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INDUSTRIAL PRODUCTION IN BRAZIL – WHAT WILL 2018 AND 2019 BE LIKE?

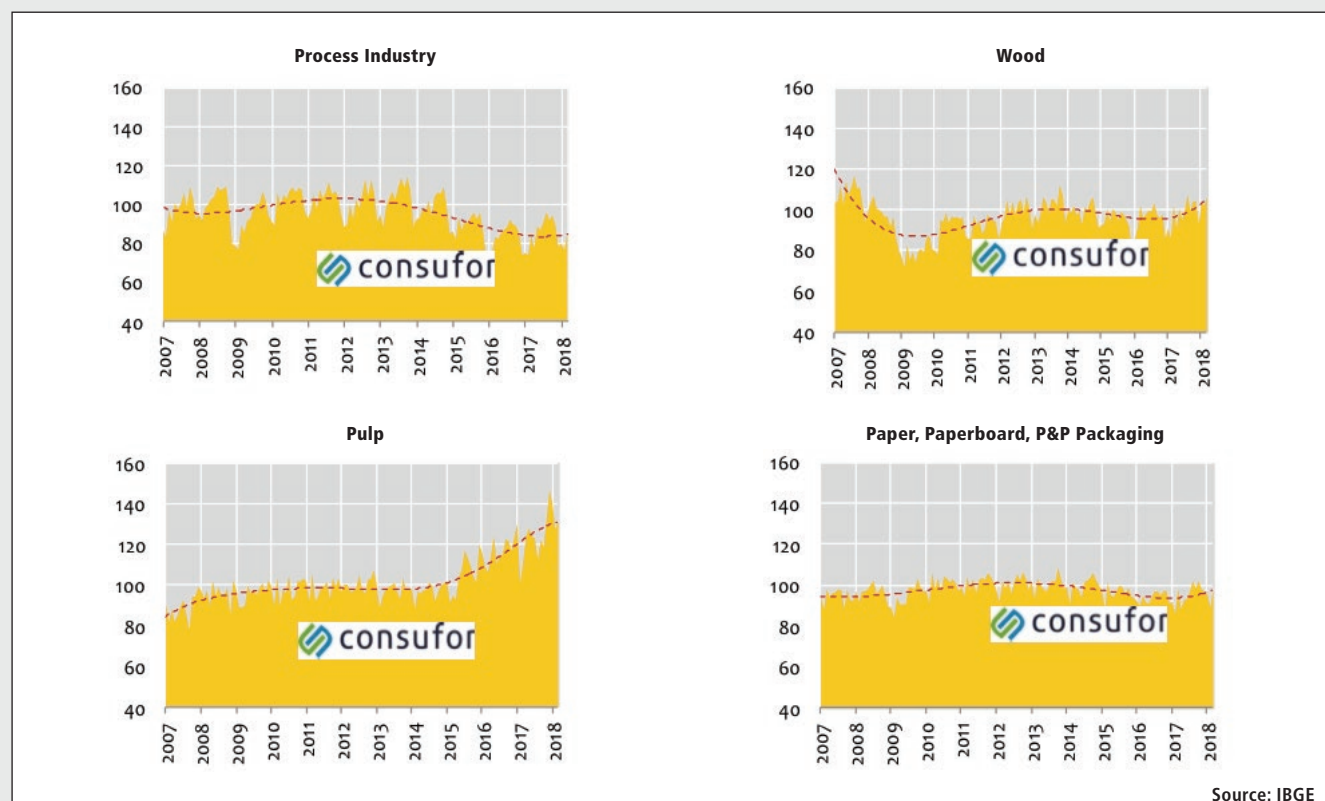
Analizing market conditions is a full-time job for those looking to understand the health of given productive sectors. Every month, in this column, CONSUFOR provides readers a series of analyses regarding the pulp and paper productive segment.

Taking advantage that official data on Brazil's industrial production was recently divulged for the first quarter, CONSUFOR presents this month a comparison of industrial production behavior in Brazil over the last ten years.

Figure 1 shows the evolution of Brazil's industrial production

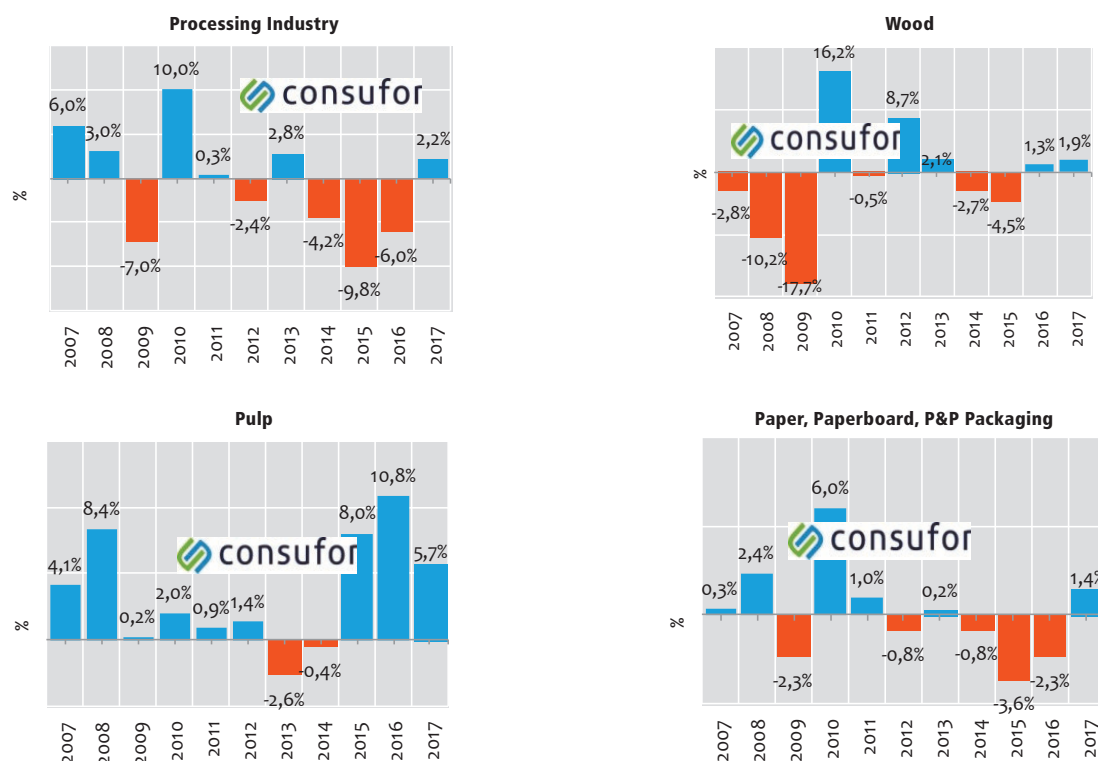
over the last decade together with the 1st quarter of 2018. In addition to the Pulp and Paper, Paperboard and Paper and Paperboard Packaging Industries, this figure also shows the average production behavior of the country's Processing Industry, together with the Wood Industry. For comparison purposes, production levels for 2012 equal 100.

Looking at general data on the Processing Industry, we see a clear reduction in production levels as of 2013, showing signs of stability in the beginning of 2018. In turn, the Wood Industry experienced a small retraction between 2014 and 2016,



Source: IBGE

Figure 1. Industrial Production Evolution (2012 average = 100)



Source: IBGE

Figure 2. Industrial Production Evolution (% variation in relations to previous YEAR)

recovering as of 2017. However, it's important to point out that the industrial production peak of this segment occurred in 2005, due to exports. Since the global financial crisis (subprime crisis in the USA), the Wood Industry never again resumed its former production level.

On the other hand, the Paper, Paperboard and Paper and Paperboard Packaging Industry has maintained regular production levels throughout the time horizon analyzed, with a small drop in 2014, but with recovery signs as of 2017. Lastly, production in the Pulp Industry remained stable between 2010 and 2014. Since then, this industrial segment has been breaking new production records year after year.

The question now is what paths will these industries follow in 2018/2019? Figure 2 shows that the growth rhythm (variation year by year) in Pulp production already shows signs of slowing down. The Paper, Paperboard and Paper and Paperboard Packaging Industry began demonstrating the same general behavior as the Processing Industry over the last four years, but with less amplitude: three consecutive years of negative growth, and the latest with positive growth. In turn, the Wood Industry has accumulated the last two years with positive annual growth.

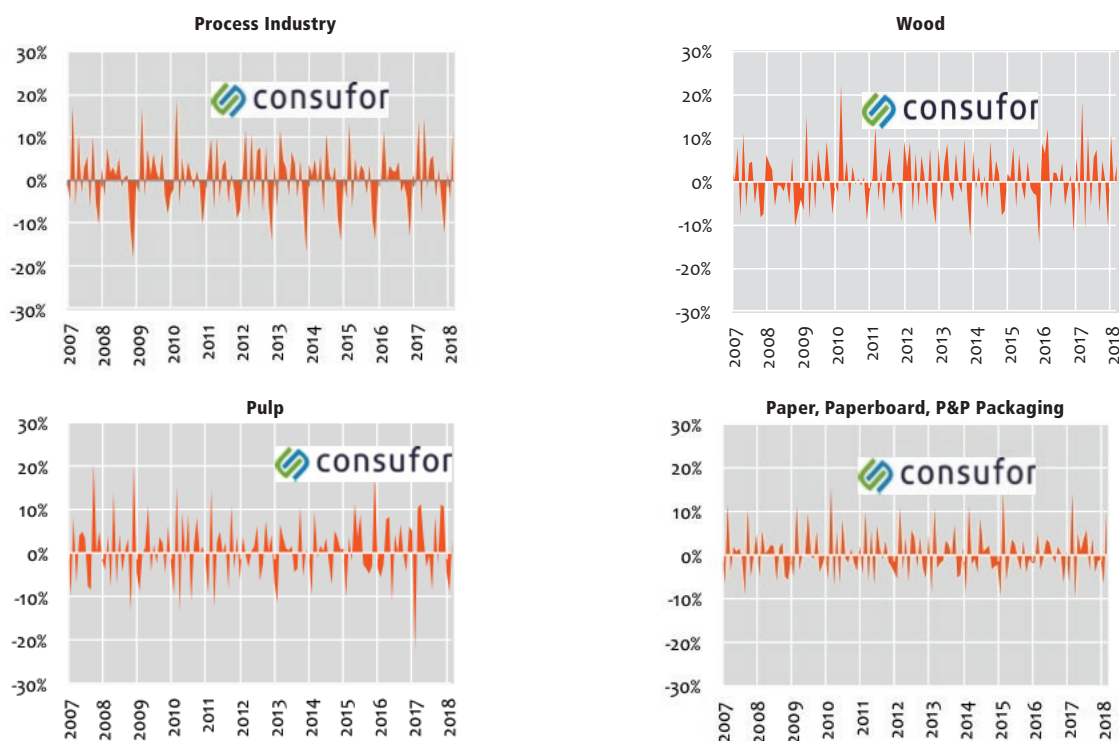
According to these statistics, the segment with the most

favorable situation, among the industries selected, is the Pulp Industry. Maintaining the scenario observed over the last few years, 2018 and 2019 are expected to be growth years, albeit at levels slightly below those registered in recent years. In turn, the Paper, Paperboard and Paper and Paperboard Packaging Industry can continue its growth trajectory, as long as the economy's general indicators remain positive, in view that each year it posts the same evolution signs as the Processing Industry.

If the positive growth in the country's economy continues, the Wood Industry shall also maintain its growth trajectory. If not, it's improbable that exports alone will guarantee the segment's continued industrial production growth.

To conclude the analyses, Figure 3 shows the industrial production evolution according to monthly variation. This analysis is important to check the effects of production seasonality on each month.

The data shows that, overall, the Processing Industry shows obvious signs of seasonality. During practically the entire time horizon of analysis, the 1st semester is represented by production growth and the 2nd semester by a retraction in industrial activity. This means that the country's industry is usually more active in the first semester than the second.



Source: IBGE

Figure 3. Industrial Production Evolution (% variation in relation to previous MONTH)

In the Wood Industry, this same seasonal movement existed until the middle of 2010, but has not been as evident in recent years. It's obvious that the 1st semester generally represents a peak period of industrial activity. However, it's clear that there are several production growth peaks and retractions in industrial production throughout each year, causing production levels to vary considerably. This increases the complexity of the industrial Processing significantly, since it directly impacts inventory controls and cost levels.

The same situation occurs in the Pulp and Paper, Paperboard and Paper and Paperboard Packaging Industries. In general, the 1st semester comprises the months with positive industrial production peaks. In turn, the 2nd semester registers several months with production drops. Additionally, positive and negative peaks are frequent in all years.

But what can be concluded from the data and analyses?

Considering the data behavior from previous years and figures for the 1st quarter of 2018, it's quite probable that industrial production levels will continue to grow in 2018-2019. Clearly, projecting the future looking only through the rear-view mirror is risky and premature, since no statistical or strategic-based forecasting exercise was performed here.

Nonetheless, in an abbreviated analysis, if Brazil's macroeconomic scenario continues as it is, it's possible to conceive that production levels will continue to increase in the country, but at more restrictive levels than in the past. Additionally, it's important to keep in mind the seasonal effect on production evolution. The relative "good" signs observed in the beginning of 2018 do not mean the same standard trajectory for the industry in the entire year, since the second semester usually operates at a slower pace. Nonetheless, the most important is to see that the country's industry is seeking ways to remain competitive and operating. ■

CONSUFOR provides business and strategic consulting, and specializes in the wood industry, pulp and paper, bio-energy, steelworks, forestry and agribusiness sectors. CONSUFOR develops services in the following business areas: Mergers and acquisitions, Market intelligence, Diagnostics and strategy, and Business engineering.

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