

# The Perfect Storm<sup>2</sup> – Less severe than anticipated?



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Pessimistic outlook with a nuance of hope  
Results from Q1-2023 StepChange Economic Outlook Industry Study

Pessimistic outlook remains but slightly improved expectations vs. Nov 2022 | Deteriorating demand and selling prices | Energy, transport and raw material costs expected to decline | Companies prioritize cost cutting but strategic topics back on agenda | Geopolitics –single biggest worry | Digitalization back in focus again | Sustainability source of competitive advantage, talent and customers

The following publication is based on the global economic outlook study conducted in March 2023 amongst top managers and decision makers in the wider forest products industry (wood, pulp, paper, packaging, tissue). Additionally, participants of the Fastmarkets Forest Products Europe Conference 2023 were surveyed. Over 81% of the respondents are top executives or in managerial roles (68% and 13% respectively).

The aim of the survey is to gauge the sentiment of the respondents regarding macroeconomic expectations for 2023 as well as corporate trends and priorities. The second part of the survey is dedicated to the subject of digitalization and sustainability.

## Highlights of the study

- Macroeconomic outlook continues to be bleak
- Industry expectations slightly improved versus survey from November 2022
- Demand and selling prices expected to fall
- Energy, transportation, and raw material expected to decline
- Reduced availability of financing expected
- Companies focus on margin management and cost cutting while business developing initiatives are placed on the back burner
- Digitalization and environmental aspects among the top long-term factors that will influence the industry
- Companies focus on digitalization initiatives that offer cost reduction potential
- Barriers to digitalization are mostly related to change management and IT infrastructure
- Sustainability gives companies a competitive edge, both among potential clients and on the labor market

## Dreary macroeconomic outlook

The general macroeconomic outlook sentiment remains at multi-year record lows although higher than in November 2022. A vast majority of respondents predicted that the economy in their region would either stagnate or further deteriorate [see Figure 1].

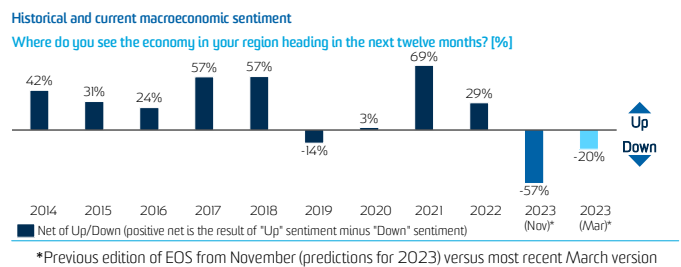


Figure 1: Macroeconomic development

The outlook related to the particular sectors of the PPP industry is even less optimistic. Most respondents in paper & paperboard manufacturing expect to see a decline in their segment, although results in the converting sector are marginally more bright, with 20% predicting an upward development. The outlook for the wood segment is the most negative.

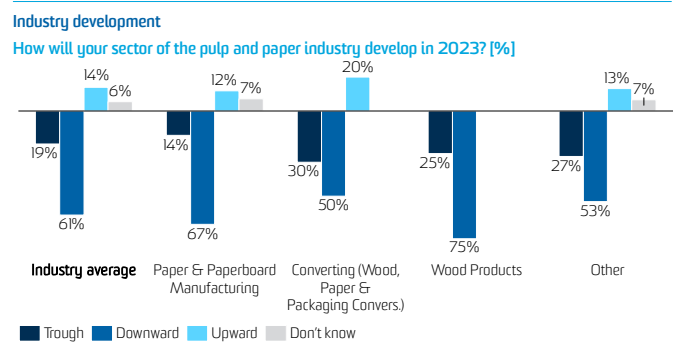


Figure 2: Outlook on industry segment development



An analysis of market-related trends indicates most respondents expect a recessive environment in 2023. Demand, selling prices and the availability of financing are expected to plummet. Input costs for energy, transportation and raw materials are expected to decline by a majority of participants - a trend that was already visible in the previous Economic Outlook. The most notable change compared to November '22 are energy costs. Additionally, it can be seen that more strategic trends are expected to be up again (M&A, Sustainability, Digitalization) [Figure 3].

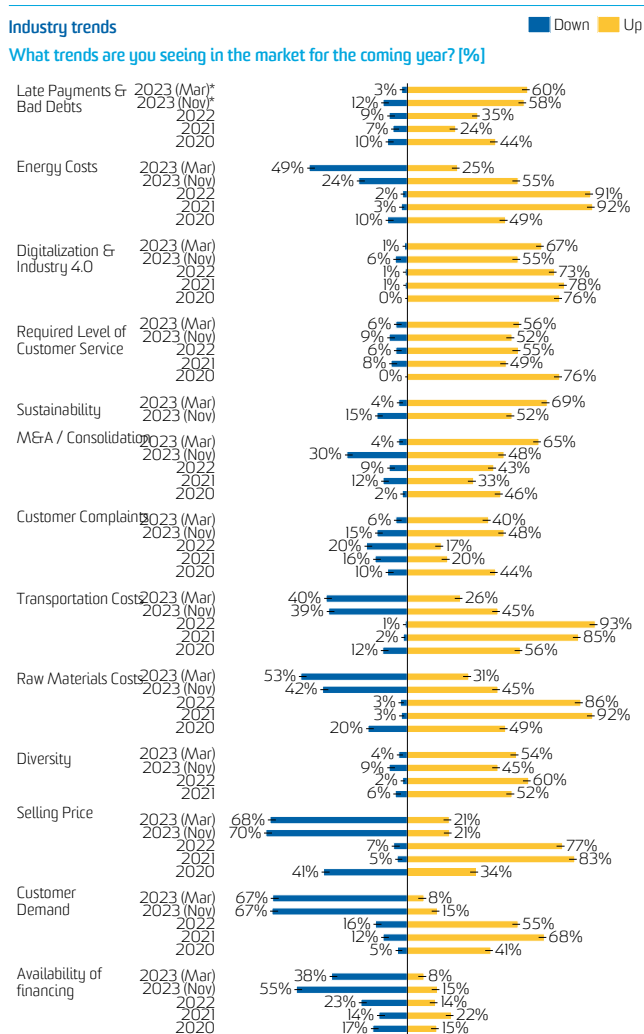


Figure 3: Industry trends

2022 has been marked by economic disruption resulting from the war in Ukraine and post-pandemic supply chain impacts. Nevertheless, industry profitability remains very high. The latest StepChange B3NCH publication shows that despite difficult market conditions, the pulp and graphics segment managed to further improve the already high EBITDA % in 2022. The

packaging peer group remained stable at a high level. Net profits were up in 3 out of 6 segments. The pulp segment further improved to new record net profit levels. [see Figure 4].

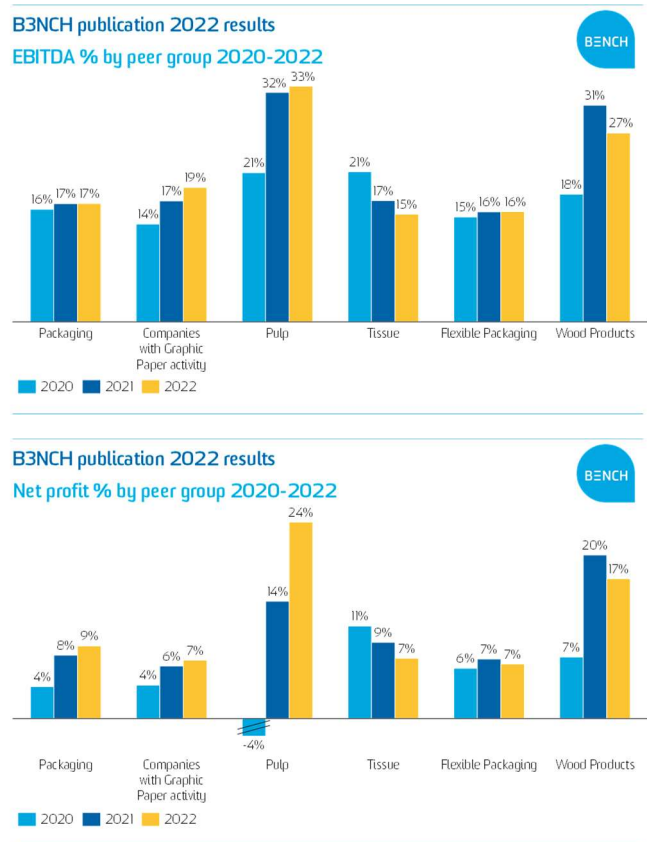


Figure 4: 2020-2022 EBITDA & Net profit % by B3NCH peer group

The expectation of a challenging market environment is reflected in a shift in company priorities for 2023 [see Figure 5]. Although pricing and margin management remains at the top for most peers, cost reduction has made a comeback now after sliding in priority in recent years.

Forward facing and business expanding initiatives, such as digitalization, sustainability and product development remain high on the list of company priorities, although their relevance has lessened slightly in comparison to previous years.

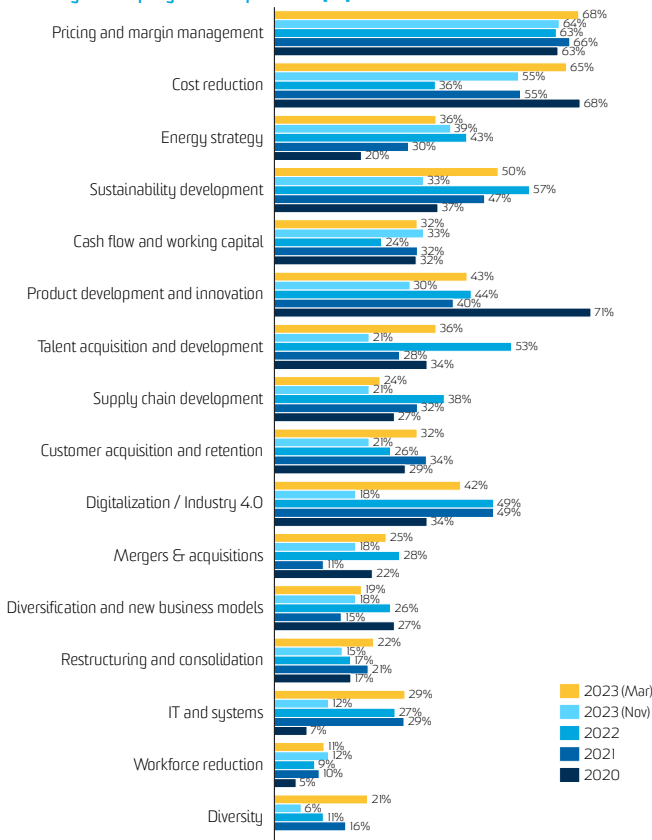
Energy strategy, which was the 3<sup>rd</sup> priority in the previous survey conducted in November 2022, has dropped substantially in the list of priorities since then. This further supports the sentiment that energy prices peaked in 2022 and there is potentially less focus on energy now.



The Perfect Storm 2 – Less severe than anticipated?  
Results from StepChange Global Outlook Industry Study March 2023

Company priorities

What are your company's current priorities? [%]



\*Previous edition of EOS from November (predictions for 2023) versus most recent March version

Figure 5: Historical comparison of current priorities

Short-term priorities are not exactly aligned with long-term industry expectations. In a longer perspective, strategic topics such as digitalization and sustainability will play an important role in shaping the industry. Both drivers are expected to have a mostly positive or very positive influence on the industry [see Figure 6].

Respondents see geopolitics, energy costs and legislation, new production capacities and imports as being the most important drivers with a negative impact.

Due to the long-term relevance of digitalization and sustainability they are explored in more detail in later sections of this publication.

Industry drivers

What influence do you expect these drivers to have on the industry in the next 5 years? [%]

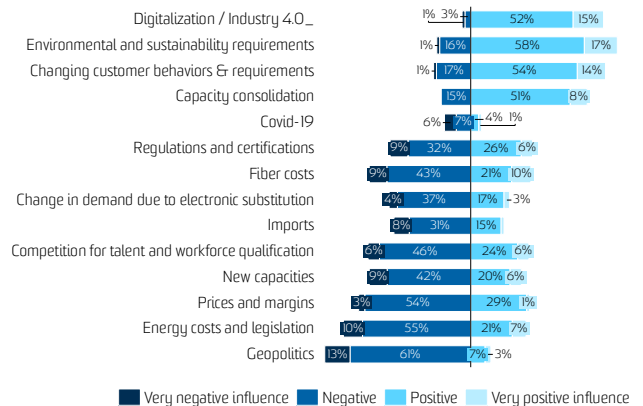


Figure 6: Main drivers and influence expectations

Digitalization focus shifts

Digitalization is back on the agenda (compared to the Nov. 22 survey) and continues to be a major area of focus for most companies, although to a slightly lesser extent than in previous years [see Figure 5].

With regards to the focus of Digitalization projects, digitalization of administrative processes ranks on top followed by production processes [see Figure 7]. A likely explanation is that digitalization in administration processes is typically more easily implementable, and solutions tend to be readily available. Smart products and machinery rank last, while Supply Chain and Marketing receive medium priority.

Digitalization

What projects concerning Digitalization / Industry 4.0 is your company currently engaged with?

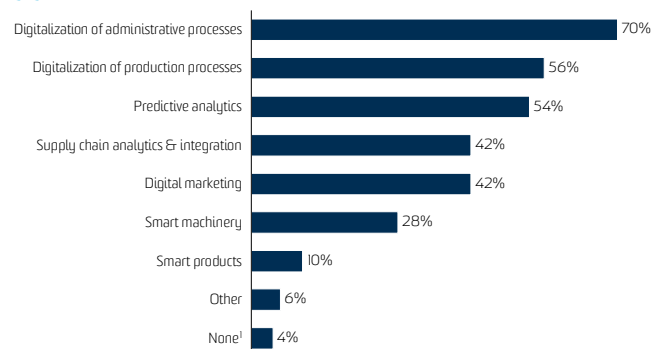


Figure 7: Digitalization projects

With regards to expected benefits from introducing digital solutions, productivity and cost reduction rank on top followed by energy efficiency with a surprisingly big gap. Energy efficiency has ranked higher in previous surveys. New business models



and sales have surprisingly low perceived benefits with products and sustainability at the bottom of the list [see Figure 8].

#### Digitalization

Please select the areas where you expect the highest benefits from Digitalization / Industry 4.0 for your business?

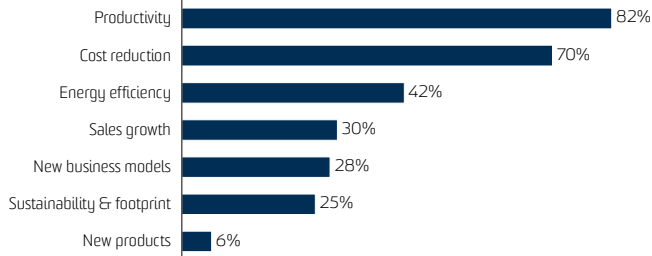


Figure 8: Expected benefits from digitalization

With regards to barriers to digitalization, two main drivers remain in the top three. Cultural and organizational barriers remain on top as well as existing IT systems and Infrastructure. [see Figure 9]. Security and calculating ROI additionally remain a challenge.

Securing financing is not considered to be a barrier in the introduction of digital solutions anymore. Earlier studies pre 2019 had this topic identified as a main barrier. This indicates that it is commonly understood that investments in digitalization are essential even though the ROI might not always be immediate.

#### Digitalization

In your opinion, from a company perspective, what are the 3 greatest challenges / barriers to implementing Digitalization / Industry 4.0?



Figure 9: Barriers to digitalization

Digitalization plays a key role in sustainability as well. However, only slightly over 50% of respondents have access to

tools that can provide integrated and automated measurement of sustainability performance [see Figure 10].

### Sustainability a source of competitive advantage

The results demonstrate that sustainability focus is further increasing, despite challenging market conditions. Over 83% of companies have defined a sustainability strategy that will help them reduce their footprint [see Figure 10]. The share of respondents that track their footprint has also increased since November.

#### Sustainability

Please indicate if you agree to the following statements concerning sustainability and footprint in your organization

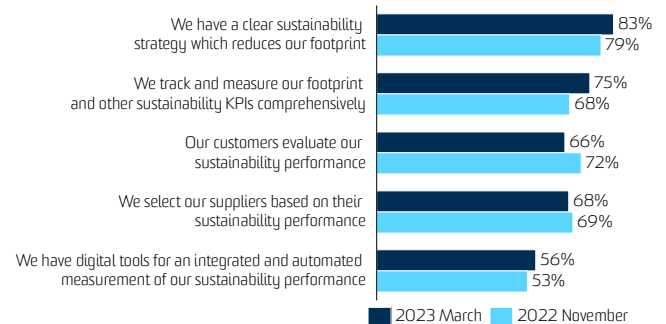


Figure 10: Sustainability strategy perception

Although noticeable improvements are being made, there remains a long road ahead to becoming carbon neutral with regards to energy sources. It is worth noting, however, that in direct comparison to the previous study the focus on renewables has increased again [see Figure 11]. Especially some European companies had to temporarily take a step backwards in 2022 to substitute energy demand during the disruption in energy markets caused by the war in Ukraine.

#### Sustainability

Our Energy strategy is based on...

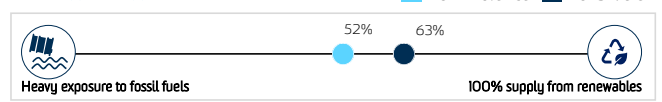


Figure 11: Energy strategy [% of Renewable energy planned to be used]

Interestingly, more and more respondents are viewing sustainability as a competitive advantage even though it doesn't pay off in terms of financial returns.

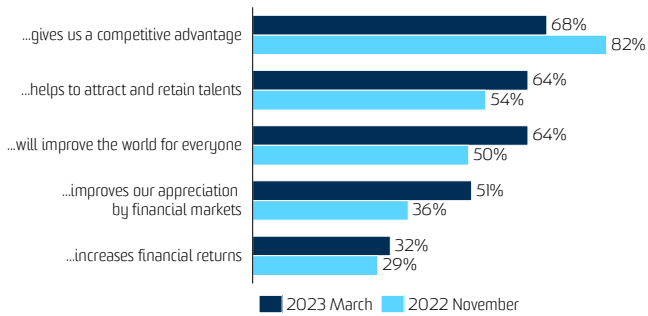
The benefit of a sustainability strategy is also seen as a lever to attract and retain talent, as environmental awareness is increasing, especially among younger generations. [see Figure 12].



## Sustainability

Please complete the statement (multiple answers allowed).

Our sustainability strategy...



While the industry is used to cyclicalities it is currently subject to strong headwinds such as inflation, increasing interest rates (in a capital-intensive industry) and declining demand combined with overcapacities in some segments. However, input costs are expected to decline further therefore mitigating some of the effects. With all these headwinds, the threat of a perfect storm remains, but potentially with less adverse effects than perceived just a few months ago.

Figure 12: Benefits of increasing sustainability

## Summary & outlook: Challenges & opportunities ahead

A financially strong 2022 leads into an uncertain 2023 for most companies in the industry. Companies prepare themselves for a gloomy future while trying to lead companies forward.

- Significant decline of demand and sales prices indicate a recessive environment
- Input costs are expected to decline
- Priorities have shifted towards housekeeping, i.e., cost cutting and price & margin management
- Manager focus on strategic, long-term topics such as digitalization, sustainability, and M&A back on the agenda
- Digitalization as a topic is undisputed even though many challenges still exist from choosing the right projects and capturing benefits
- Sustainability focus is increasing, and the topic is perceived as a differentiator
- Building a sustainable business model will secure future clients and employees, while at the same time hedging against regulatory changes
- Geopolitics is the key single driver with a perceived negative influence on further growth and development



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### About StepChange Consulting

StepChange is an industry focused and independent management consulting company with a proven track record in supporting clients to achieve sustainable value. StepChange provides support to top tier organizations in the industry from strategy development to implementation of operational improvements.

With an international team of industry experts StepChange can hit the ground running. StepChange provides innovative and yet pragmatic solutions, placing an emphasis on delivering measurable business results.

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