

# Impact China: The Global Transformation of Board and Packaging Grades

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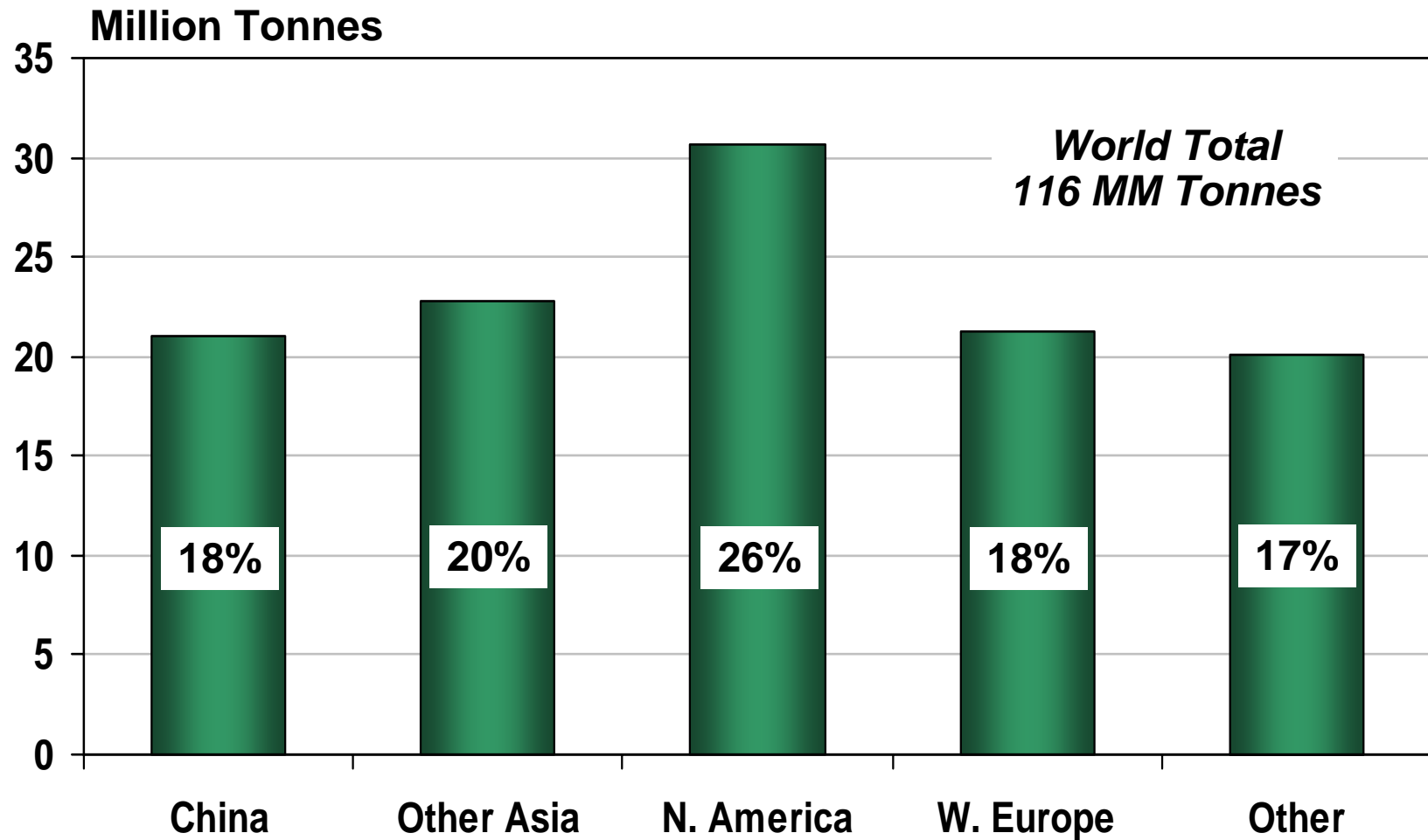
May 22, 2006



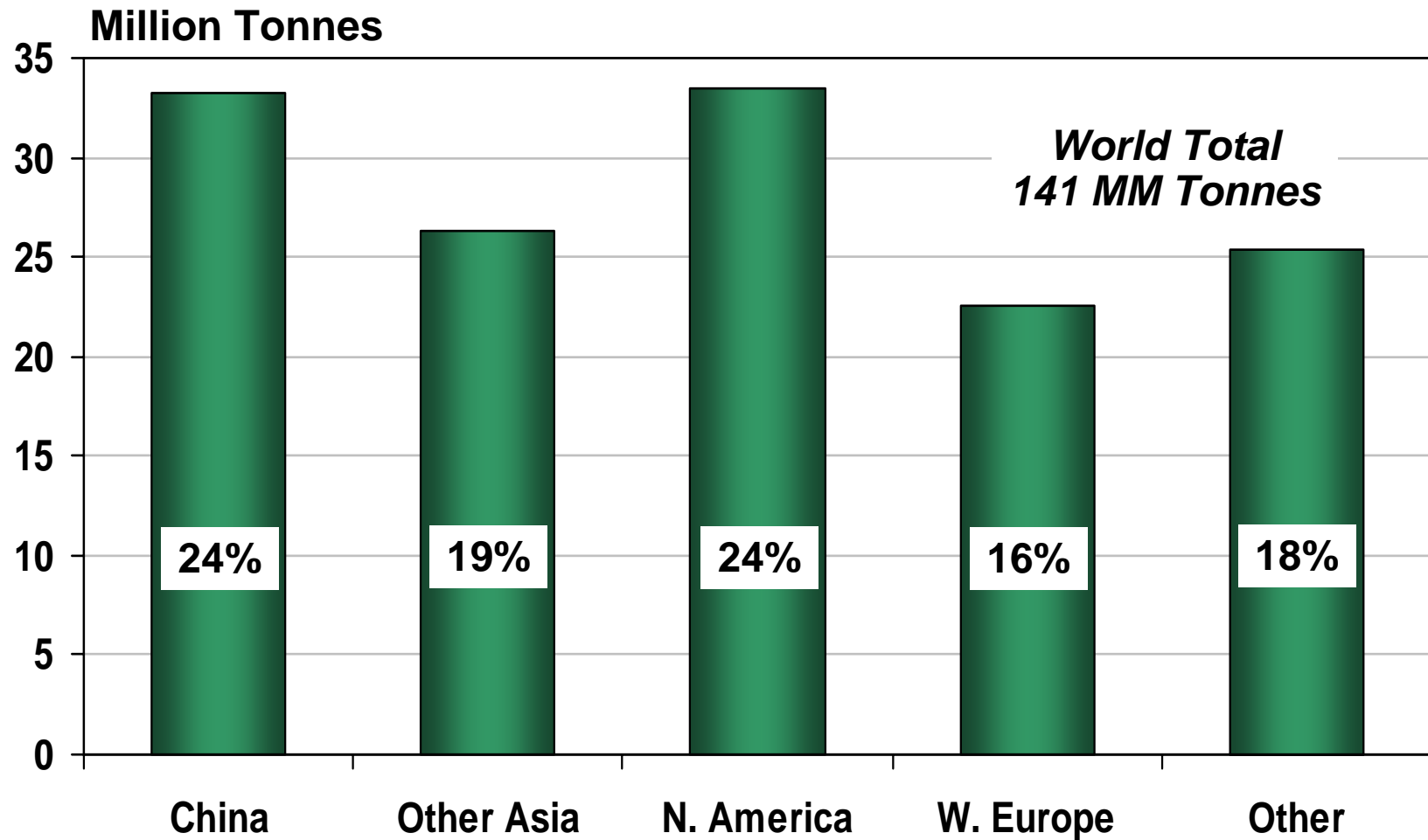
# Impact China: The Global Transformation of Board and Packaging Grades

- ▶ China Well On Its Way to Becoming Largest Global Market for Packaging Materials
  - Exceptional demand growth during last four years
  - But capacity growth is now outpacing demand
  - This will affect the global trade balance
- ▶ Even Without Additional Chinese Capacity, Oversupply Will Be an Issue in Many Overseas Markets
- ▶ Implications for the North American Paper Packaging Producers

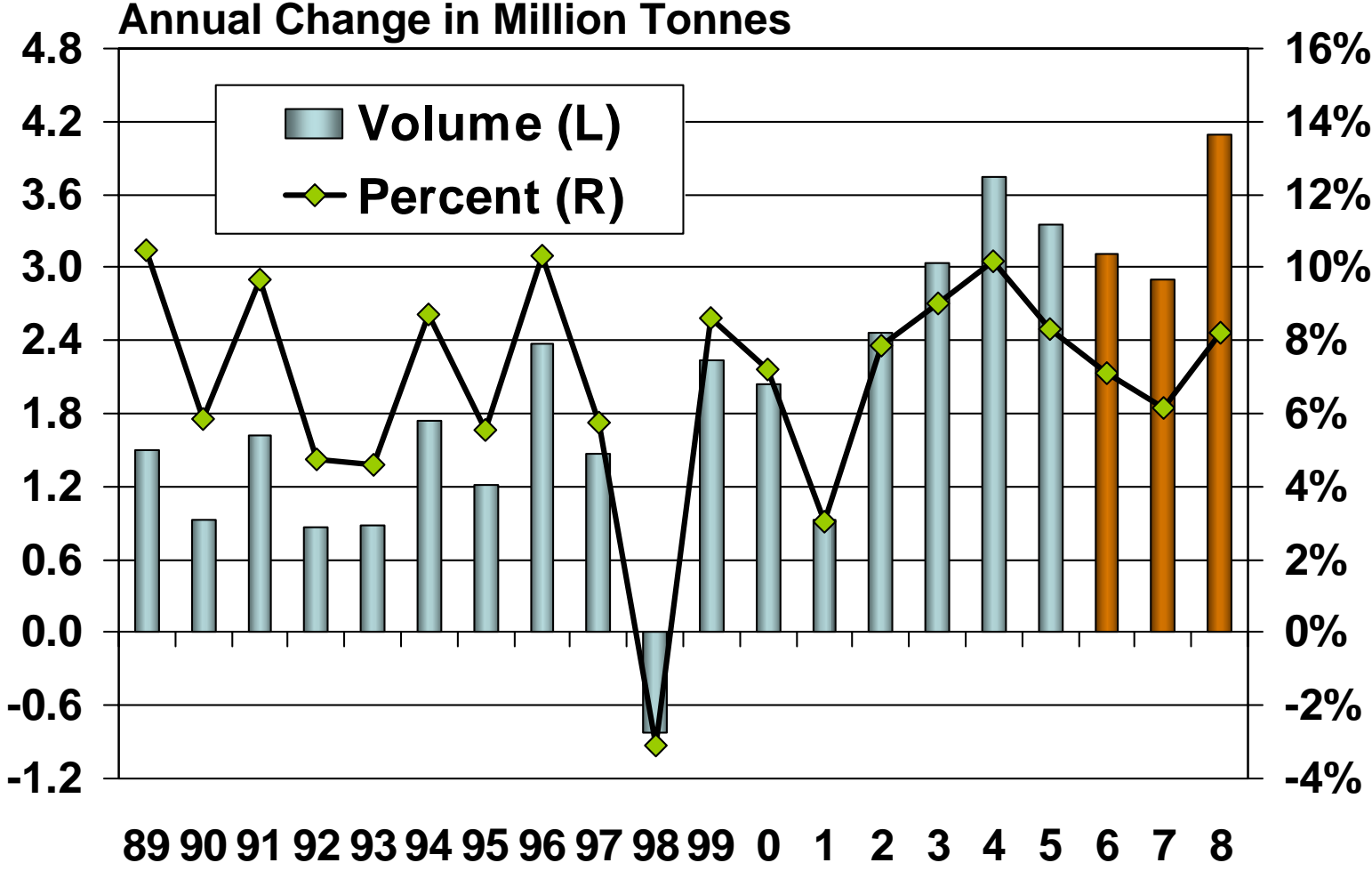
# China Is Now the Third-Largest Containerboard Market in Terms of Demand (2005)...



## ...and China Should Become the Largest Market by 2010

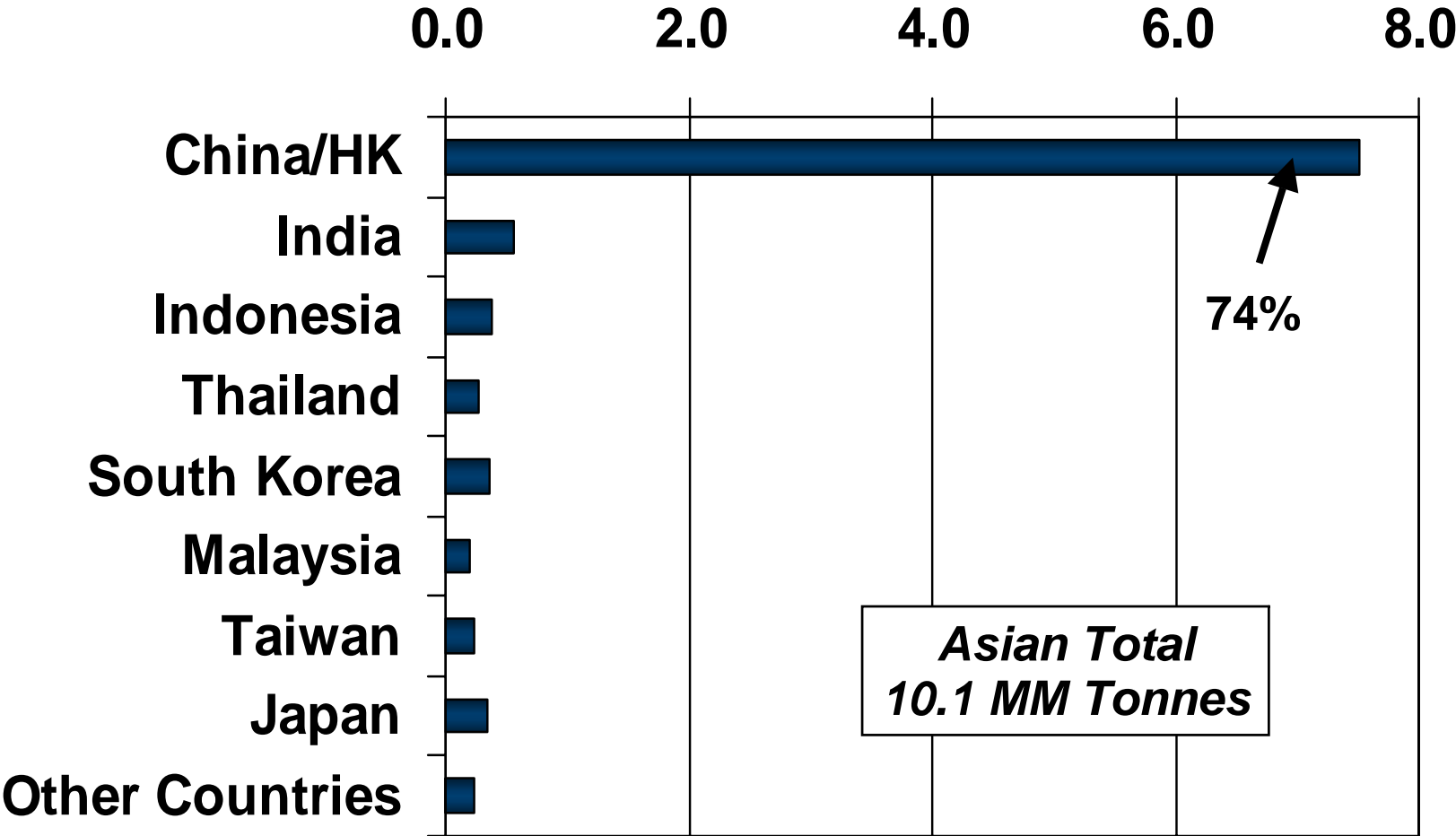


# Asian Demand Growth Still Strong, But Slipping

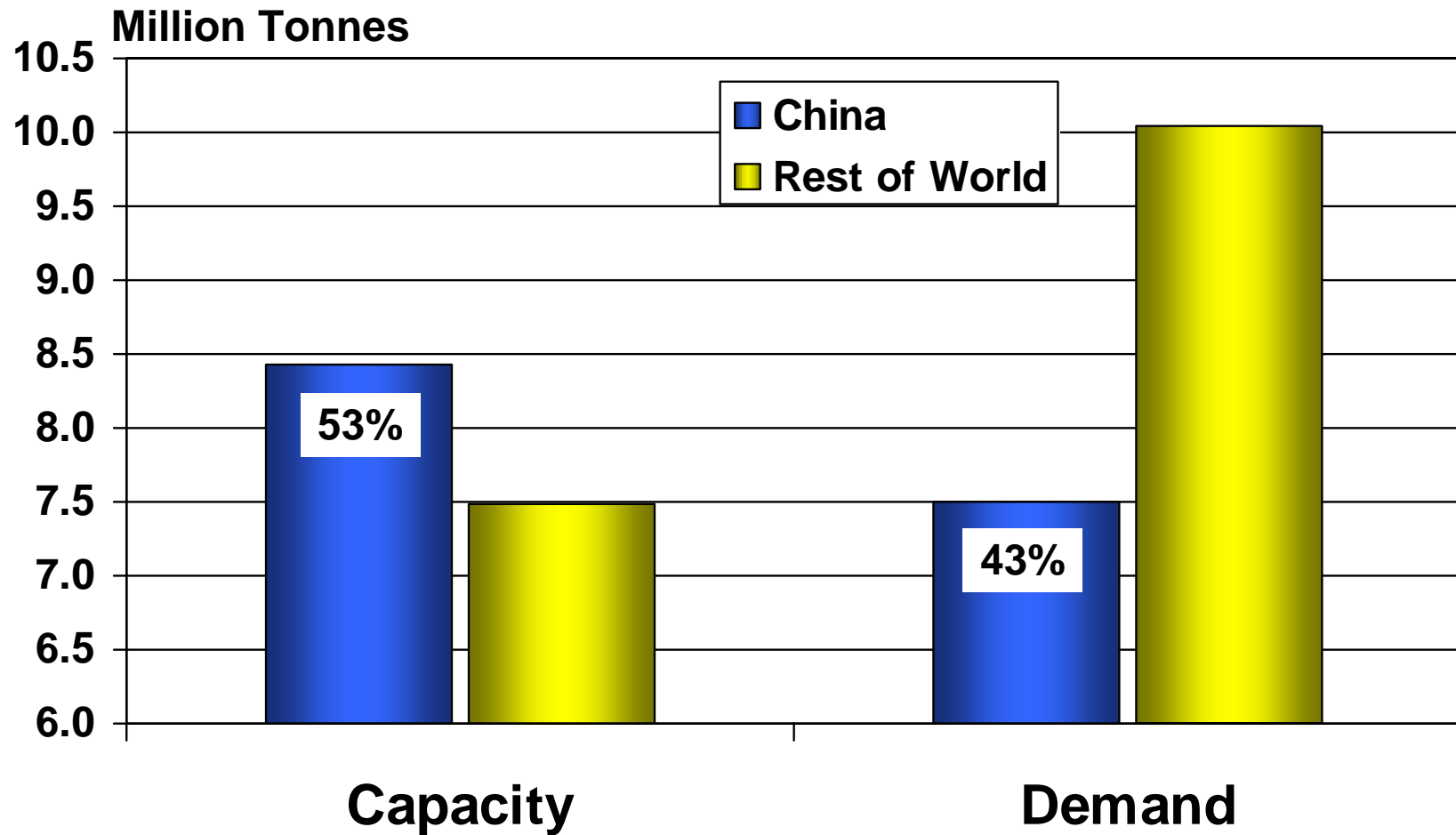


# Chinese Growth Will Dominate the Asian Market

(Total Increase in 2006–2008; Million Tonnes)



## Capacity Growth in China Outpacing the Rest of the World (2006–2008)



## Chinese Containerboard Capacity Expansion (000 Tonnes)

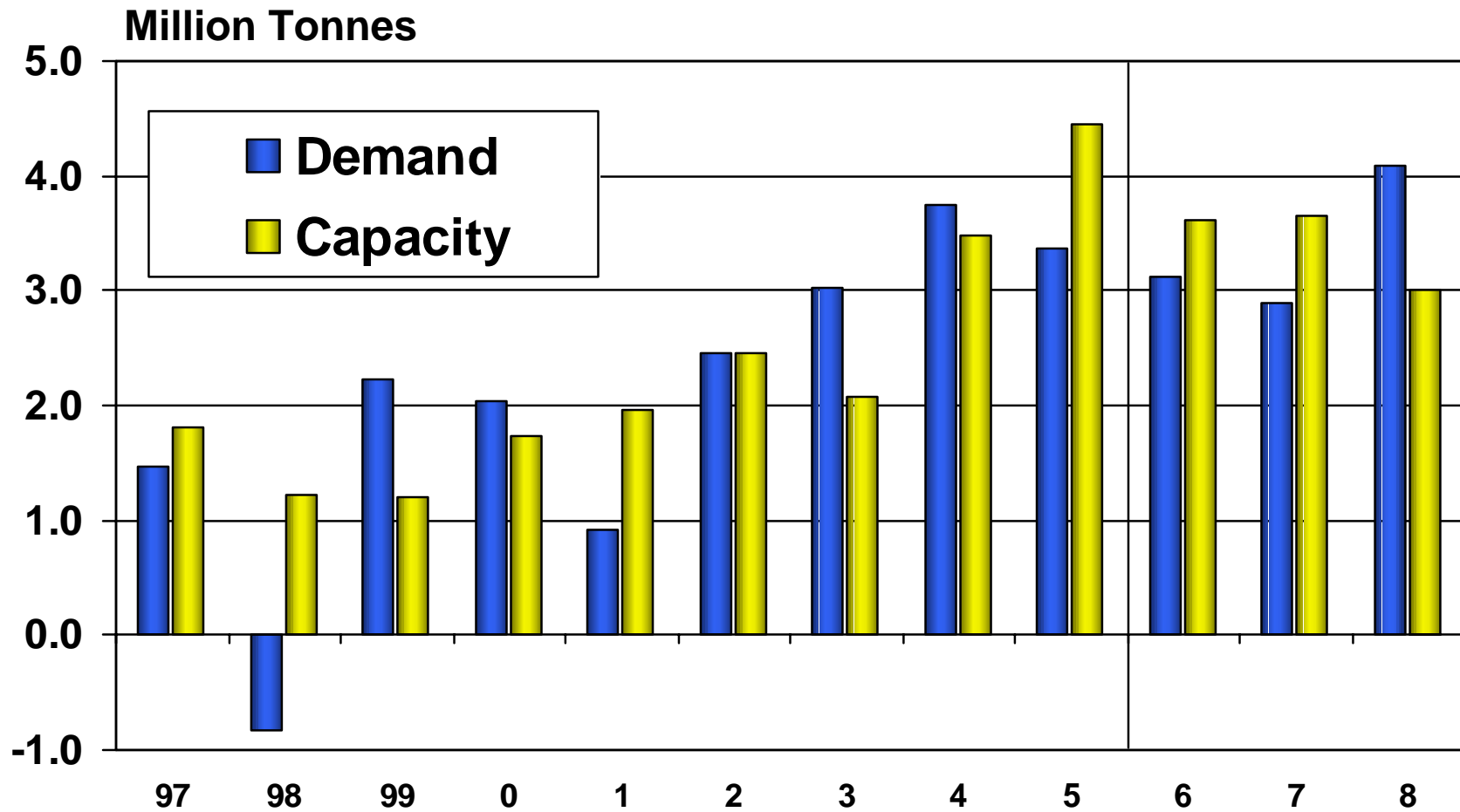
<b>TOTAL 2005</b>	<b>1,300</b>	<b>5 projects</b>
<b><u>Company</u></b>	<b><u>Capacity</u></b>	<b><u>Startup</u></b>
Lee & Man (PM 7)	400	Q1:2006
Nine Dragons (PM 10)	200	Q1:2006
Hop Fung	150	Q1:2006
Jian Paper Packet	300	Q1:2006
Yuen Foong Yu	150	Q2:2006
Fujian Qingshan	250	Q3:2006
Zhangjiagang Huaxing	150	Q3:2006
Shanying Paper	300	Q4:2006
Yuen Foong Yu	250	Q4:2006
Lee & Man (PM 8)	450	Q4:2006
<b>Total</b>	<b>2,600+</b>	

# Chinese Containerboard Capacity Expansion

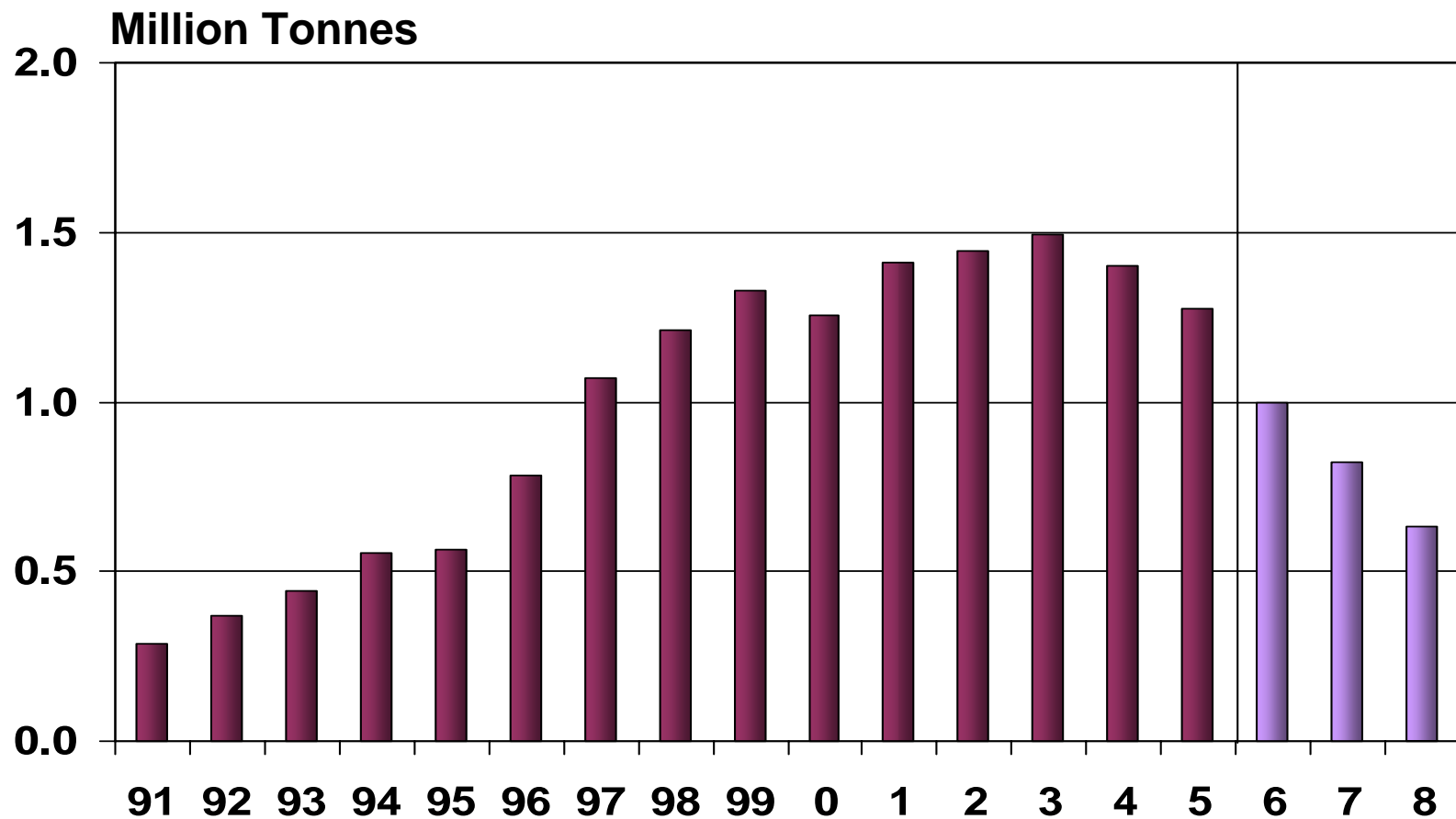
(000 Tonnes)

<u>Company</u>	<u>Capacity</u>	<u>Startup</u>
Zhejiang Jingxing	400	Q1:2007
Lee & Man (PM 9)	300	Q3:2007
Lee & Man (PM 10)	300	Q3:2007
Lee & Man (PM 11)	300	Q4:2007
Wuxi Long Chen	400	2007
Nine Dragons (PM 12)	400	2008
Nine Dragons (PM 13)	400	2008
<b>Total</b>	<b>2,500+</b>	

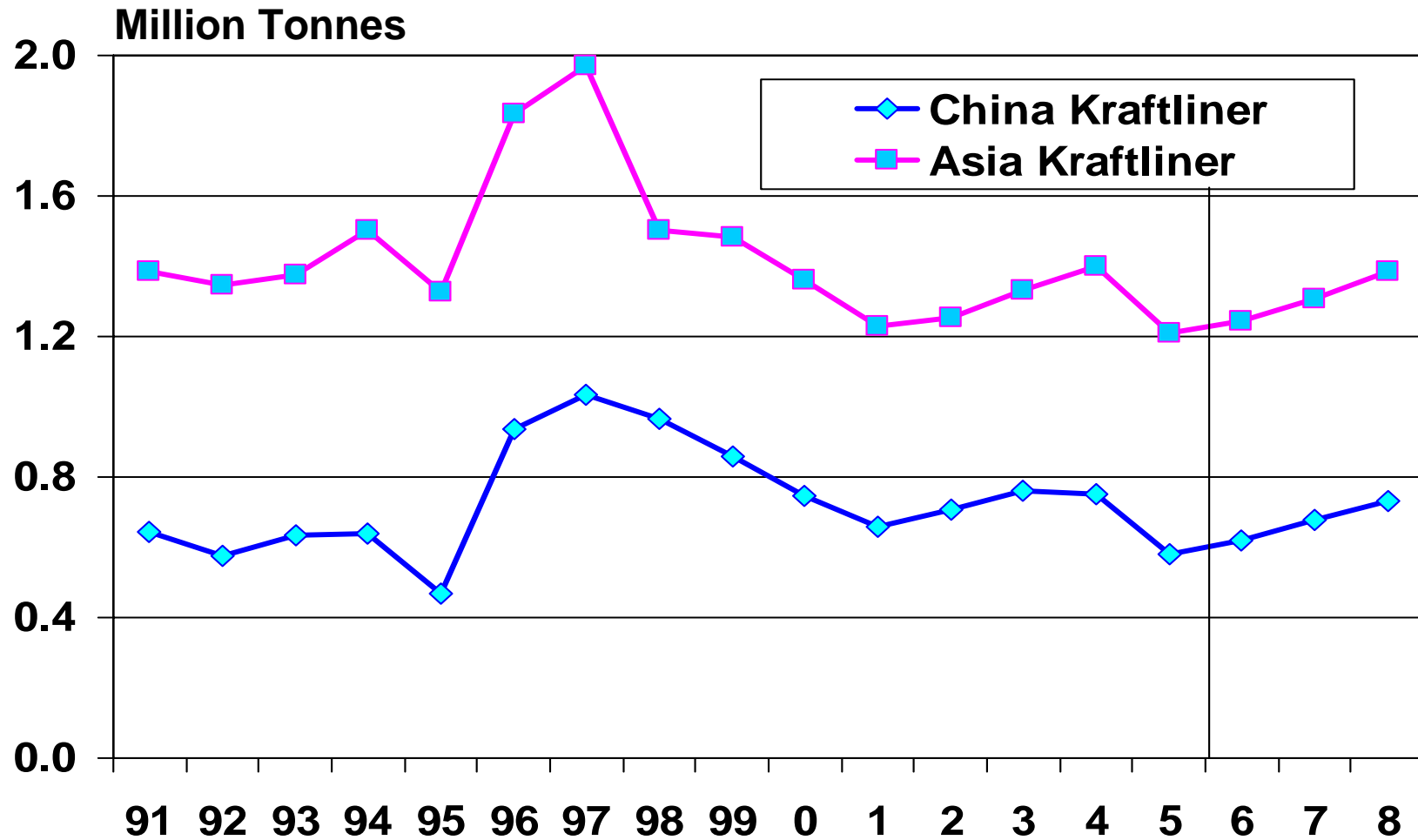
# Change in Asian Containerboard Demand and Capacity



## Chinese Recycled Containerboard Imports Are Expected to Slide Further in 2006–2008



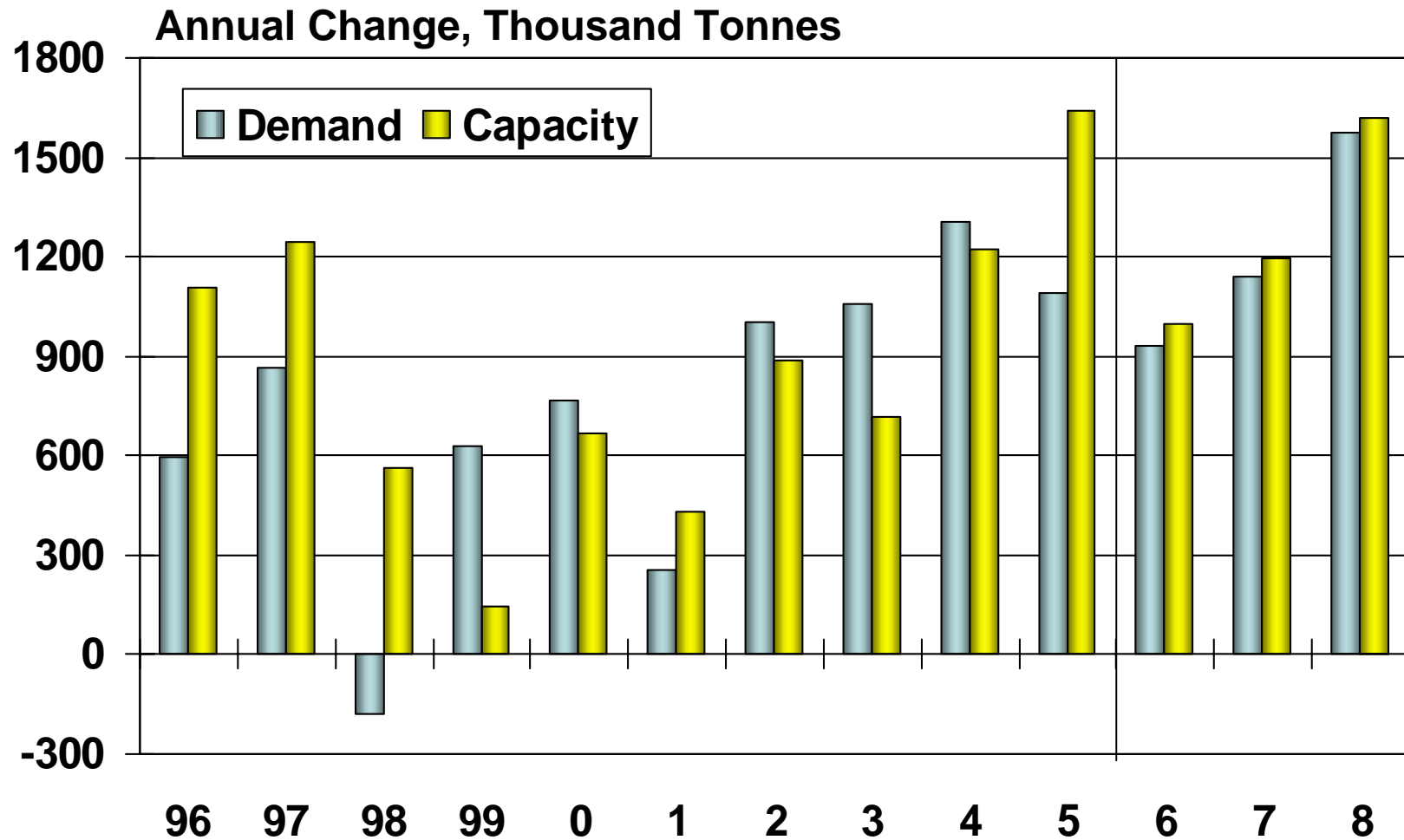
# Kraftliner Imports Expected to Modestly Revive



# Is China Over Investing in Containerboard Capacity?

- ▶ Yes, Relative to Demand
  - Growth in production is outpacing demand
  - Thus holding down prices and profitability for recycled grades
  
- ▶ Yes, Due to Policies
  - Paper and paperboard “encouraged” industry
  - Favorable tax treatment and loan terms
  
- ▶ No, from Chinese Perspective
  - China policies designed for rapid expansion
  - Still large trade deficit
  
- ▶ What Can We Conclude?
  - Oversupply in China will haunt the global market thru 2007

# Asian Boxboard Markets Facing a Similar Situation as Containerboard



## Surging Asian Capacity Led by China

- ▶ Asian Capacity Increased 1.6 Million Tonnes in 2005
- ▶ Additional 2.2 Million Tonnes Due in 2006–2007
- ▶ Almost All of the Increase Takes Place in China
  - 6 projects (1.2 million tonnes) started in 2005
  - 5 projects (0.9 million tonnes) due in 2006
  - 2 projects (0.8 million tonnes) announced for 2007
  - 2 small projects announced for rest of Asia

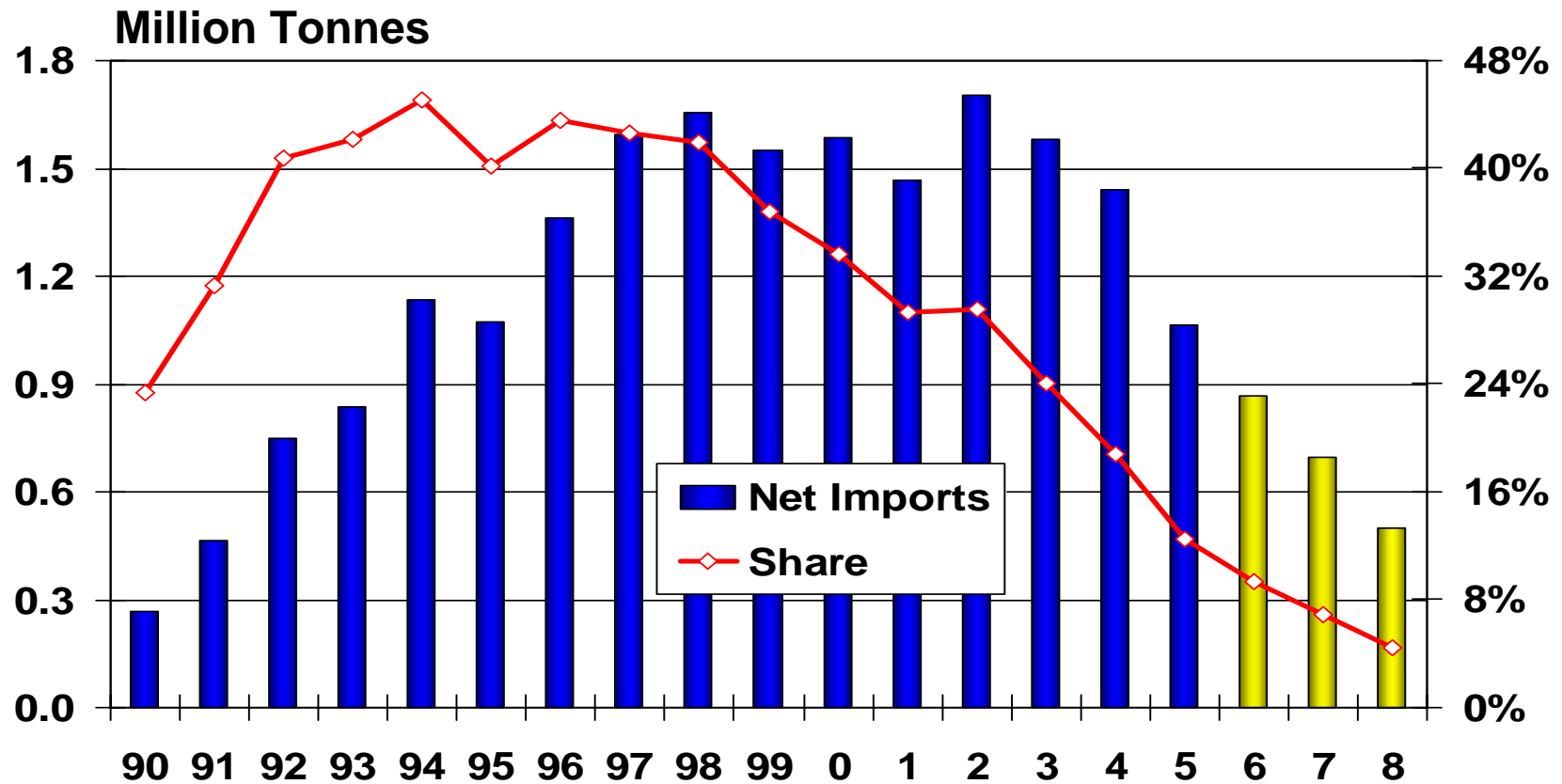
## Announced Chinese Boxboard Capacity Expansion in 2006–2007 (000 Tonnes)

<u>Company</u>	<u>Capacity</u>	<u>Startup</u>
Hangzhou Yongli	50	Q2:2006
Zhuhai Hongta Renheng	50	Q2:2006
Foshan Huafeng	300	Q3:2006
Yongtai Paper	200	Q4:2006
Ningxia Meili	300	End 2006
Nine Dragons	500	Q1:2007
Int'l Paper/Sun Paper	300	Q4:2007
<b>TOTAL</b>	<b>1,700</b>	

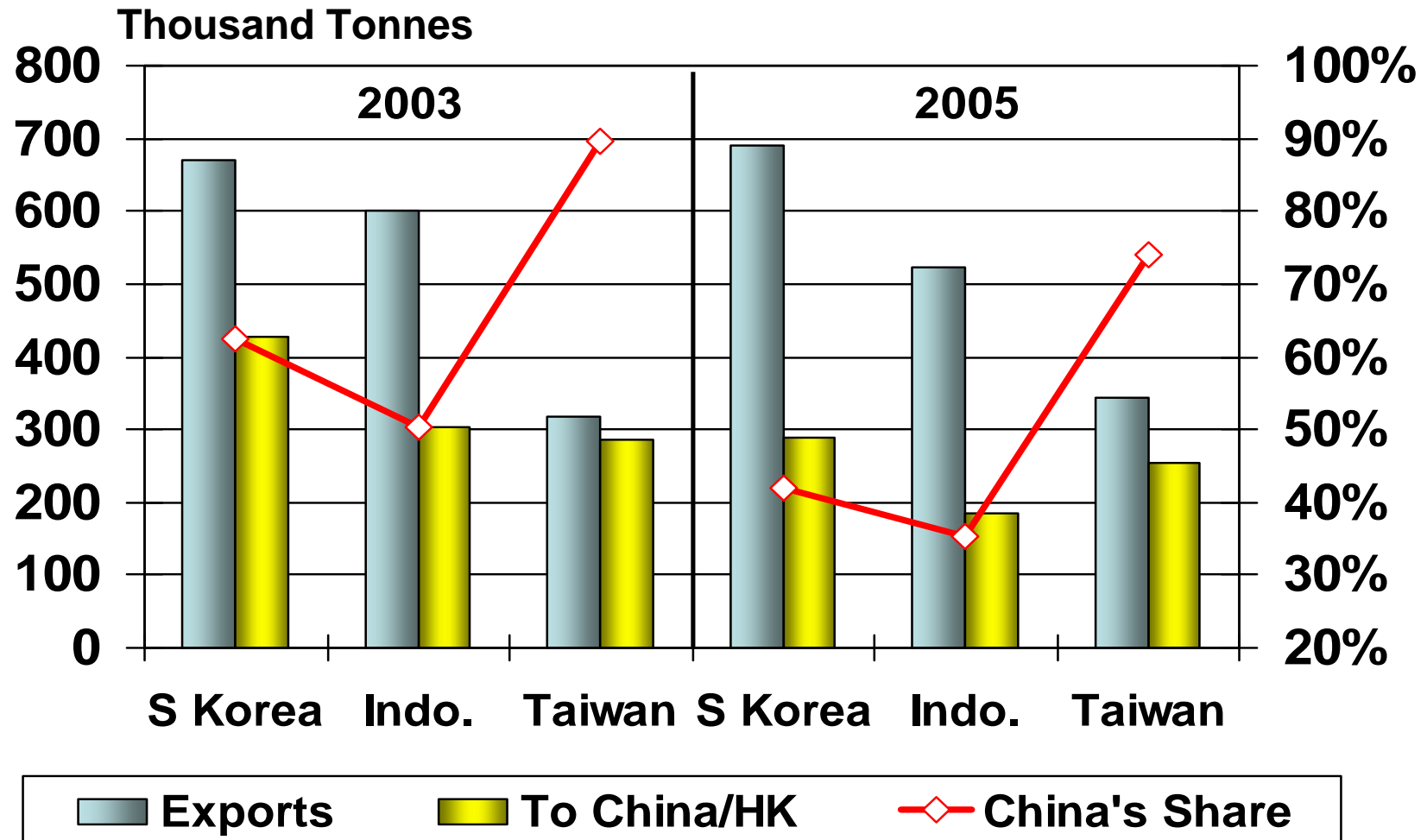
## What Will Happen to Asian Boxboard Trade in 2006–2008?

- ▶ Chinese Net Imports Will Continue to Slide
  - Rising production displaces imports
- ▶ Asia's Major Exporters Will See Some Further Declines in External Shipments
  - Will look for new markets to offset loss of China market
  - Aided by substantial gap in prices between Asia, Western Europe and the U.S.

# Chinese Boxboard Net Imports and Share of Apparent Consumption



## Asia's Major Exporters Still Highly Dependent on China/HK Market, But Levels Decreasing



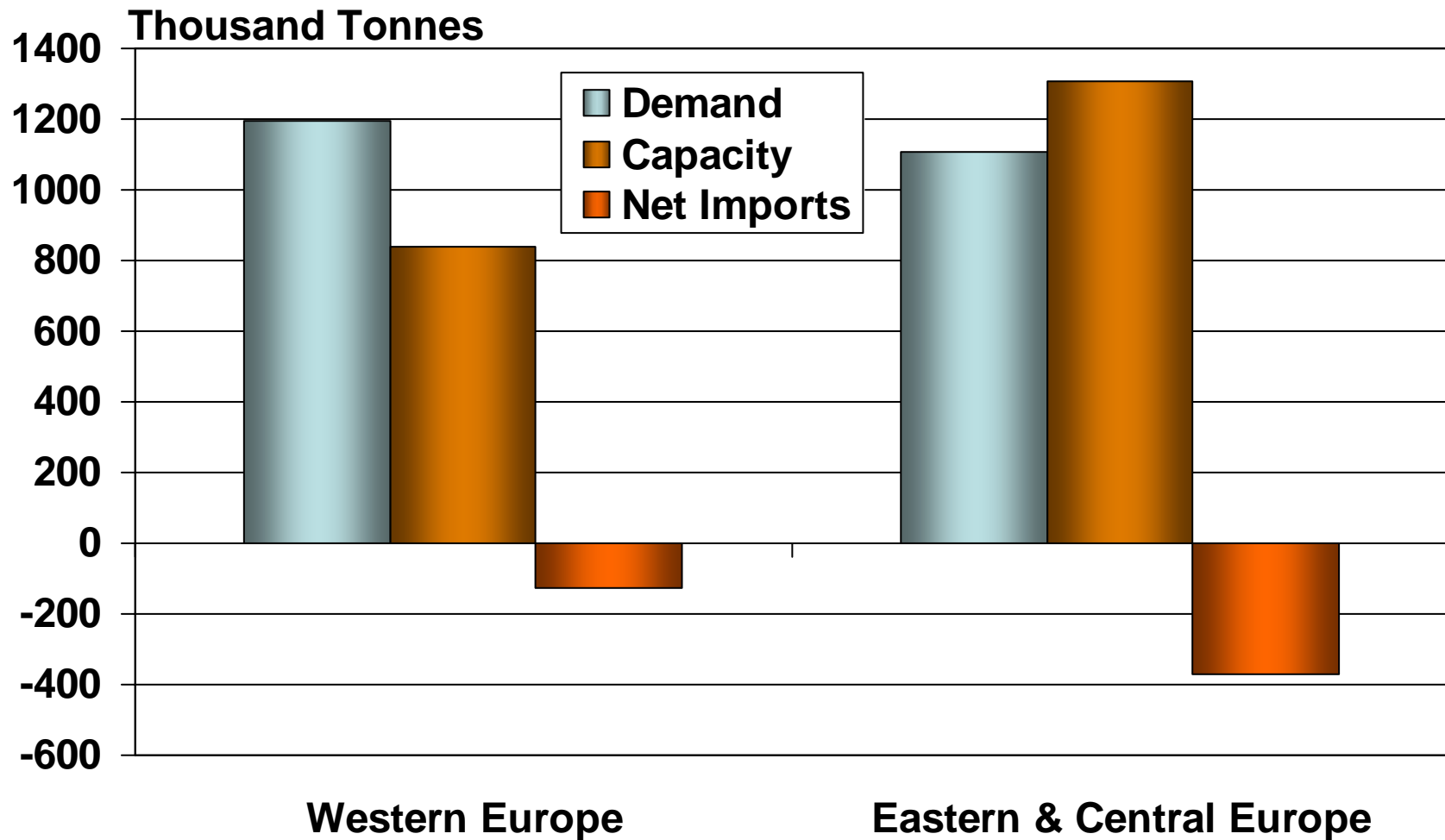
## Asian Boxboard Summary

- ▶ Boxboard Demand Sees Mild Deceleration in 2006, Gradually Moves Higher in 2007–2008
  - Risk is to the upside and depends on developments in China
  
- ▶ Chinese Capacity Continues to Expand at Rapid Rate in the Near Term
  - Operating rates remain stable, but expect market balance to continue to favor buyers
  
- ▶ Asian Net Imports Will Continue to Retreat
  - Import displacement
  - Strong potential for increase in exports outside the region
  - Will China participate in this?

## **Globalization of the Containerboard Industry: Other Overseas Markets Facing Imbalances**

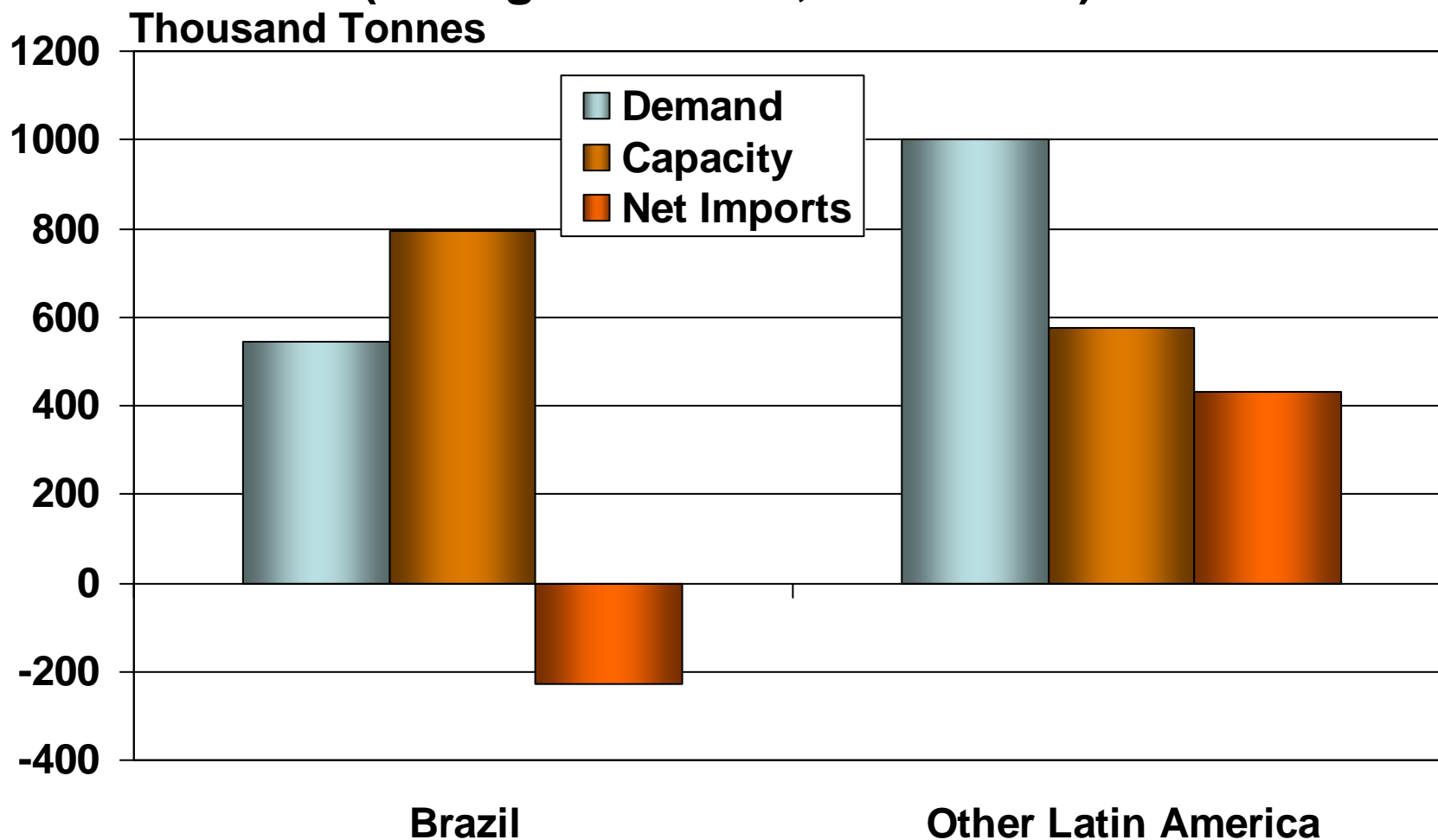
- ▶ Capacity Surge in China Has Been Receiving the Most Focus
- ▶ Europe Feeling Lingering Effects of Its Capacity Bulge
- ▶ Rest of the World Is Not Idle on the Capacity Front
- ▶ Net Result: Exceedingly Poor Growth Prospects for North American Exports

## European Net Imports Will Decline During Next Three Years (Change in Levels, 2006–2008)



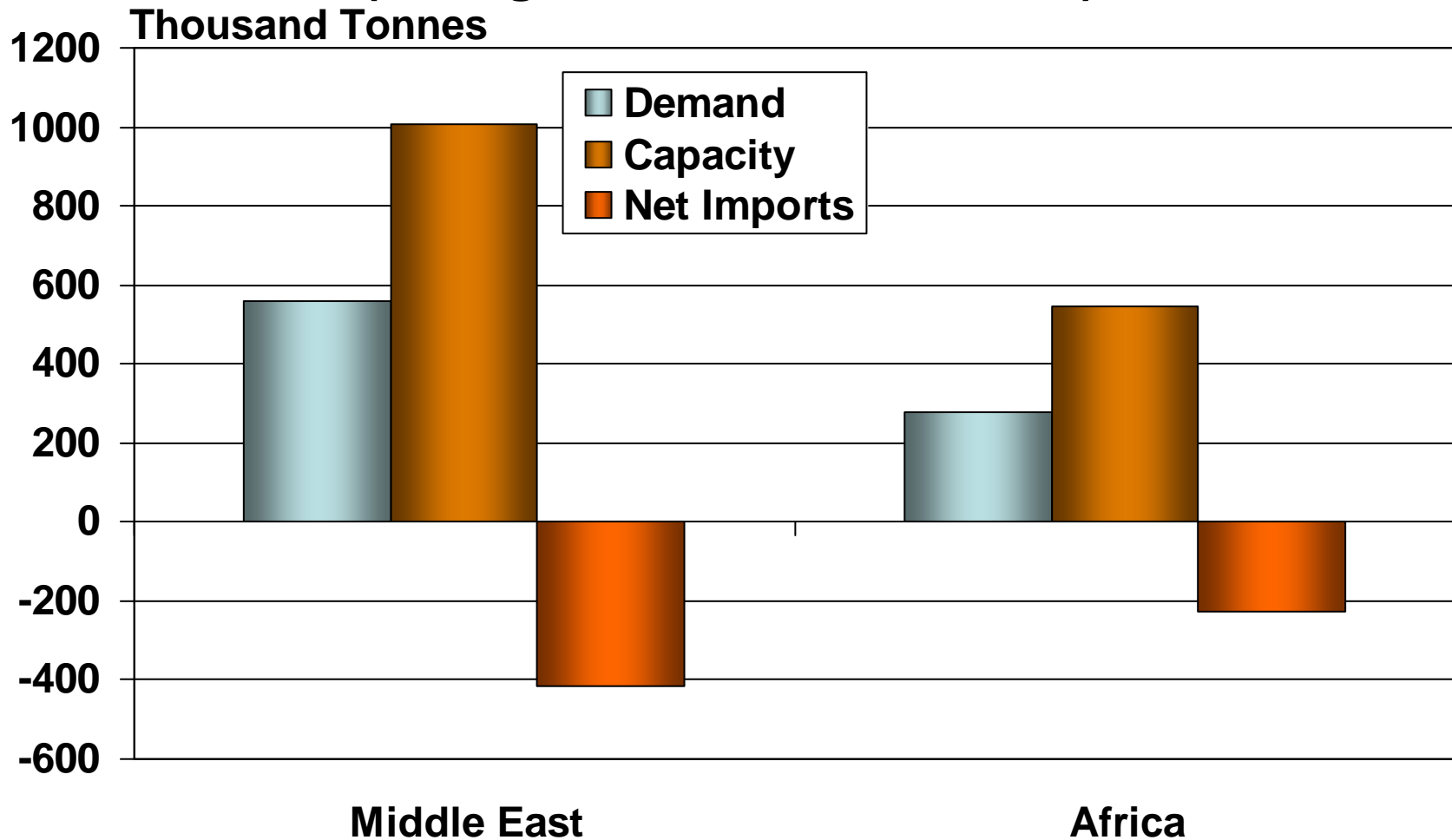
# Latin American Capacity Growth Is Finally Catching Up to Demand

(Change in Levels, 2006–2008)



# Africa and the Middle East Will No Longer Be Outlets for Excess Tonnage

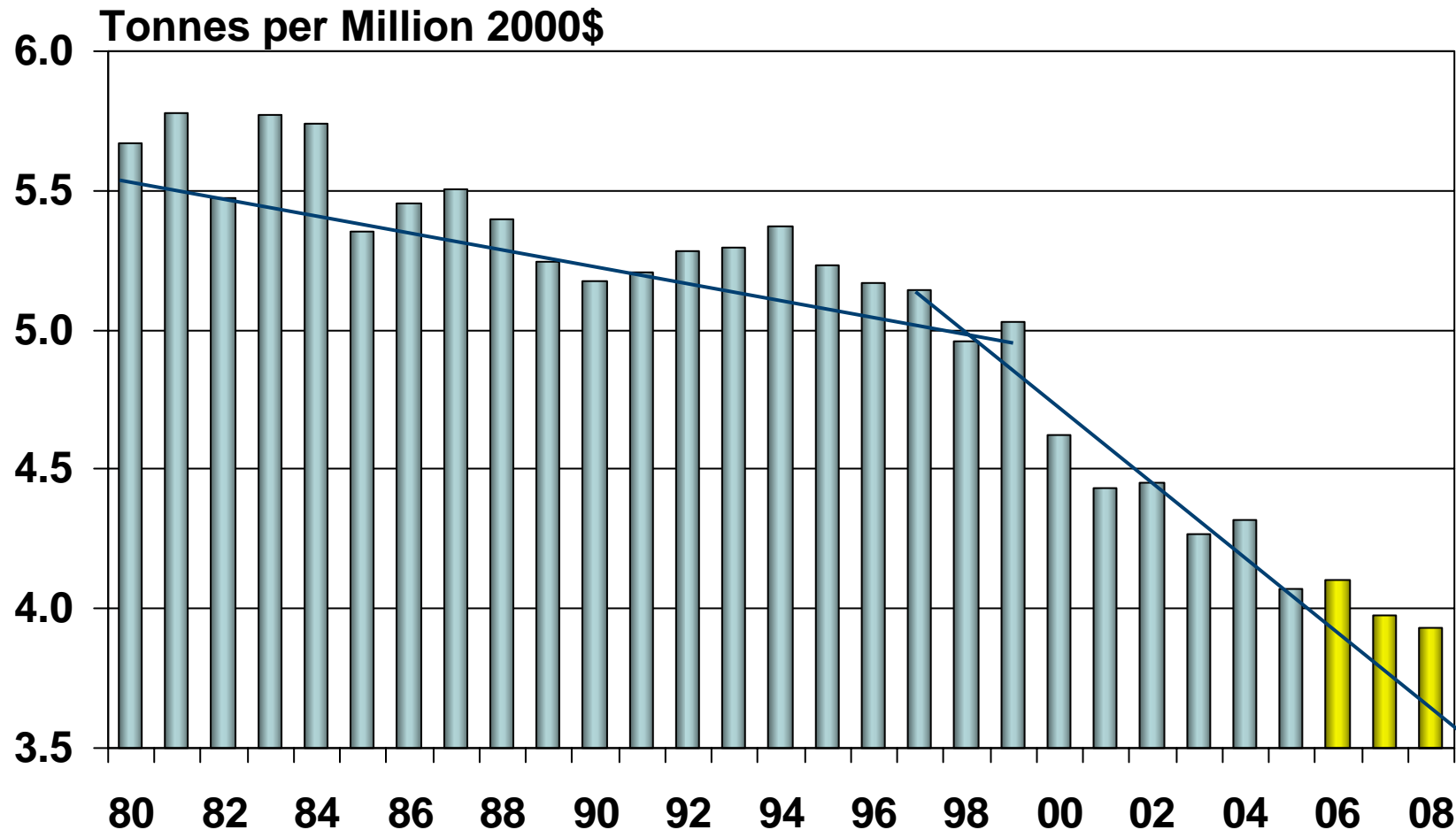
(Change in Levels, 2006–2008)



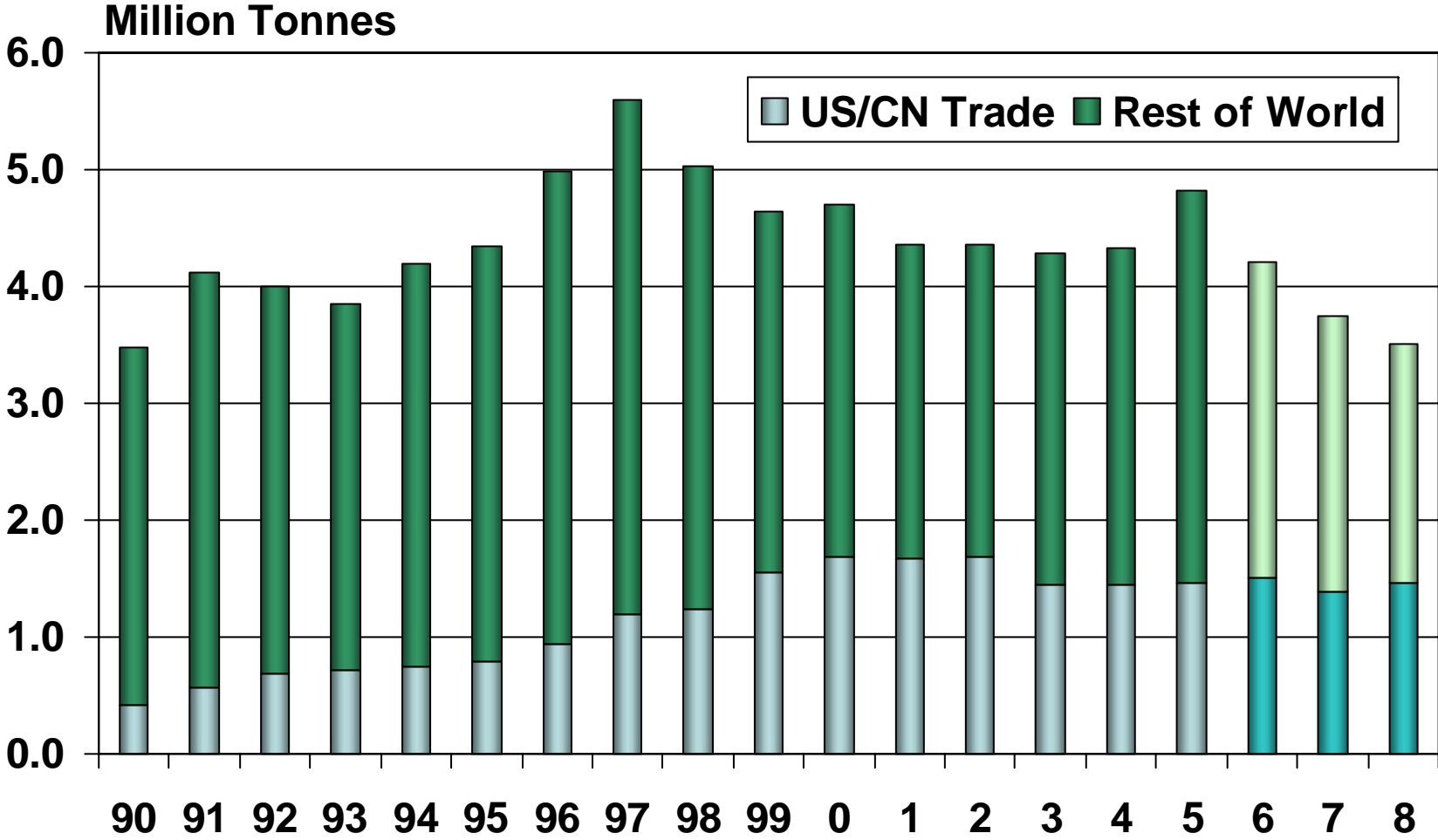
## Impact China: Implications for the North American Paper Packaging Producers

- ▶ Domestic Demand for All Grades Will Continue to Lag Well Behind Historical Levels
  - Growing imports of consumer goods
- ▶ Containerboard Markets Facing Sharp Decline in Exports
  - U.S. kraftliner exports reached 3.1 million tonnes
  - But are expected to decline to 2.2 million tonnes by 2008
- ▶ Boxboard Markets More Likely to Be Impacted by Sharp Increase in Imports from Producers Displaced Out of Asia
- ▶ Net Result: Additional Capacity Closures Likely Over Time

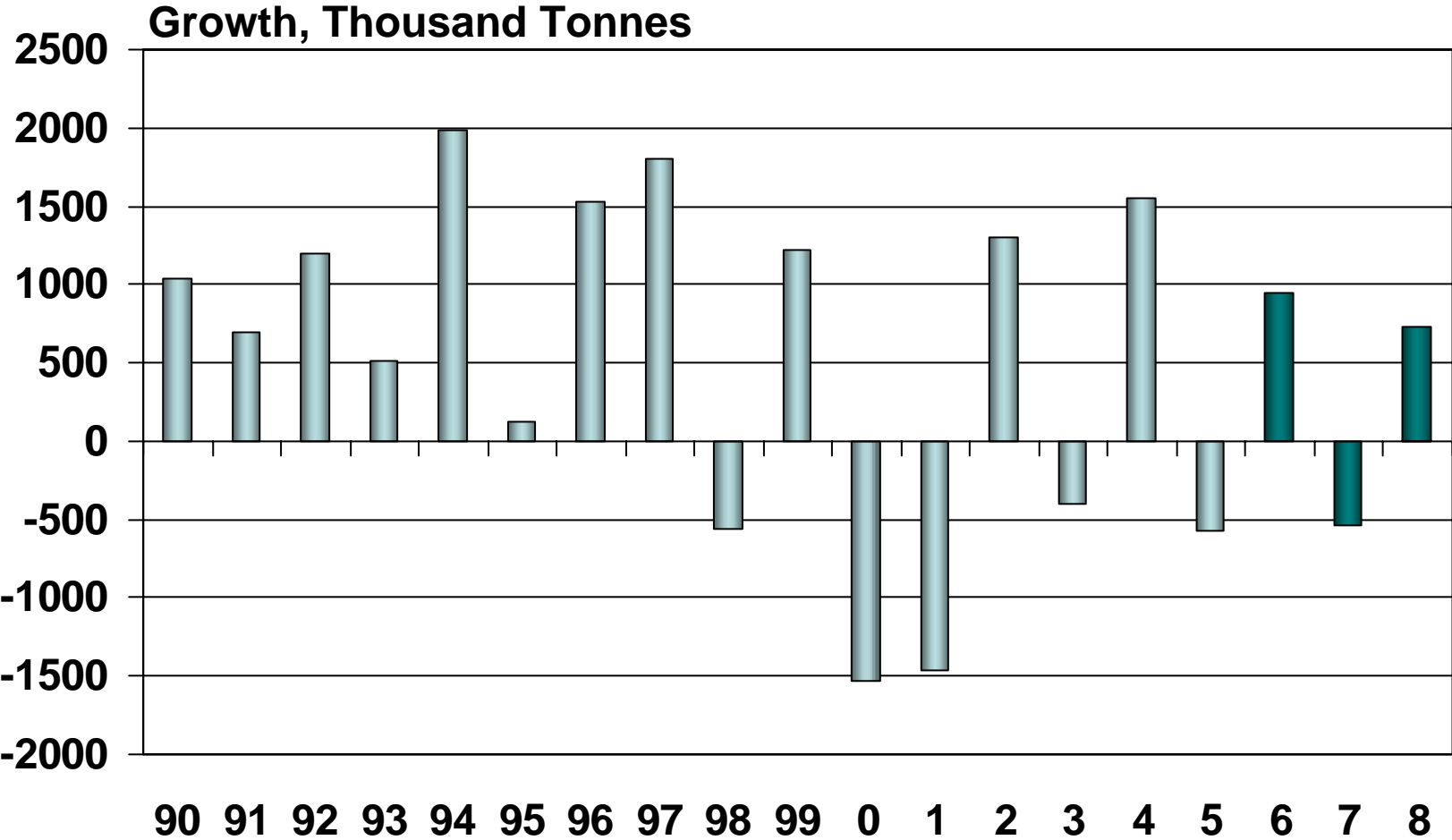
# The Rising U.S. Merchandise Trade Deficit Has Accelerated the Decline in N.A. Paper Packaging Demand Relative to GDP



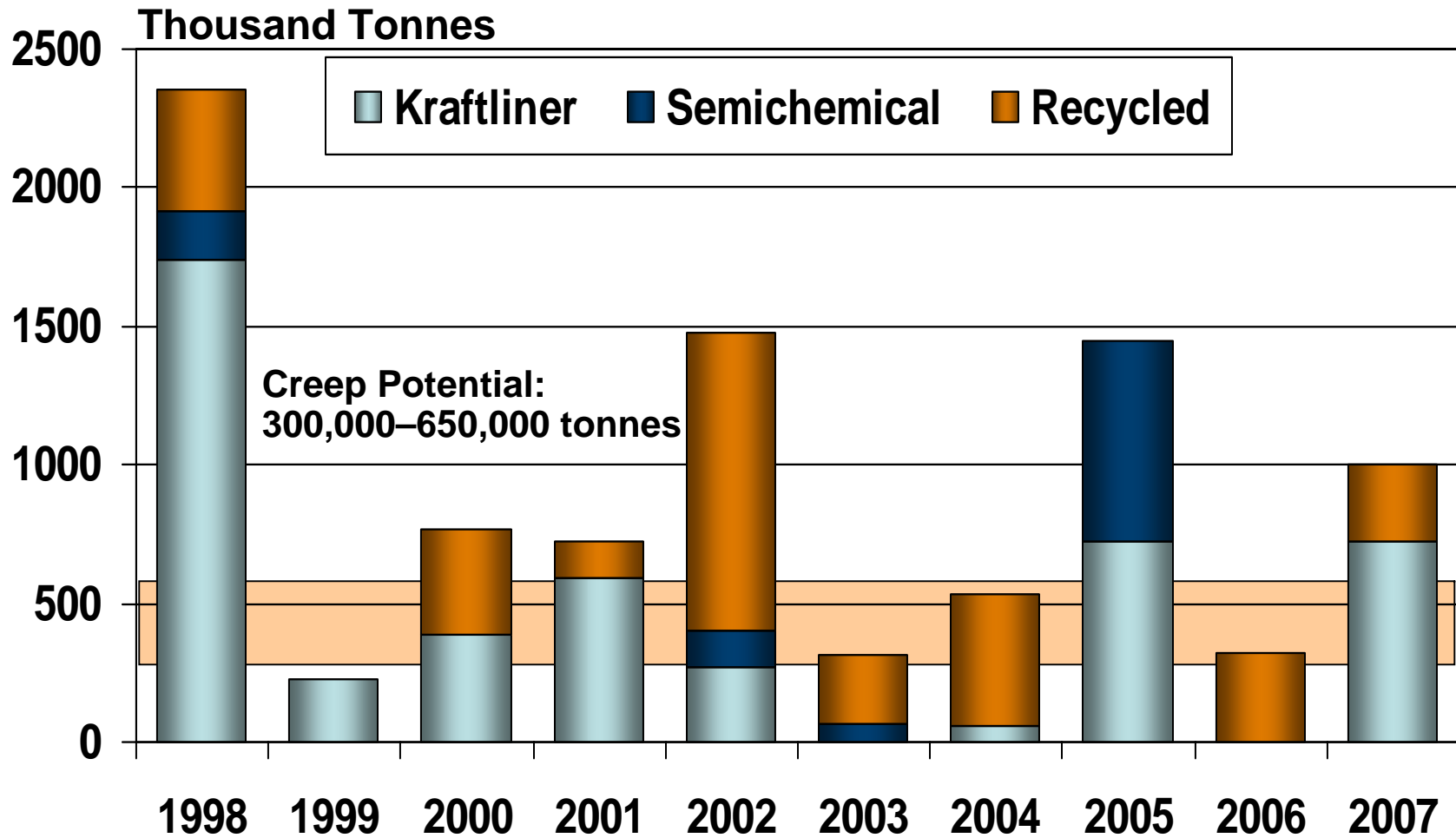
# North American Containerboard Markets Facing a Steep Decline in Exports



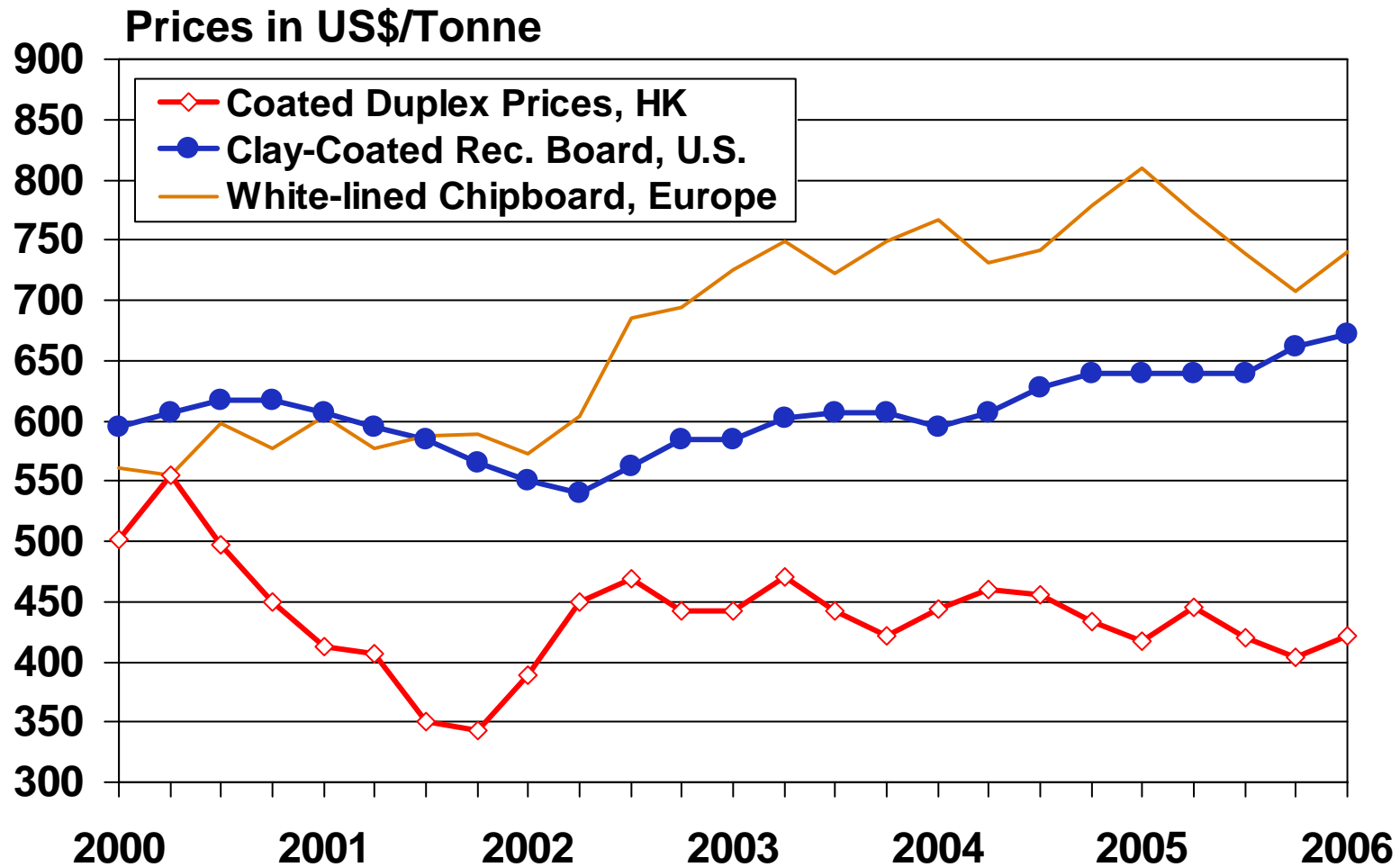
# North American Containerboard Production Will Remain Choppy at Best in 2006–2008



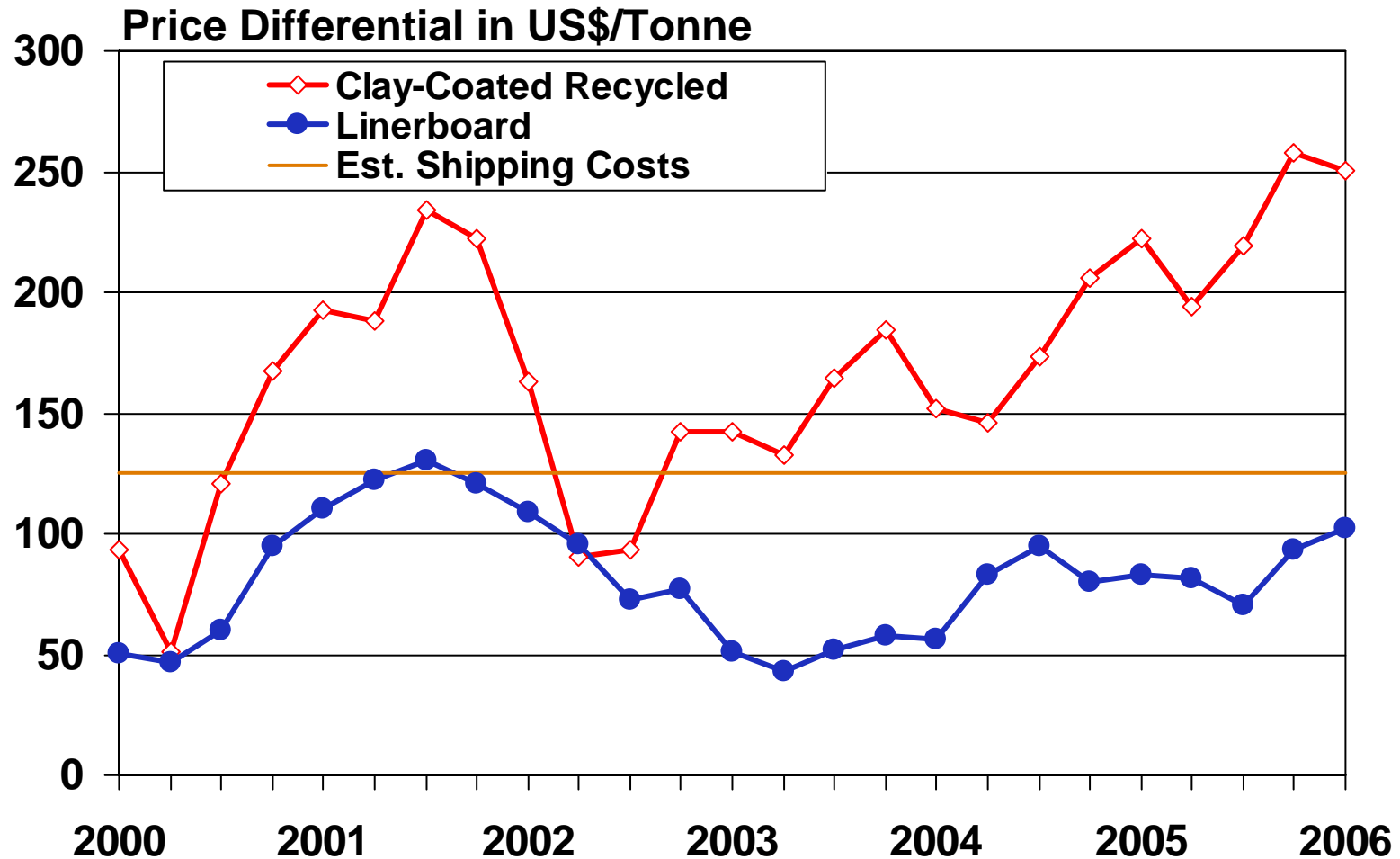
# North American Capacity Closures Continued in 2005: More Are Likely by 2007



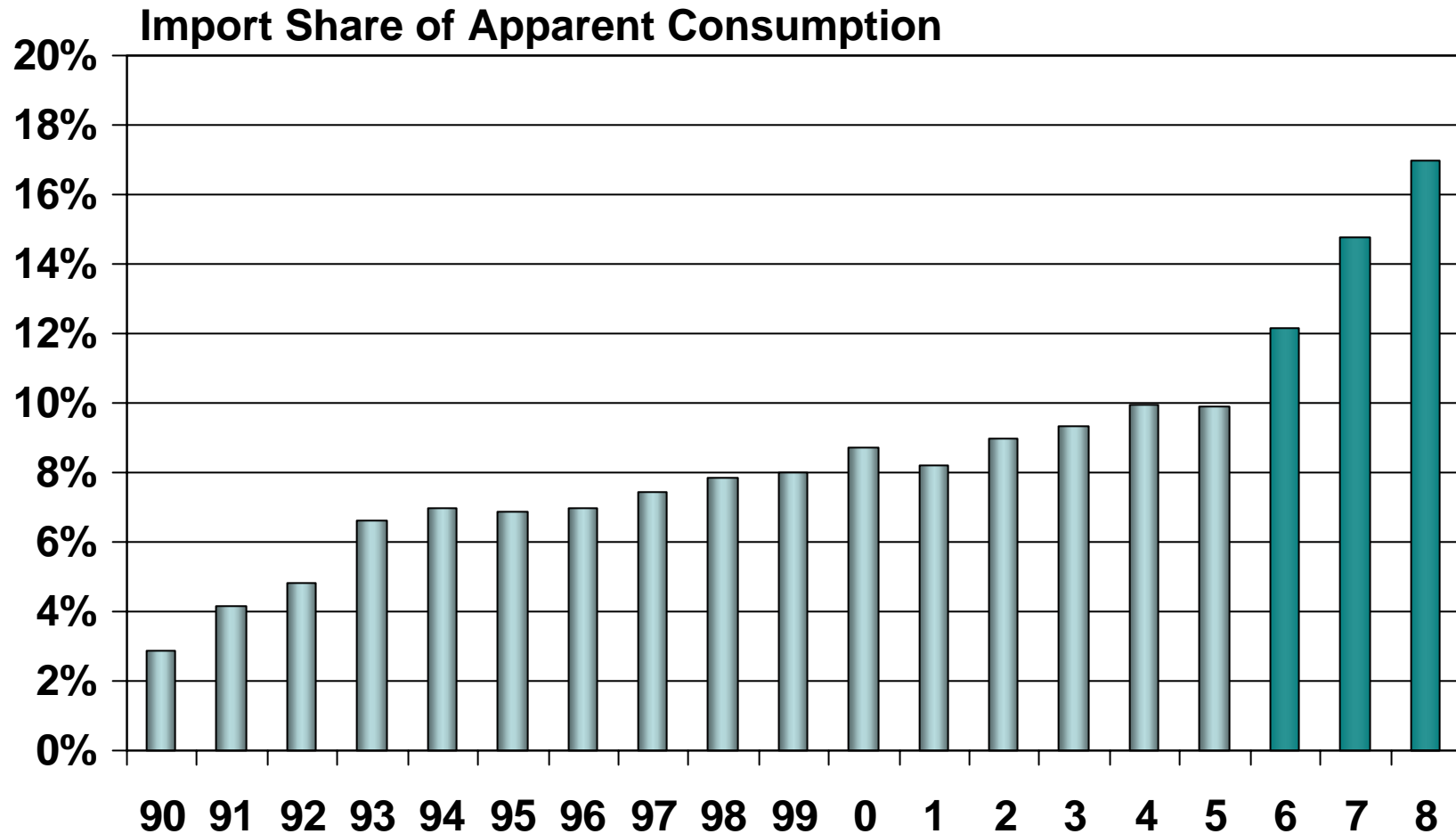
# Asian Cartonboard Exports Will Pose a Threat in U.S. and European Markets



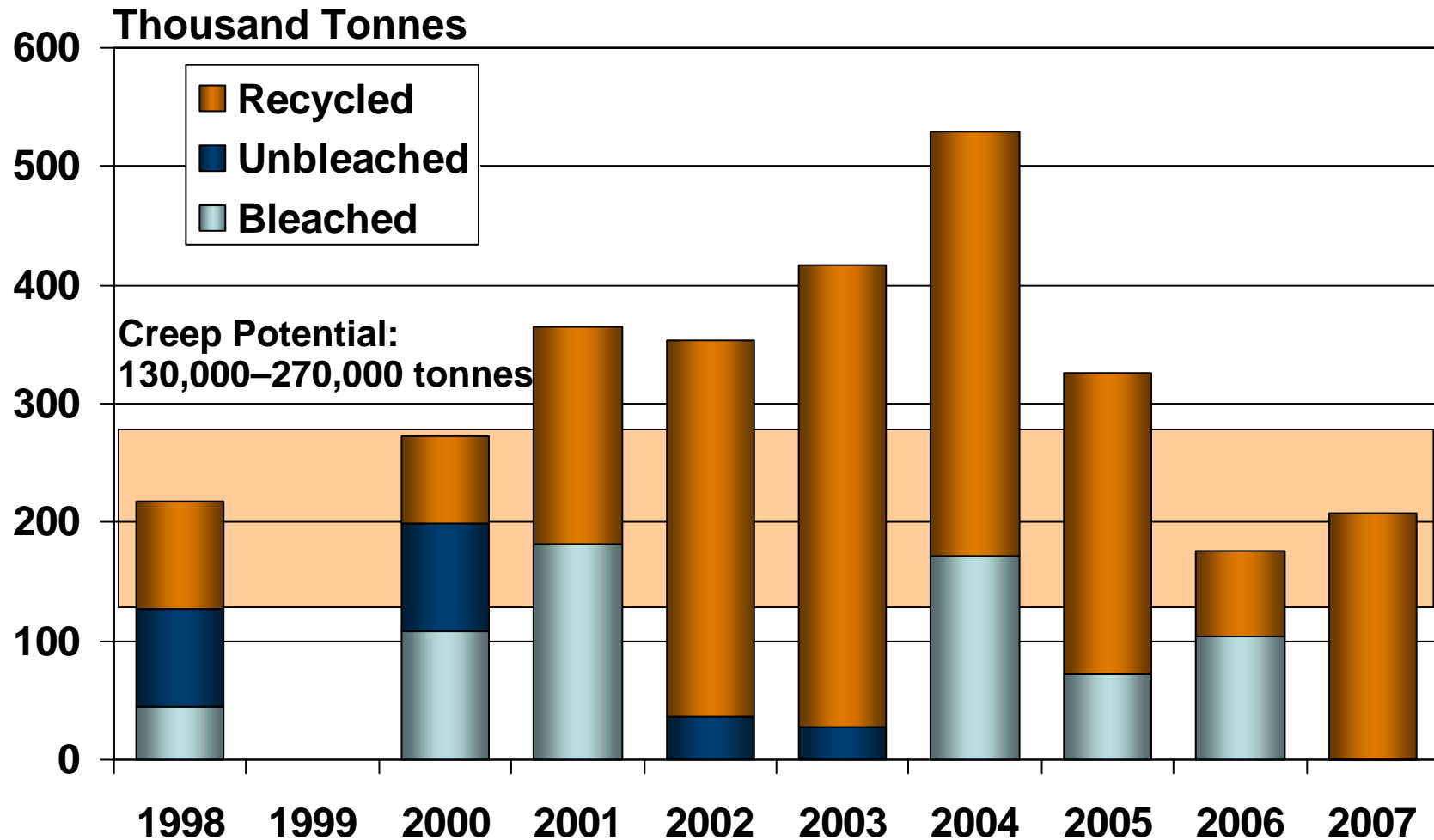
# U.S. Folding Boxboard Markets Are Facing a Much Bigger Threat from Imports than Containerboard



# The U.S. Is Expected to Face a Steep Increase in Folding Boxboard Imports



## Boxboard Capacity Closures Less Aggressive Than Containerboard, But Still Sizable



## **Conclusion: China Will Have a Large Impact on the Packaging Markets Between 2006 and 2008**

- ▶ Direct Impacts:
  - Weak domestic demand due to consumer goods substitution
  - Declining export demand
  - Threat of direct imports?
  
- ▶ Indirect Impacts:
  - Traditional suppliers to China will be displaced
  - Many of these markets experiencing strong capacity growth
  - Cartonboard facing huge threat of a shift in global trade
  
- ▶ Net Impact on North American Paper Packaging Production Will Be Negative