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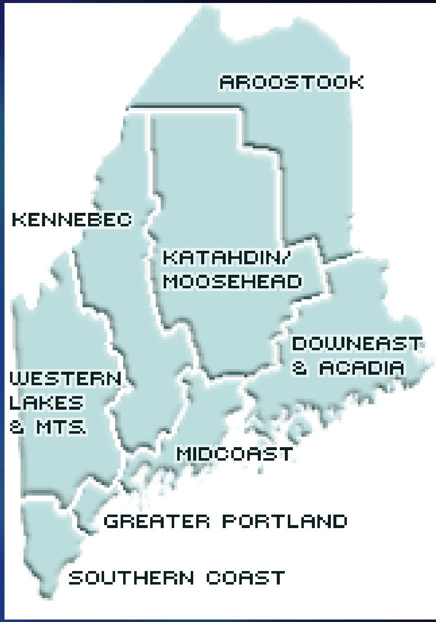
The Current State of Maine's Pulp & Paper Industry
-- A Competitive Assessment --



PIMA Northeast Division 83rd Annual Meeting

Kennebunkport, Maine – September 19, 2003

Jim McNutt

Center for Paper Business & Industry Studies -- CPBIS

OVERVIEW

- Maine's P&P Industry – Where Are We?
- North America Printing & Writing Paper Market
- Maine's Primary Grades Review – Grade-by-Grade
  - ✓ *UCFS*
  - ✓ *SC*
  - ✓ *Directory*
  - ✓ *CGW*
  - ✓ *CFS*
- Where Can We Go?

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Where are We?

- In The Mind's of Many – Maine's Forest Products Industry Has Entered *The Beginning of The End* – Much Like *Textiles & Steel*
- Yet – Others View Maine's Forest Products Industry As Being *On A Doorstep To Revitalization*
- In Truth – Maine's Forest Products Industry's Future Is *In The Hands Of Those Who Do* . . . Not In The Hands Of Those *Who Can't & Won't* . . . Not In The Hands Of Those Who Only *Complain, Point Fingers & Criticize*!
- *Yet – The Challenges Are Real, & They Are Major*

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So -- Where are We Now -- Really?

- Maine's P&P Industry Is An Industry in Transition . . .
  - ✓ Older Infrastructure & Dated Technology
  - ✓ Declining Capacity, Jobs, Taxes Paid
  - ✓ Older Workforce With Age Structure Imbalance
  - ✓ Higher Factors of Production Costs – *Especially For:*
    - *Energy, Fiber, Labor, Maintenance*
    - *Taxes, Worker Compensation . . . .*
  - ✓ Cost Competitive Pressures *Are Severe*
- Markets In Transition & *Under Great Pressure . . .*
  - ✓ Global Competitiveness Has Escalated
  - ✓ Demand Growth Is Much More Constrained
  - ✓ Customers Are Stressed & More Demanding . . .

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And – What Are Some Key Realities?

- Maine Is Not Viewed As A Premium Place For Basic Industry Operations & Investment . . .
  - ✓ *Past Political Polarization*
  - ✓ *Tax Structures & Systems*
  - ✓ *State Regulations & Regulatory Processes*
    - Site Permitting Requirements
    - Environmental Arena
    - Timberlands & Multiple Use Needs Balancing . . . .
- Industry Attention Seriously Strained
  - ✓ *Management Focus On Maine's Operations*
  - ✓ *Investment History And Patterns*
- Special Interest Groups Public Conflicts . . . .

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So – Where Do We Start & Look?

- **The Key Today to Maine's P&P Industry Is Found in the Printing & Writing Paper Grades**
  - ✓ *Uncoated Freesheet -- UCFS*
  - ✓ *SC Grades*
  - ✓ *Directory*
  - ✓ *Coated Groundwood*
  - ✓ *Coated Freesheet – CFS*
- ***Let's First Look At Key Printing & Writing Paper Grades For North America As a Whole***

Grade Outlook – *N. Am. P&W Papers*

Recent *Economic Slowdown & Alternative Media Substitution* Have Impacted P&W Demand Negatively:

- Uncompetitive Capacity Being Closed & Modest Demand Increases Will Tend to *Reign in Excess Capacity*
- CFS, CGW, UCFS & GW Grades *Seemingly Collapsing Into One* Relatively Inter-changeable/somewhat Flexible Grade Structure From Consumers' Perspectives
- These Changes Brought on by *Collapsing Price Structures* of the Grades on Top of Each Other Is a Major Sea Change
- In This Context -- CFS Quickly Becoming *Commoditized -- Displaced* by Improved CGW Grades

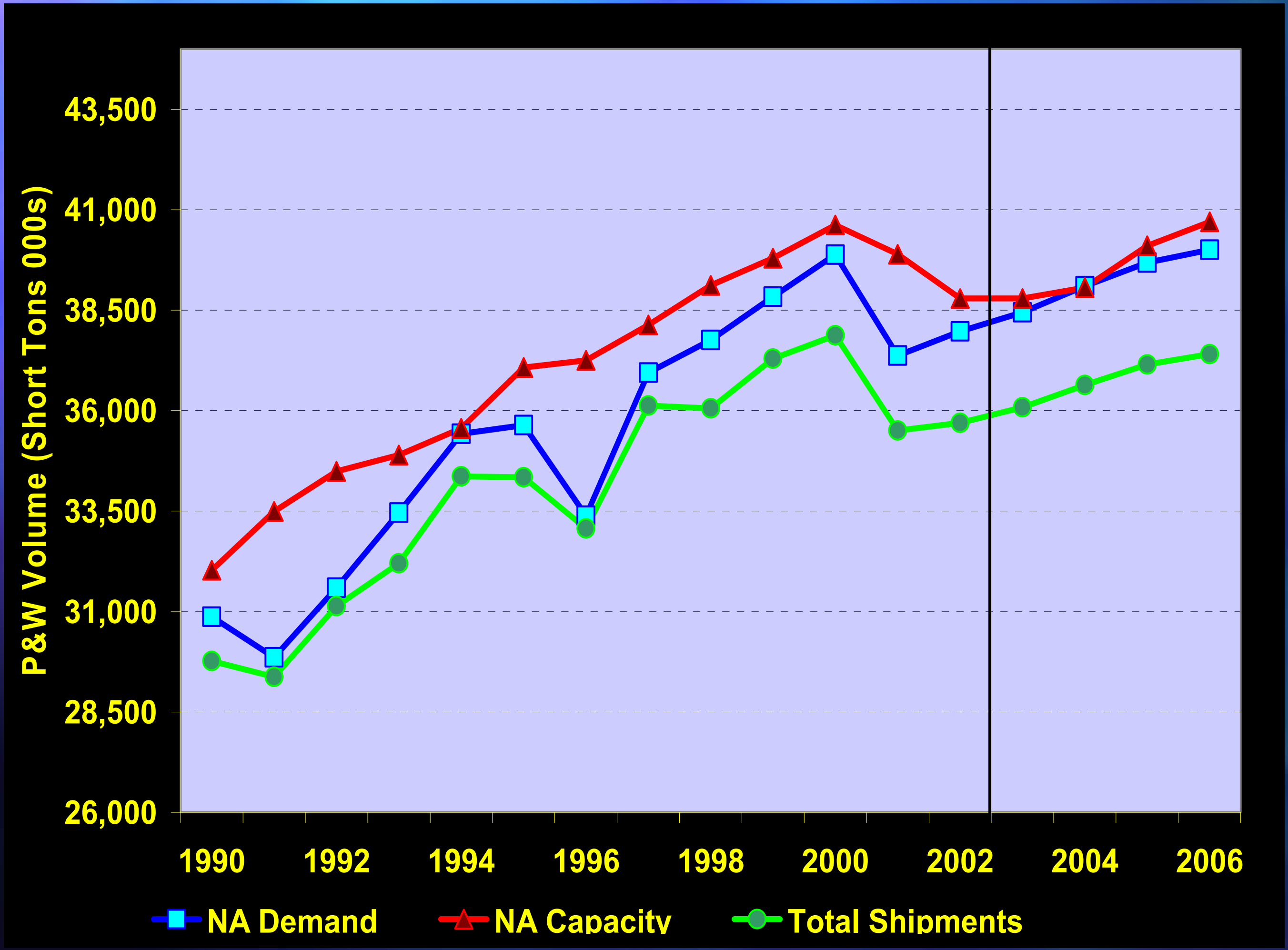
Grade Outlook – *N. Am. P&W Papers*

In Addition -- High End Uses -- Auto Brochures/annual Reports -- *Are Being Replaced by Website Versions*

- **High Volume *UCFS Under Pressure* From Overseas Competitors, and Newsprint Producers Are Converting Capacity to UC and CGW Grades**
- **Financial Returns & Growth Prospects Are Similar to Industry Average & Room Does Exists for *Continued M&A Activity***

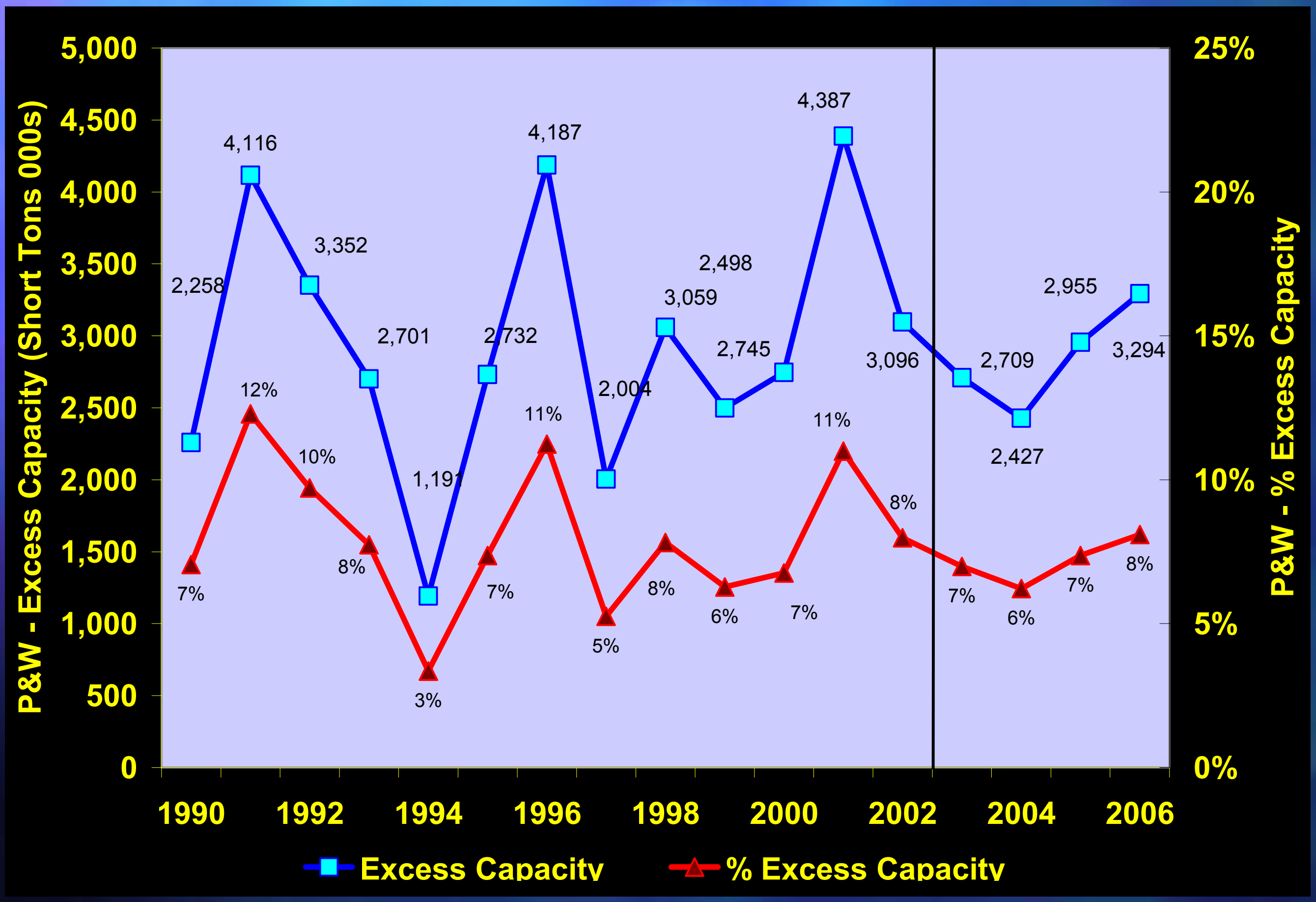
Implications: **This grade grouping is in *major sea change* with grades collapsing on one another. Significant repositioning and redeployment of assets – continued M&A & financial constraints. Certain segments will suffer net capacity reductions.**

Grade Outlook – *N. Am. P&W Papers*



N. Am. P&W Demand & Capacity Contracted Between 2000 and 2002 – *A Moderate Recovery* Has Begun In 2003

Grade Outlook – *N. Am. P&W Papers*



Significant N. Am. P&W *Over-capacity Should Dissipate* By 2004

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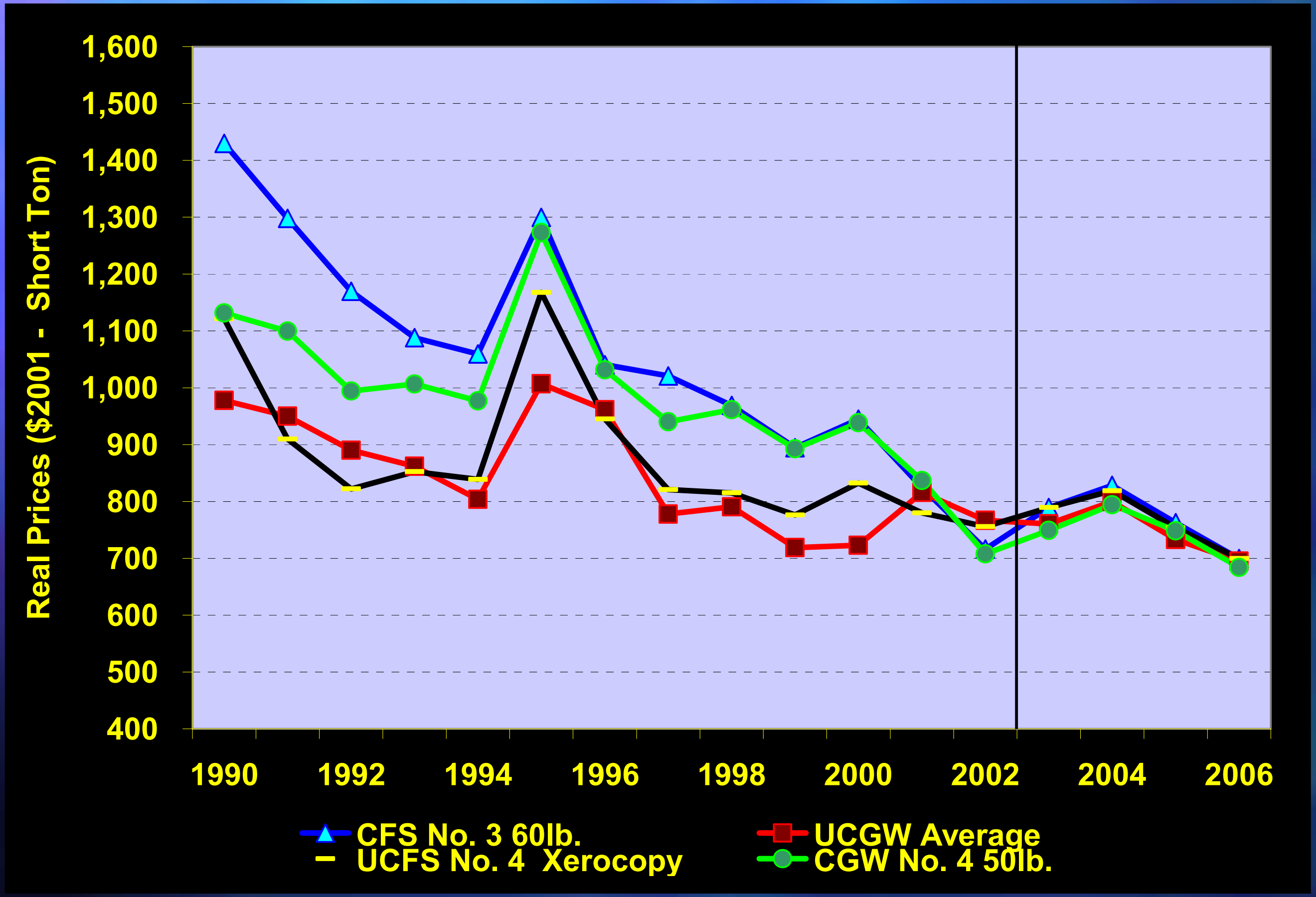
Grade Outlook – *N. Am. P&W Papers*



N. Am. P&W *Real Pricing* Is At Historically Low Levels – *Grade Prices Have Converged*

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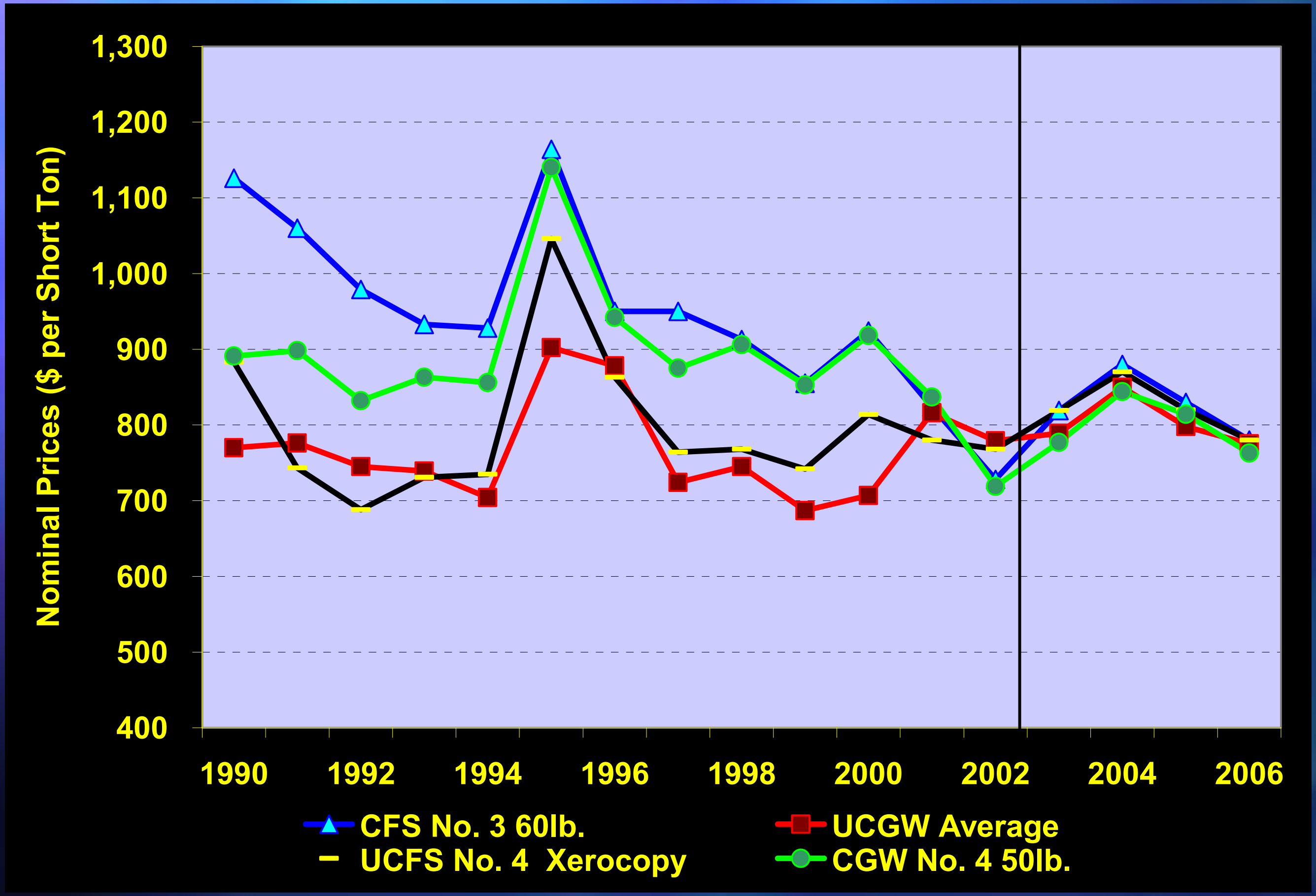
Grade Outlook – *N. Am. P&W Papers*



N. Am. P&W *Nominal* *Prices* Will Likely Improve *Some* In 2003 & 2004

Now – Let's Take A Look At Key Grades In Maine

- All Mill Cost Competitive Data Here Are Provided By Paperloop's Pulp and Paper Benchmarking Services Group
- Data are:
  - ✓ Fourth Quarter 2002 *Basis In 2003 Dollars*
  - ✓ Mill Level *Cash Manufacturing Costs*
  - ✓ *Based on* Publicly Available *Information & Data*
  - ✓ *Representative of* Relative/Typical Operating Configuration *Assumptions at Each Mill Assessed*
  - ✓ *Based on* Regional Unit Cost Data *Inputs*

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Our Competitiveness Assessment Approach

- First – A Brief Macro Overview of Key Factors of Production *For Printing & Writing Paper Grades*
  - ✓ *Focus on* Fiber, Energy & Labor
  - ✓ *And* Aggregate Cost Levels
- *Then A Grade-by-Grade With Key Mills Review*
  - ✓ *Uncoated Freesheet*
  - ✓ *SC Grades*
  - ✓ *Directory*
  - ✓ *Coated Groundwood*
  - ✓ *Coated Freesheet*

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Key Competitive Issues – P&W Papers

Factors of Production Cost Comparisons For Maine Mills

[All Data in USD per Short Ton]

Cost Element	*Industry Average*	Mill A	Mill B	Mill C	Mill D	Mill E	Mill F	Mill G	Mill H	Mill I	Mill J	Mill K	Mill L	Mill M	Mill N	Mill O
Fiber	*156*	180	134	101	93	104	150	93	78	78	159	134	70	97	202	384
Power	*66*	55	44	44	45	62	71	109	75	75	45	100	63	90	129	85
Manpower	*71*	81	88	125	138	164	114	118	137	137	161	198	178	198	192	139
All Other	*123*	137	195	218	216	169	168	183	300	241	225	162	299	229	211	206
Total	*416*	453	461	488	492	499	503	503	521	531	590	594	610	614	734	814

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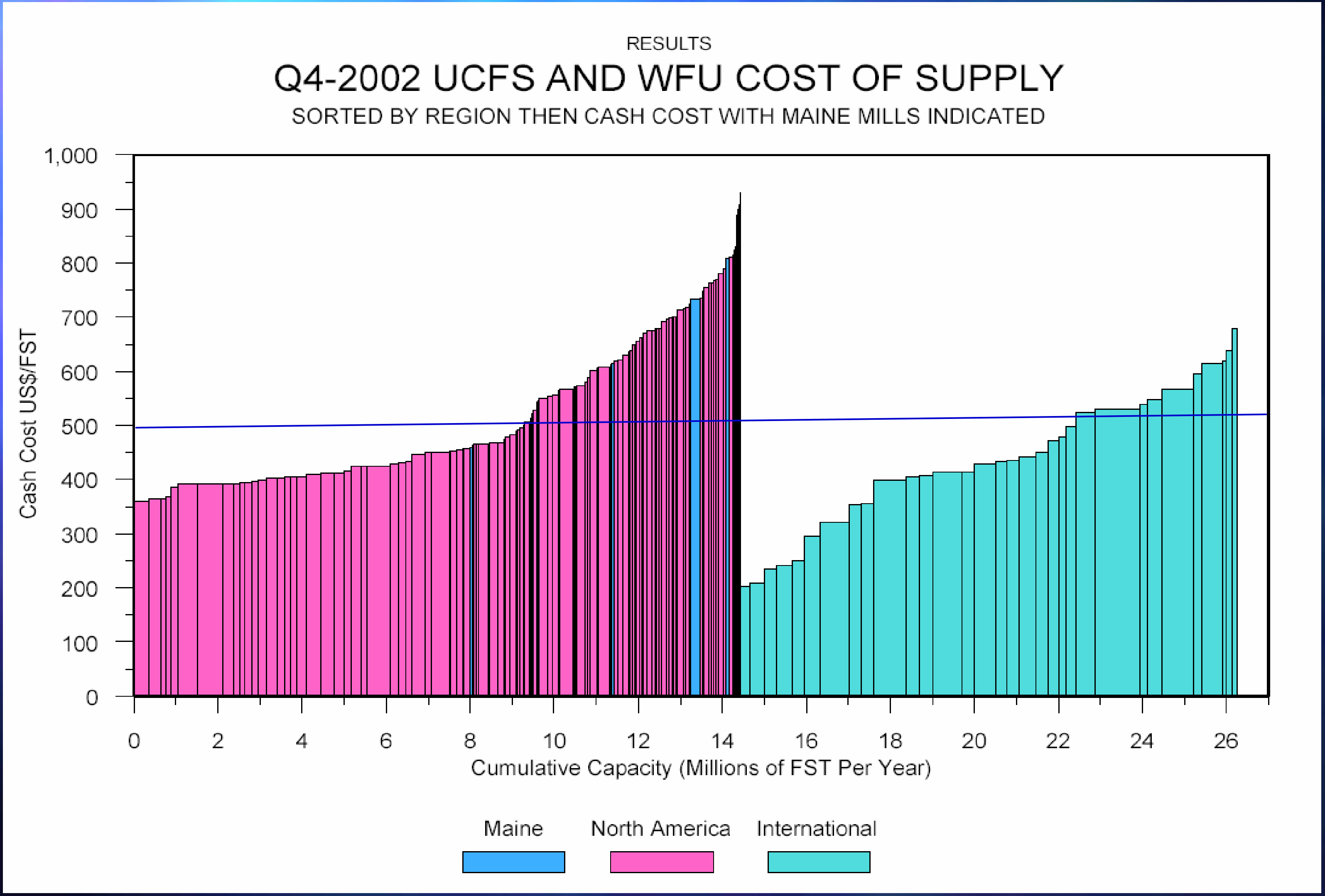
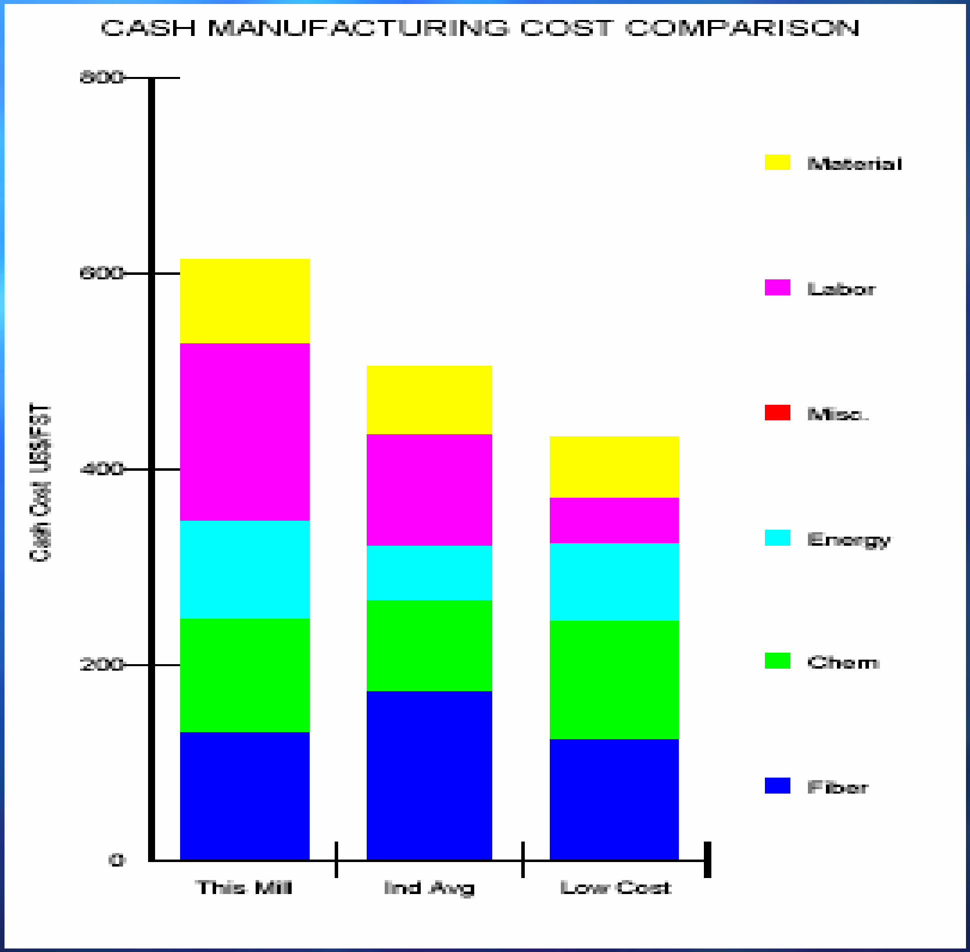
Maine's UCFS Competitiveness

- Product Quality Is Rated as *Competitive*
- Mill Cash Cost Competitiveness = Very High, *4th Quartile*
- Key Cost Issues Are:
  - ✓ *Labor* = High – *Unit Costs & Efficiency*
  - ✓ *Energy* = Very High
  - ✓ *Materials & Chemicals* = Generally Competitive
  - ✓ *Fiber* = Very Competitive

UCFS Cost/Supply Curve



UCFS Cost Curve



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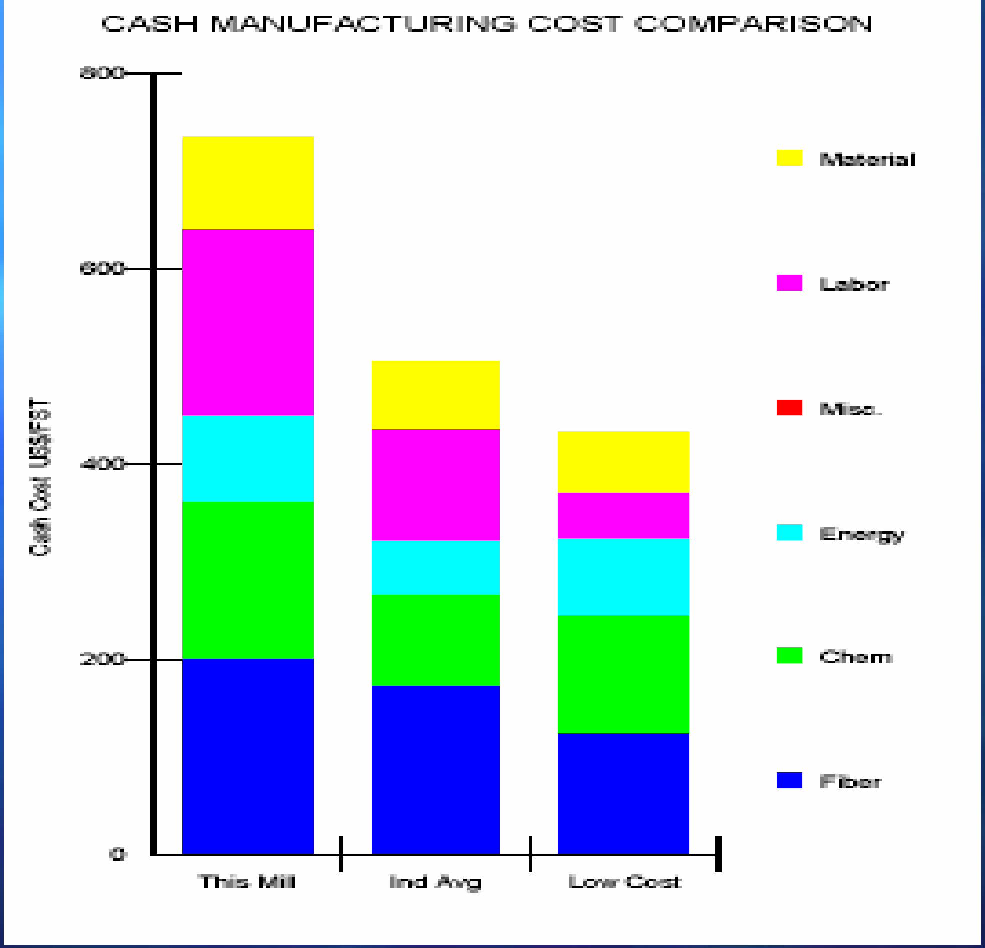
UCFS-Value Added Cost Curve



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Maine's SC Competitiveness

- Product Quality Is Rated as *Very Good*
- Mill Cash Cost Competitiveness = *4th Quartile*
- Key Cost Issues Are:
  - ✓ *Labor* = Very High – *Unit Costs & Efficiency*
  - ✓ *Chemicals* = Relatively High
  - ✓ *Fiber & Materials* = Competitive
  - ✓ *Energy* = Very Competitive

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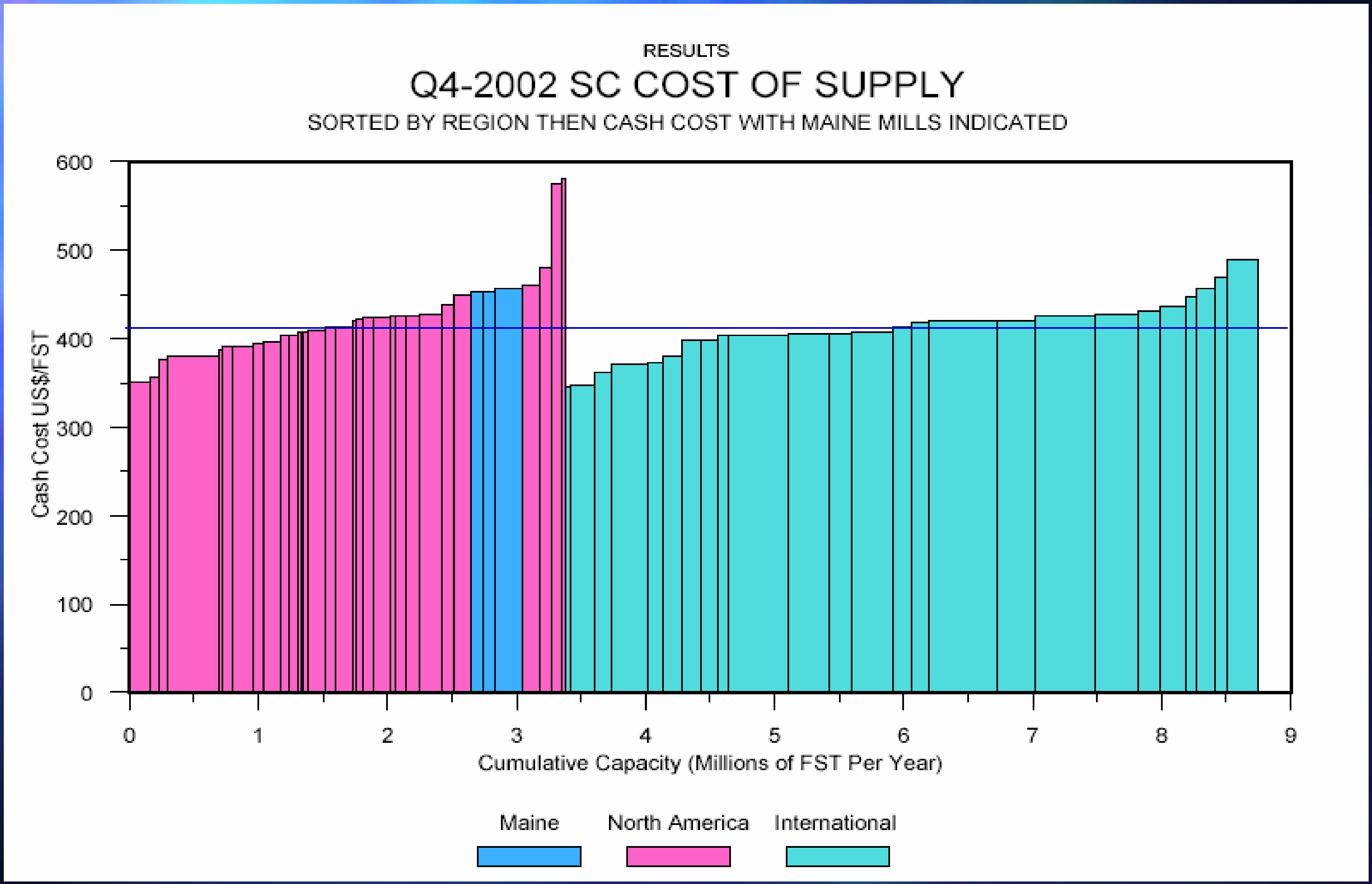
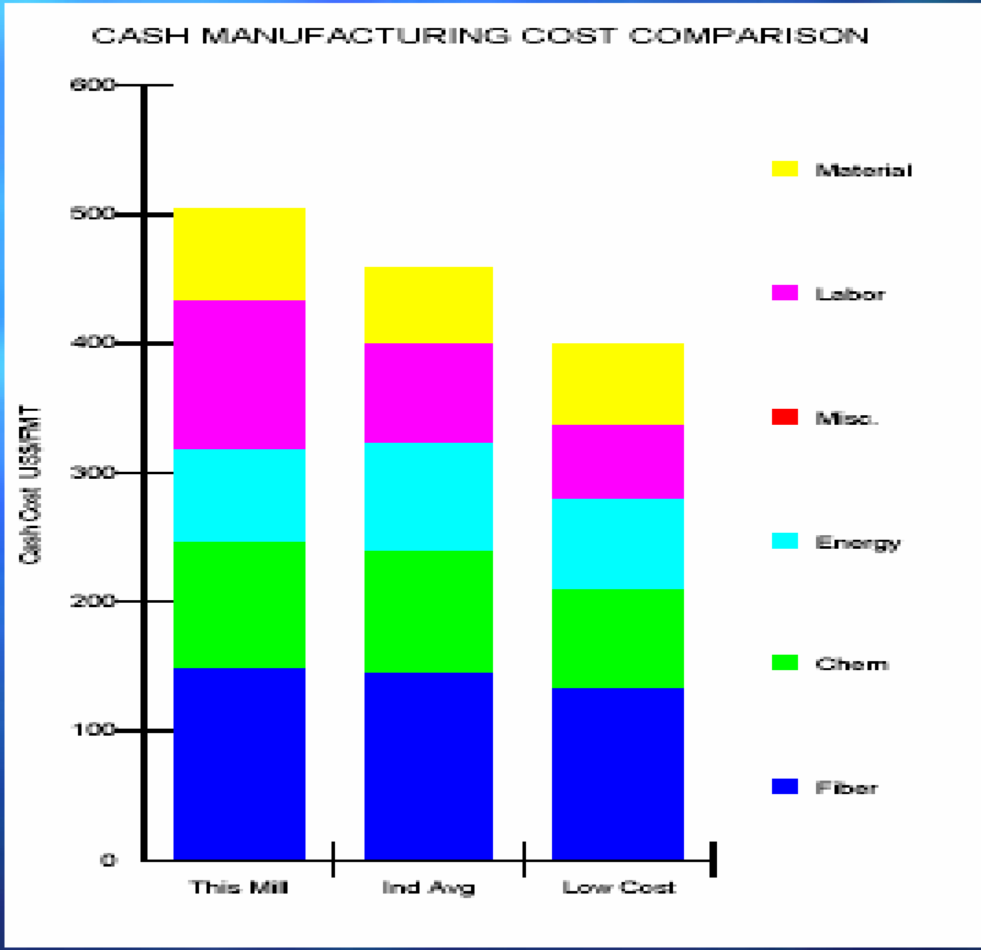
SC Cost/Supply Curve



SC Cost Curve



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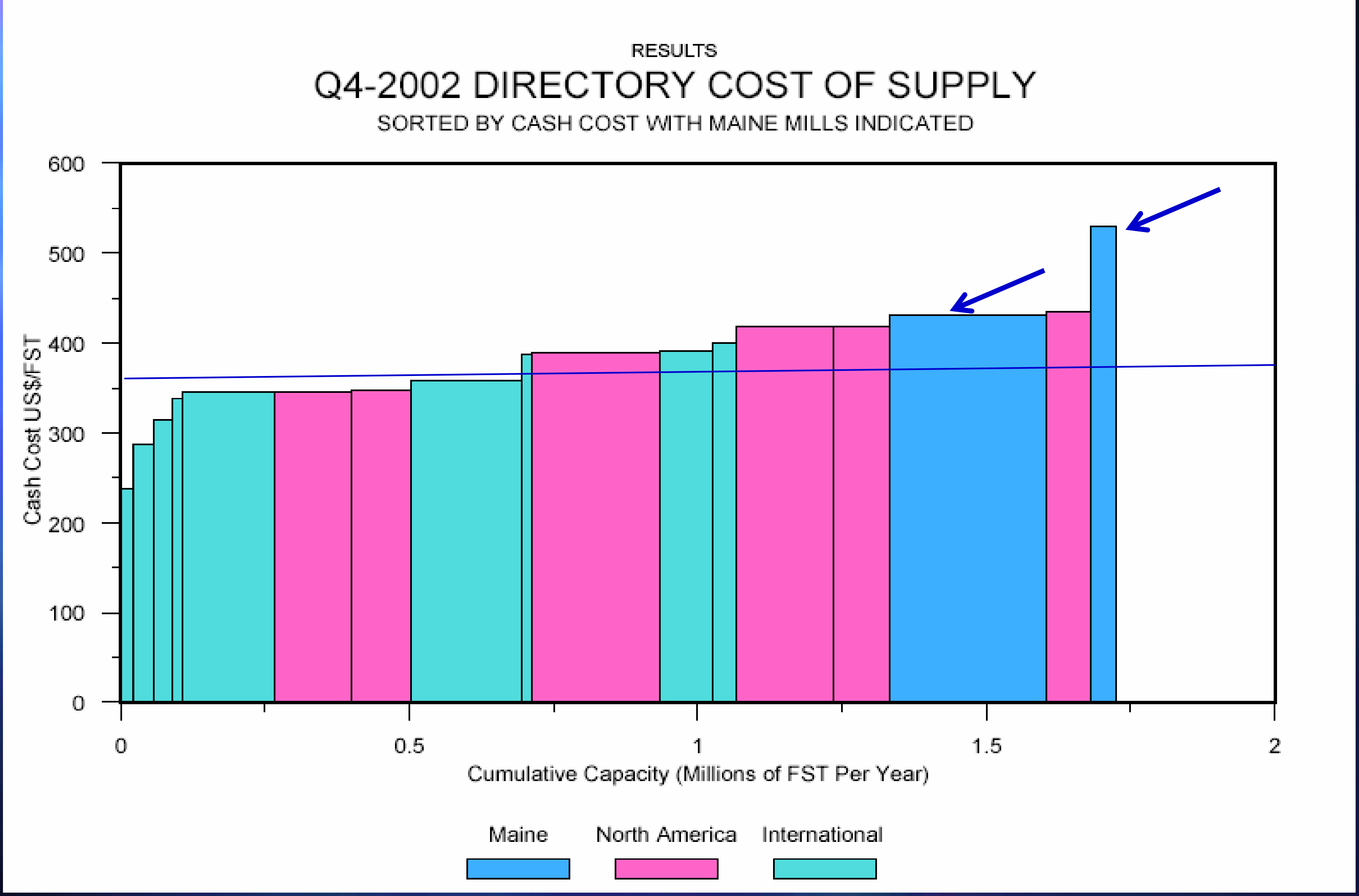
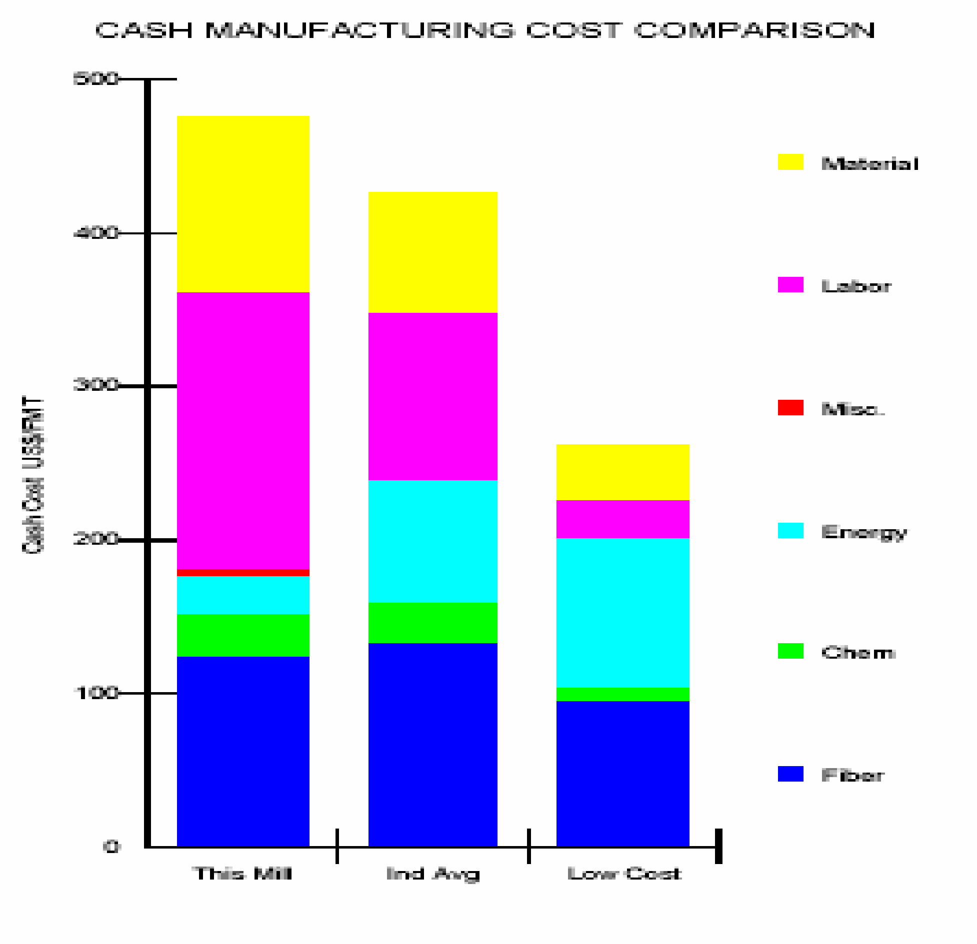
Maine's Directory Competitiveness

- Product Quality Is Rated as *Very Good*
- Mill Cash Cost Competitiveness = Very High in The *4th Quartile*
- Key Cost Issues Are:
  - ✓ *Labor* = Very High – *Unit Costs & Efficiency*
  - ✓ *Materials* = High
  - ✓ *Fiber & Chemicals* = Competitive
  - ✓ *Energy* = Very Competitive

Directory Cost/Supply Curve



Directory Cost Curve



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Maine's CGW Competitiveness

- Product Quality Is Rated as *Good To Very Good*
- Mill Cash Cost Competitiveness = Varied, Ranging Across *1st to 3rd and 4th* Quartiles
- Key Cost Issues Are:
  - ✓ *Labor* = Somewhat High – *Unit Costs & Efficiency*
  - ✓ *Materials & Chemicals* = Competitive
  - ✓ *Fiber* = Competitive to High
  - ✓ *Energy* = Very Competitive

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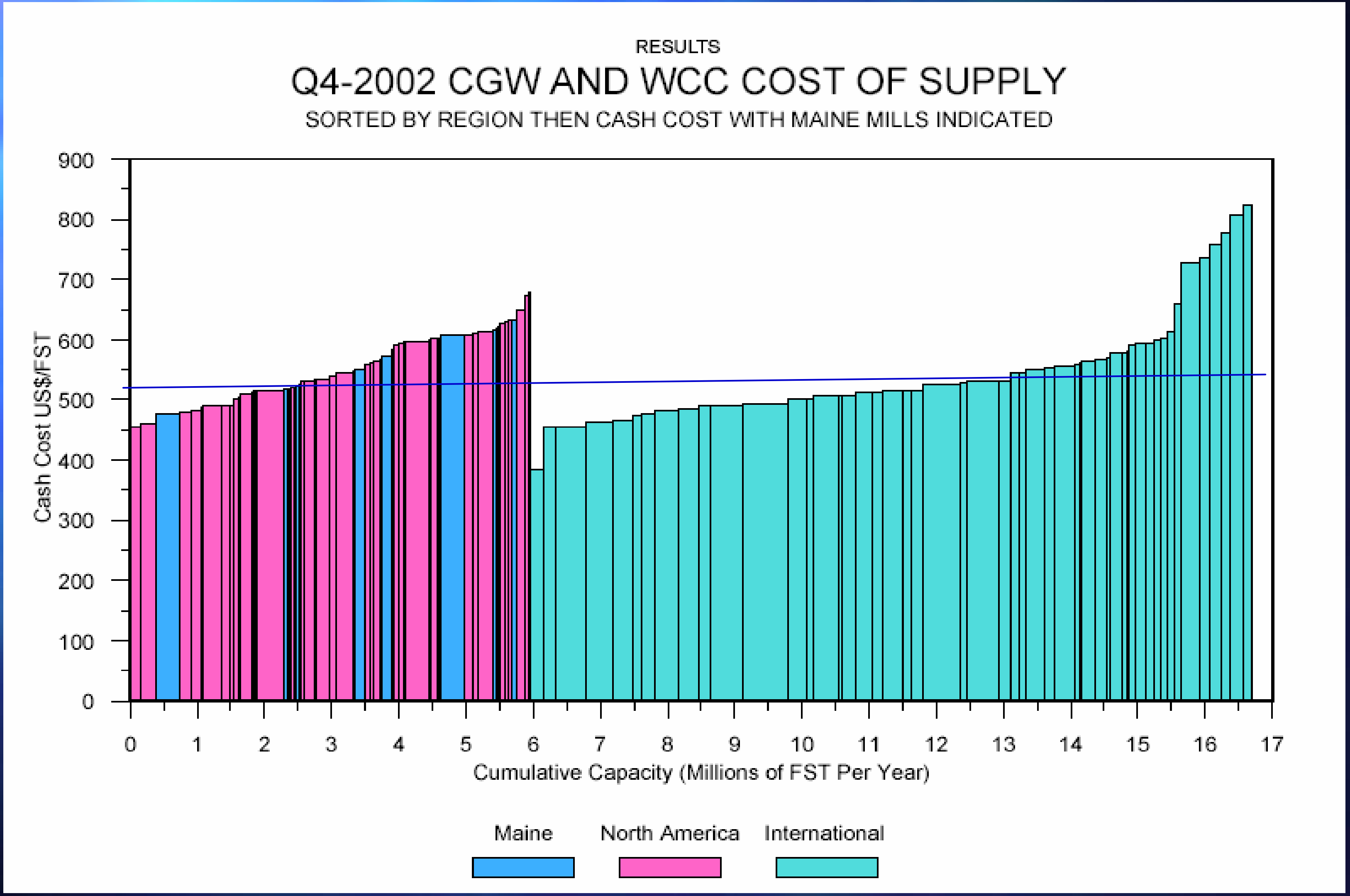
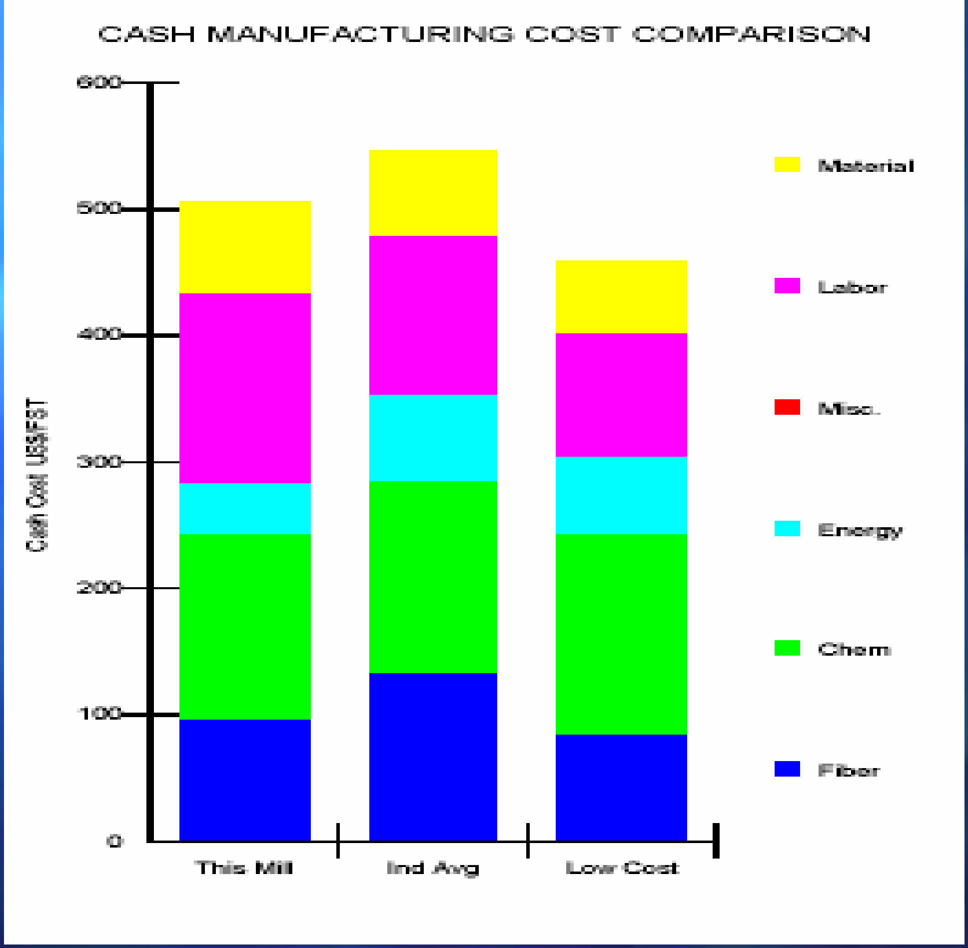
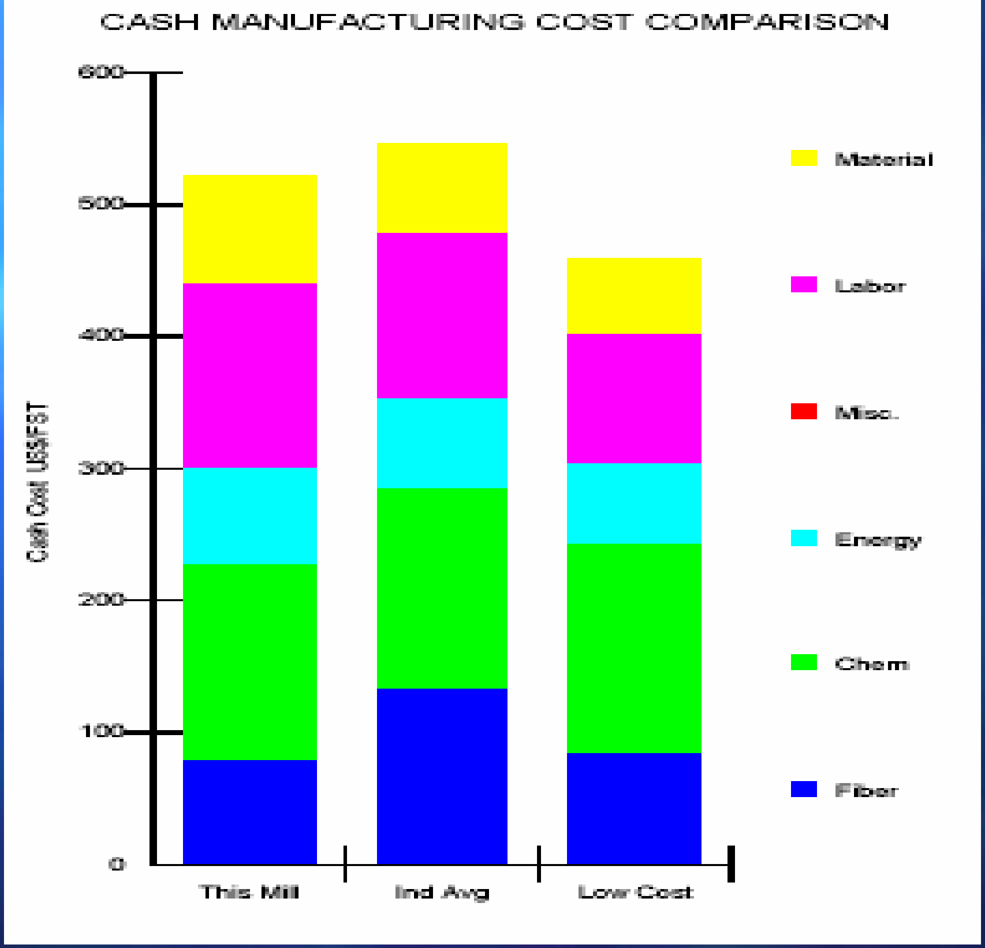
CGW Cost/Supply Curve



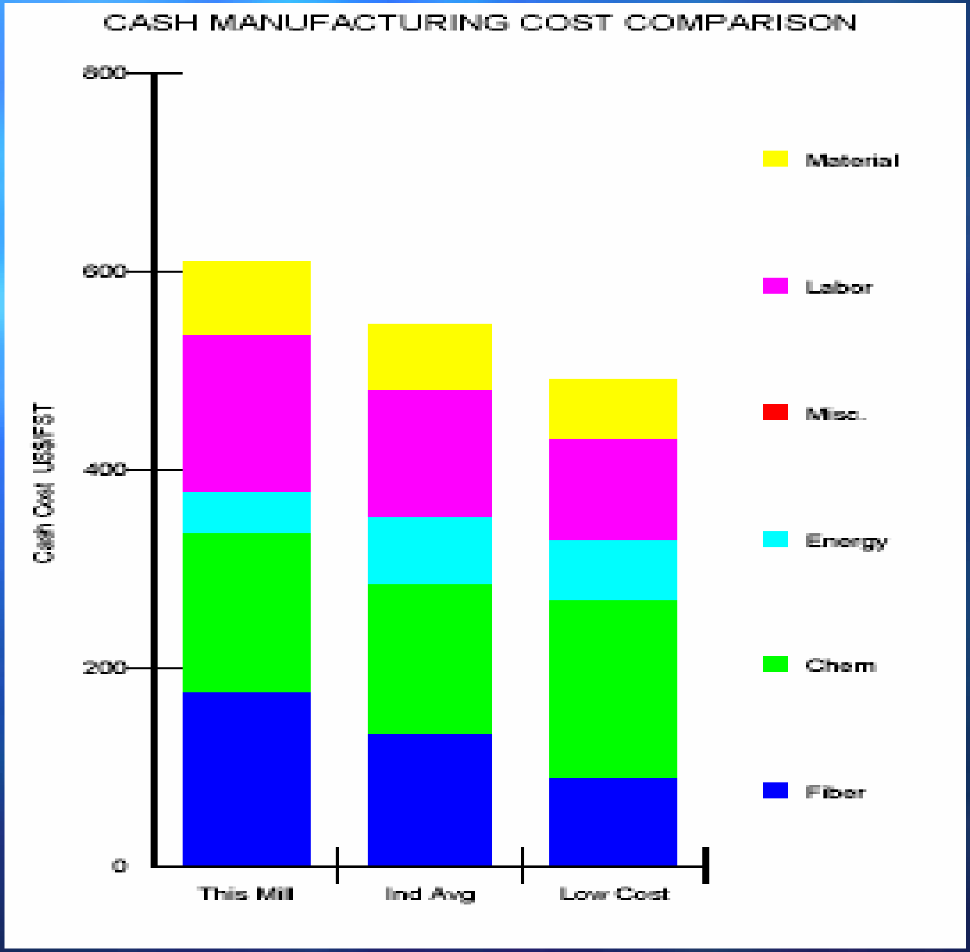
CGW Cost Curve



CGW Cost Curve



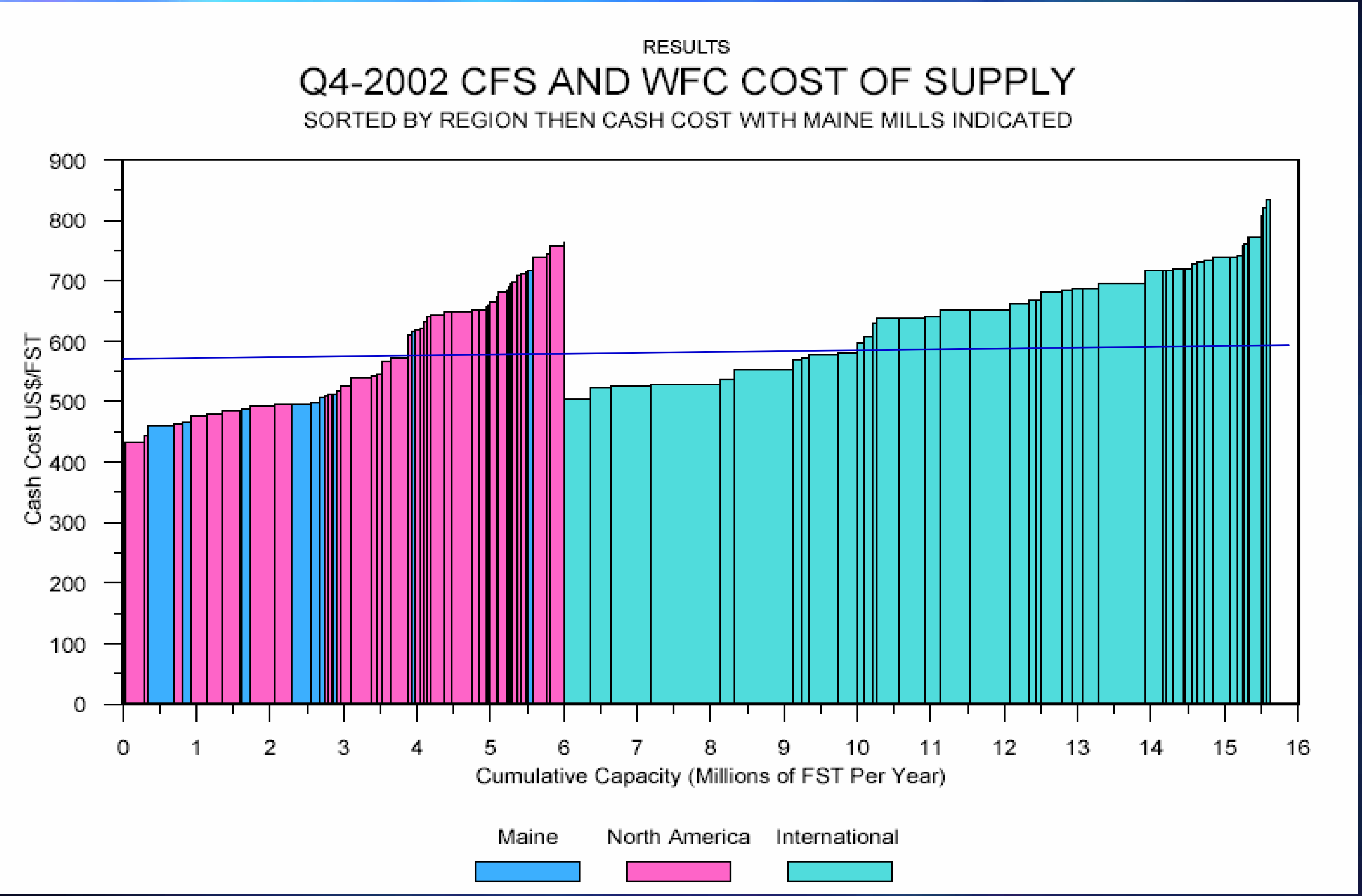
LWC Cost Curve



Maine's CFS Competitiveness

- Product Quality Is Rated as *Very Good*
- Mill Cash Cost Competitiveness = Good, Mostly in *1st and 2nd* Quartiles
- Key Cost Issues Are:
  - ✓ *Labor, Energy, Materials, Chemicals, & Fiber =* All Competitive

CFS Cost/Supply Curve



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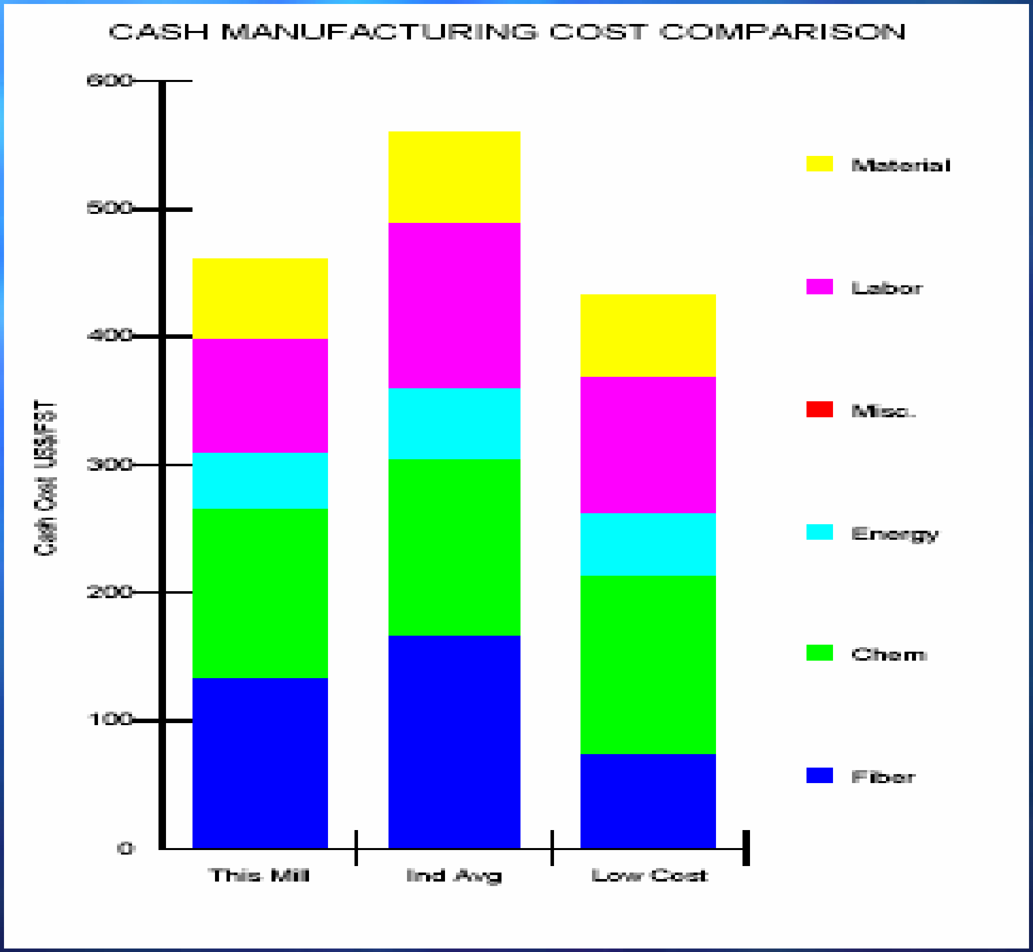
CFS Cost Curve



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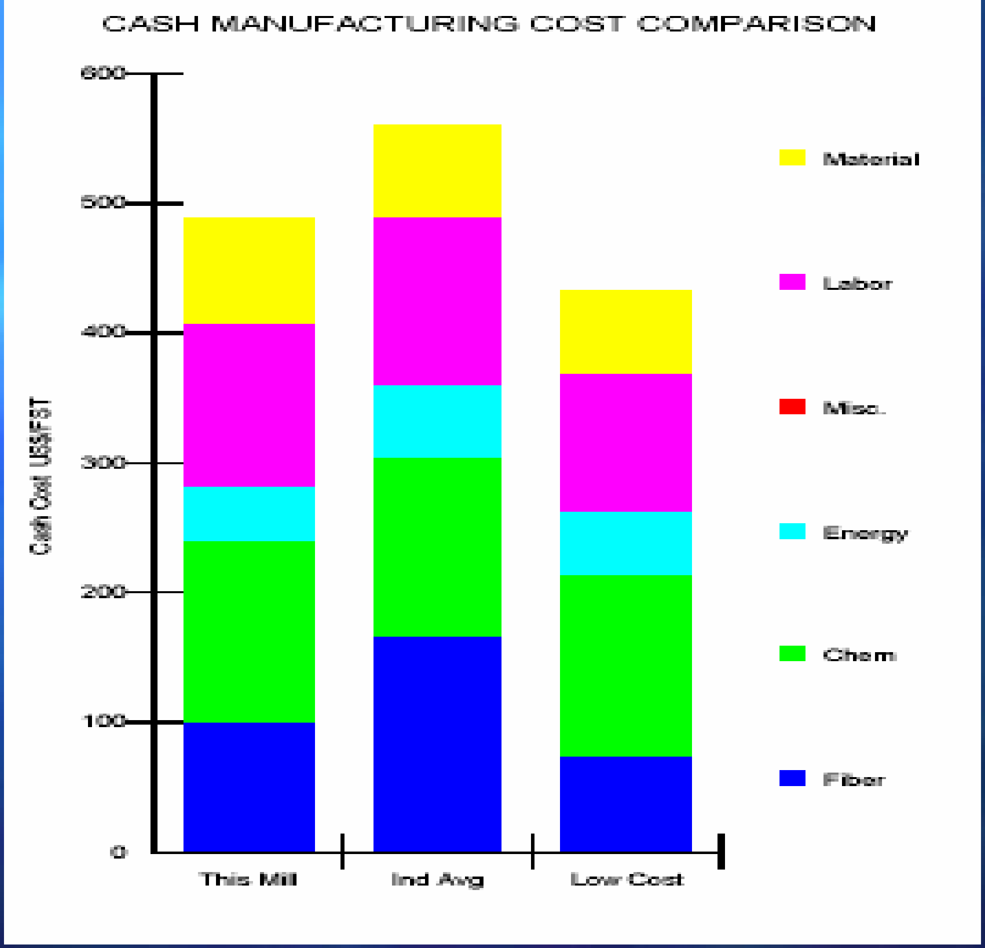
CFS 60# No. 3 & 4 Cost Curve



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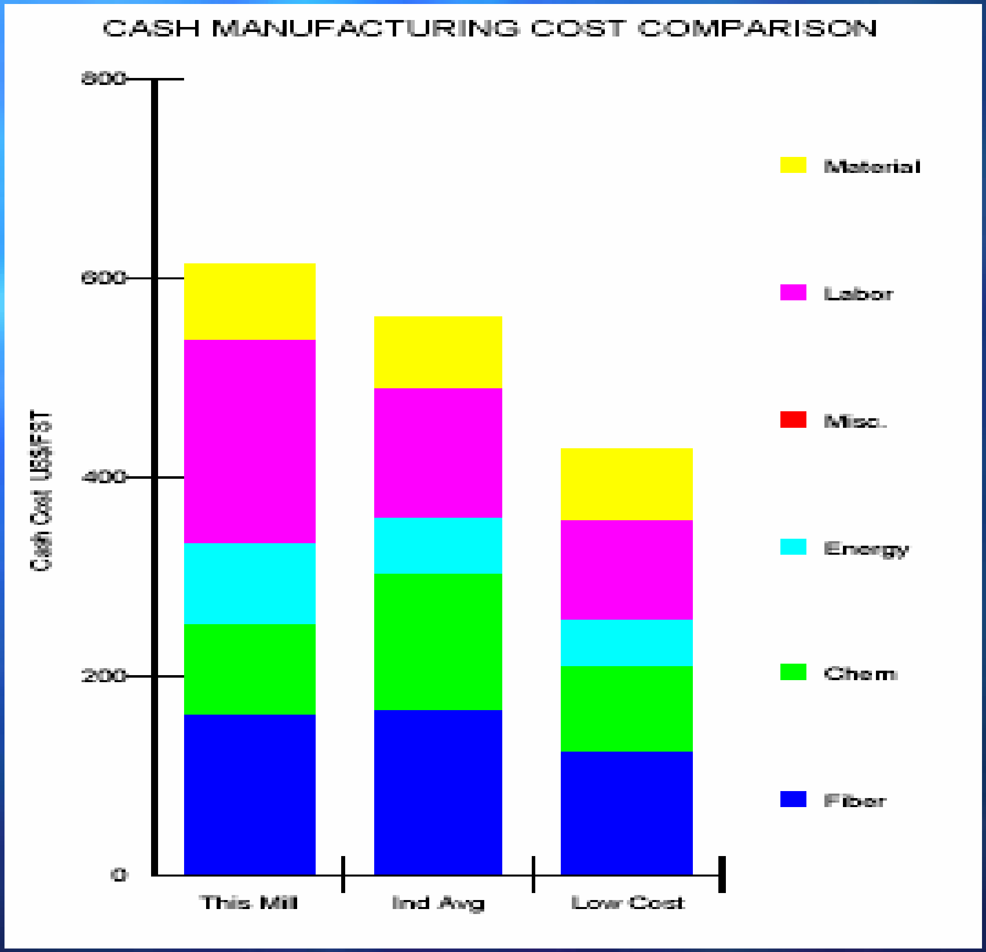
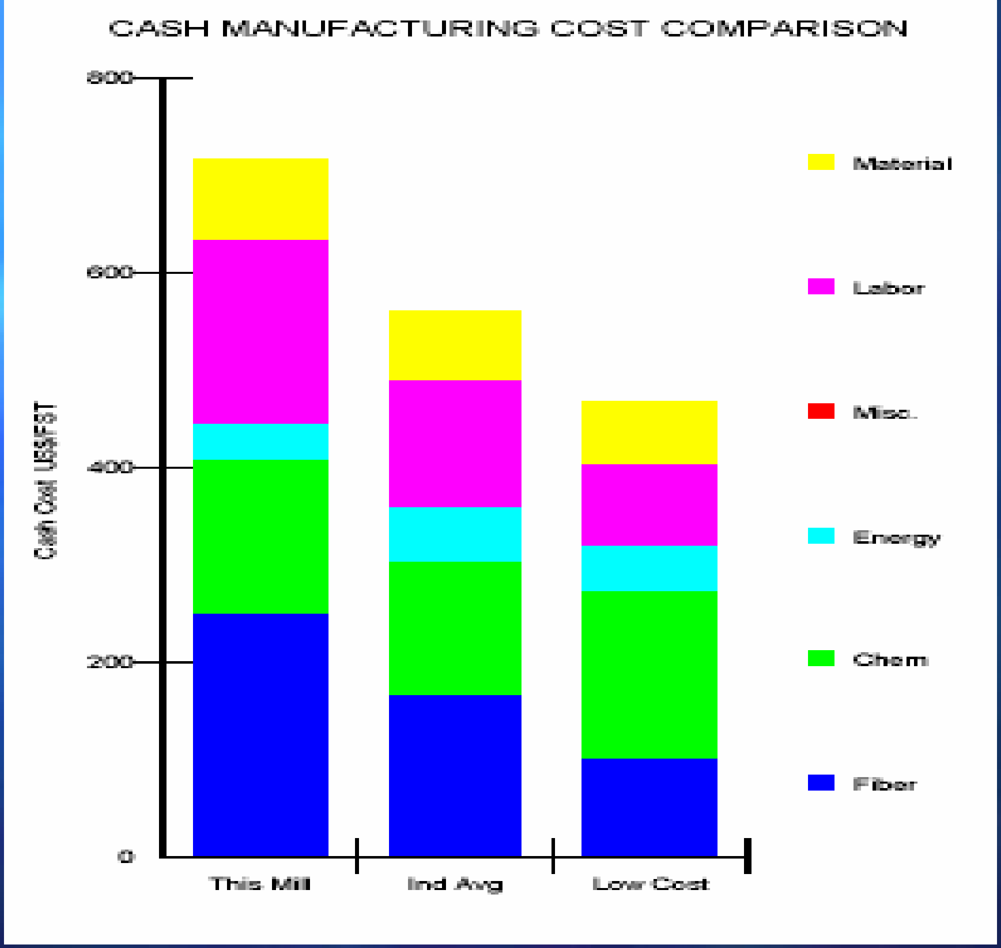
CFS-One Sided Cost Curve



CFS-Premium Cost Curve



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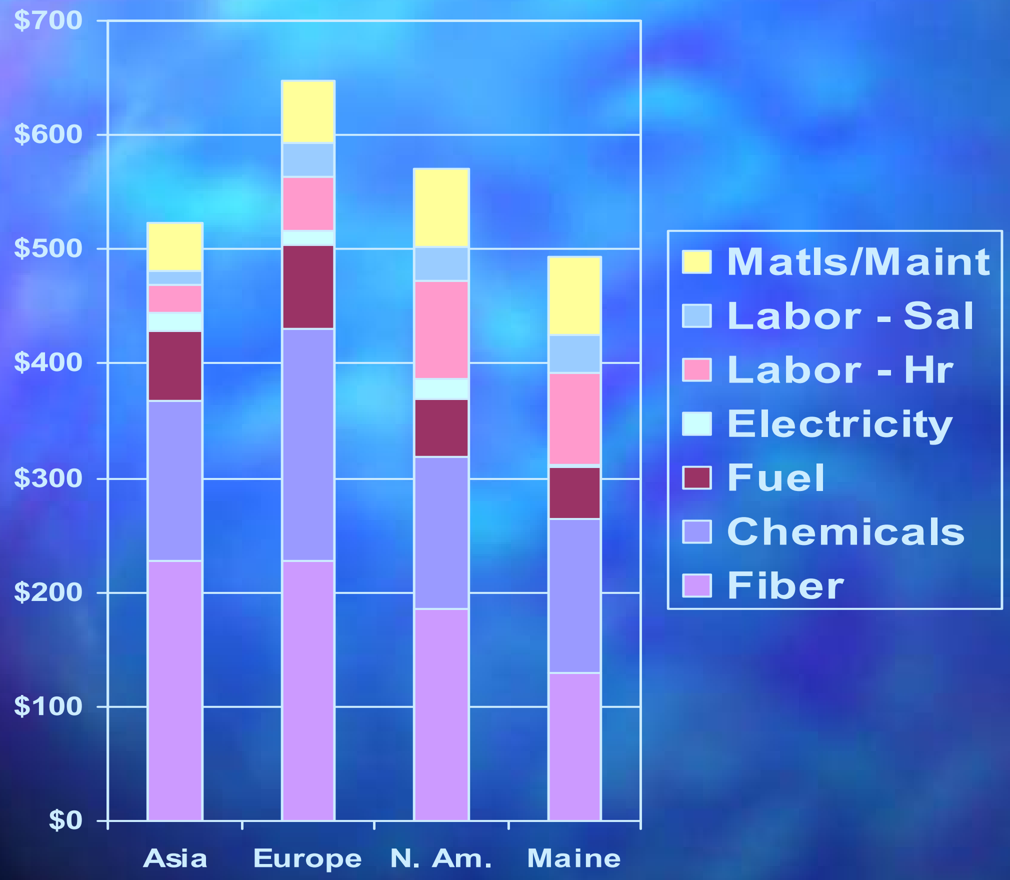
Current -- Typical CFS Commodity



	Asia	Europe	N. Am.	Maine
Cost Ranges	405-650	525-850	460-880	485-505
Product	105 gsm	115 gsm	60 lb #3	60 lb #3

- Data = Q2 2003 & USD/ST
- Maine not as well positioned
  - ✓ *Labor – Hourly*
  - ✓ *Materials & Maintenance*
- Maine very well positioned
  - ✓ *Fiber*
  - ✓ *Energy*
  - ✓ *Fuel*
  - ✓ *Total Cash Cost*
- Note -- Asia/Europe Fiber Costs = Purchased Pulp Driven and Imported Chips for Asia

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So -- Where Can We Go?

- Maine Is Blessed With Tremendous Potential . . .
  - ✓ *Abundant* Natural Resources
  - ✓ *Wonderful Logistics* Infrastructure
  - ✓ Superb Location *To Largest Global Market*
  - ✓ *Very* Experienced & Motivated *Work Force*
  - ✓ Substantial Dependency *on P&P Industry*
  - ✓ *Renewed Attention of* Political, Labor & Industry *Leaders*
  - ✓ *Great Need of* Local Communities *To Rally*
- There Are *Great Opportunities To Enhance* The Competitive Position of Maine's Pulp & Paper Mills *For The Right Grades*
- *However --*
  - ✓ *This* Will Not Be Easy
  - ✓ *It Will Require The* Combined *Attention of Government, Labor & Industry* Working Closely Together
  - ✓ *Many Critical Factors Need Change . . .*

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In Essence Then . . .

- Maine's P&P Industry's Future Has Great Opportunities To Seize -- In Reality -- *It Is In The Hands Of Those That Will Do* . . .
  - ✓ The Right Things . . .
  - ✓ In The Right Way . . .
  - ✓ For the Right Products/Grades . . .
  - ✓ At The Right Time . . . *And That Time Is Now*
  - ✓ Or Maybe Never. . . *Choose Wisely With Sense of Urgency* – Your Future is At Stake!

And Remember . . . .

In Spite Of The Current State of Affairs For Maine’s P&P Industry -- As that Famous Arm Chair Philosopher *Ziggy* Once Said . . . .

“You **can Complain** ***Because Roses have Thorns,*** **or you can Rejoice** ***Because Thorns have Roses”***

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