



# Do Lower Stocks, Improved Demand Mark A Turn In The Pulp Market?

The pulp market may be headed in a new direction as demand improved and stocks fell during the third quarter. In turn, the change brought an end to the slip in prices that occurred over the summer. The current round of price increases has a good chance of succeeding, notably for NBSK, but continued sluggish demand coupled with upcoming capacity additions may make any gains tenuous.

By Harold M. Cody

**P**ulp markets have been the epitome of a cyclical commodity market over the last several quarters. Following a record run up in prices that began in early 2009 and ran for months, market pulp prices settled in at record levels and remained there for several months. NBSK, for example, hit \$1025/tonne late in 2010 and stayed near that level until early 2011. However, beginning in early to mid-2011 the market headed in the other direction.



**The biggest event on the horizon is the startup of Eldorado's 1.5 million tonne/year hardwood pulp mill in Brazil, which is on target for startup by the end of the year.**

As demand weakened and stocks rose prices fell steadily by over \$150/tonne before reaching a plateau in early 2012. Prices started to slip once again beginning in the spring and dropped modestly over the summer, but by the third quarter the market appears to have changed direction once again.

The unpredictable twists and turns followed by the pulp market have been driven by a global economy that has gone through a crisis in Europe and sluggish growth in the U.S. In turn, key pulp end uses such as printing and writing papers have continued to decline in the mature economies. Last year's fall in pulp prices was certainly aided by weak global demand for printing and writing grades, which along with tissue are the two major consumers of market pulp. European and North American demand slipped as U.S. economic weakness and the crisis in Europe undermined demand and advertising during the second half of 2011. And while emerging markets continue to expand, economic problems have also

dramatically slowed growth in areas such as Asia.

The slide continues as North American printing and writing paper demand is off by 7.5% through September 2012 according to the Pulp and Paper Products Council. Demand through nine months of the year was just over 15 million tonnes and North American shipments were down by a similar amount at 13.8 million tonnes. The largest decreases posted were for uncoated mechanical grades,

where demand was off by over 15%, but all major grades posted decreases in demand compared to prior year levels, and shipments were off by similar amounts. Similar declines occurred in Europe as well.

In contrast, the market for tissue continues to expand around the world, even in some mature economies, and world demand rose 3.3% last year. While global tissue growth may slow a bit, it is expected growth will remain at about 3% this year and continue solid growth next year.

## The Tide Turns

Beginning in late-summer and into September 2012 the pulp market began to shift. The impetus behind the change was stronger demand, seasonal factors, a decrease in mill inventories and the impact of reduced supply due to mill outages, including maintenance and unplanned shuts.

Improved demand during the third quarter was driven in part by increased buying by Chinese mills. Pulp shipments

to China are up nearly 18% year to date. Total pulp shipments during the quarter rose to 11 million metric tons, an increase of 5% and 4%, respectively, over prior quarter and prior year levels.

However, a decrease in pulp stocks in September was probably the major reason behind the recent market shift and subsequent upward movement in prices. Inventories had reached 37 days at the end of July. However, as market conditions improved due to higher shipments in August and September, pulp producer inventories dropped to 33 days of supply in September. This larger than normal drop in inventories had a big impact on the market. Stocks were down 325,000 tonnes to 3.9 million tonnes according to industry estimates. This is more than double the normal decline of about 125,000 tonnes.

Almost immediately producers moved to raise prices, which rose modestly in October, representing the first increase in several months. NBSK prices rose about \$20/tonne. And in late October, the major producers announced a second straight increase, with U.S. NBSK prices set to increase \$20/tonne on Nov. 1. As noted, pulp prices had fallen for three months as list prices dropped from a 2012 high of about \$900/tonne at the end of the second quarter. At this point, hardwood Kraft markets are generally more over supplied and pricing weaker, with discounts off of list prices varying by area and region. In contrast, the short term outlook for softwood grades is more positive and pricing better.

### New Capacity Looms on the Horizon

As noted, capacity changes have also been a factor recently but may be even more important over the next few months. Current downtime includes maintenance shuts and an unplanned shutdown of the Mackenzie NBSK mill in British Columbia. In addition, however, the Terrace Bay mill restarted in Ontario.

By the end of the year and in 2013 some major projects will come on line that could also have an impact. The biggest event on the horizon is the startup of Eldorado's 1.5 million tonne/year hardwood pulp mill in Brazil, which is on target for startup by the end of the year. Reportedly most of the output of bleached eucalyptus pulp is targeted for China but about 10% is expected to be sold to the U.S. market.

Market observers note that the drop in hardwood stocks wasn't as significant as for long fiber grades and many consider hardwood inventories to be well above a balanced market level. Thus, it may be that hardwood producers want to raise prices prior to the startup of the new Brazilian capac-

ity. The impact of this tonnage may be modest in the beginning but by sometime in the first quarter of next year the tonnage will really be hitting the market and that is likely to have more impact on hardwood eucalyptus markets.

Two major additional hardwood pulp projects will come online next year and add nearly 3 million additional tonnes of capacity. They are the Arauco/Stora mill in Uruguay and Suzano in Brazil. Several others are planned but not confirmed in Latin America. In addition, early next year Ilim's new 500,000 tpy Bratsk mill in Russia, a joint venture with International Paper, will start producing softwood pulp.

### Cycling Up or Going Down?

Boding well for future pulp demand is a rapid increase in production capacity for key pulp consuming grades in China, which will help to offset the continued decline in printing and writing paper demand in the large traditional markets of North America and Europe. China's tissue capacity is estimated to rise 2.4 by million tons and printing and writing paper by about 2 million tons by the end of next year.

Tissue capacity will also increase in North America, with a bulk of it online by early next year. The combination of new machines and upgrades to existing production lines will result in about 475,000 tons of new capacity, or about 5% of North American capacity.

A final ingredient to the mix that may help sustain price gains is exchange rates. The most notable has been the rise of the Canadian dollar, which hit \$1.03 in mid-September — the highest level in over a year. The Euro also hit a four month high in mid-September. The increases make the cost of producing pulp in those regions higher, which may have the effect of raising the floor on pricing.

While pulp prices have stabilized and have moved up on NBSK, the outlook remains cautious over the next few quarters. First, the sluggish economic outlook for the global economy, including continued uncertainty about Europe, will suppress printing and writing paper demand in most markets, and hold down growth in Asia. The surge of capacity is the other reason for caution as a major restart in Canada and significant new capacity in Russia and Latin America may put a damper on any upswing next year. If China pulls back on purchases, which would slow shipments and allow inventories to creep up, the uptick in the market could stall before it really gets started. So, we'll have to wait and see if the cycle is in fact swinging back up, or if recent gains were just a blip on the screen. ■

*Harold Cody is a contributing writer for PaperAge. He can be reached by email at: HCody@paperage.com.*