Prospects for Europe

The U.S. paper industry seems to have imposed strict discipline on production and costs, and these measures are beginning to pay off. But much of European industry is still struggling with an ongoing recession.

By David Price

Although there are some fragile green shoots of revival sprouting in Europe, the underlying news is still depressing. Europe’s top 10 forest and paper companies posted overall losses of $670 million for the third quarter of 2009 — a figure slightly “better” than the loss in 3Q 2008. But they’re still bumping along the bottom. Eight of the ten said they had managed to improve their financial performance by improved supply and spending discipline. In plain language this means good housekeeping.

What’s Happening?

Basically, there is too much production for static or shrinking markets. A few analysts believe that Europe needs more permanent capacity closures; not just just mothballing of machines that could someday be brought back online.

However, a number of Finnish and Swedish pulp and paper mills have closed forever and more closures are on the way.

One German analyst shared my view about Norske Skog, a company I believe should no longer be making paper in Norway, its home base. It’s simply too expensive.

What’s needed in Europe, apparently, is more M&A and more closures, as happened in the U.S. One observer I spoke to is quite excited about U.S. prospects as he could see distinct signs of recovery.

Wood for Energy

But there is also a historic change underway in European industry — a change that takes the form of growing demand from energy companies who see forests, or woody biomass, as an important renewable energy source. Europe has been a leader in this technology so far, encouraged by EU renewable energy targets and generous financial support. Other regions and countries are also moving in this direction. Despite the economic recession, the one consistent trend in Europe has been a strong demand for energy derived from wood.

Competition will intensify as demand for traditional woodfiber-based products recovers. Conventional wood processing companies – pulp and paper manufacturers – are already adapting existing, or designing new technology, to develop this new business opportunity. For example, European mills producing graphics paper, which face serious decline in their market sector, may decide that wood energy could be a new or additional source of revenue.

It’s not an easy one to call. The traditional mill will have to rethink its assets and processes and mull over the prospect of growing, harvesting, and supplying woody biomass to produce clean heat and power. This move towards clean energy will include the production of transport fuels, which Stora Enso and Volvo are trialing in northern Sweden.

Value-added chemicals and other bioproducts are still in the design stage.

There is a planning application underway in Germany, as I write, to develop a market for deinked pulp linked to an energy-from-waste project. The initial phase will be completed by March.
Yet, all this R&D is expensive and there are serious doubts whether the forest products industry can afford it. So the deep-pocket partners will be the energy companies like Shell, BP, and possibly carmakers like Volkswagen and Mercedes Benz. Our own industry will bring a lot to the partnerships as it has long used woody biomass to generate its own energy. I can’t even guess, at this stage, how these partnerships will evolve, but they will happen.

Russia: Europe’s Enigma
Europeans tend to think of Russia as a European country, but most of it extends into Central Asia, the Far East, and ends at the Pacific. It has more forested land than anyone else, yet it still has only a modest presence in our industry.

Conversely, China, which has hardly any forests, has a massive presence in the market.

International Paper and Ilim are progressing in their cooperation, and there are pulp and paper projects in European Russia and the Far East, but the production will be for China.

Russia’s behavior towards its European customers hit a low spot two years ago when a wood export tax seriously upset its Scandinavian neighbors. The tax has been delayed and modified. But value-added wood products, and possibly wood energy, is where the money is for Russian exporters.

Before that sector can meet Western standards though, its forest code must be strengthened to clean up parts of the industry, foreign investors need to be reassured, and forest certification, which is almost invisible in current Russian forest audits, must be enforced and transparent. One consequence is that there will be a huge market for certification in Russia.

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