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I N D U S T R Y
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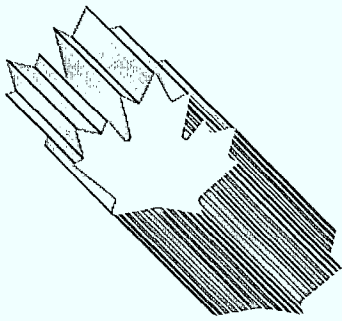


Industry, Science and
Technology Canada

Industrie, Sciences et
Technologie Canada

Sanitary Tissue Papers

Canada



I N D U S T R Y

P R O F I L E

SANITARY TISSUE PAPERS

1988

FOREWORD

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In a rapidly changing global trade environment, the international competitiveness of Canadian industry is the key to survival and growth. This Industry Profile is one of a series of papers which assess, in a summary form, the current competitiveness of Canada's industrial sectors, taking into account technological and other key factors, and changes anticipated under the Canada-U.S. Free Trade Agreement. Industry participants were consulted in the preparation of the papers.

The series is being published as steps are being taken to create the new Department of Industry, Science and Technology from the consolidation of the Department of Regional Industrial Expansion and the Ministry of State for Science and Technology. It is my intention that the series will be updated on a regular basis and continue to be a product of the new department. I sincerely hope that these profiles will be informative to those interested in Canadian industrial development and serve as a basis for discussion of industrial trends, prospects and strategic directions.

1. Structure and Performance

Structure

Sanitary tissue papers include facial tissue, bathroom tissue, paper towels and paper napkins. The main raw material is primary mill rolls, which are converted through a second manufacturing process into "converted tissue products" sold to retail stores, commercial/industrial users, hotels and educational institutions.

The production of sanitary tissue papers entails a significant amount of integration with the production of mill rolls. Industry data indicate that about 85 percent of mill roll production in Canada is converted within integrated operations. The value added from the converting operations is about 40 percent.

Ownership of the sanitary tissue paper industry is mainly Canadian, although two of the largest companies are at least 50 percent owned or controlled by U.S.-based companies. The industry is dominated by four major integrated companies which control an estimated 85 percent of the consumer retail market and a major share of the commercial/industrial market. Four other medium-sized companies, which specialize in industrial products or private label, consumer retail and commercial/industrial brands, control much of the remaining market.

Sanitary tissue papers have a high volume-to-weight ratio so that transportation represents a major cost in the final delivered price. Consequently, offshore trade is virtually non-existent and converting operations tend to be located near major consuming regions.

Most Canadian capacity is concentrated in Quebec and Ontario, particularly in Montréal and Toronto. Significant capacity is also concentrated in Vancouver, British Columbia. A small amount of capacity is located in other parts of Canada.

Because a number of sanitary tissue products are grouped in broad categories with other pulp and paper products, detailed data on this industry are not available. However, analysis of information from both industry and government sources indicates that, in 1986, the industry comprised some 30 establishments which shipped products worth \$520 million. International trade was valued at \$20 million in exports and \$40 million in imports. Approximately 3000 people were employed in converting operations in 1986.

Two types of raw material resources are used to make primary mill rolls. They are market pulp (including groundwood, chemical and thermal mechanical pulp) and recycled waste paper. Virgin fibre, which is purchased in the form of market pulp, tends to be considerably more expensive than recycled waste paper, especially now that international prices for market pulp are at record levels. However, collecting and processing recycled waste paper can pose significant problems.

Canadian production tends to rely more heavily on virgin fibre than its U.S. counterpart. In general, products made with virgin fibre are of a higher quality than those of recycled waste paper. Most of the virgin fibre used to manufacture primary mill rolls is produced in Canada. An estimated 25 to 30 percent of the recycled waste paper used in Canada is imported from the United States.

Robert S. Roberts
DEPARTMENT OF REGIONAL
INDUSTRIAL EXPANSION
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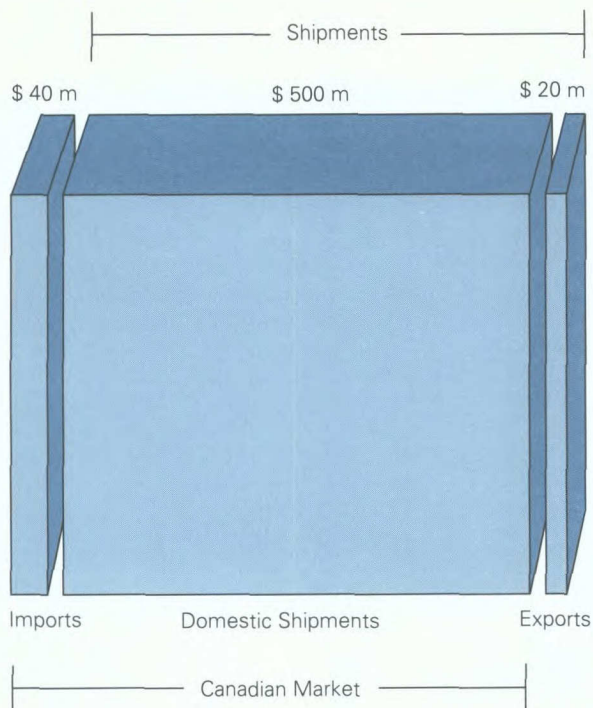
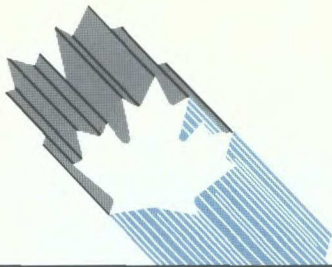
MINISTÈRE DE L'EXPANSION
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Canada



Industry, Science and
Technology Canada

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*Imports, Exports and Domestic Shipments
1986*

Performance

In general, product demand is not subject to as many cyclical swings as other forest products. However, some under-utilization of capacity occurred during the 1981 recession. Since 1983, consumption of consumer retail products has increased by an estimated two to three percent annually, while growth in the commercial/industrial market has averaged about five percent per year. During 1986, industry sources indicate that the industry operated at approximately 90 percent of capacity. Since the recession, some new investment in modernization and capital projects has been undertaken.

Trade has not been significant. Exports have represented only about four percent of shipments and imports about seven percent of the domestic market over the last decade. The limited trade that does take place tends to be related to markets close to the Canada-U.S. border.

The basic structure of the industry has not changed in the past 10 years. It continues to be dominated by the same four integrated companies. In recent years, several producers have made significant efforts to increase productivity through capital expenditures on new equipment and other cost-reduction projects. However, the industry can certainly improve competitiveness through additional modernization, especially compared to its American counterpart.

On the basis of the limited published financial information, it would appear that the industry has performed well over the years. Profitability, as a percentage of sales, has been in the order of four to six percent. Some of the smaller firms have achieved even higher profit margins. A number of companies have reduced their debt load substantially over the last four years. In general, the industry maintains high working capital levels and low debt-equity ratios.

2. Strengths and Weaknesses

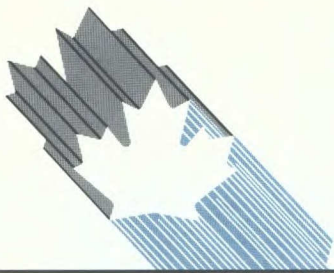
Structural Factors

Raw material represents the largest single cost factor in the production of converted tissue products, at between 25 and 35 percent. The Canadian industry, unlike its U.S. counterpart, uses more market pulp and less recycled waste paper. This practice has important cost implications because the price of recycled waste paper is about one-half to two-thirds that of market pulp. Moreover, market pulp prices are more subject to cyclical variations and are currently at a record high.

Labour costs and associated benefits in Canada are somewhat higher than comparable costs in the United States. On the other hand, energy costs are lower in Canada. Overall, productivity is somewhat higher in the United States, mainly because of scale economies and the dedication of production machinery to one grade of product. Nevertheless, certain Canadian companies may be as productive as their American counterparts.

With a high volume-to-weight ratio, transportation is a major cost element for most tissue products. It plays an important part in marketing, pricing strategies and cost competitiveness, and also limits the scope of trade. The effects of transportation costs, however, are largely offset by the close proximity of converting operations to major consuming regions. The locations of many Canadian plants not only facilitate exports to nearby U.S. markets but also allow companies to take advantage of their extensive use of trucks to haul back recycled waste paper.

The industry is characterized by a variety of plant sizes designed to meet the requirements of a small domestic market. While some plants are large by Canadian standards, they are considerably smaller than many comparable plants in the United States. This size limitation is considered an impediment to the competitive performance of the industry.



The relatively small Canadian market compels companies to produce a broad range of finished products in various sizes and grades. This situation results in short production runs and higher costs associated with more frequent change-overs, longer machine set-up times and larger inventories. Large-scale U.S. operations also benefit from reduced per-unit marketing costs. As a result, the Canadian industry is less efficient and less productive than its U.S. counterpart.

As previously noted, two of the large companies in the industry are owned, substantially or wholly, by U.S.-based companies which manufacture the same product lines on both sides of the border. As a result, corporate policies developed in American head offices could have a bearing on Canadian corporate decisions on exports to the United States, production and plant rationalization and future directions.

Trade-related Factors

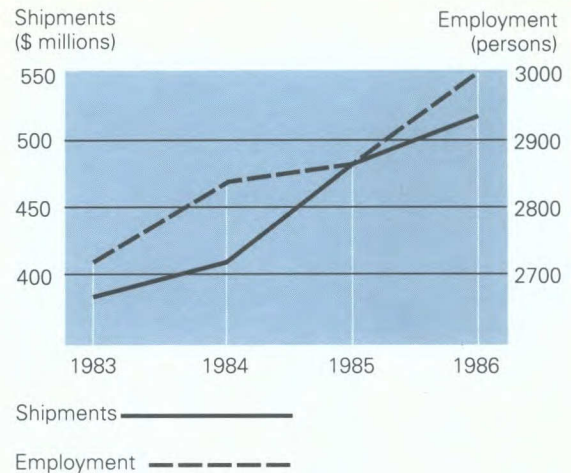
The industry has developed behind tariff protection which has been reduced substantially over the last 20 years. Canadian tariffs are currently at 10.2 percent for converted products, while American tariffs are set at either three or 5.3 percent, depending on the classification. Under the Canada-U.S. Free Trade Agreement (FTA), these tariffs will be eliminated within five years. Non-tariff barriers (NTBs) are not significant.

Technological Factors

Technological innovations for converting operations have tended to emphasize replacement and modernization of machinery. Technology innovations have been primarily process related, although some have been product oriented. In general, the level of technological development in Canadian mills is similar to that in American plants, although most Canadian operations are smaller. Much of the new technology is either American or European and is generally available to all manufacturers.

Other Factors

Forest resources in Canada fall mainly under provincial jurisdiction. The provinces administer various reforestation programs. They lease forest land to forest products companies, which pay stumpage fees as they harvest. As a result of a trade dispute with the United States, a 15-percent export charge on certain softwood lumber shipments to the United States was initiated in December 1986. As part of the bilateral agreements arising out of this trade dispute, some provinces are in the process of raising stumpage fees to offset the export charge, which will increase raw material costs to all wood-using industries.



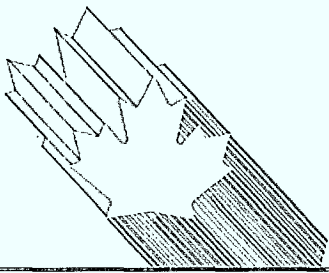
Total Shipments and Employment

3. Evolving Environment

Markets for sanitary tissue products are largely unaffected by the cyclical swings of the economy because many of the products are considered non-discretionary. Industry forecasts indicate that an annual growth rate of about two to three percent for consumer retail products and three to five percent for commercial/industrial products can be expected to continue in the near term. Growth is based primarily on demographic factors and changing taste patterns that favour the disposable nature of tissue. Less robust growth is expected by the middle of the next decade because of demographic factors. In the commercial/industrial market, demand for some products, such as paper towels, has decreased.

Many of the non-integrated converters purchase their market pulp on the open market and have been subjected to substantial increases in material prices during recent years due to increased worldwide demand. Wholesale selling prices of converted products have not increased, however, because of intense competition and marketing programs by the major producers. Companies have responded to the price squeeze in part by reducing both the sheet count and sheet size of the finished products.

By eliminating tariff protection within five years, the FTA would likely increase competition from American producers in the Canadian market. Increased competition would force some domestic firms to invest in plant modernization. For other Canadian companies, the increased competition could result in a slow slide on profit margins. Lower profit margins may make it more difficult for these firms to obtain financial support for initiatives such as modernization and expansion. Ultimately, lower profit margins could lead to decreasing capital investment and increasing obsolescence despite the need for modernization and expansion to be competitive.



Domestic adjustment to bilateral free trade will likely include plant rationalization and some possible dislocation of workers, along with implementation of new marketing, promotional and distribution strategies.

4. Competitiveness Assessment

A significant portion of the Canadian sanitary tissue industry is not as cost competitive as the American industry. Canadian products are generally more expensive than American products because of higher material, labour and transportation costs; smaller scale of operations; and non-dedicated machinery. Industry sources have emphasized the importance of Canadian-U.S. currency fluctuations on competitiveness.

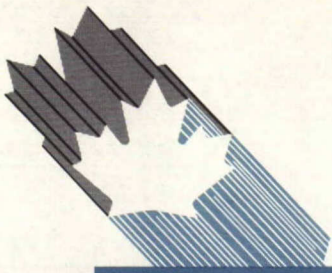
Some opportunities have been created by aggressive marketing in regions close to the Canadian border. In some cases, Canadian mills have limited their exports by choice or by corporate policy developed in foreign head offices. The American industry continues to modernize and increase plant scale. Increasingly, it could represent a threat to Canadian producers in the domestic market.

The FTA will eliminate tariff protection for Canadian producers over a five-year period. However, high transportation costs and the need to locate converting operations close to large cities will influence the volume of trade and thereby limit the scope of competition to regional markets. To improve their competitive position, Canadian companies will need to continue to modernize and reconsider their marketing strategies in terms of a North American market.

For further information concerning the subject matter contained in this profile, contact:

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Ottawa, Ontario
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PRINCIPAL STATISTICS¹

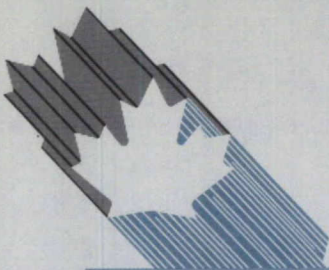
SIC(s) COVERED: 2793 (1980)

| | 1976 | 1983 | 1984 | 1985 | 1986 |
|-------------------------|------|-------|-------|-------|-------|
| Establishments | N/A | N/A | 30 | 30 | 30 |
| Employment | N/A | 2 720 | 2 840 | 2 860 | 3 000 |
| Shipments (\$ millions) | 282 | 385 | 410 | 480 | 520 |

TRADE STATISTICS

| | 1976 | 1983 | 1984 | 1985 | 1986 |
|--|------|------|------|------|--------|
| Exports (\$ millions) | 3 | 15 | 15 | 16 | 20 |
| Domestic shipments (\$ millions) | 279 | 370 | 395 | 464 | 500 |
| Imports (\$ millions) | 25 | 22 | 40 | 30 | 40 |
| Canadian market (\$ millions) | 304 | 392 | 435 | 494 | 540 |
| Exports as % of shipments | 1 | 4 | 4 | 3 | 4 |
| Imports as % of domestic market | 8 | 6 | 9 | 6 | 7 |
| Source of imports (% of total value) | | | U.S. | | Others |
| | 1984 | | 100 | | — |
| | 1985 | | 100 | | — |
| | 1986 | | 100 | | — |
| Destination of exports (% of total value) | | | U.S. | | Others |
| | 1984 | | 98 | | 2 |
| | 1985 | | 98 | | 2 |
| | 1986 | | 98 | | 2 |

(continued)



MAJOR FIRMS

| Name | Ownership | Location of Major Plants |
|----------------------------------|-------------------|---|
| Atlantic Packaging Products Ltd. | Canadian | Toronto, Ontario |
| E.B. Eddy Forest Products Ltd. | Canadian | Hull, Quebec |
| Facelle Company Limited | Canadian | Toronto, Ontario |
| Les Industries Cascades Ltée | Canadian | Kingsey-Falls, Quebec |
| Kimberley Clark of Canada Ltd. | American | Rexdale, St. Catharines and Huntsville, Ontario Saint John, New Brunswick ² St-Hyacinthe, Quebec |
| Perkins Paper Ltd. | Canadian | Laval and Candiac, Quebec |
| Scott Paper Limited | Canadian/American | New Westminster, British Columbia Lennoxville and Crabtree, Quebec |
| Wyant & Company Limited | Canadian | Montréal, Quebec Toronto, Ontario |

Notes:

1 Detailed statistics are not available for this industry, as many of the products are grouped by Statistics Canada in broad categories with other pulp and paper products. The statistics provided represent best estimates based on analysis of information from industry and Statistics Canada.

2 Irving Tissue purchased this facility in 1988.

N/A Not available

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