

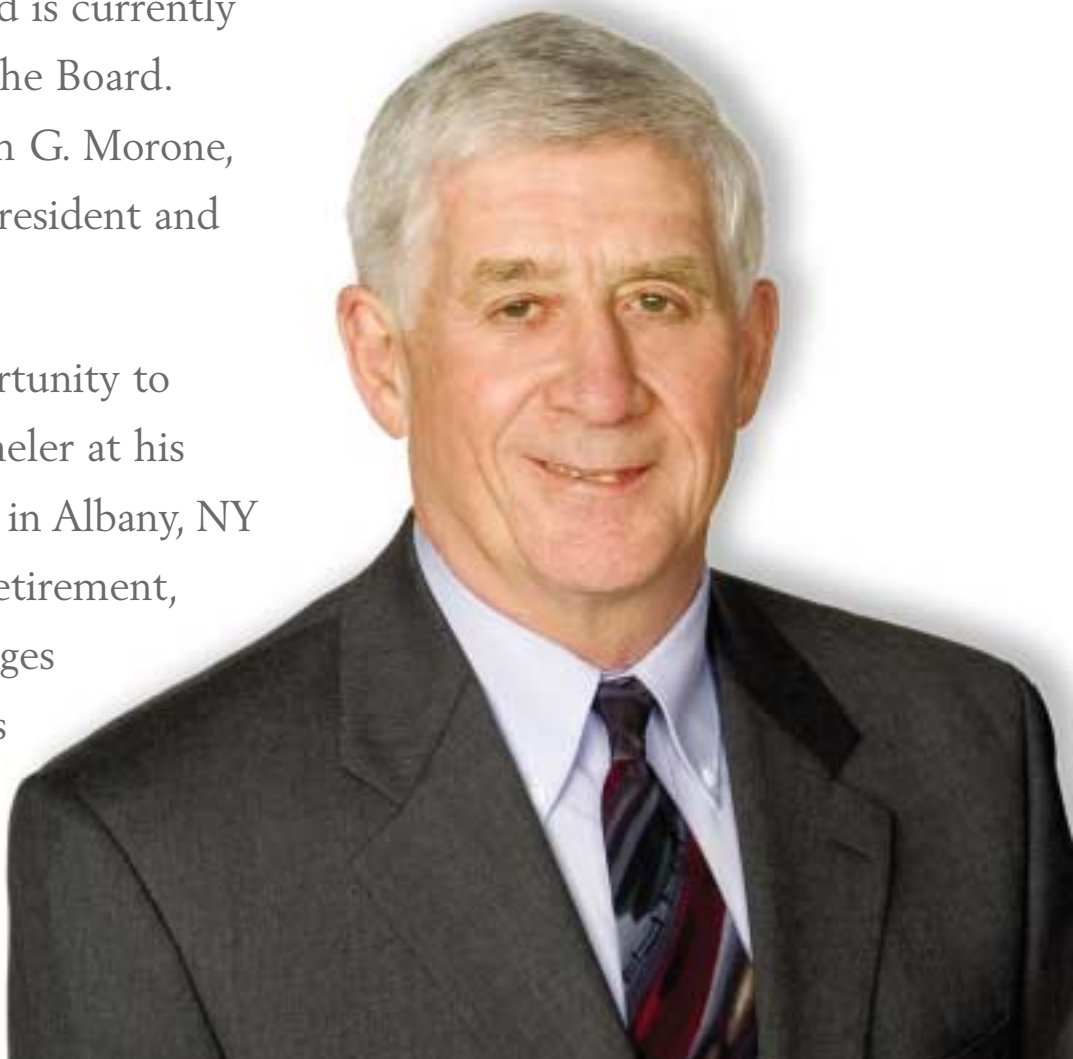
A Changing Landscape

It's not your grandfather's paper industry anymore.

By Jack O'Brien, editor in chief

*F*rank Schmeler has seen a lot take place in the pulp and paper industry during his 42-year career. He officially retired as CEO of Albany International on December 31, 2005, and is currently serving as chairman of the Board. His successor, Dr. Joseph G. Morone, now holds the title of president and chief executive.

PaperAge had the opportunity to sit down with Mr. Schmeler at his company's headquarters in Albany, NY on the occasion of his retirement, and talk about the changes taking place in what has truly become a global industry.



Give us some perspective from the time you entered the industry, some 42 years ago.

Back then papermaking was enjoying what we could now call the “good old days.” In the 1960s, paper companies were making healthy profits and were reinvesting in new machines and technology. The paper machinery builders kept making machines wider and faster. Increased demand supported increased capacity, not only in the U.S., but with massive exports going to Latin America and Asia.

Naturally, the paper machine clothing (PMC) industry grew as the paper makers prospered, and at the same time we saw many technological advances in paper machine clothing.

What technological change in PMC stands out in your mind?

Without a doubt, the introduction of synthetics. The change from metal wire literally transformed our industry. Metal wires lasted only three to four days on the machine. Wet felts made of wool were changed every week. During the 1960s when we changed to synthetics, our products began running thirty days. The PMC industry changed overnight, and investment in technology became critical. Today, PMC life is measured in months, not days.

The paper industry is a different animal now. Your thoughts?

I’m not sure if the industry could be any more different than it is now. The boom we saw in the 60s-70s couldn’t go on forever. The huge demand for paper settled down and consumption stayed close to GDP. In the late 90s, consolidation began and business became more difficult. Profits narrowed and paper companies were forced to merge or be taken over. Many outside factors put pressure on the industry, from the influx of electronic media to environmental mandates. The cost of making paper has soared, especially with increased energy costs, and demand in North America has flattened.

Today’s profitable paper machine is big and fast and includes shoe press technology for higher efficiencies. These new machines are both more cost-effective to operate and produce a better product. Unfortunately, with the rising cost of doing business in the United States, compared to manufacturing in other areas of the world, the American paper industry has been at a competitive disadvantage in some global markets.

Where do you see U.S. paper manufacturing headed?

Considering the most recent rounds of restructuring, it’s clear the industry is still trying to gain traction in balancing supply and demand and redefining itself. For those who remain here in the U.S. and are willing to reinvest, I believe there will be opportunity even though there is increased pressure from the investment community to deliver improved return on investment and cash flow.



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What is your view on China?

As you know, China is installing a substantial number of new paper machines. But paper makers in China face some of the same rising costs as we do, such as raw materials and energy. I also see the possibility that the Chinese will begin shopping for pulp and paper operations in North America.

How long has Albany been established in China?

Albany has been in China for more than ten years. We acquired an operation there in 1995 and just announced in January that we are expanding our existing dryer fabrics manufacturing plant and constructing a new forming and press plant. With the growing populations in nations such as China, there is a lot of speculation as to future markets. However, much of the region’s demand for paper products will depend on the rate of cultural change, and this is true for all developing nations.

What other regions do you see as growth areas?

Latin America certainly has room to grow—especially Brazil. Eastern Europe also has long-term potential. But again, the biggest region for growth is in Asia—China in particular. This isn’t a bad situation, unless China reaches a point where its capacity exceeds demand and the Chinese start exporting huge amounts of paper. With some of the



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most advanced paper machines in the world, we'd be facing some tough competition if that scenario was to take place. We are all hoping that China's internal demand will exceed supply, but only time will tell.

What about North America?

Growth in North America has slowed considerably. But keep in mind that right now the U.S. is still the largest consumer of paper and paperboard products in the world. It is an enormous market for paper manufacturers. I don't think anyone has written off the U.S. when it comes to the consumption and production of paper.

Like the paper manufacturers, industry suppliers are also faced with decisions about redeployment of capital. At Albany, what is one of the more important areas when it comes to capital investment?

In addition to capital investment for growth in China and Latin America, retooling our existing production facilities is something we have been adamant about. It's a big capital expenditure, but it's worth it in the long run. We have done this in conjunction with shutting down some older operations and machines, which is also a substantial expense. As a result, our existing operations are well-tooled and world class.

Currently, do you have an excess of capacity in the machine clothing business?

Because of restructuring over the last five years throughout the PMC industry, the supply and demand for PMC is

pretty much in balance. Could there be further consolidation in our industry? That will depend on what the paper makers do in the future. However, there's no doubt that growth is expected to continue in Asia, and local supply will be critical.

Where is the PMC business headed?

That's a good question, and I think there's a two-part answer. First, the future of paper machine clothing will depend on supplying world-class technology on a local basis. It's a matter of getting closer to the customer and right-sizing to meet customers' needs. An example of this is our expansion in Asia.

Second, the future success of our business lies in new technology and service. As you know, the paper industry has cut back drastically on technical people and R&D. However, the mills can't operate efficiently without technical know-how and will not prosper without R&D. It is in these service areas that we can play a vital role to the people who make the paper.

When the paper industry began to really tighten its belt about five years ago, PMC manufacturers were faced with customers shopping on price alone. What have you done to battle the bargain shopping?

About four years ago we created the Albany Value Concept (AVC) in an effort to stop "acquisition price" pressure, which was hurting us and our customers. The AVC program documents measurable economic benefits that our customers gain by using our products and process support in terms of reduced costs, improved paper products, and increased profitability. With AVC, our joint efforts in 2004 and 2005 identified millions in economic benefits for our customers globally.

Is it safe to say you've had a good run with Albany International?

You often hear the phrase "it's been a great ride" used by someone about to retire, and I suppose in some ways it's become a cliché. But when I think back over my career with the paper industry and Albany International, it has been just that. Yes, the paper industry has changed a lot, but what I am very proud of is that Albany International has also been able to change. And that's been critical to meet our customers' evolving needs. It wouldn't have been possible for us to do that without the people of Albany International and their focus on delivering value to our customers. I fully expect our management team, under the leadership of Joe Morone, will further expand our ability to deliver value to this industry. ■