

# Coated Freesheet Outlook Clouded by Import Issue



A surge of imports in 2006 led to lower shipments by domestic mills and some price slippage despite increased demand. Demand in 2007 is expected to be sluggish, but the impact of proposed duties on Asian paper imports make it particularly difficult to predict the direction of prices.

By Harold Cody

The coated free-sheet market in North America faces an unusual degree of uncertainty in 2007. Normal supply and demand factors will continue to determine in large part whether the market is weak or strong and in turn the direction of prices. This year however, a new factor—proposed duties on coated freesheet imports from Asia—will impact the market by altering the supply side of the equation. The question is to what degree they have an impact.

The bad news is that demand in 2007 is expected to at best be flat owing to a sluggish U.S. economy and the impact of a rise in U.S. postal rates. Both factors will suppress advertising and direct mail and in turn demand. In first quarter 2007, North American coated freesheet demand was down 5.4 % from the prior year and shipments and imports were off 3.9% and almost 10%, respectively. Thus some pull-back in imports may already be occurring.

North American coated freesheet demand posted a solid gain of 3.6% in 2006, reaching 4.4 million tons. This was the best gain posted by any printing and writing grade. Shipments fell by over 3% as imports jumped 24% to reach 1.6 million tons. In contrast, overall printing and writing paper demand rose just 0.1% in 2006. The import surge was mainly supplied by Chinese mills and was driven by a 2.5 million ton capacity increase (annualized basis) in China since 2005. Imports from China nearly doubled to over 300,000 tons last year (or even higher depending on the source of data used) and imports from Indonesia and Korea also rose. And a key factor is that this tonnage is produced on high volume, low cost machines, making it increasingly difficult for older, higher cost North American and European mills to compete, even at relatively high prices.

NORTH AMERICAN PRINTING/WRITING PAPER STATISTICS				
(000 tonnes)	December 2006	% change year ago	Year-to-date 2006	% change year ago
<b>COATED FREESHEET</b>				
Shipments	354	-3.6	4,379	-3.5
Operating rate	87	85 <sup>1</sup>	91	89 <sup>1</sup>
Imports	130	6.1	1,621	24.3
Demand	468	-1.7	5,792	3.6
<b>TOTAL PRINTING &amp; WRITING</b>				
Shipments	2,176	-2.8	27,316	-2.2
Operating rate	87	86 <sup>1</sup>	92	90 <sup>1</sup>
Imports	280	14.5	3,767	19.0
Demand	2,377	-1.3	30,143	0.1

1. Shipments/capacity. Actual figure, not a percentage change. Source: Pulp and Paper Products Council

## NORTH AMERICAN PRINTING/WRITING PAPER STATISTICS

(000 tonnes)	March 2007	% change year ago	Year-to-date 2007	% change year ago	
<b>COATED FREESHEET</b>					
Shipments	383	-7.7	1,117	-3.9	
Operating rate	94	97 <sup>1</sup>	95	93 <sup>1</sup>	
Imports	116	-19.8	345	-8.9	
Demand	480	-10.9	1,407	-5.4	
<b>MILL INVENTORIES</b>					
	March 2007	February 2007	March 2006	Tonne change from Month ago	% change from Year ago
Coated freesheet	620	602	614	18	6
Coated mechanical	309	300	270	9	38
<b>Total printing &amp; writing</b>	<b>2,546</b>	<b>2,489</b>	<b>2,231</b>	<b>57</b>	<b>315</b>

## Will Imports Drop Enough To Support Better Pricing?

The potentially good news—for mills—is that imposition of a special countervailing duty (CVD) on imports of coated freesheet from Asia that has been announced, specifically on paper from China and to a lesser degree Indonesia, will certainly have an impact on supply. It appears that the CVD on paper from Korea will only be minor and thus Korean imports could actually increase if those from the other Asian suppliers fall. In fact, as noted, imports have recently dropped some although it's not clear if the proposed CVD is the reason. In addition to the CVD, an even larger anti-dumping duty could also be imposed, but it's uncertain if this will occur.

A rising tide of imports in 2006 was certainly one reason for the slip in coated freesheet prices that occurred during the second half of the year and which halted a price run-up that had lasted for 2-3 years. The growing role of Asian coated paper on world markets was noted in our last coated freesheet column and thus the 2006 surge wasn't unexpected. Price slippage was also the result of overall weak markets in North America during the second half as well as an oversupply of coated freesheet globally—not just in Asia—and the weakness in coated groundwood markets where prices slipped considerably.

Domestic producers continue to do their best to manage supply to meet demand. In reaction to rising imports and to expectation of limited demand growth, additional U.S. capacity closures have been announced. European mills are also reacting to growing Asian capacity by trimming capacity,

although this is also in part due to a weakened competitive position for European mills owing to the strong Euro, which makes it difficult for European mills to ship paper profitably to the U.S. and other regions.

With demand in 2007 expected to post much smaller gains than in 2006, markets are likely to be considerably weaker and thus pricing could favor buyers. However, if imports decrease and North American producers continue to rationalize capacity the market will be more in balance. In turn, prices may actually recover, particularly in market

segments where imported paper is a more important factor, such as on the west coast. And costs continue to be a factor supporting pricing, with energy prices rebounding and fiber prices remaining high.

The bottom line is that it's difficult to assess the degree to which imports, and in turn pricing, will be impacted by an import duty. And while imports may decrease, Asian paper will certainly not completely disappear. If pricing improves, this also makes it easier for Asian producers to ship product to the U.S. even with the duty. And finally, the full impact of such duties may not occur until later in 2007, making it a tough year to forecast when and to what degree this action will have an impact. One likely track is that pricing remains a bit weak until mid-year when the impact of lower imports and reduced capacity allow producers to recover some pricing leverage, which will lead to improved pricing in the second half of the year. ■

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