



**ABTCP-PI had about 13,000 visitations: all looking forward to what will happen in the sector after the crisis**

# Crisis exposes the advantages and challenges of Brazilian companies

*Demand for pulp grows, but the devaluation of the dollar worries exporters who should be more and more competitive to continue in the market. In the paper market, corrugated and tissue paper should continue on a high, while other segments search for renewal and new applications. With this scenario, executives and professionals debated at ABTCP-PI 2009 what the future holds for the pulp and paper sector in Brazil.*

**By Marina Faleiros**

*Just over a year ago, executives and professionals from the sector attempted to define during ABTCP 2008 what the world economic crisis was and what the consequences would be on the pulp and paper sector and in Brazil. Now, at the same venue at ExpoTransamerica in Sao Paulo, during ABTCP-PI 2009, the debates gained a new context, due to the impact and challenges being much clearer now and for the future. "Periods of crisis catalyze and accelerate changes, necessity promotes innovation and strong and weak points become more explicit", explains Carlos Farinha e*

*Silva, Senior Vice-President at Pöyry Tecnologia and one of the speakers at Panorama Setorial (Sectorial Overview), a panel that took place on the first day of the event.*

*On the list of advantages for Brazil in the production of pulp, forest productivity and low production costs continue in first place. On the other hand, the fall in the price of the commodity and the devaluation of the dollar have become of great concern at the moment, especially since sales have returned to normal levels, but the earnings are still greatly below the levels before the crisis. "Our production of pulp did not fall in 2009, much the contrary, for the year we registered a 16% increase in sales volume, but our income was 22% lower, being that our prognosis is for a further fall",*

explained Elizabeth de Carvalhaes, President of Bracelpa (Brazilian Association of Pulp and Paper).

This concern with the exchange rate influenced conversation and the latest balance figures of the sector. Suzano, as an example, sees a structural change in the post-crisis market, especially since, before the fall in the pulp price, the exchange rate rose and compensated for the losses, which is not the case this time, with a much slower improvement in price. "Around 80% of our costs are in Reals, and this is why the value of the Real worries us and we need to reduce costs to remain competitive" explains Antonio Maciel, the President of the company.

To avoid further losses, Suzano managed to reduce administration and sales spending by 24%, and the cost per ton of pulp today is around the R\$ 373 mark. "This value is already one of the lowest in the world, and 18% lower than in the third trimester of 2008. Our aim is to reduce it still more, so that we can continue in an advantageous commercial position" points out Investor Relations Director of the company, André Dorf.

In Farinha's point of view, the current recession is teaching many lessons, among them being that economical changes today are much faster and the companies that survive are the ones that pay attention, and not necessarily the largest ones. "In the pulp sector we already are in a better situation. We have to continue with the most efficient plantations in the world and the best forest technology", he says.

Even with the natural competitive advantages and good sales figures, Elizabeth points out that top economic analysts calculate that the world will consume 12% less of the product than in 2008, a figure that is difficult to interpret, but which also explains the downturn of prices. Until September, the sector produced 9.9 million tons of pulp, and the price fell

to US\$360 in March, today they are at US\$600. However, the devaluation of the dollar was much faster and did not compensate for the losses. "We recognize the improvement, but we cannot say that we are out of the crisis, because we have expressive losses of income and the exchange rate will be of great concern from now" she says. Elizabeth affirms that the prediction of the sector is that the price of the dollar will be around R\$1.50 and there is nothing yet that points to a change in this figure. "Not even the 2% tax on international capital, because with our high interest rates it is still worthwhile to invest money in the country" she explains.

Another major change in 2009 was the destination of exports. China used to account for 19% of sales, but now it accounts for 33% of Brazilian pulp sales. "If on one hand the country was our salvation to not entering into a deeper recession, on the other hand the growth of the Chinese market will continue to strengthen and we need to pay attention to this market and its necessities" Farinha affirms. The President of Bracelpa agrees, and even stresses that the growth of the Chinese market in 2008 reaches 84% in volume. The Asian market, she explains, even though it is still speculative – considering that in November last year they cancelled all buying of Brazilian pulp – brings good perspectives with the arrival of new machines and a real necessity by the country for pulp, since it does not have sufficient forest resources. "China wants to be a great seller of paper and needs good quality pulp, and even if they are currently stocking the commodity, the expectation is that they will continue to buy. What we do not know is if this movement will continue growing, in a constant and definitive manner" he explains.

According to Farinha's forecasts, the future of Brazilian eucalyptus pulp is guaranteed, as he calculates that the participation of short fiber could reach 80% in certain paper grades until 2015. "China, India and Russia should be responsible for 70% of the increase in demand of paper and cardboard between 2007 and 2025, and this favors eucalyptus pulp because of the differential in prices, different properties of fiber and in the advancement of paper machine technology".

### EYE ON THE FUTURE OF PAPER

Different theories try to predict what will happen with the consumption of paper from now on. Electronic readers such as Kindle, a portable screen that can store tens of book texts, are more and more popular and adopted by the new generations. The Internet, in part, is already responsible for the fall in pub-



lications of many newspapers and other types of print media. There are still doubts if the computer will be to the editorial market what the MP3 was to the music industry, which lost its traditional market and had to adapt to continue in the market without depending on the sale of CDs by its artists. "We cannot ignore what will come with new generations, which are much more adapt to new technology" Farinha points out.

According to the executive, the average annual growth of paper consumption decreased faster than the general economic growth, principally because of market saturation, substitution for other mediums of communication and changes in the technology of paper production, such as paper with lower weight. He believes that the idea that the paper business is only regional will not be true in the future as changes can occur at a much faster pace. "I have already seen APP exporting even tissue paper to Brazil, so these concepts of market can sooner or later be broken. We cannot be fixed to preconceived ideas if we want to have an important role in the global paper market" says Farinha.

In Kurt Brandauer's view, President of Paper Machines

Division at Voith, the greatest world producer of paper will be China in around five years, passing European producers. "In the short term, I believe that the paper market is becoming more specialized and there will be an expansion of emerging markets. But in the long term, what the sector needs is to search for alternatives for its investments and concentrate on the reduction of fixed costs such as energy, water, fiber and chemicals".

Farinha predicts that in a scenario of significant growth, world demand for paper and cardboard should reach 533 million tons until 2025. "But projections of medium or low growth indicate levels of 499 and 474 million tons respectively" he says, restating that the increase in production will be destined to different markets such as China, India, Russia and the Middle East. "This is why it is necessary that new innovations do not focus only on traditional markets, but that they also understand the necessities of these new, expanding regions".

In Latin America, his prediction is that the production of paper continues growing at an average annual rate of 3.1%.

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*“Between 2005 and 2020, there should be an increase of 10 million tons, reaching around 27 million tons of paper produced in the region by 2020.”*

*In the year of the crisis, the paper sector all around the world suffered from price and demand falls, and only a few have managed to recover completely. Brandauer states that the production falls in Europe vary according to the segment, being 17% lower for graphic paper and 10% lower for packaging paper. “Many companies chose to stop production instead of selling at much lower prices and all the major manufacturers had to close some plants, and it is because of this that it will take around three years to recover all losses”. In his opinion, the period of closures has not finished yet, as demand for consumption is still in a period of transition in some segments, such as in paper destined for written communication.*

*The impact of the recession is variable according to the type of paper. “In the United States, for example, sanitary paper sales grow even in times of recession, while news-paper material sees significant losses” points out Farinha. In Brazil, the crisis of 2009 resulted in a fall of 1.3% in the production of paper during the period from January to September, but there is a gradual monthly growth in tons. “There was a peak of 2.6% in the production in September in relation to the previous month, but still well below 2008 figures” explains Elizabeth.*

*Here, packaging paper has accumulated a loss of 3.2% and print paper is 11.3% down. Segments such as print, writing and tissue paper have already returned to positive figures. Paulo Peres, President of ABPO (Brazilian Association of Corrugated Paper) and ABRE (Brazilian Association of Packaging), explained that in total, over a period of 12 months until August, the segment of corrugated paper registered a reduction of 3.2% in volume, but since March the shipping of paperboard has increased. “Of great surprise was the month of September of this year, when we almost reached production peak, with 205 thousand tons shipped”.*

*In his opinion, Brazilian producers will comfortably survive this turbulent time since they have been working on the evolution of their technology for years now. “Before it was impossible to think of fluting paper of less than 120 grams, but today we have products of 80 grams” he says. Paperboard follows the same trend. Before, a certain board needed to be of 420 grams but today there are products of 350 grams that can package the same product without a loss of quality. “In this time of crisis, we need to think in technology that fits the consumer’s budget, and companies need to find reductions in costs in all areas as it is not enough to have a cheap product if the packaging is expensive”.*

## **The post-crisis world**

During the Sectorial Overview at ABTCP-PI 2009, executives discussed different factors that should influence the pulp and paper sector in the next few years. Confer some of them:

“ Subsidies for the sector in developed countries, as was done in the United States and Canada, should be one of the greatest barriers and sources of concern to maintain Brazilian competitiveness in the production of pulp”  
**Alberto Mori, President of ABTCP**

“The crisis did not change environmental awareness in consumption. To the contrary, the green image will be demanded more and more from companies and those that do not invest in this are condemned in the long term”.

**Carlos Farinha, Senior Vice-President at Pöyry Technology**

“There has been a remodeling of markets and new areas of sales have appeared. The post-crisis world will be more active, crueller, and more aggressive with competition, and it will be more difficult to sell our products”.

**Elizabeth de Carvalhaes, President of Bracelpa**

## **What would your company do if the dollar was worth R\$ 0.95?**

*This question was one that caused the most unease during the debates at ABTCP-PI 2009. The question was made by Gustavo Franco, partner and executive director at Rio Bravo Investimentos, and also ex- President of the Central Bank (BC), to the participants at the Siderquímica workshop, where questions were raised about the future for exporters if the Real continued to strengthen. “Imagine if your company has five years to prepare itself for an exchange rate of R\$ 0.95. What would you do to maintain your business?”*

*To him, the proposal is specific to each company and should portray the points in which it is possible to improve production or cost cutting. The government also needs to be active in this process, he believes, providing tools with which industries can survive this type of challenge, offering cheap infrastructure and helping in the training of a more qualified labor force and less stringent labor laws. “The post-crisis world is different, who does nothing will die, there are those that reinvented themselves, built plants in India, other changed their business, each case is unique, but Brazil has great natural advantages, and even with adverse exchange rate conditions there is no reason to believe that we do not have a way to sustain ourselves in the area of pulp” concludes.*

*Francó, however, affirms that the scenario is not encouraging for exporters, for now. “External demand fell and did not return, prices are low and the markets are bad. The profitability of exports is falling, because the exchange rate hurts now more than before and exporters have all the right to complain, because they have not yet earned back half of what the exchange rate has made more expensive” The bad news, he says, is that the price of the dollar will probably keep falling. If the scenario follows the last gains by the Real, there is still another 10% to 15% fall in the value of the dollar to come, which will depend on the action taken by the Government” he ends.*

*However, Franco stresses that companies that depend on international trade cannot focus only on the problems of the exchange rate, but must focus on the points that make them competitive, always searching for long term actions. “We want the companies to be competitive, but this cannot be only by the way of an artificial exchange rate, but from the elements that we are used to call the Brazilian cost”. He explains that this Brazilian cost starts at paying of taxes on investments and infrastructure, to the stringent labor laws, which make production more expensive. One of the principal actions that should be taken by the government is to help business people, show him the right path, and a reduction of taxes. “It is necessary to have national agenda to confront these challenges, an agenda with many reforms. It does not help to wait for the exchange rate to reach R\$1.50, when people will become worried, to begin to think about this”, he concludes.*

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**Francó: “We want to have competitive companies, but not due to an artificial exchange system”**