

Newsprint Price Gains Help Offset Continued Demand Shrinkage, Surging Costs



While 2007 was a bleak year overall, newsprint producers regained pricing power in late 2007 by masterfully managing supply by continuing to shutter high cost capacity. Despite a steady drop in consumption, newsprint prices have risen dramatically—\$180/tonne over nine months if the latest increase is enacted—and helped mills stay ahead of huge cost increases.

By Harold Cody

In mid-2007 it would have been tough to write a column on the newsprint market and find anything good to say. Every major market indicator was negative. The US newsprint market was tilted substantially in the favor of buyers as an excess of tonnage was looking hard for a home while demand was plunging and prices falling. The U.S. economy and American consumers were struggling with a weak economy along with uncertainty brought on by the sub-prime mortgage mess and dramatically higher gas costs.

In turn, newspaper publishers were cutting consumption to lower costs in the face of a rapid fall off in advertising revenues due to substantial declines in classified (job and real estate) and other advertising. For example, Gannett reported 2007 domestic newspaper advertising revenues off by over 9% and Q1 revenues down 11%. Analysts project newspaper advertising overall to fall about 10% this year due to the slumping economy.

Fast forward to the hot summer months of 2008 and the picture looks significantly different due to a big turn in one key indicator. Revenues and, most importantly, margins on newsprint sales are surging due to a series of price increases that if fully enacted in 3rd quarter 2008 will have brought newsprint prices up \$180 per tonne in just 9 months. This is a radical change given that newsprint prices had persistently

fallen from a cyclical peak set as recently as mid-2006 and were off peak levels by about 15% going into the fall of 2007.

Newsprint demand, however, wasn't better and for 2007 finished the full year down significantly. Consumption by daily newspapers—the bulk of consumption—was off by 10.8% vs. 2006 at 6.27 million tonnes, according to the Newspaper Association of America. Overall North American demand was 8.7 million tonnes, a 10% drop according to Pulp and Paper Products Council.



Give Producers a Hand

What was behind such a noteworthy turnaround? As has been the case for a long time, the mature newsprint business in North America is all about supply management. U.S. and Canadian mills learned long ago that due to changes in readership and shifts in advertising expenditures, U.S.

demand for newsprint was sinking. Thus, they have become experts at the tough game of shrinking supply. That's exactly to a large extent what occurred in the latter part of 2007 as supply curtailments finally caught up with the downturn in demand. This shifted the market from loose to tight and at times even a shortage situation, which subsequently rather quickly shifted pricing power back to the mills.

North American newsprint mills are now piling on the increases despite the howls of publishers, as they seek to right

their ships, which had been bleeding red ink in large part due to severe cost pressures. Producers pushed through a \$60/tonne increases in the first quarter of 2008 following on late 2007 gains and have announced another increase for the third quarter. The standard approach has been to split the increase into \$20 per month increments. Abitibi-Bowater has announced plans to remove 600,000 tons of newsprint in capacity, or 5% of North American capacity. This example underscores the industry's commitment to matching demand and supply.

The recent price gains are fundamentally necessary for survival as mills face intense cost pressures. The biggest – of many important ones – is the Canadian dollar, which has eased a bit from the mid-4Q peak of US\$1.10 to parity. Wow. What a change for Canadian mills when parity, which until recently was simply unheard of, is an improvement.

These financial struggles have also provided a shove to merger activity, culminating with two large ones, Abitibi-Bowater (concluded 3Q07) and White Birch's purchase of SP newsprint, making them the #2 player in North America.

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Can the Current Market Weather Further Turmoil?

With all of that said the outlook for the fall and into 2009 is looking up from where it was a few months ago, but certainly it's fraught with uncertainty. The big question really is whether the cur-

rent state of affairs can survive a more serious downturn. Well, it's possible we might see a bump up in consumption due to the elections and the Olympics, which historically help all advertising. But it may be just a blip at best. So far things are scary, as May consumption was down 16% and North American consumption through April was down 6.2% vs. 2007 levels.

Obviously, underlying weakness in the U.S. economy has yet to show signs of improvement and it continues to wobble on the edge of a recession. A full blown recession would decimate an already weak newspaper publishing business. On the bright side, the weak dollar has helped U.S. exports of newsprint and other products, which has been good for the economy.

On a global basis, newsprint demand is better and in fact world demand led by continued growth in areas such as Asia is up. In addition, European producers are doing their best to avoid a serious downturn, announcing that one million tonnes or a full 10% of newsprint capacity will be closed.

On balance, a more optimistic outlook is based on the belief that capacity consolidation gives producers a chance to manage supply such that pricing gains can be sustained. With three producers accounting for about three-quarters of North American supply in a post-merger world, they might just be able to sustain recent price gains and weather another in a long series of storms. While that is unfortunate for newspaper consumers, it's necessary for survival of the few mills and newsprint companies left. ■

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NORTH AMERICA NEWSPRINT STATISTICS				
December 2007. (000 metric tonnes)				
	CURRENT MONTH		YEAR-TO-DATE	
	2007	% CHG. 2007/2006	2007	% CHG. 2007/2006
Operating rate, %	90	94 (1)	93	94 (1)
Shipments to North America	708	-11.7	8,663	-9.8
Shipments to USA	625	-13.3	7,634	-10.5
Shipments to Canada	83	2.8	1,029	-4.2
Overseas exports	171	-25.6	2,406	7.3
Imports	6	13.0	82	-42.3
Total demand	714	-11.5	8,744	-10.3
Mill inventories	367	12.6	-	-
All US users inventories	705	-15.5	-	-
Days of supply - All US users	34	-12.8		

Actual figure, not a percentage change.
e=estimate. p=preliminary. n.a.=not available.
Source: Pulp and Paper Products Council

US Daily Newspaper Consumption, Inventory				
US dailies consumption	505	-19.3	6,266	-10.8
US publisher inventories	622 (p)	17.3	-	-
Days of supply - US dailies	37 (p)	2.8		

Actual figure, not a percentage change.
e=estimate. p=preliminary. n.a.=not available.
Source: Newspaper Assn. of America.