," in that people are reading less, watching more of the expanded cable TV market, and perhaps also ordering less catalogs because purchasing is becoming an option on certain cable channels.

HARAD: Because the U.S. pulp and paper industry remains competitive on a worldwide basis, we see opportunities in Latin American and Asian markets as their respective economies liberalize. Our greatest threats are the increasingly strict environmental regulations, often enacted by uninformed or misinformed individuals. Some proposed "nondetect" regulations are taking these laws too far and become disruptive to our business environment.

KENNEDY: I believe the U.S. paper industry is still relatively strong, but our greatest opportunity is in product improvement, i.e., improved quality and manufacturing efficiency. Our greatest challenge is dealing with environmental groups, having their own agendas and often misinforming the public. We in the industry have responded to most of their demands, but our activities seem to get less recognition than theirs in the media.

TJ: *The world has seen a lot of change in the last few years. What national and international events have most influenced the pulp and paper industry?*

CLAYPOOL: Worldwide exchange rates and their fluctuations have impacted us the most. Also, we become subject to the government policies of other countries. In Asia, particularly, many countries are building their own infrastructure around paper companies. As a result, our exports to Asia at some point will be reduced or eliminated.

HARAD: The major influence on our industry is the communications revolution. This revolution will create some new markets for various paper grades and will eliminate others. Growth in demand for specialty computer forms is one example of these changes.

KENNEDY: Although the European Economic Community did not blossom in 1992 as expected, its fundamentals are still in place and economic growth is bound to occur in this region. Developments in China and Southeast Asia are most positive for our industry, and we expect these areas will become large consumers.

SMITH: Our industry has rapidly become global, and a major influence on the industry has been the international economy. Specifically, currency devaluations in Finland and Sweden now permit them to be global, low-cost producers.

TJ: *Global competition seems likely to grow over the next five years. From where do you anticipate the strongest competition?*

HARAD: Our strongest competition will vary by grade, but those countries having a strong fiber base—Chile, Brazil, and South Africa—will be our biggest competitors.

KENNEDY: In addition to the reduction in Scandinavian wood and labor costs, currency devaluation has made market pulp from their mills strong U.S. competition. We must also be mindful of our tariff barriers in dealing with all overseas customers.

NEMIROW: The Eastern European paper industry (the former East Germany, Poland, and Russia) will emerge as a major force in our global economy, primarily because they have substantial natural resources. These developments may not be fully seen in five years but will surely emerge within 10 years.

SMITH: In addition to Sweden and Finland, who have profited from currency changes, countries with low wood and labor costs, and with fast-growing trees, will be successful. Specifically, we see Brazil, China, and Indonesia as strong global competitors.

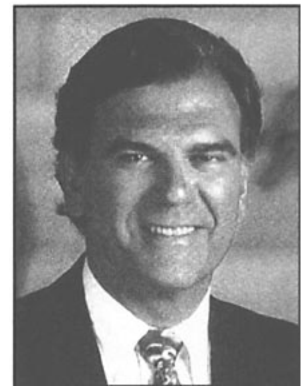
TJ: *What do U.S. companies need to do to remain competitive or become competitive in a global market? Are there specific regions or markets that you would consider "attractive?"*

BENEDICT: To remain competitive, we must maintain our customer focus and continue to strive for increased productivity. It is also important to appropriately spend our capital dollars. We see Europe, Latin America, and the Pacific Rim countries as the most attractive markets in the coming years.

BRENNAN: We must continue to increase our productivity without adding capacity. In the long term, I believe we will be the most viable pulp and paper manufacturing country. Regarding the issue of attractive markets, our coated papers are already in virtually every market. Our goal must be to maintain or grow these markets.

HARAD: We need to reinvest to keep our technology current. We must also handle our environmental issues in terms of fiber supply and air/effluent emissions. Our most attractive regions are Asia, which is fiber short, and China.

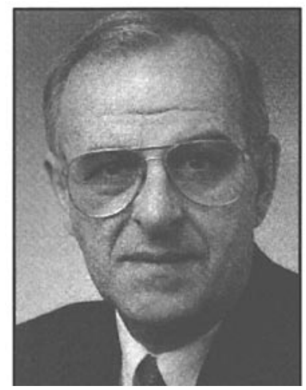
NEMIROW: Autonomy and decision-making must be conducted at the local or division level, especially in large companies. I believe decentralization within a company will be a key to its success. The Pacific Rim region will be the most attractive for us in the next five years. Its population is large and its economies are thriving.



Arnold M. Nemirow
President and CEO
Wausau Paper Mills Co.
Wausau, WI

TJ: *Environmental issues, such as dioxin, the spotted owl, wetlands, and recycling, have certainly had a major impact on the pulp and paper industry in recent years. Which of those issues has had the greatest impact on your business? What do you consider the most critical needs to comply with specific requirements in the next few years?*

BENEDICT: The chlorine issue (removal of dioxins) has had the greatest impact on Mead. We see no scientific basis for zero-chlorine processes. It is important to get this message to the right government regulators so that realistic environmental goals may be set.



Wesley Smith
Executive VP, Printing Papers
International Paper Co.
Purchase, NY

CLAYPOOL: Recycling has impacted us the most. We have been recycling for a long time, but the Clean Air and Clean Water Acts now dictate a large part of our recycling efforts. We will need to add air emission equipment and effluent cleanup systems to comply with ongoing stricter regulations.

KENNEDY: All of the above issues have affected our company. However, we feel the push for a totally chlorine-free pulping technology is unnecessary. It seems that the various environmental groups have their own agendas in this area and these agendas are often not based on solid scientific data.

SMITH: Dioxins and recycling have had the strongest impact on IP. Our request is that environmental regulations be defined farther into the future, because in many cases, our reaction times are necessarily long. These longer lead times would help us spend our environmental dollars more effectively.

TJ: *What do you anticipate will be the three most profitable grades for your company during 1994? What about the least profitable? How might these rankings change over the next five years?*

BRENNAN: Our most profitable grade is our No. 1 super premium coated paper, and we anticipate our No. 5 grade will also soon be strong for us. Coated grade Nos. 2 through 4 are generally the least profitable. In the next five years, we are optimistic that the No. 3 grade will firm up for us.

CLAYPOOL: The high-strength grades that we sell to converting operations are our most profitable grades. The chip grades are least profitable. I do not expect substantial ranking changes over the next five years.

HARAD: Our coated and uncoated freesheet and groundwood grades, i.e., writing and printing papers, will continue to improve our profitability. The pulp commodity grades are our most troublesome, and a slower profitability recovery is expected in these grades. I find it difficult to predict or rerank grades over the next several years.

SMITH: The profitability of most of our products is dictated in part by the economies of the countries in which we sell them. We see pulp remaining competitive longer than other grades/products due to major expansions in Indonesia and South America. Only a change in the current supply/demand balance will help the pulp market recover over the next few years. Specific country economies will have the most impact on our other grades in the foreseeable future.

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