A REVIEW OF WORLD MARKETS

FROM OUR CORRESPONDENTS

CANADA: PACE SHOULD QUICKEN IN 2000

DEPENDING ON WHERE YOU WERE STANDING, Canada's pulp and paper industry had a fairly quiet year in 1999. With two major—and entertaining—exceptions, most companies went about their business concentrating on making money and getting out of the deep red hole they fell into in 1998. The two exceptions were MacMillan Bloedel Ltd. (MB) and Fletcher Challenge Canada Ltd. (FCCL), both British Columbia companies based in Vancouver and both much in the news as a result of takeover plans.

MB absorbed by Weyerhaeuser Canada

In MB's case, U.S.-based Weyerhaeuser Co. was doing the taking over in an all-stock offer for Canada's largest forest products company. There was some heart-rending complaint about BC's "heritage" falling into the hands of a U.S.-based owner. But Weyerhaeuser is hardly a new kid on the Canadian block. It began operations in this country in 1965 and has a reputation for good operational and management practices. Indeed, George H. Weyerhaeuser, Jr., the company's senior vice-president of technology, is the chairman of the board of the Pulp and Paper Research Institute of Canada (Paprican). He is also chairman of Weyerhaeuser Canada's board of directors and was formerly the company's president, so he knows the Canadian industry well.

Weyerhaeuser is the world's largest producer of market pulp, with a total capacity of some 2.3 million metric tons/year. Of its nine pulp mills, three are in Canada: in Kamloops, BC (456,000 metric tons/year); Prince Albert, SK (155,000 metric tons/year); and Grande Prairie, AB (155,000 metric tons/year). In October 1998, it bought the 345,000-metric ton/year fine paper mill in Dryden, ON, from Bowater, Inc.

Some MB shareholders, including the largest single shareholder at 8%, the Ontario teachers pension fund, opposed the takeover. The opposition was not on nationalistic (nor provincialistic) grounds but because they thought Weyerhaeuser's shares had fallen too far since the June 21 offering to make them any money. However, the takeover became final in November, and MB is to become a division of Weyerhaeuser Canada.

In 1998, MB's sales were CAD 4.18 (US$ 2.83) billion and it earned CAD 42 (US$ 28.4) million. It has been pulling away from the purely pulp and paper side of the business over the last few years, concentrating mainly on wood products. It still has paperboard packaging operations but they are all in Alabama.

A different script at FCCL

FCCL's situation was different: It was to be the buyer. In fact, it was to buy its parent company's CAD 5 (US$ 3.4) billion worth of pulp and paper assets, most of which are situated in the Asia–Pacific region. Fletcher Challenge Ltd. (FCL) is a diversified company based in New Zealand, and it owns 50.8% of FCCL, which was to pay CAD 3.6 (US$ 2.43) billion for the properties. The deal fell through in November, again because of a minority shareholder veto. They felt that FCCL was paying too much. Ironically, the New Zealand shareholders in FCL and its paper division, Fletcher Challenge Paper, had accepted the plan. While FCCL underwent a lengthy strike in 1998, it still had a healthy bottom line in its fiscal year, which ended June 30, and was (and still is) cash rich.

FCCL's board of directors resigned two days after the negative vote and a new management team stepped in. Alexander Toldte, a former consultant to the pulp and paper industry, replaced Robert Stewart as chairman of the board. Stewart and five other directors resigned after the deal's rejection.

The new president and CEO at FCCL is the well-respected Russ Horner, who started out as an engineer at the Elk Falls mill. He was then moved to New Zealand, where he put FC Paper's Australasian operations back in shape. *TAPPI JOURNAL* readers may remember Horner as a particularly effective chairman of the Technical Section, Canadian Pulp and Paper Association (now the Pulp and Paper Technical Association of Canada, or PAPTAC) in 1992–1993. The new three-member board is composed of Horner, Toldte, and MB's former CEO, Tom Stephens.

Capital spending down

The industry decided early on that it was not going to spend a lot of money on new equipment in 1999. In fact, capital equipment will likely account for the lowest pile of bills for five years. Capital spending was CAD 3036 (US$ 2052) million in 1994, CAD 5145 (US$ 3478) million in 1995, CAD 4731 (US$ 3198) million in 1996, CAD 3810 (US$ 2576) million in 1997, and CAD 2936 (US$ 1985) million in 1998.

According to Canadian Pulp and Paper Association statistics, the industry's 1998 sales totaled CAD 52.6 (US$ 35.6) billion and net earnings were CAD 432 (US$ 292) million. Some of this revenue came from a slumping Canadian dollar whose exchange rate averaged US$ 0.67, a benefit for exporters. Overall, cash flow from operations was CAD 4.5 (US$ 3.0) billion in 1998.

Pulp spending was down by CAD 60 (US$ 40.6) million to CAD 569 (US$ 385) million. Newsprint was only CAD 721 (US$ 487) million compared with CAD 1.4 (US$ 0.95) billion in 1997 as Stora Enso completed its CAD 750 (US$ 507) million project in Nova Scotia.

Support from U.S. industry

The Canadian industry has fought vigorously against the U.S. softwood quota. Drilling holes or adding notches to two-by-fours and their like to upgrade them from ordinary lumber was met with a U.S. Customs ruling that it was still just softwood lumber and therefore fell within the 14.7 billion FBM/year allowed in from British Columbia, Alberta, Ontario, and Quebec. Towards the end of 1999, several companies were shutting sawmills to avoid exceeding their quota share, which causes high penalties to kick in.

This business isn't going to go away—on either side. Meanwhile, BC is helping its lumber manufacturers to promote their points of view, which tend to be against managed trade for lumber. The Quebec lumber manufacturers are also pressing for an end to the quota. Naturally, the U.S. lumber industry wants to keep it.

However, U.S. house builders are now voicing concerns. In November, the National Lumber and Building Materials Association and the National Association of Home Builders said they wanted an end to the quotas. They said that the deal has raised prices on new homes in the United States by between US$ 1000 and US$2000, and lumber supply is not responding to demand. Moreover, builders are shifting to alternatives such as aluminum and plastic, so the forest products industry on both sides of the border will feel the effects because some builders will stay with the new materials.

Why should Canadian pulp and paper mills worry about softwood lumber? It's all a matter of the bottom line. Many Canadian companies have extensive lumber operations as well as paper operations, and lumber often supports paper. The pulp and paper sectors are the most finely balanced when it comes to markets and demand. The flutter of the butterfly's wings in the Brazilian jungle and its effect on global weather is as nothing when the paper markets in Asia get a hiccup.

Paprican research goes international

One of the really interesting things that's transpired recently is the move by Paprican to offer its scientific research services outside Canada. Until recently, the Institute's mandate has been sacrosanct: "For Canada's industry only." With a CAD 36 (US$ 24.3)-million budget, Paprican describes itself as "an independent, precompetitive research organization." It is the principal source of research for the industry from its laboratories in Pointe Claire, QC, and Vancouver, BC.

Two years ago, the Institute decided to terminate its longstanding joint membership policy with the Canadian Pulp and Paper Association, and its board has given it a global mandate to support the business and technology needs of its members, wherever their mills may be. In short, Paprican says it is "open for business with new vigor." Thus Joseph Wright, Paprican's president and CEO, is spending a lot of his time on the road promoting the benefits of being a member company of the organization, which will celebrate its 75th anniversary in 2000. As well, Paprican is actively marketing its existing products and services and has appointed Ron Crotogino as its marketing manager.

This program is directed not just at Canadian companies—not all are Paprican members—but also at U.S. companies. This is not to say that there are no U.S. influences among the existing members. Bowater, F.F. Soucy, Fort James-Marathon, Fraser Papers, Louisiana-Pacific, Repap, and St. Anne-Nackawic are all U.S. based. And of course, the previously mentioned Weyerhaeuser connection obtains.

Members pay a fee on a per-ton basis (metric ton). According to Wright, U.S. companies would pay a maximum net cost of some US$ 1 per metric ton after various allowances are factored into the bill. Associate membership is also available to member companies' mills situated outside the member's home country and Canada. Associates pay lower fees but also get fewer services. Paprican also offers contract research, but only to member companies.

The Institute has recently upgraded its pilot plants with a new paper machine and improved bleaching and pulping facilities. There are also pilot-scale facilities for high-intensity drying, calendering, and coating.

Among the technologies Paprican is promoting are an adaptive controller that has saved Tembec more than CAD 100,000 (US$ 67,597) per year in lime mud addition. There is also the Fiber Quality Analyzer, an alkali sensor, a control loop monitor, a felt permeability tester, and a variety of other systems or devices that can improve the quality of pulp and paper and increase manufacturing efficiency. One of its services is boiler air flow optimization, which involves no capital cost and can increase recovery boiler capacity by 5%–20%. Most of the hardware is sold by licensed agents.

Overall, 1999 will probably go down as a "not-bad" year for Canada's pulp and paper makers, and 2000 promises to be slow but steady. At the time this article was written (mid-November 1999), a strike hit BC's ports. Other than giving a huge boost to revenues at ports in the U.S. Northwest, the long-term effects cannot be foreseen, but the strike will certainly slice into the year's forest products results.

— Peter N. Williamson is a freelance writer based in Hudson, QC. He has covered the Canadian pulp and paper industry for many years

LATIN AMERICA: MILD OPTIMISM DESPITE EXCHANGE RATES

There are strong indicators that the world economy may grow more intensively in the year 2000. The International Monetary Fund (IMF) is expecting 3.5% growth in response to revitalization in important countries such as Japan and the Asian tigers. However, the vigor and uniformity of this projected growth depends largely on the uncertain trends in the American economy. Nevertheless, market prices for pulp and paper are expected to increase, which will be a relief after three years of depressed markets, low prices, and shrinking profit margins. Unfortunately, these improvements are not expected to reach the Latin American countries with the same intensity. Most of the countries in this part of the world are facing external accounts difficulties involving exchange rates, which will affect the overall Latin American economy. Brazil and Argentina are particularly sensitive to these economic forces.

Brazil

Early in 1999, Brazil changed its economic model, which was based on a strong currency (the "real"). Since 1994, the country's economic policy had placed the Brazilian currency at an artificial exchange rate level. The real was overvalued, which had a profound effect on the export-oriented Brazilian pulp and paper industry. Despite sustained and successful efforts to increase production efficiency and cut costs, production costs were still high in terms of dollars. On the other side, incomes remained low because of the depressed markets and the conversion of sales to the Brazilian currency. The nation's economic model was gradually reducing the competitiveness of its usually robust pulp and paper industry. At the same time, conditions in the international market provided a strong incentive to increase paper imports, since products made abroad (mainly in Asia) were considered low priced in the domestic market because of the artificial exchange rates.

This situation changed dramatically in early 1999, when the Brazilian government decided to allow the exchange rate to be naturally adjusted with "moderate freedom." The sudden 50% devaluation of the real (more than expected) restored the competitiveness of the pulp and paper industry along with other exporting industries. At the same time, it protected the domestic market from invasion by low-priced imports. The recovery received an additional boost by a slight increase in market pulp prices in mid-1999.

The mood in the industry has perked up noticeably, and modernization and debottlenecking projects are being actively implemented. For example, Aracruz, Klabin, and Riocell have all announced new production plans thanks to upgrades in their mills. Nevertheless, there is still an air of caution regarding future investment within the industry. Proposed greenfield mills (Celmar, Veracell, Champion) are awaiting green lights, although their prospects appear brighter in the current economic climate. There is also speculation about mergers and takeovers as the industry continues its trend toward consolidation. In a year as turbulent as 1999, the growth in pulp and paper production is expected to be small compared with growth rates posted in recent years. Larger projects to increase production capacity for pulp and paper are being postponed until the new millennium.

Argentina

Brazil's mood of optimism in the face of better prices and a favorable exchange rate is not evident in Argentina. Since the "peso" is still tied to the dollar, according to the country's economic policy, the Brazilian devaluation brought a big turmoil in the Argentinean markets. In a matter of hours, Brazilian products became very attractive as imports, including wood and paper products. These disturbances are leading to delicate negotiations as the two Latin American giants attempt to work out this issue without destroying the umbrella afforded by the Mercosul trade agreement. There is no doubt that a country with 36 million inhabitants and a GDP of US$ 330 billion is a very attractive market. This has been borne out by the flow of foreign capital—via acquisition or alliances within the Argentinean pulp and paper industry—from several sources in recent years. Such activities are a strong indication of potential growth in the short term. Indeed, the Argentinean pulp and paper industry is showing signs of improvement in the form of debottlenecking projects and upgrades. Protisa is adding a second tissue machine in Zarate; Kimberly Clark & Klabin are growing their tissue market share; Alto Parana is debottlenecking to raise its long-fiber market-pulp capacity. Papel Misionero is upgrading a paper machine and its unbleached kraft pulp line to increase production of kraft liner and kraft sack paper.

Chile

Chile, the other South American giant, also suffered through the depressed wood-products market and the Asian crisis. Chile, of course, has a natural road to the Asian markets via the Pacific Ocean. With the crisis in Japan, Korea, and the other tigers, prices for wood products went down as demand dropped. However, the Chilean industry was very creative in searching for alternative markets and developing new products. Since mid-1999, total exports in dollars have reached the same level as they were before the crisis, thanks largely to increases in production volume. Projections through the year 2000 are optimistic. Mills are upgrading and gradually increasing capacity. New greenfield mills are still in negotiations (e.g., Arauco Valdivia), awaiting the go ahead signal.

After some difficult times, the year 1999 may prove to be a turning point for South American producers of pulp and paper. The path to continued growth appears to be clear again.

— Celso Foelkel is a consultant at Celsius Degree, Porto Alegre, Brazil

Europe and Scandinavia: A year of consolidation

The year 1999 was a time of consolidation and marginal growth for the European paper industry, largely in line with the 2% increase in GDP (gross domestic product).

Slow growth

The current phase of slow growth started in mid-1998 after a spectacular first half that saw a 5% increase in paper and board output. Output fell dramatically in the second half, dropping the yearly increase to 2.3%. Nevertheless, 1998 saw a record output of 82 million metric tons—some 27% of world output, slightly behind North America's 34% and Asia's 29%.

The reasons for the slowdown are various, and there are marked differences from country to country. However, the stringent financial controls required in the run-up to European Monetary Union (EMU) seem to have played a significant role in many cases.

In the United Kingdom, which has not joined the EMU, five years of expansion were brought to an end by the strong British pound and a 7.5% increase in interest rates, designed to prevent the economy from overheating. Growth in GDP fell from 3.4% in the first quarter of 1998 to 1.6% in the fourth quarter, and UK manufacturing suffered consecutive quarterly reductions in output.

The outlook for 2000 and beyond is optimistic. In the short term, the "millennium effect" is expected to boost demand for printing, publishing, and packaging grades. Longer term, the Euro will play a positive role in the European economies, and EU expansion will increase the population of the single market by 28%. Some 13 new countries from Central and Eastern Europe and the Baltic could be members by 2010. They would add nearly 7% to papermaking capacity and just over 8% to pulp capacity.

The weak start of the Euro effected a 10% devaluation in the currencies of France and Germany, improving their trading positions while penalizing the UK, with its strong pound sterling. The Euro is showing signs of a recovery, and it is expected to reach parity with the U.S. dollar and become a major force for a strong European economy.

The profitability of European paper companies is improving slowly in spite of overcapacity and low prices in most sectors. This reflects the trend to consolidation, which brings economies of scale, synergies, and discipline in capital spending. There are four European countries in Pulp and Paper International's 1999 list of the Top 150:

- Stora Enso of Finland and Sweden: No. 2 after International Paper in terms of sales, but No. 1 in terms of tonnage
- UPM–Kymmene of Finland: No. 4
- SCA of Sweden: No. 7
- Arjo Wiggins Appleton (AWA) of the UK and France: No. 10

Consolidation

Consolidation is taking place along three main paths: regional, global, and product line.

Regional: Arjo Wiggins Appleton has restructured its carbonless, fine papers, and thermal divisions to improve efficiency and shareholder value. Carbonless production is now concentrated in four rather than five mills with the shutdown of the Cardiff mill in the UK and the switch of Guerimand mill in France to other grades. AWA remains No. 1 in the European carbonless market with production from Fort William and Dartford in the UK and Virginal and Nivelle in Belgium. The loss-making thermal division has been closed, and AWA's 13% share of the European thermal market is now being serviced from North America. In fine papers, the Buckland mill at Dover is being closed down, and production will be transferred to Stoneywood mill in Scotland during 2000. This will increase throughput at Stoneywood and enable it to run at full capacity. Some GBP 9 (US$ 4.4) million is earmarked for modernization.

This round of consolidation has boosted the value of AWA shares dramatically. Having fallen from GBP 3.15 (US$ 5.03) four years ago to GBP 0.93 (US$ 1.49) in the autumn of 1998, they are on the rise, up by GBP 0.18 (US$ 0.29) to GBP 1.63 (US$ 2.61) on news of the restructuring of the carbonless and thermal divisions, and up another GBP 0.16 (US$ 0.26) to GBP 1.94 (US$ 3.10) on the restructuring of the fine paper division, adding some GBP 134 (US$ 214) million to the company's market value.

In Finland, where consolidation is at its most advanced, three big groups dominate the pulp and paper industry: Stora Enso, Metsalitto, and UPM–Kymmene. These companies epitomize the trend to global and product line consolidation.

Global: In addition to two big UK mills—Shotton in North Wales and Caledonian in Scotland—UPM–Kymmene has three French and one German mill. It also owns Blandin Paper in the United States and has a 49% stake in Suzhou in China. Altogether, Finnish companies own 49 mills outside Finland: 42 in western Europe; four in North America; one in South America; and two in the Far East.

Product line: In the four years since the 1995 merger with Repcal, UPM–Kymmene has focused on printing papers and converting, which account for 57% and 20% of turnover, respectively, while divesting noncore activities such as board mills, hygiene materials, etc.

Swedish companies are moving in the same direction, and in early 1999, SCA and MoDo announced the merger of their fine paper businesses into what is now the No. 3 fine paper group in Europe, after Stora Enso and UPM–Kymmene.

SCA is consolidating into one of Europe's biggest groups in the hygiene and packaging sectors. In September

1999, SCA acquired AM Paper, a privately owned UK tissue group, and Panosa, the No. 4 tissue maker in Spain. The latter acquisition makes SCA the Spanish market leader, with a market share of 26%.

In the packaging field, SCA acquired the packaging division of Danisco—except for the UK division—in late 1999. The DKr 1.5 billion (US$ 203.9 million) acquisition includes the Danish, German, and Norwegian operations of Danisco Pack plus the Grenna recycling mill in Denmark, which produces packaging grades. Danisco is holding onto the UK division, comprising two mills and 33 converting plants, because the UK corrugated market is rising and they expected to get a better price in a year or so. In Ireland, SCA acquired Len-Pak, a privately owned packaging company that produces 9 million m^2 of corrugated board in two converting plants near Dublin and in Dundalk.

The trend to consolidation is expected spread to the specialty papermaking market, a highly fragmented sector characterized by small companies. In the fight for survival, the balance has been tipped against small UK mills by the strong British pound and rising costs. Indeed, nine mills have closed down in the last 18 months, including Glory, Silverton, and New Waterside.

One route to survival is acquisition by a large international player, e.g., the recent acquisition of Devon Valley Industries by Mead. However, it is getting more difficult to raise funds for management buyouts, since venture capitalists want a high rate of return, typically 30%–40% within a time scale of two to three years. In addition, it is difficult for venture capitalists to redeem their shares, since the exit option of flotation is now limited to the largest companies in the London stock market. Consequently, there has been "a flight to quality" in the city. Investors are more interested in big consolidated companies with the liquidity that gives the option of easily moving in or out of the investment.

Strategic alliances may offer a more realistic alternative for specialty companies. Such alliances would allow companies to form working relationships without a change in ownership. Stefan Kay, MD [?managing director?] of the Inveresk Group, notes that "the evolution of more focused investment banks, such as that recently set up by Jaakko Poyry, may allow funds and realism to work on companies and bring likely partners together into larger blocks." The specialty sector will need access to levels of capital that can support the inevitable restructuring (i.e., mill closures) that must occur if tolerable running rates and economies of scale are to be achieved.

— Margaret Marley is editor of Paper Technology

SCANDINAVIA

Sweden. Stora Enso is in the midst of major renovations at its Skutskär mill, which produces 520,000 metric tons of softwood and hardwood pulps annually. The mill has three separate fiber lines with Kamyr continuous digesters and oxygen bleaching. Among the ongoing projects is a new debarking drum, modification of the continuous digester to shorten it, and changing the bottom of the soda recovery plant. The work represents a total investment of approximately US$ 260 million and will be completed in 2000.

Stora Enso's Gruvön mill is building a new soda recovery plant at a cost of approximately US$ 100 million. The plant is scheduled for completion in April 2000.

One other major project in Sweden is a complete rebuild of the woodyard at Sodra Cell Mönsterås mill. The US$ 200-million project is expected to be completed before the end of the year. Sodra is also planning to expand production at the Mönsterås mill, increasing the capacity from 550,000 to 750,000 metric tons/year of TCF (totally chlorine free) bleached kraft pulp. The investment in the project will be approximately US$ 210 million.

AssiDomän Skärblacka is planning a major rebuild of three paper machines (PMs 7, 8, and 9). The mill is also replacing its electricity supply, upgrading the soda recovery plant, constructing a common R&D center and laboratory, rebuilding its effluent treatment plant, and replacing its wood-handling plant. Total investment is approximately US$ 153 million.

MoDo is planning major investments at its Hallsta and Husum mills. The Hallsta mill is upgrading two paper machines. PM 11 is getting a new winder and a new peroxide bleaching plant, and PM 3 will get a new forming section, new rewinder, new TMP refiner, and screening plant. Total investment at the mill will be approximately US$ 105 million. The Husum mill plans to rebuild PM 7 and build a new evaporation plant for a total investment of US$ 140 million.

Finland. Metsä-Botnia is rebuilding its Äänekoski pulp mill. The delignification line is being rebuilt, and two double diffusers will be installed. The biggest project in Finland is a new pulp line at Stora's Enso Imatra mill. The new line is replacing one that has been operating since the 1950s. Total investment will be approximately US$ 460 million.

In addition, UPM–Kymmene is rebuilding PM 1 at its Lohjan Paper mill, purchasing a new coater for its Voikka mill, and doing another rebuild at its Wisaforest pulp mill. A new two-stage oxygen delignification plant will be installed.

Norway. Peterson Linerboard has finished a major rebuild at their Moss mill. During 1998 and 1999, a total of US$ 75 million was invested in pulp washing equipment, a rebuild of the recycled fiber plant, and a total rebuild of their PM 5. The Beloit sack paper machine from 1965 has been rebuilt by Valmet to produce two-layered linerboard.

The major ongoing project in Norway is a 140,000-metric ton/year deinking plant at Norske Skog's Skogn newsprint mill. The investment of approximately US$ 65 million will be fulfilled during the first half year of 2000.

The major Norwegian project abroad has been the PM 2 at Norske Skog Golbey in France. The 350,000-metric ton/year machine was started up in May after an investment of approximately US$ 290 million. The mill's newsprint production capacity is now about 600,000 metric tons/year.

Optimism for the future

After three quarters, the results for the Nordic pulp and paper companies are generally quite good, and managers are optimistic for the year 2000. However, the big question is who is going to buy whom.

In Sweden, some type of deal between MoDo and SCA seems likely. Norway's biggest company in the industry, Norske Skog, is cooperating in Asia with Abitibi. The company also has mills in France, Austria, and the Czech Republic. The president and CEO, Jan Reinås, often talks about growing by merging. Of course there are no details available, but many analysts are expecting both Norske Skog and MoDo to make bold moves in the year 2000.

— Karl Gurandsrud is chief editor, Skog Industri, *in Oslo, Norway*

SOUTH AFRICA: POLITICAL STABILIZATION AND MODEST GROWTH

In South Africa, for a democratic election to be almost a "nonevent" is indeed an achievement. The country has weathered the retirement of Nelson Mandela and the inauguration of Thabo Mbeki with barely a ripple. On the money front, Tito Mboweni is the new governor of the Reserve Bank. Again hardly a ripple, and best of all, the country has maintained a tight fiscal policy. Prime lending rates are 10% below what they were a year ago during the height of the emerging market crisis. This is probably the most cheerful Christmas that South African consumers and papermakers will have experienced in a long while.

Growth projections are not marvelous, but they do exist. GDP data for the third quarter are expected to reflect growth of around 2.5%, and growth as a whole for 1999 will probably be close to 1%. Growth in 2000 is expected to increase to 3%–4%.

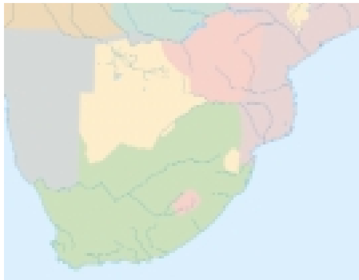
Forestry

Mondi Forests was granted Forest Stewardship Council accreditation for the 561,000 hectares of forests that it either owns or manages in South Africa. Sappi, in turn, has already implemented the ISO 14001 environmental management system. South Africa's forests are among the best managed in the world. A low light on this front, though, has been the tardiness of the privatization process of government-owned Safcol forests. While this issue continues to simmer, a number of originally interested overseas buyers have moved elsewhere. The partial privatization of the state forests is the largest transaction of its kind in the world, involving the long-term lease of about 500,000 hectares, of which about 330,000 hectares are planted. Yet, because of various difficulties, it remains to be seen whether suitable offers will be forthcoming.

Promulgation of new legislation is also set to try the forest products industry: the new water act for one and, more recently, the proposed land tax, which the Forest Owners Association says could cost the industry R 60 (US$ 1) million a year.

Company movement

Anglo American plc, owners of Mondi Ltd., listed on the London Stock Exchange in May 1999. The Forest Products division comprises Mondi International and Border Timbers. The division's 1998 turnover was US$ 2 billion, and operating profit was US$ 230 million. Mondi's focus is in two main sectors, packaging and graphic papers. In line with this strategy, they recently acquired Kohler Corrugated from Malbak for R 538 (US$ 89.7) million and subsequently sold two of its Mondipak corrugated packaging plants to satisfy a Competition Board recommendation.



Mondipak executive chairman Derrick Minnie said that "vertical integration is an international trend in line with the globalization of the markets in which we operate. Mondipak as it is now structured brings the Mondi group closer to the consumer in a business that has good dynamics and is less cyclical and less commodity driven."

Sappi, the world's largest producer of coated wood-free papers, is SA's most global company. About 87% of its sales of R 24 (US$ 4) billion were made outside of South Africa in the last financial year, and 67% of the products it sold were produced outside of the region. It is majority foreign owned (currently 53%, but Sappi is aiming for 65%), and 75% of its operating assets are in the United States and Europe. Liquidity in the share has increased five times since its U.S. listing.

In October, Sappi made an offer to buy out the minorities in Leykam Mürztale for US$ 92 million. It already owns 74% of the company. Shareholders approved the funding of this purchase in November through a US$ 200 million global equity offer. Sappi has also agreed in principle to acquire the minority interest in Swaziland-based Usutu Pulp. Eugene van As, executive chairman of Sappi, said that the timing of the equity raising was appropriate because prospects in the pulp and paper sectors were expected to improve.

Mill developments

Lignotech South Africa, a joint venture between Borregaard Industries Ltd. and Sappi, the world's largest producer of chemical cellulose pulp, was opened on March 29 at Sappi Saiccor. The plant cost R 110 (US$ 18.4) million. Lignosulfonate is no longer discharged into the sea as part of the mill's effluent via its marine pipeline. This has meant a reduction of solids content in the effluent, which reduces the incidence of water discoloration and foam stabilization on the beaches.

Further development at Sappi Saiccor included the extension of their marine pipeline by 3.5 km to bring the total length to 6.5 km. Sappi Adamas changed to neutral sizing in May and now produces deep-dyed ream wrapper that meets Sappi Europe requirements. They have also developed a new copier paper made from recycled paper for duplication of low-volume copies.

Sappi Stanger achieved a world first when they changed their bleach sequence to C(QPaa)P (chlorine; chelant with activated peroxide [peracetic acid created *in situ*]; hydrogen peroxide). Reduced optical brightening agents, long-fiber savings, and reduced environmental impact offset the additional bleaching costs.

For Mondi Richards Bay, the only large local investment in 1999 was on the mill's PM 2 board machine upgrade and new recovery boiler. Total project cost was in the region of R 600 (US$ 100) million. Capacity has been increased by 240,000 tons of brown and white top liner. Valmet was the main supplier on the board machine, which has a mechanical design speed of 1000 m/min, a drive design speed of 900 m/min, and a production speed range of 360–900 m/min. Its reel trim is 4950–5000 mm, and trim off the winder is 4900–4950 mm. The machine started up in October, and despite initial delays, they are very close to their projected output. The new recovery boiler (900 metric tons/day) was completed in a record time. The original delivery schedule for the new boiler was only 16 months, but the supplier Kvaerner beat this by one week and the previous world record by two months. The recovery boiler was up and running on October 24, increasing existing recovery boiler capacity by 40%.

R&D

Funds for research and development in South Africa tend to be focused on forestry, principally on clonal developments and tree improvements. There is also research being done in the biotechnology field, particularly on biopulping processes.

Paper outlook for 2000

Pulp prices are going up, with insiders predicting an increase during the first and second quartiles of 2000 before dropping in the third. Analysts close to the market estimate that there will be a moderate 1% growth in newsprint consumption, while consumption of magazine grades (LWC and SC) will increase by about 2.5%. Growth in uncoated wood-free grades will be around 4%, while coated wood-free grades will increase by 6% and tissue wadding by 6%.

Sappi's Eugene van As is bullish about the industry's future and expresses hopes for increasing investment in the company's Stanger and Tugela mills during 2000. Mondi will probably consolidate recent investments before committing to further scheduled investments at Richards Bay.

— *Jane Molony is editor of* TAPPSA Journal

PACIFIC RIM: SIGNS OF IMPROVEMENT

Four significant trends appeared in 1999 that will have long-term effects on the development of the pulp and paper industry in Asia.

Economy

The past year has seen a marked improvement in the economies of most countries in Southeast Asia. This, in turn, has helped the pulp and paper industry to get back on its feet.

Unfortunately, the climate of political uncertainty in Indonesia has held back the economic recovery in that country. However, the first democratic election was held in June, and Abdurrahman Wahid and Megawati Sukarnoputri were elected as president and vice president, respectively. It is expected that this combination of popular politicians and political parties will restore political stability to the country, leading to increased investment in new projects.

During 1998, the GDP (gross domestic product) in Indonesia fell by 13.7%, while inflation increased by 78%. The Indonesian pulp and paper companies that were supplying the domestic market had major problems, as demand was drastically reduced, and they had difficulty financing their production. Other companies such as Asia Pulp and Paper (APP) and Asia Pacific Resources International Holdings Ltd. (APRIL), which use mostly domestic raw materials and export the majority of their production, were not affected to the same degree. More details of their activities are provided later in this report.

India has also had the uncertainty of political change, but in the largest democratic country in the world, the effect on the economy was not so great. In October, the Hindu-nationalist Bharatiya Janata Party formed a 24-party alliance, which will bring some degree of reform to the economy. The extent of these changes is difficult to predict because of the pressures of coalition politics.

India's1999 GDP growth is expected to be about 5.5%, and inflation is low. Paper and board prices have started to increase, and the government has granted increased tariff protection on some imported papers. However, due to potential political risks, the government has not tackled the problem of establishing raw-material plantations.

The political situation in China has been very stable, and they managed to maintain their GDP growth rate at about 8% while holding their exchange rate during the economic downturn. A number of small mills were shut down for environmental reasons, and logging was banned in some areas that had been devastated by recent floods. Both factors contributed to a major increase in pulp and paper imports. The People's Republic of China (PRC) celebrated its 50th anniversary on October 1. When PRC joins the World Trade Organization, the local pulp and paper industry will have to become more competitive to cope with the lower import duties.

Globalization

The downturn in the Asian economy increased the rate of globalization in the pulp and paper industry, as several foreign companies took the opportunity to expand into the region at a relatively low cost. The main field of activity was in the newsprint industry, but there were also some mergers in fine paper and packaging grades.

In recent years, several companies in South Korea expanded rapidly into the recycled newsprint business, but they ran into financial difficulties when the currency was devalued. Norske Skog of Norway initially bought a majority interest in the Shinho recycle newsprint mill (120,000 tons/year) in Thailand, and subsequently bought the Shinho mill (180,000 tons/year) at Chong Won in South Korea.

Hansol of South Korea had also run into financial problems and decided to leave the newsprint business. Norske Skog, Abitibi-Consolidated, and Hansol then decided to establish a new company, Pan Asia Paper Co. (PAPCO), to control the Norske Skog newsprint production in South Korea and Thailand, and the Hansol newsprint activities in South Korea and China. The Hansol production at Chonju, South Korea, totals about 1 million tons/year, and they have a majority share holding in the Shanghai Hansol Potential mill (130,000 tons/year) in China.

The three partners have an equal share in PAPCO, which has a total production of 1.4 million tons/year of newsprint in four mills. This comprises a newsprint market share of about 30% in the Asia–Pacific region, excluding Japan. PAPCO, which set up a sales office in Singapore in March, will handle all sales of the export capacity of the four PAPCO mills. They will also market 400,000 tons/year of newsprint imported from Europe and North America.

The Halla Group, of South Korea, also ran into financial difficulties, and their 250,000-ton/year Halla Pulp and Paper recycle newsprint mill at Mokpo was sold to the Bowater Corporation of Calhoun, TN. Output from this mill is marketed in South Korea and other Asian countries.

Malaysian Newsprint Industries (MNI) started up the first 250,000-ton/year recycle newsprint mill at Mentakab in February. This mill is a joint venture between Hong Leong, Fletcher Challenge Paper, New Straits Time Press, and Rimbunan Hijau. Expansion plans for MNI include the use of nearby *Acacia mangium* plantations.

Continued expansion of Asia Pulp and Paper Co.

APP, the largest pulp and paper company in Asia outside Japan, has continued its expansion throughout the region based on low-cost pulp from its mills in Indonesia. The economic downturn forced the company to delay pulp mill projects in China and Malaysia, and orders were canceled for two fine paper machines at Perawang, in Indonesia. However, all other projects were completed on schedule. These projects included a new 60,000-ton/year tissue machine at the APP Lontar Papyrus mill in Jambi, Indonesia, and two 60,000-ton/year tissue machines at the APP Gold Hua Sheng Paper mill in Suzhou, China.

The No. 3 machine at the APP Indah Kiat mill in Perawang, Indonesia, started commercial production in the first quarter of 1999. This machine has a capacity of 370,000 tons/year of coated and uncoated fine paper. In China, the APP Jiangsu Gold East paper mill in Dadang started up two 400,0000-ton/year coated and uncoated fine paper machines.

The APP Gold Hua Sheng Paper mill also started up a new 250,000-ton/year carbonless copy paper machine in Suzhou, China. This machine is identical to the machine at Tjiwi Kimia in Indonesia, which also produces wood-free uncoated paper. The mills at Dadang and Suzhou include a wide range of converting equipment, and there is a dedicated converting plant in Guangzhou Province.

The APP Indah Kiat Perawang mill, in Indonesia, started up their expanded No. 1 bleached hardwood kraft pulp line, bringing the capacity up to 126,000 tons/year. The No. 2 pulp line was also upgraded with a 150,000-ton/year increase in capacity.

APP recently announced that it is seeking partners for its noncore businesses (i.e., tissue, packaging, and power) and has identified a number of possible partners.

Asia Pacific Resources International Holdings Ltd.

APRIL is another large Indonesian pulp and paper manufacturer and is the major owner of Inti Indorayon Utama, which operates a 240,000-ton/year bleached kraft hardwood and softwood pulp mill and rayon plant at Porsea, in northern Sumatra.

APRIL recently completed the expansion of its bleached kraft hardwood pulp mill at Kerinci, in Sumatra, from 750,000 to 850,000 tons/year. Plans are underway to install a new 450,000-ton/year bleached kraft hardwood pulp line at a total cost of US$ 520 million (US$ 1155/annual installed ton). Of this amount, US$ 174 million has already been spent, and APRIL expects to arrange financing for the remainder of the package in the near future.

Riaupaper successfully started up its No. 1 fine paper machine (350,000 tons/year) at Kerinci. However, startup of the No. 2 machine has been delayed by the withdrawal of an anticipated Finnish export credit. The machine is ready for shipment, and the company is investigating alternative financing. Because of the delay in the startup of this machine, APRIL and UPM–Kymmene, of Finland, are renegotiating their earlier joint-venture agreement.

APRIL Changshu started up their 350,000-ton/year wood-free uncoated paper machine, near Suzhou, in April. This mill is a joint venture with UPM–Kymmene, and the total cost was US$ 500 million. The company also owns a 30,000-ton/year converting plant in Suzhou, which was commissioned ahead of the paper mill.

The main economic difficulties in Asia appear to be over. While this has been a painful time, it could have a positive effect if the governments in the region take the opportunity to reorganize the financial control of their economies.

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