



Containerboard Mills Riding High, But Are Markets Stable Enough To Sustain Recent Strong Gains?

Painful capacity closures are now paying big dividends for liner and medium mills. High operating rates, higher costs, low inventories and improved box demand have led to a major price run-up in paperboard and box prices. But with markets more in balance the challenge for mills is to manage supply and thus inventories to avoid a subsequent falloff in prices late this year and into 2007.

By Harold Cody

Containerboard mills may not have got everything they wanted for Christmas last year, but since then, everything has been going their way in a big way. Most importantly, containerboard prices have surged to near record levels following an April increase in containerboard prices, the third successful increase since just last fall. The most recent increases have pushed linerboard and medium prices to their highest level since record peak price levels reached way back in 1995. Domestic prices are more than \$100/ton above late 2005 levels.

Looking back at 2005, containerboard mills fared reasonably well for much of the year, with demand rising modestly in line with continued strength in industrial production, which has risen steadily for the past two years. However, linerboard prices and demand were erratic in 2005, with prices dropping from \$450/ton to a low of \$390/ton as demand for boxes dwindled and then back up past \$400/ton. Costs also rose considerably, due to a huge surge in energy and transportation costs. But near

the end of the year, markets turned on a dime, and subsequently have improved dramatically. So what was it that caused things to get so good so fast?

Much Pain, Now Much Gain

Painful capacity reductions, which have been ongoing over a long period, are certainly a major reason for the current market strength, and in fact may be the most important overall factor behind the strong price gains. Integrated box makers, after closing

some additional linerboard and corrugated medium plants last year, are operating at almost full capacity. About 1.1 million tons of annual containerboard capacity, or 3% percent of production in North America, was shuttered by companies that just last year were struggling from too much competition, higher natural-gas prices and a slide in box prices.

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U.S. CONTAINERBOARD AND BOX STATISTICS

	Current Month May 2006	% change 2005/06	Year-to-date 2006	% change 2005/06
PAPERBOARD PRODUCTION ¹				
Unbleached kraft paperboard	2,024	5.4	9,602	3.2
Unbleached kraft linerboard	1,773	6.0	8,420	3.3
Semichemical paperboard	517	-6.3	2,590	-2.2
CONVERTED PRODUCT STATISTICS ²				
Corrugated box shipments (billion ft ²)	34.354	9.5	164.812	2.9
Containerboard inventories at mills/plants (actual)	2,385	-6.3	n.a.	n.a.
Exports of linerboard ³ April	240	-13.0	1,110	-2.8

Notes:
 1. American Forest & Paper Assn.
 2. Fibre Box Assn., AF&PA.
 3. U.S. Dept. of Commerce

extremely tight market was a sudden drop in box inventories, which fell to the lowest level in 11 years in late 2005 at about 2.2 million tons, based on statistics by the Fibre Box Association and the American Forest & Paper Association. Some inventory building, a surge in industrial production of food and other products, as well as weather related supply outages in the southern U.S. fueled the drop. With supplies short, mills were in the drivers' seat and began to aggressively push up prices. As of late summer, prices had surged to \$475 to \$500 per ton for 42-lb kraft linerboard, with semi-chemical corrugating medium prices running \$15 to \$25/ton less.

What really tipped the scales and launched a shift from a weak to an extremely tight market was a sudden drop in box inventories ...in late 2005.

Demand has also posted gains, as box cut-ups rose a modest amount in 2005 and through July 2006 are running 2.5% ahead of last year. Corrugated box shipments rose 0.2% in 2005 to 391.4 billion ft² from 2004, but still off by about 3.5% from the all-time high of 405.1 billion ft² level set in 1999. With domestic demand strong, linerboard exports are off about 3% through April 2006 vs. 2005.

Change in Direction?

Nevertheless, it now appears that the U.S. containerboard market is moving into more of a supply/demand balance following the tightness earlier this year and near shortage conditions in the fourth quarter of 2005. Inventories are still at relatively modest levels but have risen considerably above the floor of 2.2 million tons reached in late 2005.

U.S. corrugated box shipments in July declined 1.7% on an actual basis, but rose 3.5% (adjusted for one less shipping day in the current month), according to Fibre Box Assn. U.S. containerboard mills ran at 98.3% of capacity in July, bringing the year-to-date average to 97.1%.

Containerboard inventories at box plants and mills rose 162,000 tons in July from the previous month, with all of the increase at box plants. Inventories likely rose because of

2005 NORTH AMERICAN PACKAGING STATISTICS		
	2005	% change 2005/2004
CONTAINERBOARD		
Production	37,366	-1.7
Operating rate	93%	95%*
Shipments	37,415	-1.3
Demand ¹	34,450	-3.1
BOXBOARD		
Production	16,163	0.8
Operating rate	94%	92%*
Shipments	n.a.	n.a.
Demand ¹	14,341	0.9
KRAFT PAPERS		
Production	2,206	-3.7
Operating rate	89%	89%*
Shipments	2,208	-2.7
Demand ¹	2,311	-3.3

Notes:
n.a. = not available.
* Actual number.
1. Does not include export demand.
Source: Pulp and Paper Products Council (PPPC) and American Forest & Paper Association. (AFPA)

the high mill operating rates. Prices have also shown signs of peaking, a further indication that markets are shifting into a balanced condition.

It appears likely that markets will continue to favor producers into 2007. But if inventories rise significantly further, the large price gains could turn in the other direction and producers might be giving back some of the gains realized this year as 2007 goes forward. While this may occur, barring an unforeseen economic downturn, the industry appears able to steer this ship forward on a positive path, now that a massive wave of mill and machine closures have brought supply in balance with a smaller level of demand. ■

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