



**CHEMICAL MARKET  
PULP SERVICE**

**JUNE 2004**

**FLASH REPORT:  
MONTHLY  
STATISTICS**

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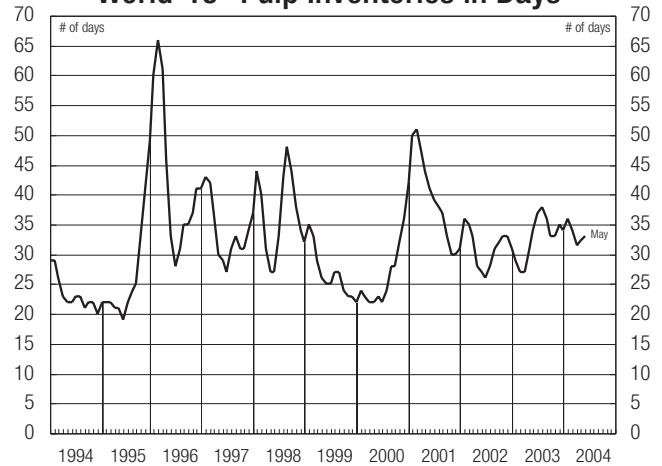
MICHEL VALOIS, MBA

- World-19 inventories fell by 14,000 tonnes in May to 3,397,000 (33 days' supply — 29.9 for bleached softwood kraft, up from 28.8 in April, and 34.8 for its hardwood counterpart, unchanged from the previous month).
- The ten-year average inventory change is a decline of 123,000 tonnes; five-year change is -47,000 tonnes.
- Bleached softwood kraft stocks rose 33,000 tonnes to 1,589,000, while hardwood inventories fell by 51,000 in May to 1,531,000. Unbleached stocks rose 5,000 tonnes to 209,000, while sulphite inventories fell by 2,000 to 68,000.
- Despite 100,000–125,000 tonnes of cancelled or delayed maintenance downtime, outages reached 337,000 tonnes in May, up from a revised 215,000 in April.
- Production in May reached 3,127,000 tonnes (94% operating rate), up from April's 3,082,000 and up 9.6% from a year earlier.
- Shipments in May reached 3,142,000 tonnes, up 6.3% from April's result (95% shipments-to-capacity); year-ago shipments were a disappointing 2,702,000 tonnes.
- Year-to-date shipments are 7.0% ahead (+1,035,000 tonnes) versus 2003, while production is 5.3% higher (+792,000).
- Chinese imports reached 480,000 tonnes in May expectedly, down from April's record-setting 641,000.
- NBSK prices in Western Europe were on the rise in June, averaging \$660, up from \$640 in May. In the U.S., NBSK prices have risen faster than in other markets and are at a reported \$680. In Asia, NBSK was still \$630–\$650 at the end of June. Many hardwood and some softwood deals were concluded in the last few days of June.
- Consumers' inventories fell marginally in May (-69,000 tonnes) following a period of strong consumption and lower purchases, as some consumers tried to draw a line in the sand regarding higher prices. Utipulp stocks fell by 28,614 tonnes in May to 1,272,641 (32 days' supply). U.S. consumers' stocks fell 38,000 tonnes to 333,000.
- Europulp stocks fell 14,580 tonnes in May to 1,470,815.
- Aggregate producers' and consumers' stocks decreased by 83,000 tonnes to 5,233,000 tonnes; at 4,945,000, the year-ago level was 288,000 tonnes lower.
- Inventories of printing & writing paper in the U.S., Western Europe and Japan fell by an estimated 51,000 tonnes in May to 4,656,000.
- Order inflows into western European paper mills are improving rapidly, but capacity remains an issue for coated woodfrees (and coated mechanicals). After week 25, year-to-date uncoated woodfree orders are up 3.5% (118,750 tonnes) versus 2003, while coated woodfrees' are up 9.4% (384,650 tonnes).
- Western European consumers will be entering Q3 with "normal" pulp stocks and the intention of putting additional pressure on suppliers as their margins continue to suffer. However, suppliers — whose stocks normally rise in July and August — are expected to be able to resist as world economies continue to improve, and as China remains in a strong growth mode.

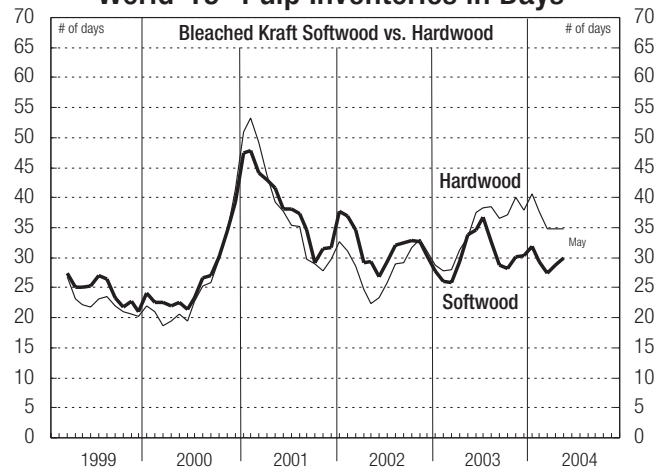
## WORLD-19\* PULP INVENTORIES IN DAYS • HARDWOOD KRAFT STOCKS AS A % OF TOTAL BLEACHED KRAFT INVENTORIES

- Despite a 6.3% increase in shipments in May over April's results, World-19\* producers' days' supply rose to 33 days, up from 32 a month earlier, due partially to statistical anomalies. While bleached hardwood stocks fell by 51,000 tonnes — leaving producers with 34.8 days' supply at the end of May (unchanged from April) — bleached softwood stocks rose 33,000 tonnes, leaving suppliers with 29.9 days' supply, up from 28.8 in April.
- For the first time since August, bleached hardwood kraft inventories were lower than their softwood counterpart. The main reason for the decline was the price differential between the two grades: it prompted consumers to buy more hardwood and pushed pulp producers to swing as much capacity as possible to softwood output. Should this trend continue, we could actually see a reduction in the price differential between the two main grades by year-end.

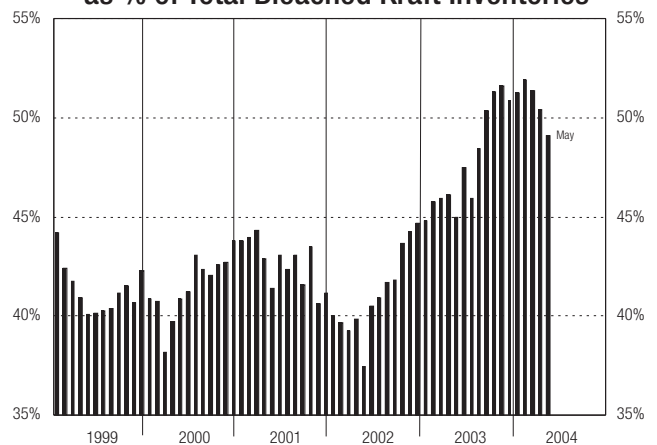
**World-19\* Pulp Inventories in Days**



**World-19\* Pulp Inventories in Days**

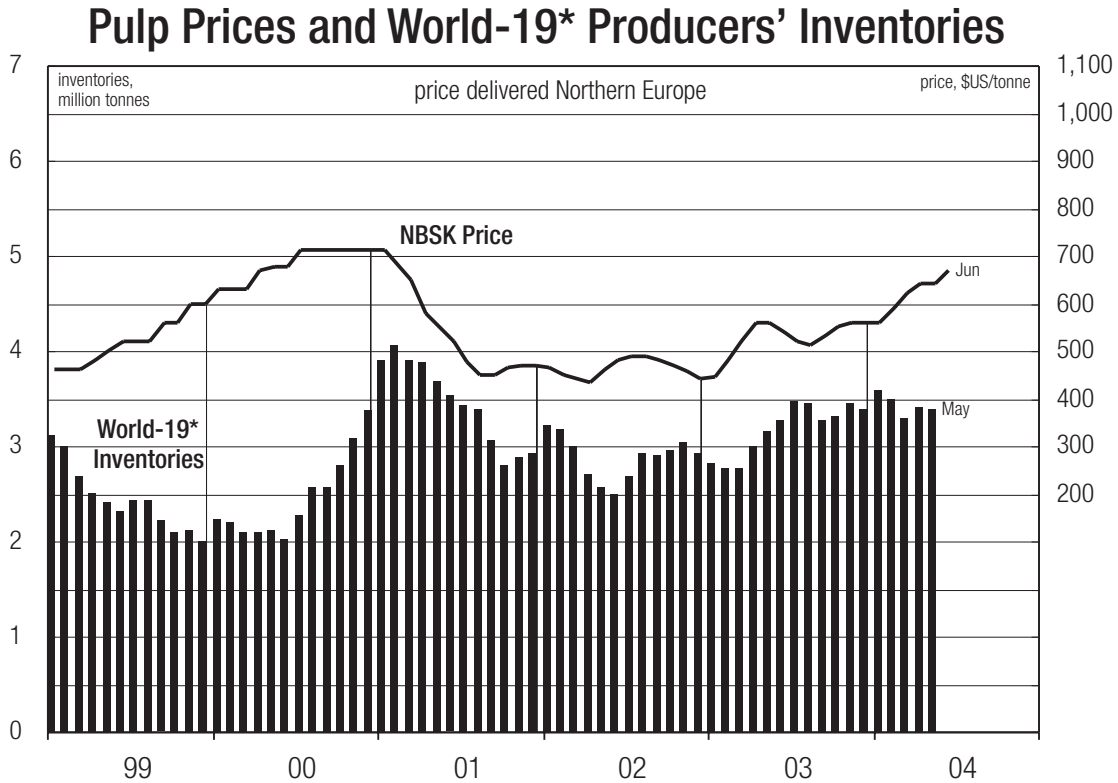


**World-19\* Bleached Hardwood Kraft Stocks as % of Total Bleached Kraft Inventories**



\*World-19 includes Canada, the U.S., Sweden, Finland, Norway, Argentina, Austria, Brazil, Chile, France/Belgium, Japan, South Korea, South Africa/Morocco, New Zealand, Portugal, Spain and Swaziland.

# PULP PRICES AND WORLD-19\* PRODUCERS' INVENTORIES



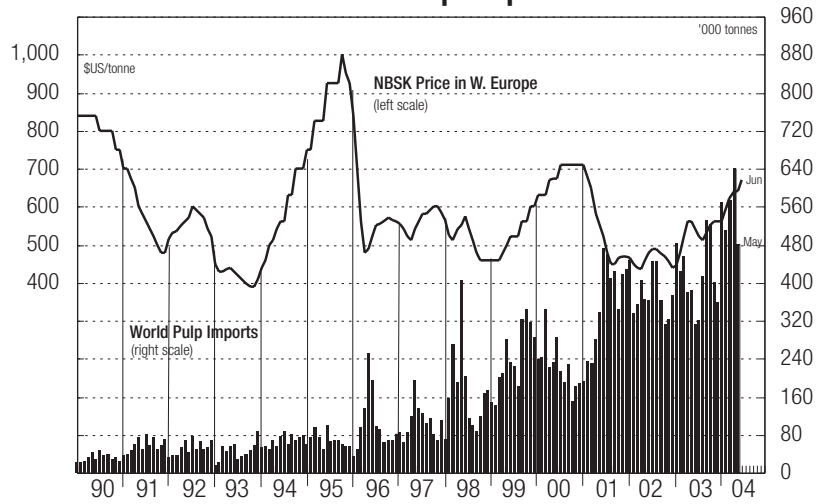
- While producers' stocks were essentially unchanged at the end of May in comparison to April, not all mills are as well stocked as the figures would suggest. Mills coming out of maintenance downtime have informed their customers that supply is limited and therefore prices are up. The message is, "take it at the higher price or leave it — someone else wants it." For those mills going down in June or July, the pressure to reduce prices simply is not there as much as some desperate customers would like to believe.
- Rumbblings out of Southern Europe and Asia would indicate that customers are getting ready to turn off the tap. Although the rhetoric is sometimes nasty, consumption remains strong, stocks are only high if hardwoods are considered.
- Historically speaking, producers' stocks are not low — but they are under control. For NBSK prices to come down, we would have to see producers' stocks well in excess of 3.5 million tonnes. Given that the weakest link in the chain has been bleached hardwood kraft, and that producers' stocks of this grade have fallen in May (while softwoods' rose slightly), the market appears to be fairly well balanced.

\*World-19 includes Canada, the U.S., Sweden, Finland, Norway, Argentina, Austria, Brazil, Chile, France/Belgium, Japan, South Korea, South Africa/Morocco, New Zealand, Portugal, Spain and Swaziland.

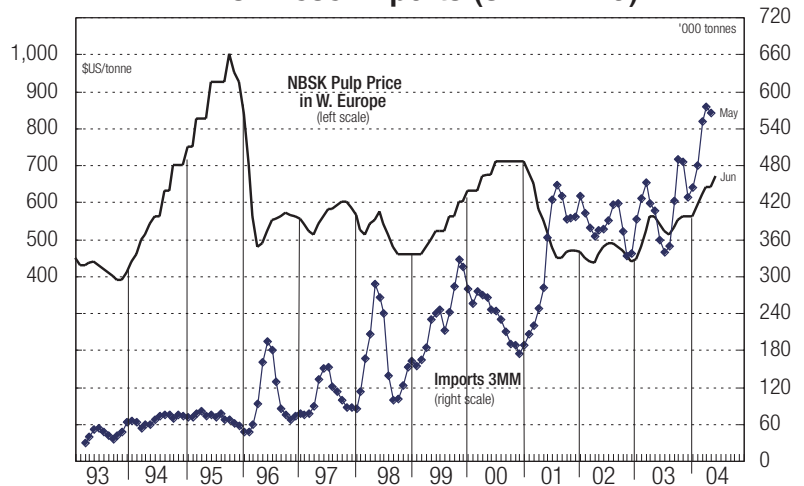
## CHINESE PULP IMPORTS

- As expected, Chinese imports fell following a very exciting period of record-setting levels in the last five months. Imports reached 480,000 tonnes, down from 641,000 a month earlier and still indicating robust buying (driven by equally strong consumption).
- Year-to-date imports have reached 2,772,000 tonnes, a 59.3% increase over 2003. Obviously, this growth in imports is unsustainable, therefore producers had anticipated what has now occurred. Imports are expected to level out during Q3, but not fall dramatically since buyers do not hold enormous stock positions (i.e., such that they could retrench from the market for months).
- The latest results and those expected in June and July have helped to keep pulp prices flat in China and the rest of Asia; since February, China and other markets have experienced premium pricing as compared to Western Europe and even the U.S. By not increasing in June and possibly July, buyers in China are likely to be paying prices closer to the transaction levels found in other markets.
- The three-month moving average imports figure fell to 564,700 tonnes, down slightly from 574,400 a month earlier and still historically very strong.

### Chemical Market Pulp Imports to China



### Chinese Imports (3 MM AVG)



*\*World-19 includes Canada, the U.S., Sweden, Finland, Norway, Argentina, Austria, Brazil, Chile, France/Belgium, Japan, South Korea, South Africa/Morocco, New Zealand, Portugal, Spain and Swaziland.*

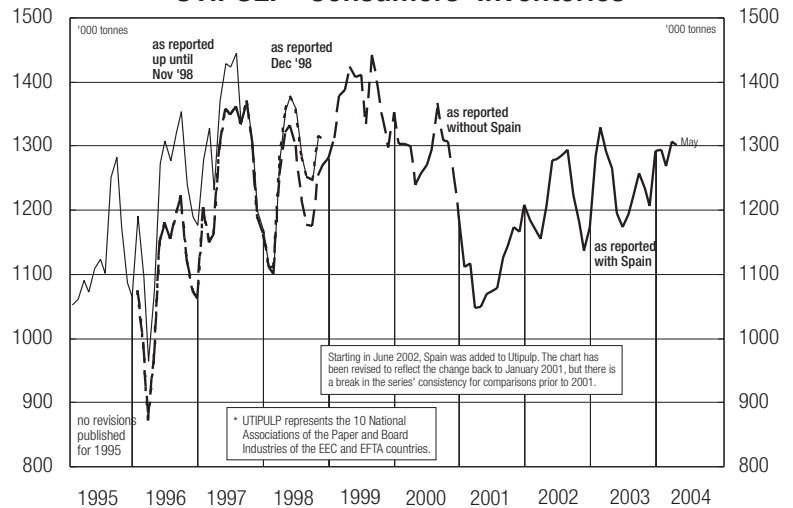
## UTIPULP AND EUROPULP

- Despite a year-over-year slowdown in May for consumption (-5.5%), Utipulp stocks declined 28,614 tonnes to 1,272,641. Bleached softwood kraft consumption rose 8,781 tonnes versus April, but fell 28,489 versus a year ago. Bleached hardwood kraft consumption rose 9,098 tonnes versus April and 9,585 versus May/03. The increased use of hardwood confirms that consumers switched to lower-cost pulps and shied away from the more expensive softwoods. This represents the economic side of pulp blends in the mix, but we continue to believe that the technical or performance-related balance has not been affected by the larger-than-usual price differential between softwood and hardwood pulps.

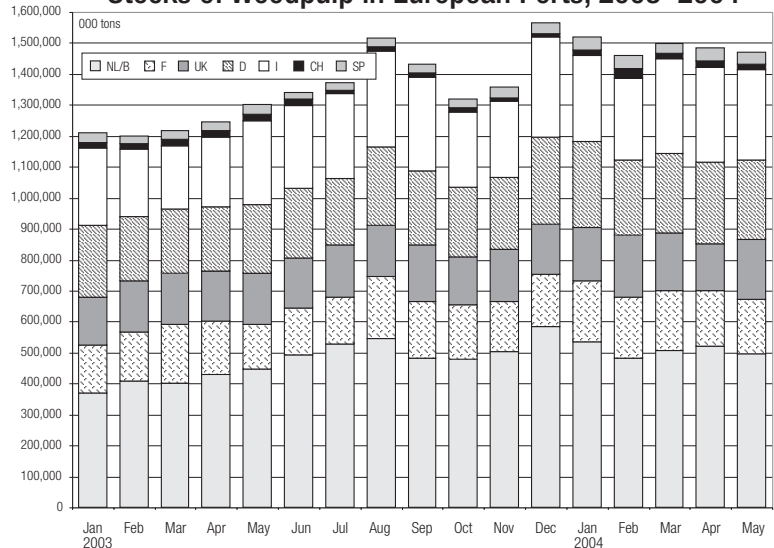
- While paper and tissue prices had not risen very much in 2004, consumers in Western Europe (and elsewhere) reportedly were concerned about rapidly rising pulp prices, to the point where purchases were down. In fact, two western European paper mills have either shut operations — and therefore stopped buying pulp, having gone into receivership — or announced closures to take effect later this year due to poor economics. Even sellers have indicated that they've begun to tighten credit lines in anticipation of future cash-flow problems among some of their customers in Western Europe.

- Although such paper-machine closures are difficult for all involved, they are a necessary evil in rebalancing the market. Excess capacity has driven down paper prices in recent years, and unlike paper operations in the U.S., Western Europe has yet to seriously rationalize its industry.

### UTIPULP\* Consumers' Inventories



### Stocks of Woodpulp in European Ports, 2003–2004



- At the end of May, Utipulp stocks were 6.6% above the year-ago level, while days' supply reached 32 days (unchanged from April), versus 30 a year ago. This confirms the assumption in our forecast that consumers have been able to build stocks.

\*World-19 includes Canada, the U.S., Sweden, Finland, Norway, Argentina, Austria, Brazil, Chile, France/Belgium, Japan, South Korea, South Africa/Morocco, New Zealand, Portugal, Spain and Swaziland.

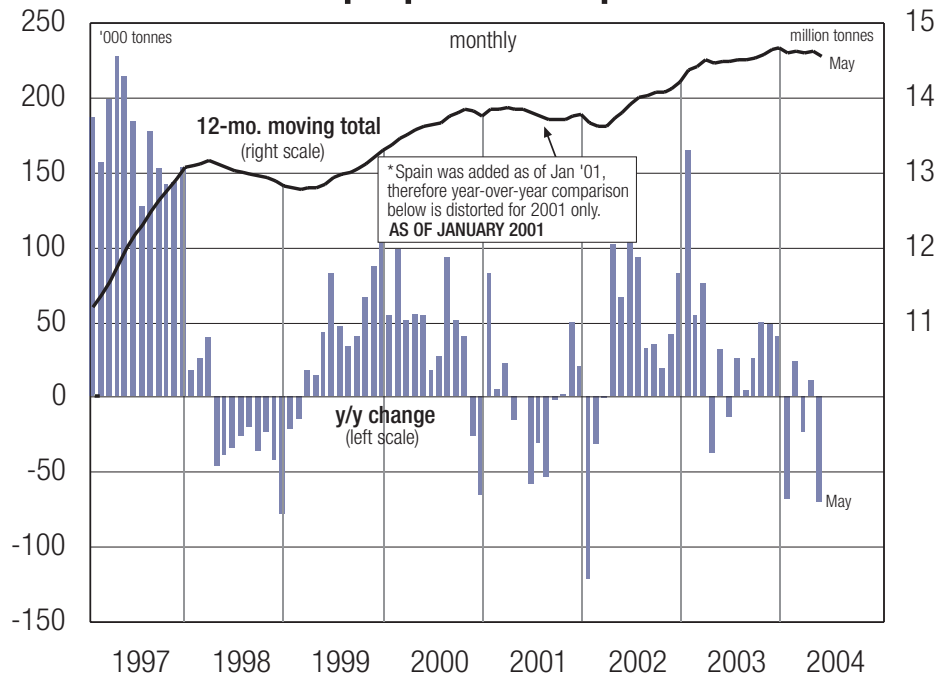
## UTIPULP AND EUROPULP cont'd

- Europulp stocks fell marginally in May (-14,580 tonnes) to 1,470,815 tonnes, mainly because pulp producers in aggregate took significant amounts of maintenance downtime during the month and were not filling port warehouses. As a result, buyers were less successful than they wanted to be in trying to hold prices in June.

- Because many consumers chose to buy or take less pulp out of the ports in May, and stocks fell in all countries with the exception of the U.K., producers appear to remain in control of the market; however, as everyone knows this could change quickly.

- Changes by country in May were as follows: Netherlands/Belgium, -25,595 tonnes; France, -2,285; United Kingdom, +40,845; Germany, -4,825; Switzerland, -2,270; Italy, -14,590; and Spain, -5,860.
- For several months, consumption on a twelve-month moving-total basis has either stopped rising or fallen slightly. Although the decline is not alarming, it does mark an end to what pulp producers were

### Utulp Consumption\*



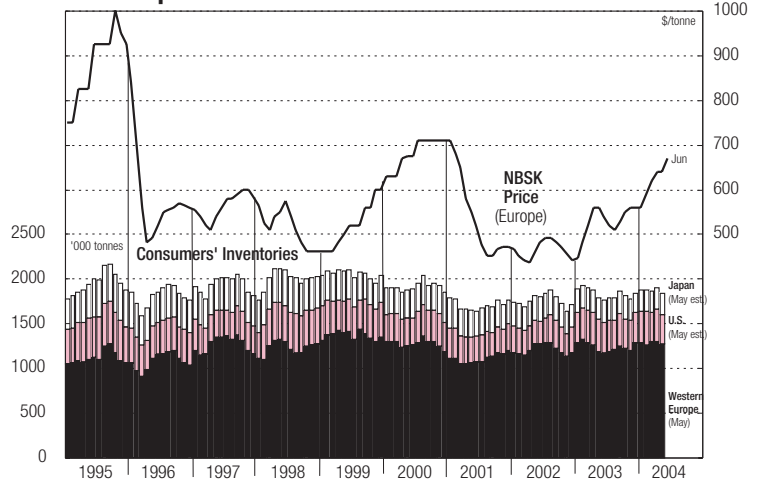
experiencing: rising demand as consumers were fighting for market share. Now that consumers are suffering from poor prices and sometimes negative margins, and some facilities have been forced to close, consumption appears to be marginally in decline in Western Europe.

- Consumption year-over-year is down by 5.4% (70,000 tonnes); year-to-date it is down by 2.0% (127,000).

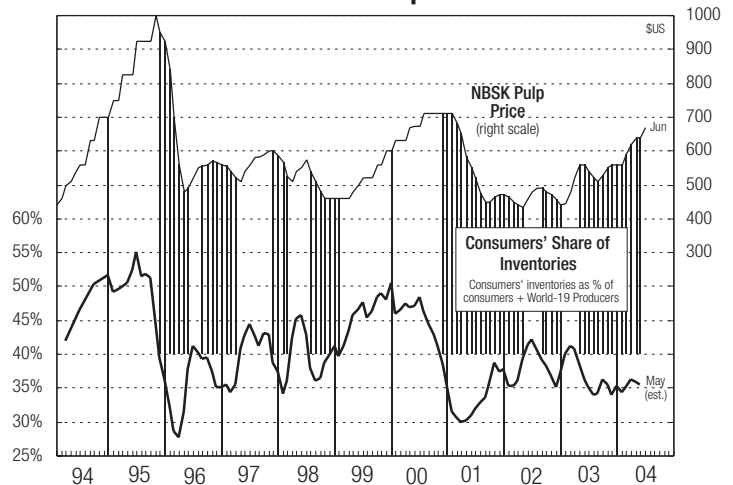
## PULP PRICES AND CONSUMER INVENTORIES & CONSUMERS' SHARE OF PULP INVENTORIES vs. NBSK PRICES

- Apparently consumers at the beginning of May believed they had enough pulp in inventory that they wanted to try sending a message to suppliers. But several consumers were in a predicament over just how big a message to send when consumption was rising versus April and paper and tissue prices were also increasing (however, paper prices were falling in Western Europe).
- At 1,836,000 tonnes, May's lower consumer total versus April (-69,000 tonnes) was partially the result of fewer purchases in late April and to some extent early May by Utipulp members; however, as the Vancouver meetings ended, consumers were not convinced that June's price increase was dead.
- Historically speaking, we could say that consumers' stocks are above normal, but economic recovery in many markets has raised the bar. Therefore, consumers may feel much more comfortable about supply and thus decide to destock once their inventories reach levels similar to those found in 1998 and 1999. For now, however, we do not foresee them destocking.
- Consumers' share of pulp stocks fell in May to 35.1%, down from 35.8% a month earlier as a result of their inventories falling faster than those of producers.

**Pulp Prices and Consumers' Inventories**



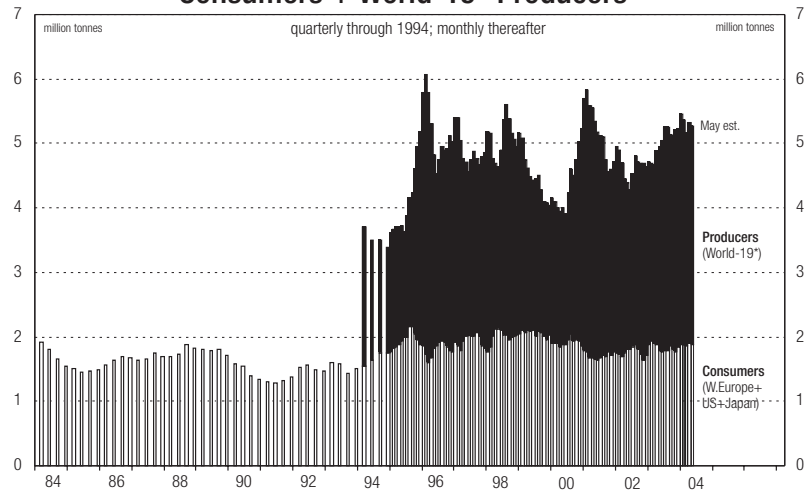
**Consumers' Share of Pulp Inventories vs. NBSK Pulp Prices**



## AGGREGATE PULP INVENTORIES • CONSUMERS + WORLD-19\* PRODUCERS

- With producers' and consumers' stocks having fallen by a combined 69,000 tonnes in May, the pulp market was a little less supplied than it was in April. Was it enough to keep prices moving up? The answer, obviously, is "yes," since they did continue to rise; but the rise was also justified given that consumers in general were demanding and consuming more pulp.
- In total, aggregate stocks stood at 5,233,000 tonnes at the end of May (the year-ago figure was 288,000 tonnes lower), down from 5,316,000 a month earlier. Compared to 2002 and 2003, the market is still better-supplied, but demand is up and producers have a compelling need and desire to satisfy consumers — especially when prices are

### Aggregate Pulp Inventories, Consumers + World-19\* Producers

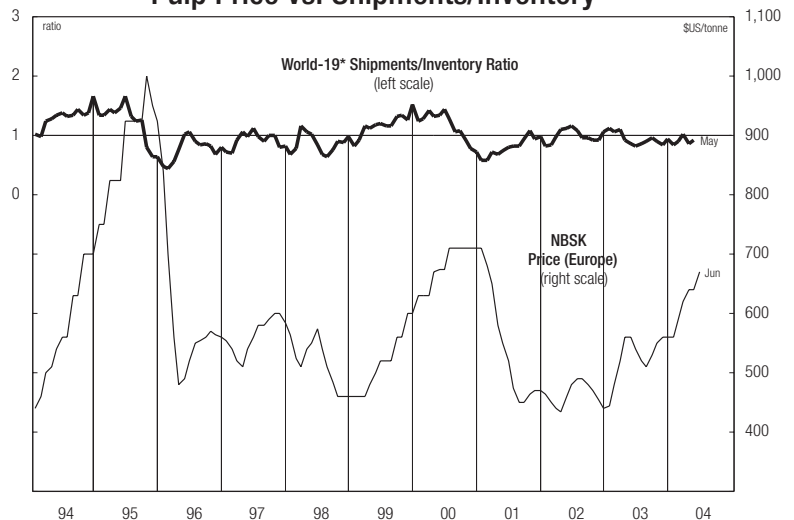


rising. As long as consumers continue to pay the higher prices and producers' stocks are in control, the market is not about to turn sour for suppliers.

## WORLD-19\* SHIPMENTS/INVENTORY RATIO vs. NBSK PRICE

- Pulp prices have been rising essentially since the beginning of 2003 — if one excludes the SARS-related dip experienced about a year ago. During this period, demand has improved steadily and supply has been more than adequate insofar as hardwood is concerned, though not in terms of softwood. Furthermore, even the swing capacity has done little to cool the tight softwood supply/demand balance. This is what has kept NBSK prices rising despite the fact that the shipments-to-inventory ratio has been relatively flat. In the end, the moderating factor here has been pricing, and as long as the S/I ratio remains in such a narrow range the market continues to be healthy.

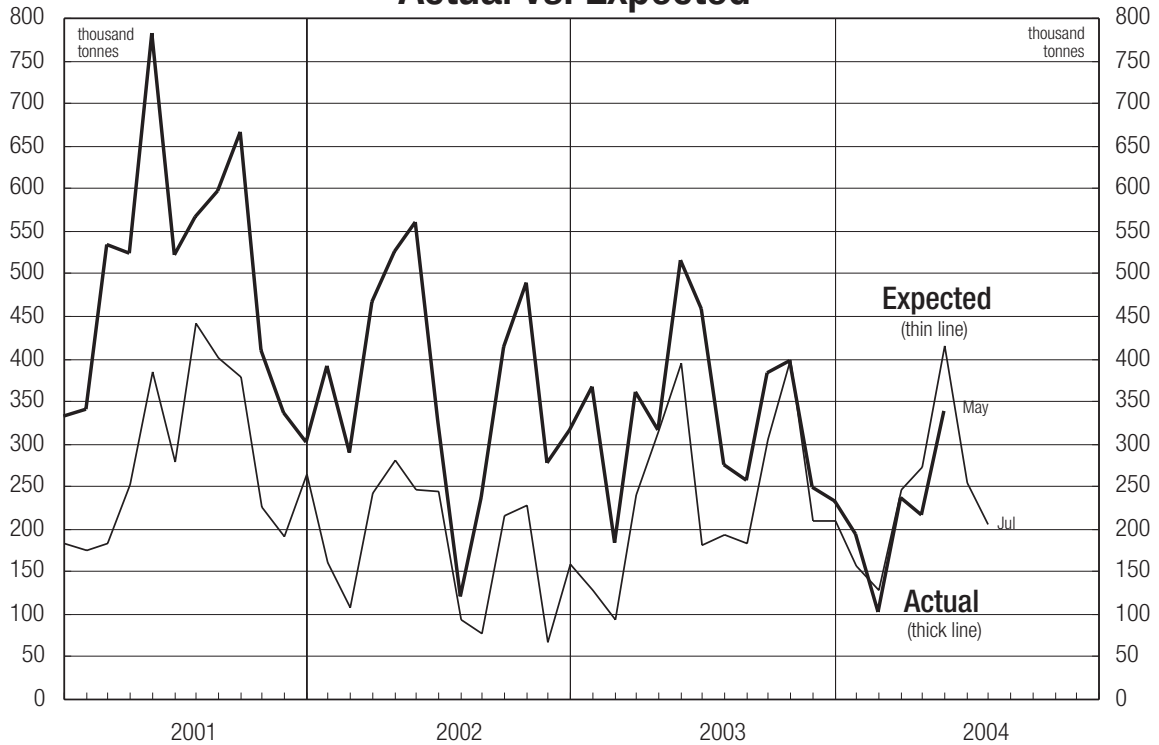
### Pulp Price vs. Shipments/Inventory



\*World-19 includes Canada, the U.S., Sweden, Finland, Norway, Argentina, Austria, Brazil, Chile, France/Belgium, Japan, South Korea, South Africa/Morocco, New Zealand, Portugal, Spain and Swaziland.

## ACTUAL vs. EXPECTED DOWNTIME

### World Chemical Market Pulp Downtime Actual vs. Expected



- In May, downtime reached 337,000 tonnes — less than previously expected — as some mills decided to temporarily cancel their outages to take advantage of strong demand. Some 100,000–125,000 tonnes of downtime were delayed or cancelled, according

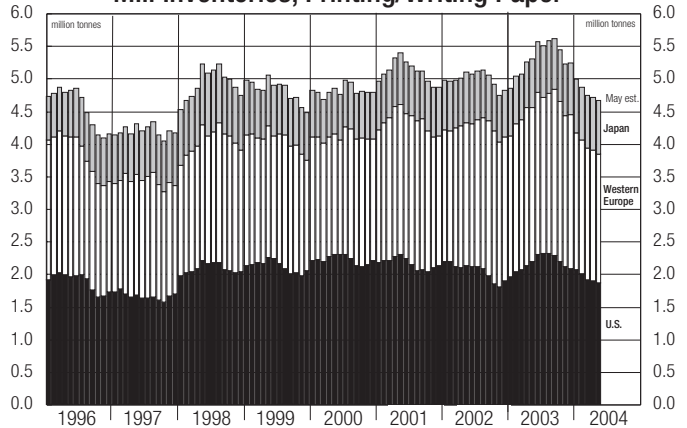
to our best information. Most of the “missed” outages will eventually have to be taken, but the longer the delay the greater the risk that unplanned downtime will impact supply negatively.

## DRIVERS OF DEMAND

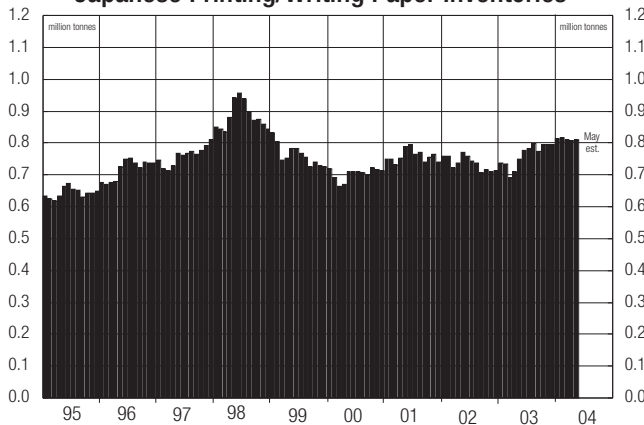
As we have alluded to previously in this report, pulp demand has been on the rise over the last eighteen months. We can all remember the strong spike in demand caused by China in December/02 that sent consumers in several markets into a panicked state of buying ahead of price increases. Since then, we have seen pulp consumption in total rise as paper, tissue, packaging and other end-use markets improve in line with economic growth and recovery. China has been a large contributor to the much-improved pulp market — but this is nothing new: it has simply reached new proportions in 2004, given that pent-up demand has largely been satisfied following the SARS outbreak in early 2003.

Today, growth in pulp demand appears to have reached a plateau or has not been growing as fast as some observers would like. To all growth spurts there comes

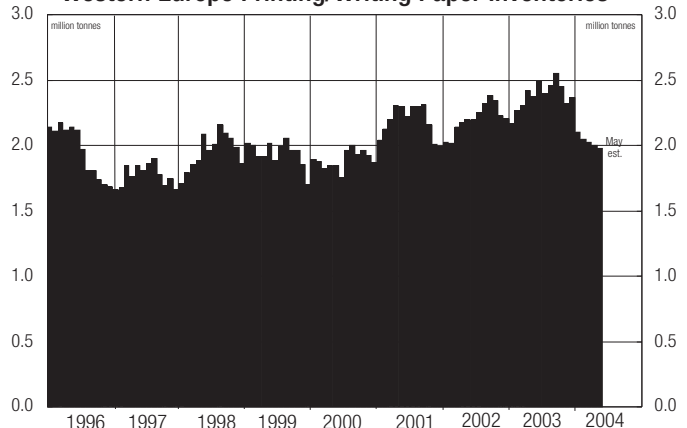
**Mill Inventories, Printing/Writing Paper**



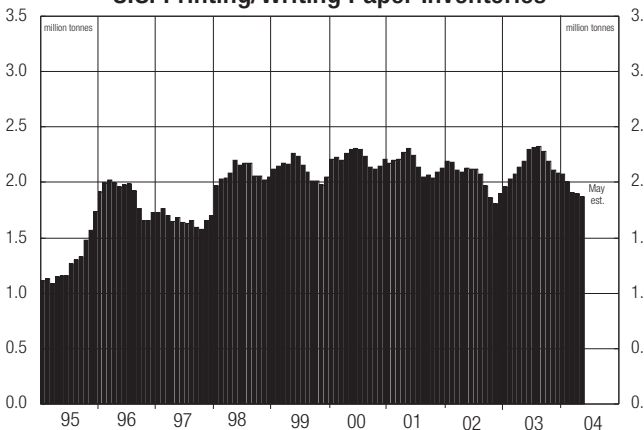
**Japanese Printing/Writing Paper Inventories**



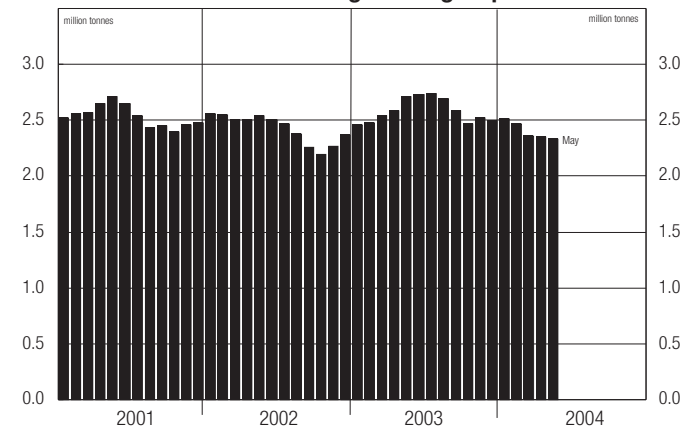
**Western Europe Printing/Writing Paper Inventories**



**U.S. Printing/Writing Paper Inventories**



**North American Printing/Writing Paper Stocks**



## DRIVERS OF DEMAND cont'd

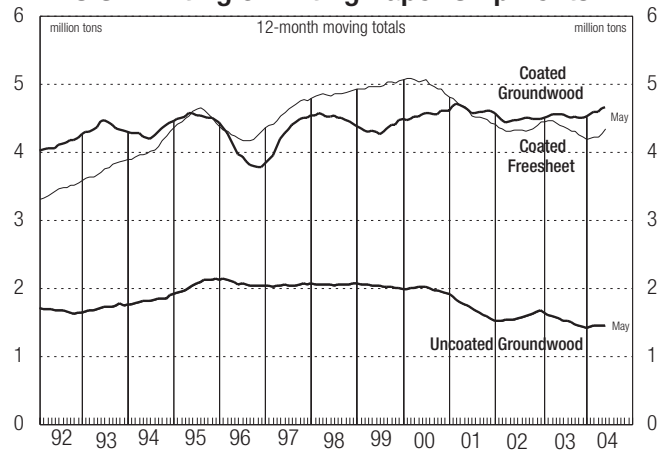
an end, and maybe even a period in which demand actually falls as consumers destock and take a breather. But where is this occurring? Not in the U.S., Japan or China (except normal declines following several record-setting months in recent times) — or in many other markets. It is happening mainly in Western Europe, where paper supply continues to outpace demand by more than a comfortable margin, preventing prices from rising; in fact, they have tended to decline even when prices for identical products have been rising in other markets! This is a western European phenomenon, and the industry will eventually have to deal with its overcapacity just as U.S. players have had to in recent years.

Nonetheless, pulp demand remains strong, and in May and June experienced a seasonal pull. It could be that during Q3 we see a decline in demand caused by prices having risen too far too fast for some consumers. Welcome to the marketplace! As always, producers will adjust and the market will find its new balance, as it always does. Price is the moderator here, and consumers will eventually have their say. But, for June and going into July, pulp prices are holding the trend toward higher levels.

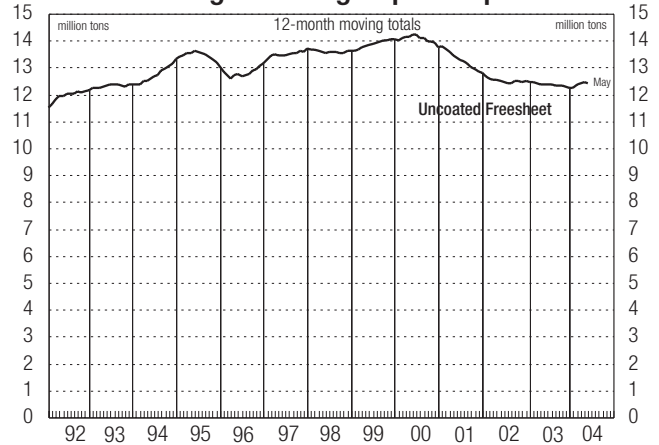
U.S. printing & writing stocks at the mill level fell by 29,000 tonnes to 1,871,000 at the end of May as the industry's recovery continues. Uncoated freesheet stocks fell by 22,000 tonnes to 990,000, while coated freesheet inventories fell by 17,000 tonnes to 635,000. However, uncoated groundwood inventories rose 8,000 tonnes to 64,000, while coated groundwood's were essentially unchanged (+2,000 tonnes to 182,000).

The U.S. paper industry continues to improve. U.S. printing & writing paper shipments on a twelve-month moving-total basis improved to their highest level in a year as producers finally saw some better pricing, even though costs had also increased more than prices. Uncoated freesheet shipments in May reached 998,000 short tons, versus 1,015,000 a year earlier. Uncoated

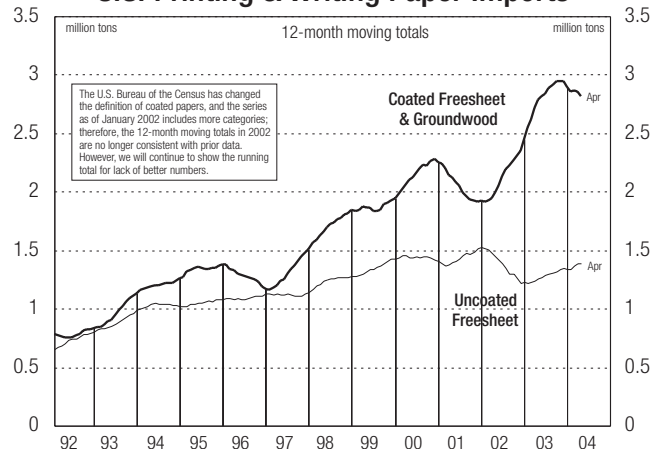
### U.S. Printing & Writing Paper Shipments



### U.S. Printing & Writing Paper Shipments



### U.S. Printing & Writing Paper Imports



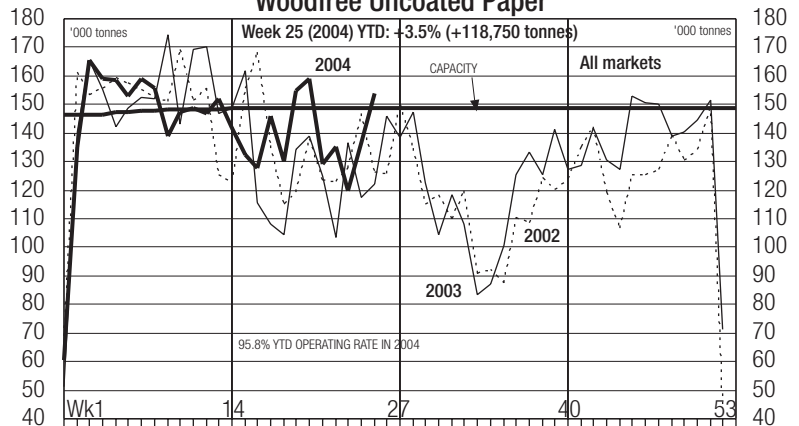
## DRIVERS OF DEMAND cont'd

groundwood shipments reached 113,000 s.t., versus 117,000 a year ago. Coated groundwood shipments reached 384,000 s.t. (May/03: 351,000 s.t.). Coated freesheet shipments rose the most of all the printing & writing grades year-over-year, reaching 396,000 s.t. (versus 319,000 a year ago).

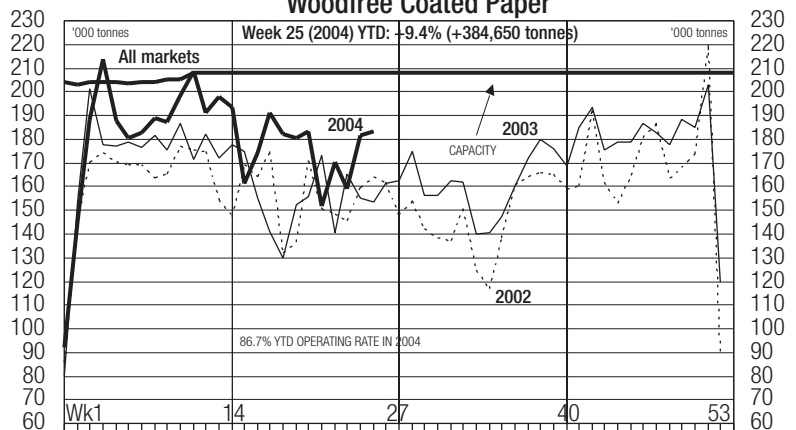
U.S. imports of printing & writing papers continued to make headlines. Imports of uncoated groundwood and coated grades fell by 32,500 s.t. to 228,400, while uncoated freesheet's dropped by 18,500 to 118,200. As a result, the twelve-month moving-total result for uncoated groundwood and coated grades continued to show a sharp decline from the high reached in November as some overseas markets improved. A stronger U.S. dollar does not appear to have been a factor here, but it may be too early to tell. Uncoated freesheet imports remain strong and have shown a gradual rise since the beginning of 2003 — in and around a period when capacity abroad was expanded and these same markets deteriorated.

In Western Europe, order inflows have improved significantly in recent weeks and year-over-year are showing signs of tremendous growth. While order inflows for uncoated woodfrees have shown a 3.5% increase from 2003 after week 25, coated woodfrees' are up 9.4%; operating rates for the two main grades are 95.8% and 86.7% respectively.

### Order inflow to mills in W. Europe Woodfree Uncoated Paper



### Order inflow to mills in W. Europe Woodfree Coated Paper



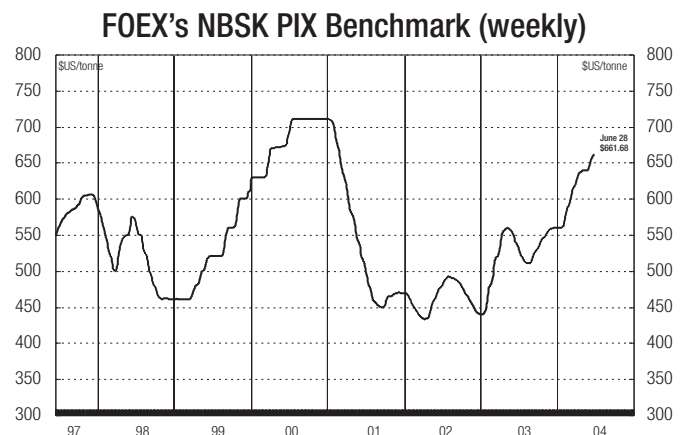
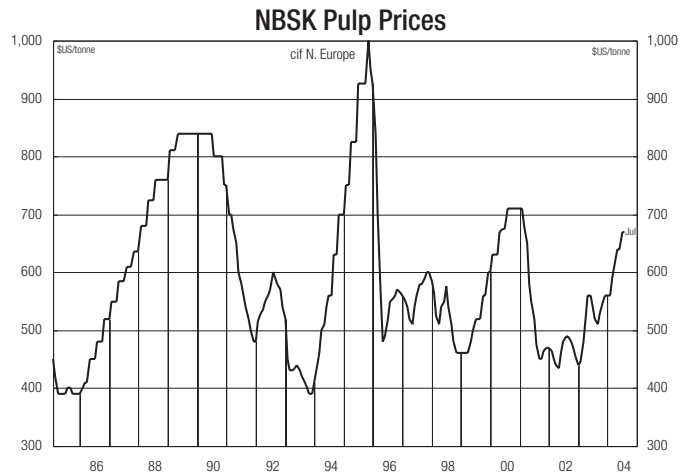
## PRICING

Throughout June, pulp prices were rising slowly as many consumers reluctantly agreed to pay more for supply. In Western Europe, they did so with the condition that “baisse clause” be added to hardwood sales; should prices fall in June or July, rebates would kick in automatically.

Because the June 1 price increase was a very sore point for several consumers (especially in Western Europe), many pricing levels were not concluded until the end of the month. Therefore, some of the pricing being reported appears to have been on the low side. Case in point: by the end of June, prices reported in Western Europe reached \$650–\$670, and were still rising as the latest PIX was released (showing a \$2.99 increase from the previous week and reaching an aggregate average of \$661.68 for the week ending June 25).

Given that stocks held by producers, European ports and Utipulp members fell in May, and that paper inventories declined in most major markets, the upward price momentum appears to retain a strong chance of surviving for a while yet. It will take a series of negative indexes to cause prices to fall.

May’s World-19 results were not as expected, mainly because of overproduction (the result of cancelled or delayed maintenance or planned downtime, as already stated). However, we all know that such outages cannot be pushed forward forever. At some point, repairs will have to be made. When the mills eventually go down —



expected in Q3 — supply will be reduced, thereby providing producers with the ability to hold prices steady or announce yet another increase.

For now, pulp prices in general are rising in all markets with the exception of Asia. Customers in this market,

### Market Pulp List Prices (unless specified) for June 2004 • US\$ unless noted

	W. EUROPE	U.S.	JAPAN	CHINA	S. KOREA
NBSK (Canadian)	660–670	680	610–620(a)	630–650(a)	630(a)
SBSK	630–640	650	590–600(a)	580–590(a)	580–590(a)
NBHK (Canadian)(b)	560–570	580–590	510–530(a)	500–510(a)	500–510(a)
SBHK	550–560	570–580	500(a)	500(a)	500(a)
UKP (North American)	—	600	—	—	—
EUCALYPTUS (US\$)	560–570	590	530(a)	530(a)	530(a)
RADIATA PINE	640–650	—	—	600–610(a)	600–610(a)
RUSSIAN NBSK	—	—	—	600–610(a)	600–610(a)
INDONESIAN MIXED TROPICALS (c)	530–540	—	—	480–500(a)	490–500(a)

— Quotes deemed to be unreliable, or transaction not sufficiently representative of overall market (a) Expected net price (b) single-species maple, add \$10–\$20 depending on market (c) Acacia add \$10

## PRICING cont'd

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who until June have been paying a hefty premium relative to other markets for NBSK, have managed to dodge the \$10 increase that many producers have attempted to implement. As a result, premiums have disappeared somewhat when comparing transaction levels; most average transaction levels for NBSK in Western Europe and the U.S. range from \$590-\$620, versus \$610-\$620 in China and other parts of Asia.

One factor that has kept pulp (even hardwood) prices rising is the shortage of supply at mills that have been forced to take downtime for repairs, or have been able to swing to softwood. We do not see an end to the effect of swing capacity on the market anytime soon, as the wide pricing differentials between softwoods and hardwoods persist.

Although we still show NBSK at \$670 in June in Western Europe, it is understood that several buyers have managed to obtain lower prices; however, it is understood that July's pricing will be at \$670 (or closer to it than it was in June) for these same buyers.

FOEX pricing for NBSK in Western Europe is at \$661.68 at the end of June, up from \$640 a month earlier. This is the highest it has been since February/01.

Anyone looking for a basic explanation for why pulp prices are up in 2004 needs only to look at shipments versus production year-to-date. At the end of May, year-to-date shipments are 7.0% (1,035,000 tonnes) ahead of 2003, while production is just 5.3% higher (792,000).

The bottom line is that producers have managed to maintain control of the market; however, Q3 will prove to be their toughest test yet this cycle.