



StepChange
CONSULTING

Pollyannaism or Realism? Hope vs. Trepidation - Cautious Optimism Ahead

Companies recommit to strategic agendas while managing near-term priorities
Results from StepChange Economic Outlook Industry Study – Spring 2024

Cautious optimism | Pricing and Demand up | Raw materials and transport costs expected to rise | Companies prioritize cost reduction over long-term strategic topics| Geopolitics continued topic of concern | Digitalization and Sustainability back as top priorities |

The following publication is based on the economic outlook study conducted in February and March 2024 amongst top managers and decision makers in the wider forest products industry (wood, pulp, paper, packaging, tissue), including participants of the Fastmarkets Forest Products Europe Conference in Istanbul. Of all the respondents, 1/3 are in C-level positions and 2/3 in other top level managerial roles.

The aim of the survey is to gauge the sentiment regarding macroeconomic expectations for 2024 as well as corporate trends and priorities. The second part of the survey is dedicated to the subject of digitalization and sustainability.

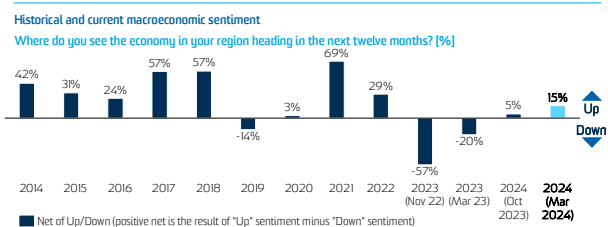
Highlights of the study

- Optimism net-positive and continues to increase since low in Nov 22 study
- Prices expected to rise
- Focus of companies on pricing, margin management and cost reduction
- Sustainability development #3 priority
- Energy strategy currently not major priority
- Transportation and raw material costs expected to rise
- Capacity consolidation and digitalization considered a positive influencer for industry developments
- New capacities, increasing costs, energy and fiber costs considered long term barriers
- Geopolitical tensions are a growing source of concern
- Sustainability developments progressing

Trending up

The recent study reveals a continued upward trend in economic expectations for the fourth time in a row. The outlook is net-positive for the first time since the 10-year low in November 2022.

This indicates a certain level of resilience and recovery, despite ongoing challenges. Considering only C-level responses, the results are even more optimistic with a net upward trend reaching 29%. Most respondents expect the economy in their region to stagnate or continue to increase slightly. [see Figure 1].



*Date in brackets signifies date of survey response collection – responses concern following year

Figure 1: Macroeconomic development

The industry outlook also shows a continued growth of optimism. Most respondents (60%) anticipate an upward trend in the pulp, paper, and packaging sector in 2024, yet a sense of uncertainty persists with 39% expecting the contrary outcome. The paper & paperboard sector displays the highest rate of optimism, with 61% of participants foreseeing a rise or a peak [see Figure 2].

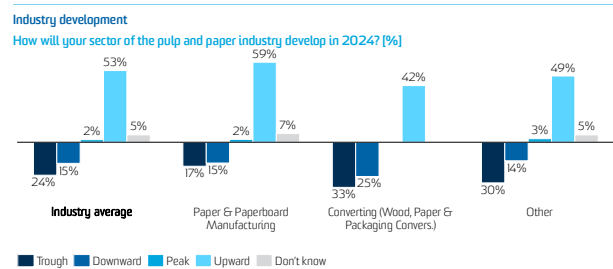


Figure 2: Outlook on industry segment development

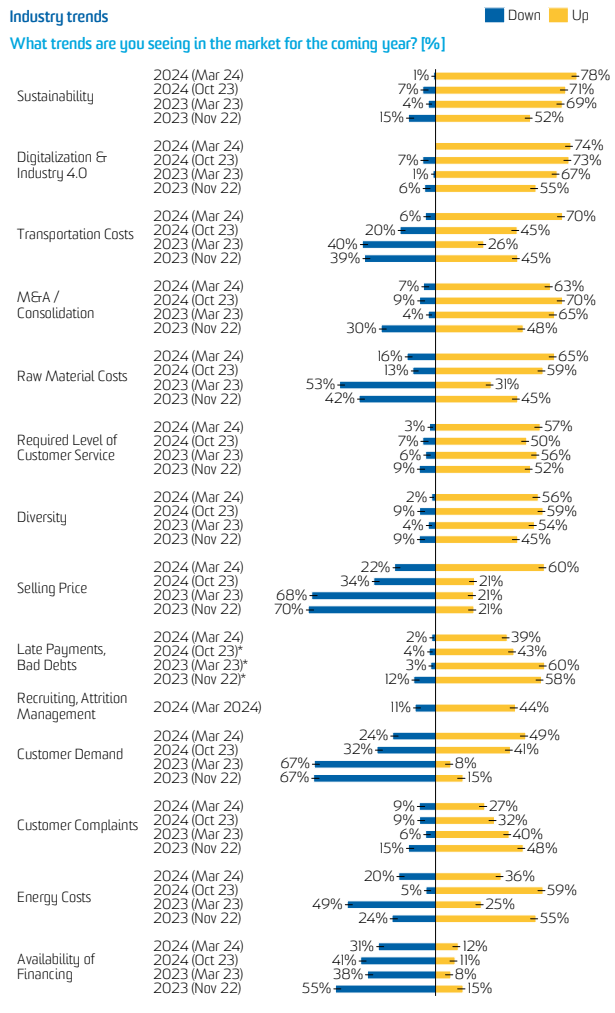
Over the past year, there has been a noticeable upward trend in industry expectations. In the study conducted in March 2023, only 14% expected an upward trend, in October of last year the results grew to 44%, and now that number has increased to 53%. This growing sense of optimism suggests a brighter outlook for the industry in 2024 compared to 2023.

Market-related trends show an overall positive picture. Customer demand and selling prices are expected to increase again. Many also expect that costs will continue to rise after



perceived drops in 2023 - especially transportation and raw material costs. Availability of financing is still expected to drop, yet to a lesser extent as interest rates remain high. Late payments/bad debts are expected to increase [see Figure 3] but trending down from the previous three surveys.

In general, the negative trends that were very prominent in the 2023 studies are no longer as prominent, indicating that the outlook has improved. Strategic topics like sustainability and digitalization are the perceived top two trends again. However, trend expectations do not fully align with company priorities [see Figure 5].



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Figure 3: Industry trends

In 2023, numerous companies faced complexities in a post-corona world. The repercussions of ongoing wars and overall geopolitical tensions reverberated, leading to a weakened global demand. These effects had a direct impact on the pulp, paper, and packaging sectors. As seen in the latest FY-23 B3NCH publication (a comparison of financial performance of

90+ stock listed companies in various segments), almost all peer groups experienced a decline in profitability compared to the previous years, mostly due to weakened customer demand except for the tissue and flexible (plastic) packaging segments, defying the overall downward trend [see Figure 4].

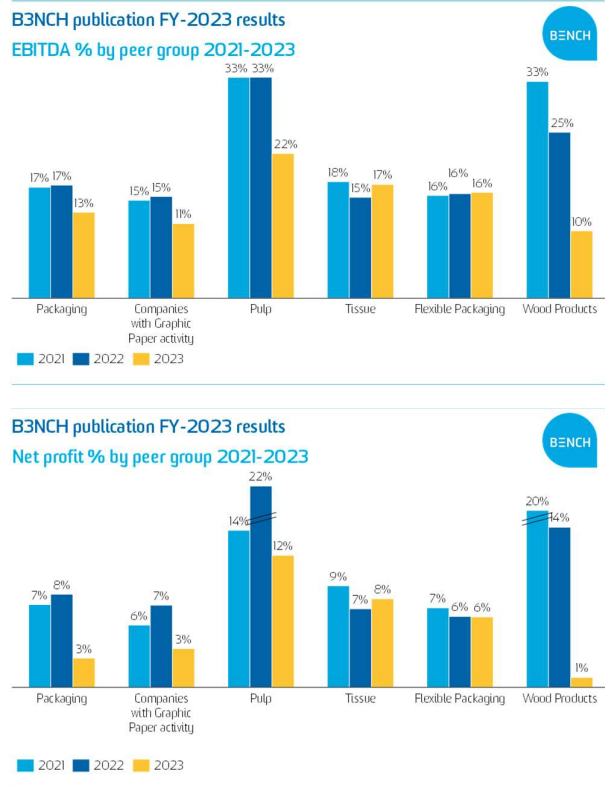


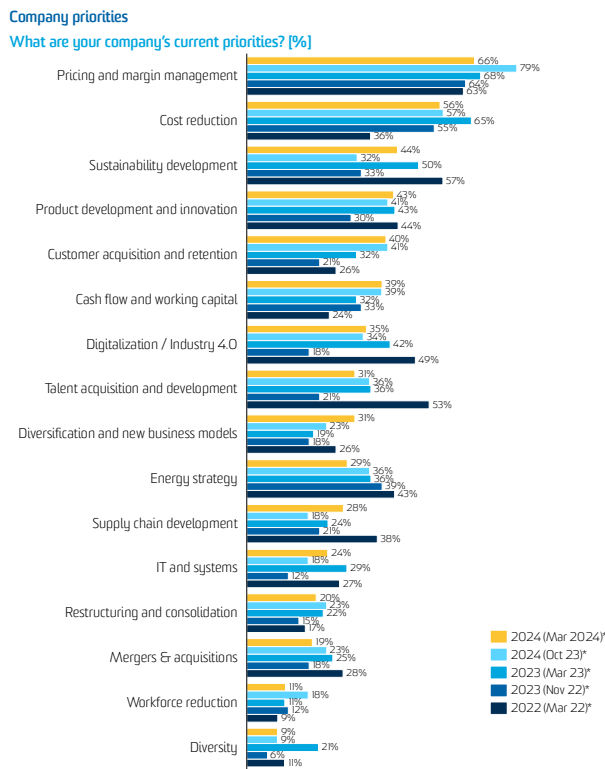
Figure 4: 2021-2023 EBITDA & Net profit % by B3NCH peer group

Most severely hit was the wood products segment which faced significant headwinds after a few years of boom with increasing interest rates and sluggish demand in construction-related industries. Net profits plummeted to a mere 1% in comparison to a 20% record in 2021.

Shift in company priorities

Company priorities [see Figure 5] have also changed with overall weaker demand. Focus areas are still related to costs and margins. Pricing and margin management is again the number one priority. Cost reduction remains in second place. Sustainability Development has moved up to third place again (increase of 12pp). Supply Chain Development increased by 10pp, likely fueled by recent logistics bottlenecks and disruptions. Workforce reduction decreases 7pp and is currently, together with diversity, found at the bottom of company priorities. M&A has declined as a priority despite recent announcements.





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Figure 5: Historical comparison of current priorities

As seen in previous publications, short-term priorities are not necessarily in line with long-term industry expectations. Strategic topics such as digitalization, M&A, sustainability, and diversity are expected to play a significant role in shaping the industry even if not currently a top priority [see Figure 6].

However, the current most important factor expected to positively drive the industry in the upcoming years is digitalization followed by capacity consolidation, changing customer behaviors & requirements, and sustainability requirements. The competition for talent is seen both as a positive and negative influence on industry growth.

Among the key drivers that are expected to have the most negative impact on the industry are geopolitics, energy costs/legislation, fiber costs, electronic products substitution, new capacities, and fiber costs. Global geopolitical tensions are creating additional uncertainty in an industry that is accustomed to global free trade.

Sustainability requirements are still expected to have a positive influence while the risk of regulations and legislative restrictions is expected to have a negative effect.

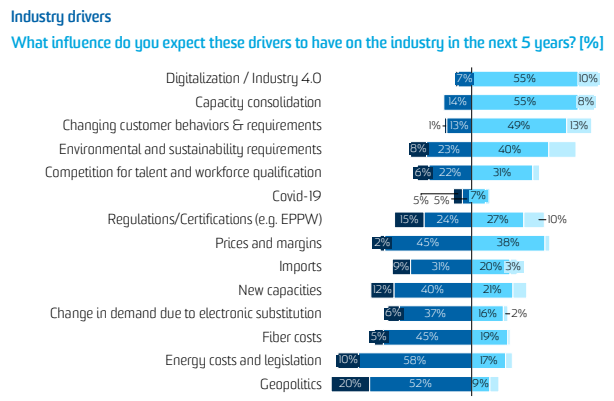


Figure 6: Main drivers and influence expectations

Status of digitalization: Processes in focus

Similarly to prior studies, and in addition to the economic part of the study, the survey also contained a section about the status of digitalization and an outlook on sustainability developments in the industry. Respondents expect digitalization to remain an important driver of change [see Figure 6] even if currently not amongst top company priorities. The focus of digitalization is on production processes, administrative processes, and predictive analytics. Interestingly disruptive Technologies including AI and Digital Sales Channels currently play no role [see Figure 7].

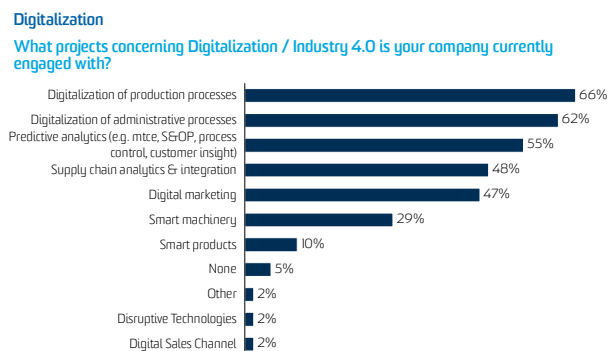


Figure 7: Digitalization projects



Expected benefits of digital solutions are productivity and cost reduction, followed by energy efficiency, sales growth, and new business models [see Figure 8].

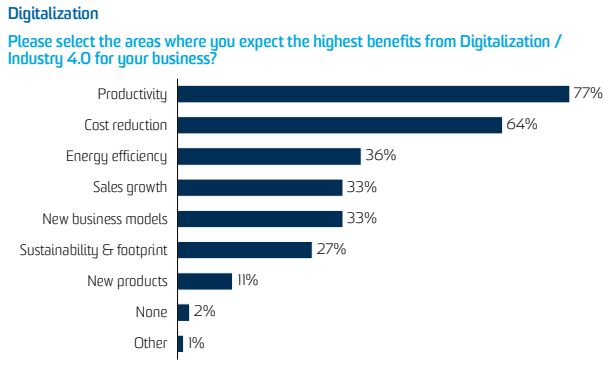


Figure 8: Expected benefits from digitalization

Energy efficiency has surpassed sales growth in terms of expected benefits relative to prior studies. Cost reduction and productivity remain at the top.

According to respondents, the top four main barriers to digitalization are Changing existing processes, IT Systems & Infrastructure, Education & Training of resources, and Ensuring security & protection. [see Figure 9].

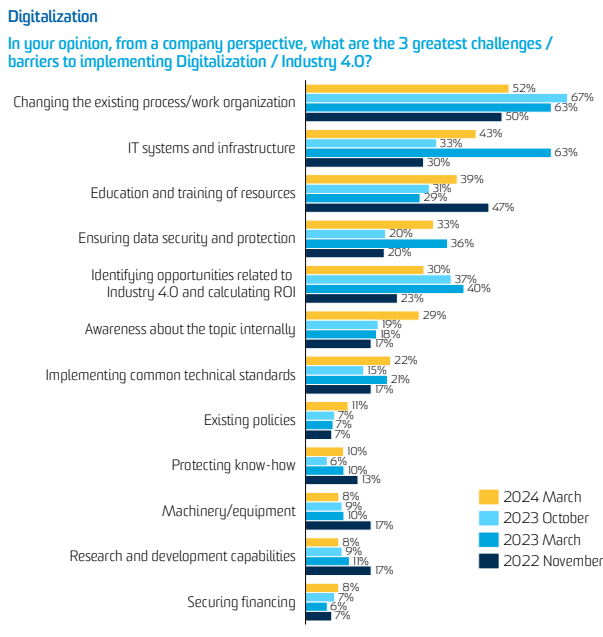


Figure 9: Barriers to digitalization

Sustainability Development: Continued Progress

Sustainability is considered the #4 trend [see Figure 6] expected to positively impact the industry, moving up from #9 to #3 in this most recent study [see Figure 5].

It appears that companies are progressing and recommitting to their sustainability agendas after having coped with more near-term challenges in prior studies. With each survey, a larger and larger share of respondents, report having a clear sustainability strategy and an increasing capability to track their footprint [see Figure 10].

Although digitalization is a key driver in enhancing and monitoring sustainability, it has been a relatively underdeveloped area. It remains at the same level as in the two prior studies. Only 56% of respondents claim to have access to tools that allow for an integrated and automated tracking of sustainability performance.

Tracking and measuring footprints has seen the largest increase since the prior survey, moving up to second place. The selection of suppliers based on their sustainability has moved down to fourth place.

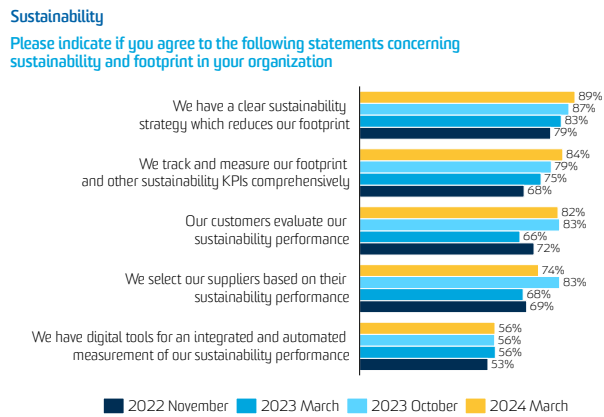


Figure 10: Sustainability strategy perception

The industry continues to reduce its dependency on fossil fuels. Based on the responses the share of renewables as part of the overall energy consumption continues to increase from study to study and is now perceived to be at 66% [see Figure 11].

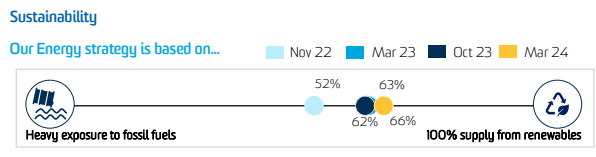


Figure 11: Energy strategy [% of Renewable energy planned to be used]



In comparison to the previous study there is an increased optimism towards the benefits of sustainability across almost all the statements. The view that sustainability has the potential to improve the world for everyone has increased again. The positive view on the potential for profitability improvement has increased by 11pp and a perceived appreciation by financial markets has risen again as well [see Figure 12]. The categorization of sustainability as a specific competitive advantage continues to decline which might indicate that it's simply a non-optional hygiene factor.

Sustainability

Please complete the statement (multiple answers allowed).

Our sustainability strategy...

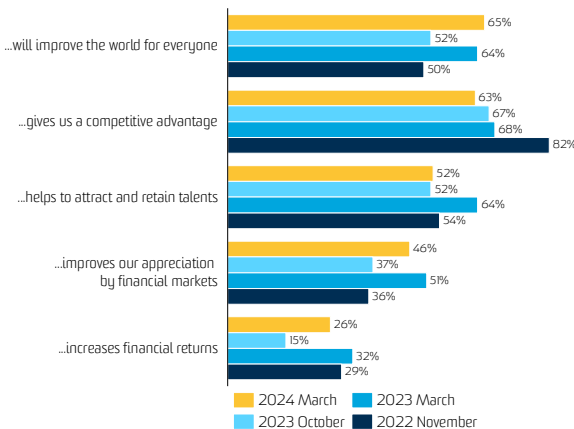


Figure 12: Benefits of increasing sustainability

Summary & outlook: Challenges & opportunities ahead

While the outlook is cautiously optimistic and net-positive, the average outcome is still well below the 11-year average. However, the sentiment has continuously increased from study to study since the low point in November 2022. Companies are focusing again on longer-term strategic topics but are keeping tactical measures in focus to secure results and manage immediate challenges.

- Mixed industry outlook– while most respondents expect an upward trend, some are still predicting a downturn in 2024
- Prices and demand are expected to increase again
- Pricing and margin management, cost reduction and sustainable development take central focus in uncertain times
- Customer demand and selling price are expected to increase again in 2024

- At the same time higher input costs are equally expected
- Cost management remains a top priority
- A growing focus on diversification and the search for new business models reflect the ongoing pressure on market players to manage demand
- Capacity consolidation and digitalization are expected to be a major positive driver of future industry development
- Geopolitical tensions are expected to impact uncertainty – also reflected in the increased Supply Chain focus
- Long-term strategic topics, such as sustainability and digitalization have found their way back to the top priorities again and are found amongst the top long-term trends
- Administrative and production processes remain at the top of the list of areas companies are aiming to digitalize
- IT & Systems are seen as large barriers to digitalization and is subsequently rising on the priority list
- More optimism again regarding the benefits of sustainability compared to the prior study

The sentiment is more positive again even if viewpoints remain divided given the current economic climate. Prices and demand are expected to increase, but there are still many macro-economic uncertainties regarding inflation and interest rates underlined by further growing geopolitical tensions and supply chain disruptions. While these drivers will continue to be a challenge, the industry has become more resilient with the various crises over the past 3 years. While expectations are somewhere between Pollyannaism and realism the new normal will remain unpredictability and volatility.





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.

StepChange is further an industry thought leader in digital strategy and on the forefront of bringing digital transformation to the fiber value chain.

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

For further inquiries and comments regarding this publication, please contact us at leapfrog@stepchange.com

