



# Pulp — A Tale of Two Markets

Hardwood pulp endures weak prices while softwood remains high as overall demand remains good.

By Harold M. Cody

So far 2014 has been a pretty good year for market pulp producers despite weak pricing that has plagued hardwood grades much of the year. However there are signs that even that problem might be turning in the favor of producers as an excess of hardwood supply appears to be coming more in balance with demand. A combination of higher shipments, strong pricing for softwood grades and modest cost increases for most major inputs, particularly recently, have resulted in improved sales and profits for many companies although results vary.

However, when you come down from the 30,000-foot view and dig deeper it's clear the market continues to have a split personality. If you're a softwood mill things have been quite good based on solid shipments and record list prices. In contrast, the last few quarters have been quite challenging for hardwood mills despite stronger shipment growth due to a supply glut leading to low operating rates and weak pricing.

Nevertheless, while the market is mixed the overall trend is positive at least according to one important measure. Global market pulp demand continues to expand, rising 3.2% last year over 2012 levels to about 55 million tonnes.



**September 2014 shipments of market pulp surged to 4.1 million tonnes, a big gain over the prior month, and brought year-to-date shipments up 1.5% over the first nine months of 2013.**

*Photo courtesy Metsa Fibre*

Through July 2014, pulp demand continued to expand — albeit more slowly — up a more modest 1% buoyed by a 4% increase in China but held back by flat demand in the U.S. and a 2% drop in Europe. Softwood demand was flat and operating rates were at 93% year to date. Hardwood pulp shipments rose 2%, but hardwood operating rates were only 88% vs. 90% in 2013.

The major markets for market pulp are Europe (29% of world demand); China (28%); North America (14%). In terms of grade, bleached eucalyptus

(BEK) accounts for 35% of shipments; benchmark northern bleached softwood kraft (NBSK), 26%; SBSK, 12% and NBHK, 8%.

## Long Term Challenges

Of course not everything is coming up roses. Major long term problems continue to challenge key customer segments. For example, major traditional uses for both softwood and hardwood pulp such as printing and writing papers continue to post steady declines in demand in the developed economies. Through the first three quarters of

2014, European demand for graphic papers is down 4% for magazine grades and 5% for newsprint, while fine paper (freesheet) demand is flat. European graphic paper demand fell 3% in the third quarter vs 2013 levels. Similarly, North American printing and writing paper demand for the first nine months of 2014 was off 4% vs prior year levels while shipments were down 5%.

### Temporary Uptick or Trend?

The good news is these declines continue to be offset by growth in Asia and most notably in China. And maybe even more importantly, demand by tissue grades — the other large use for market pulp — continues to expand globally and other specialty uses also continue to grow.

Most recently, at the end of the third quarter, the pulp market shifted direction in somewhat of a surprise according to observers. A combination of downtime, a seasonal pickup in demand from markets such as printing and writing mills that were looking to the fall printing season and a surge in shipments of pulp to China led to a 5-day drop in pulp stocks in September 2014. Overall producer inventories fell to 33 days of supply, driven by a plummet in hardwood stocks of 6 days coupled with a 2-day decrease in long fiber inventories.

September shipments surged to 4.1 million tonnes, a big gain over the prior month, and bringing year to date shipments up 1.5% over the first nine months of 2013. Shipments were led by a 2.9% surge in shipments to China and a 3.8% gain to other regions, but offset by flat (up 0.1%) shipments to Western Europe and a 1.1% decline in North America.

The sudden drop in hardwood levels may help underpin efforts to raise hardwood prices, which fell for several months during the summer, in particular for BEK. In addition, the drop in inventories overall may support NBSK where the list price of \$1030 has been under pressure by an increase in discounts and growing volume of pulp at low spot prices.

### Hardwood Capacity Hurt Prices

The weakness in hardwood prices has derived from the addition of nearly 3 million tonnes of bleached eucalyptus pulp (BEK) capacity over the last year alone. Offsetting this growth is the removal of nearly 600,000 tons of hardwood capacity via the closure of the Old Town pulp mill in Maine in August and the announced closure of the Ence mill in Spain. Major new capacity includes: 1.5 million tpy at the Eldorado mill in Brazil that came online in late 2012; the

Suzano mill in Brazil with a capacity of 1.4 million tpy in December 2013; and the 1.3 million tpy Montes del Plata mill in Uruguay that came online in June 2014. All three mills ship sizeable tonnage into both the U.S. and Western European market.

However, the pressure from this tonnage appeared to begin to ease a bit by late summer. Following on this, BEK producers set Oct. 1 as the date for a price increase, which was the first major effort to raise prices on BEK this year. Hardwood pulp prices have been so low that producers report they are having a hard time operating at current levels.

As noted, pulp prices have been on separate trajectories for some time. Softwood prices, owing to much tighter supply on a global basis, have been steadily rising since late 2012 when the benchmark price for NBSK bottomed out at under \$850/tonne. Since then NBSK prices rose steadily through last year and continued to rise before plateauing at a current list price of \$1030. In contrast, hardwood prices rose in the first half of 2013 before falling by about \$40/tonne from mid-2013 to the end of 2013 and the decline continued as prices drifted down for most of 2014. One development to note is the price differential between SBK and HBK, which has approached \$200/ton, leading industry observers to speculate that it will in effect begin to shift usage to the point that it will ultimately begin to narrow the difference. Historically SBK prices typically ran about \$75 to \$80/ton more than HBK. At current differentials, mills may consider shifting to more BHK despite the corresponding increase in chemical costs and lower machine efficiency that may result.

### Markets in Different Directions

While this mixed picture has been the story for most of 2014 there are indications that the two markets may be headed towards a bit of reconciliation. The hardwood markets appear to be a bit on the upswing while softwood markets, albeit starting at a very high point, are flat to drifting downwards a modest amount. If this were to occur, pulp mills could be in for a nice ride if the global economy expands and supports continued growth in Asia and avoids a major meltdown in the developed economies, most notably in Europe. As is often the case, the highly unpredictable nature of the pulp buying business in China will go a long way to determining which way the prevailing wind blows. And that's anybody's guess. ■

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