

## A Wall Street View of Pulp and Paper Markets

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## Presentation to International Pulp Week 2007

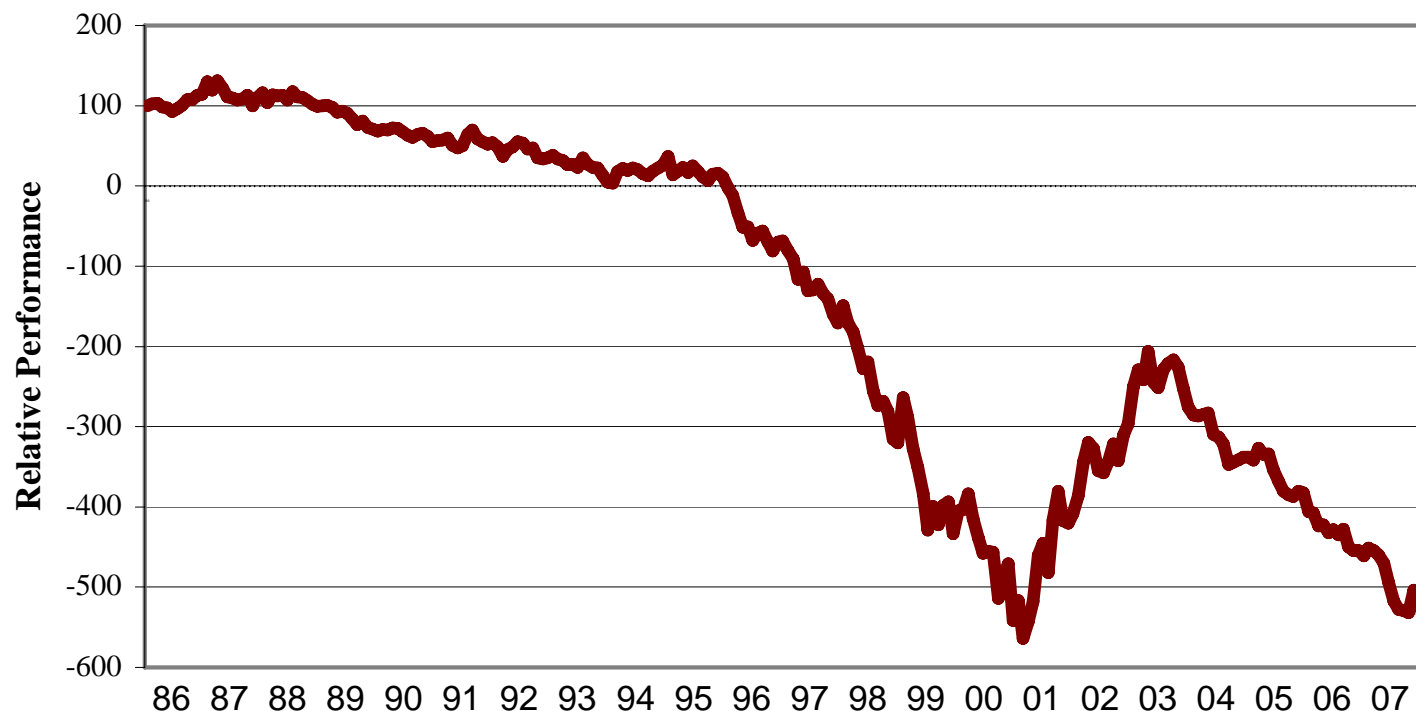
May 9, 2007

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## What Does Wall Street Think of the Pulp and Paper Industry?

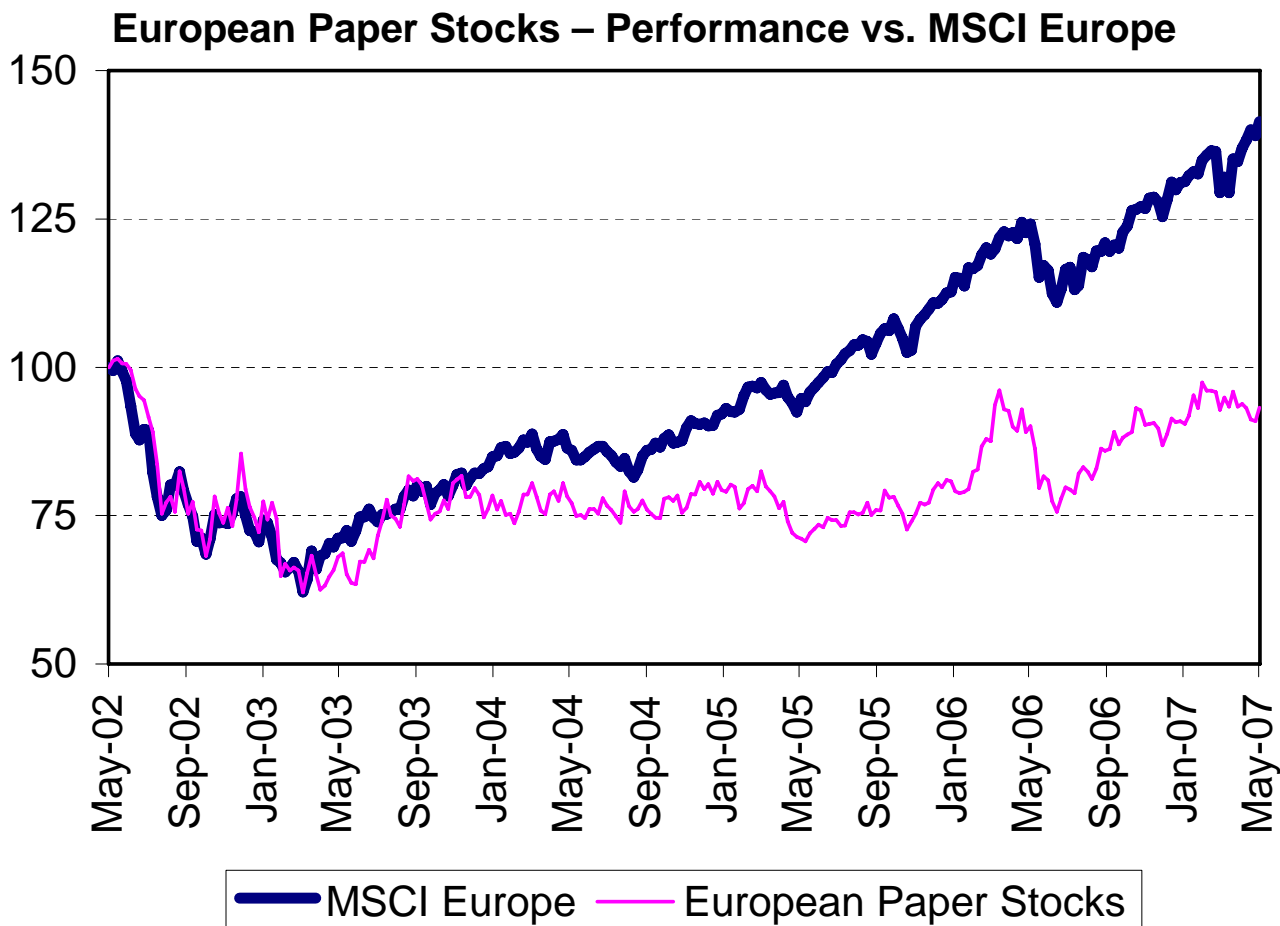
### Paper Stocks - Relative Performance vs. S&P 500



Source: FactSet, Morgan Stanley Research

Paper & Forest Products Index: UFS, ABY, CDP, CHA, LPX, PCH, BOW, GP, IP, MWV, PKG, SSCC, TIN and WY

## It's Not Just Wall Street Either

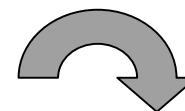
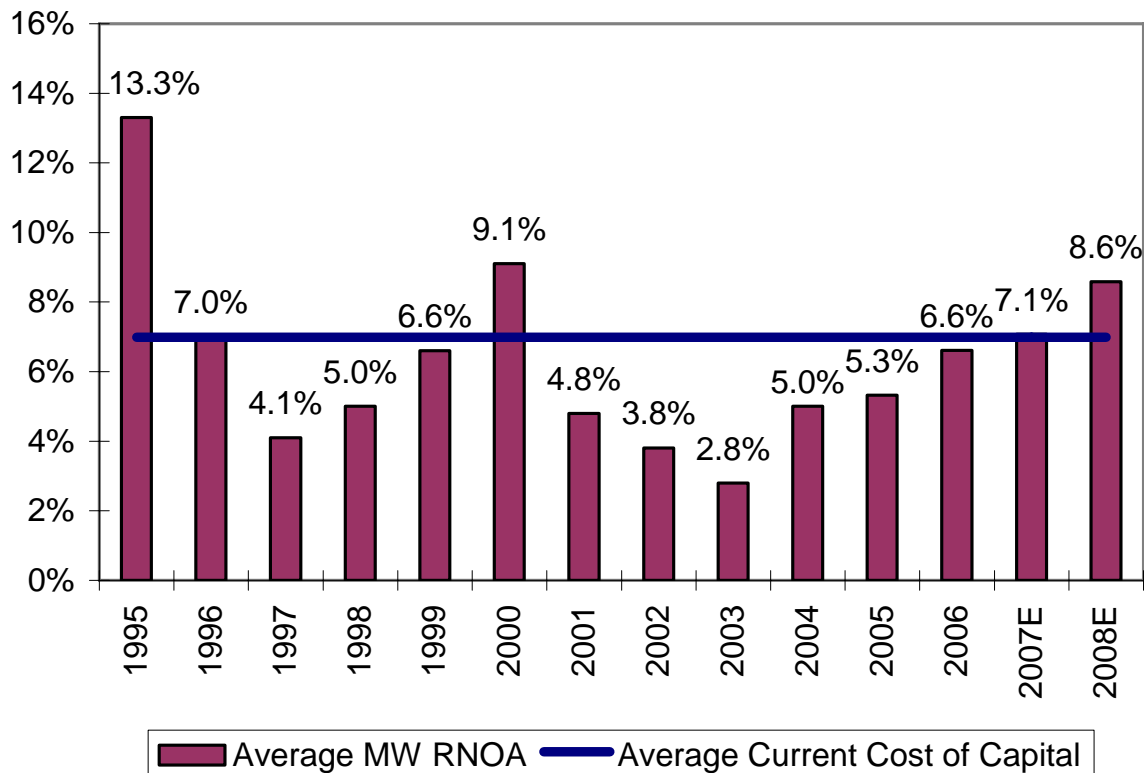


Source: FactSet, Morgan Stanley Research

European Paper Stocks include: Sonae Industria, Svenska Cellulosa, Holmen, UPM, Stora Enso, Mondi Packaging, Norske, and Billerud

## What's Behind the Poor Performance?

In North America, paper companies have destroyed value . . .



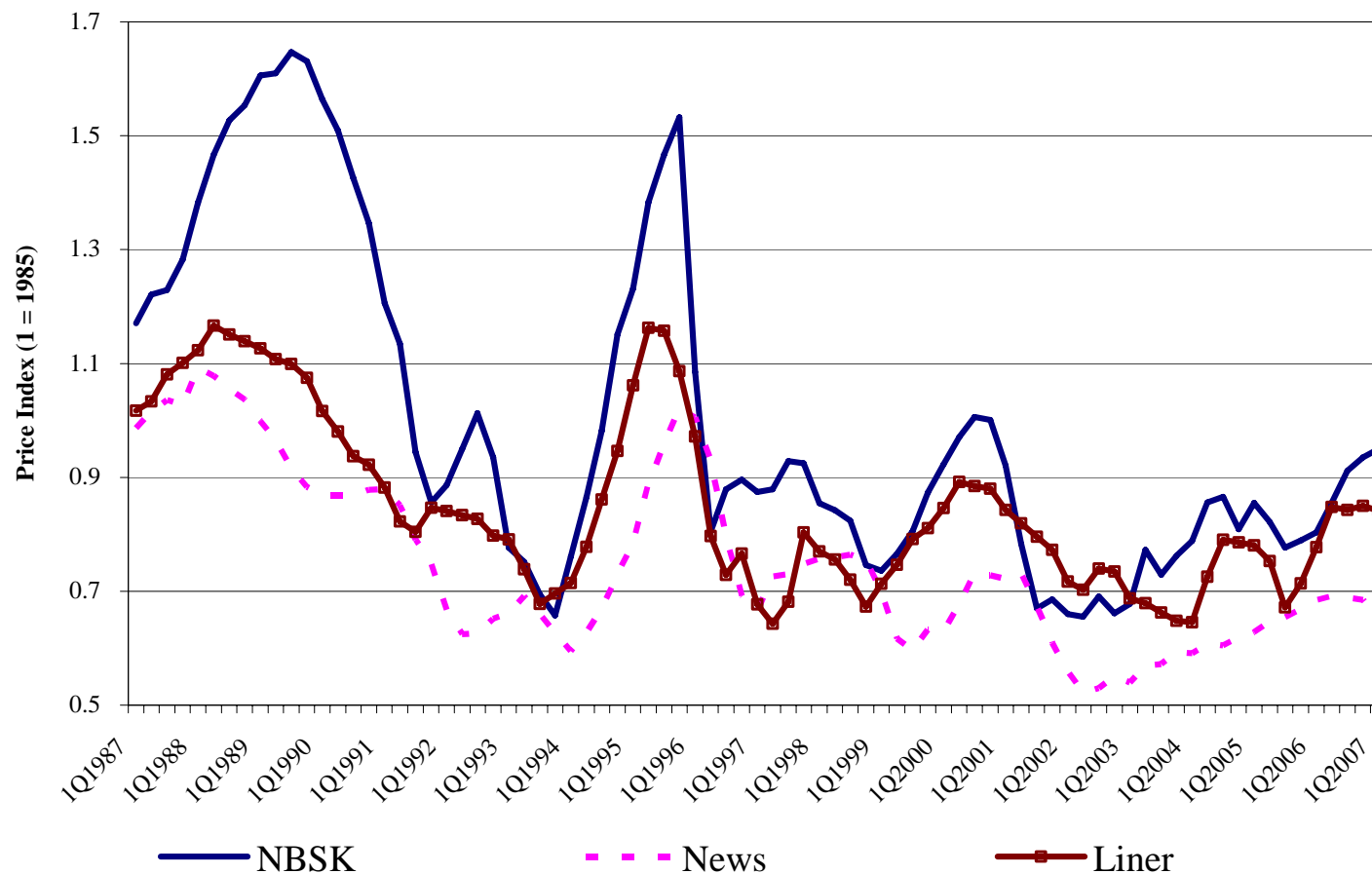
Companies have created significant value above cost of capital in only two years since 1995 – 1995 & 2000. Both years were cyclical peaks.

E = Morgan Stanley Research Estimates  
 Source: Morgan Stanley Research, Company sources

Average for BOW, GP, IP, MWV, PKG, PCL, SSCC, TIN, WY

## What's Behind the Poor Performance?

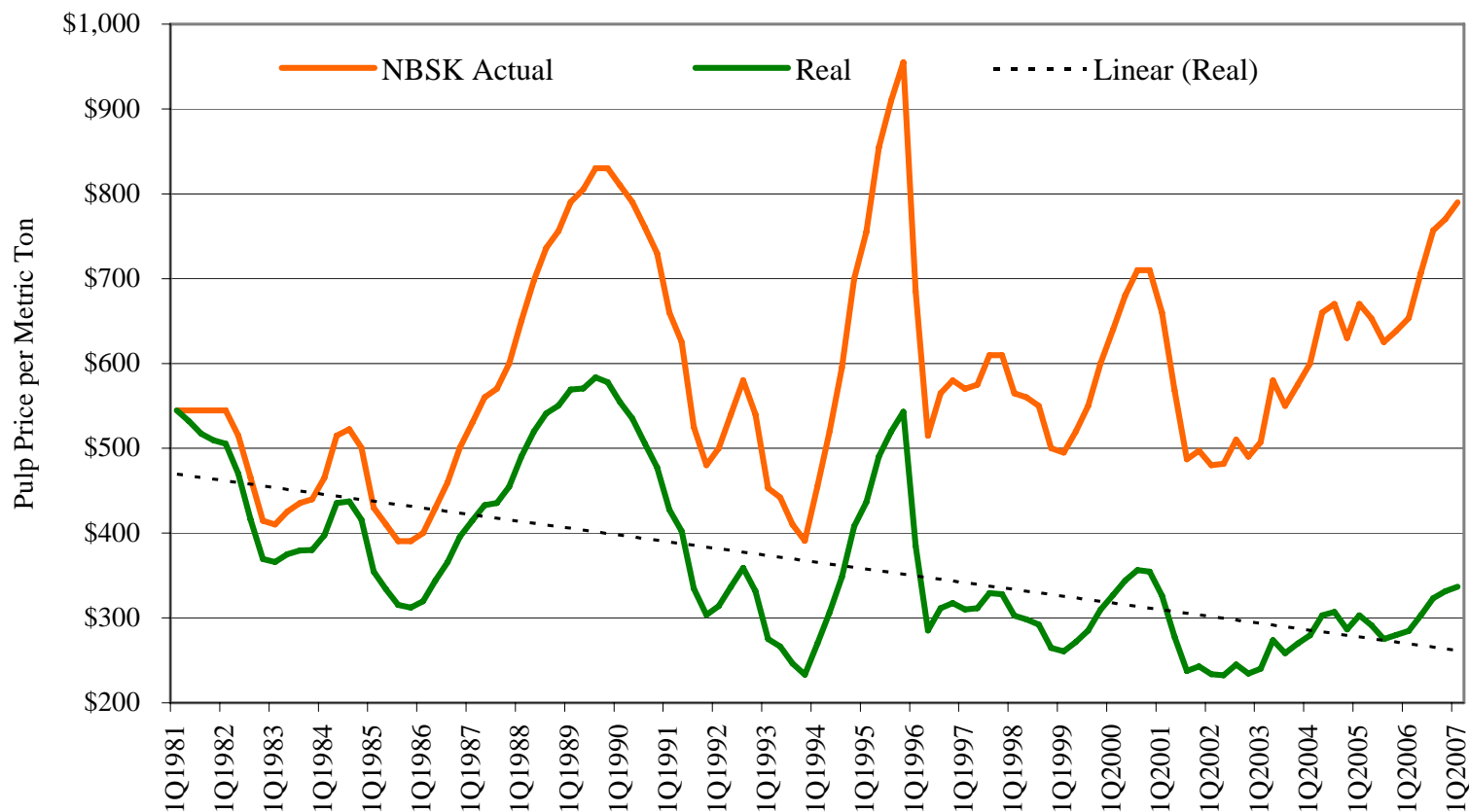
### Deflationary pricing has offset efforts to cut costs



Source: RISI, Paperloop, AF&PA, FactSet, Morgan Stanley Research

## What's Behind the Poor Performance?

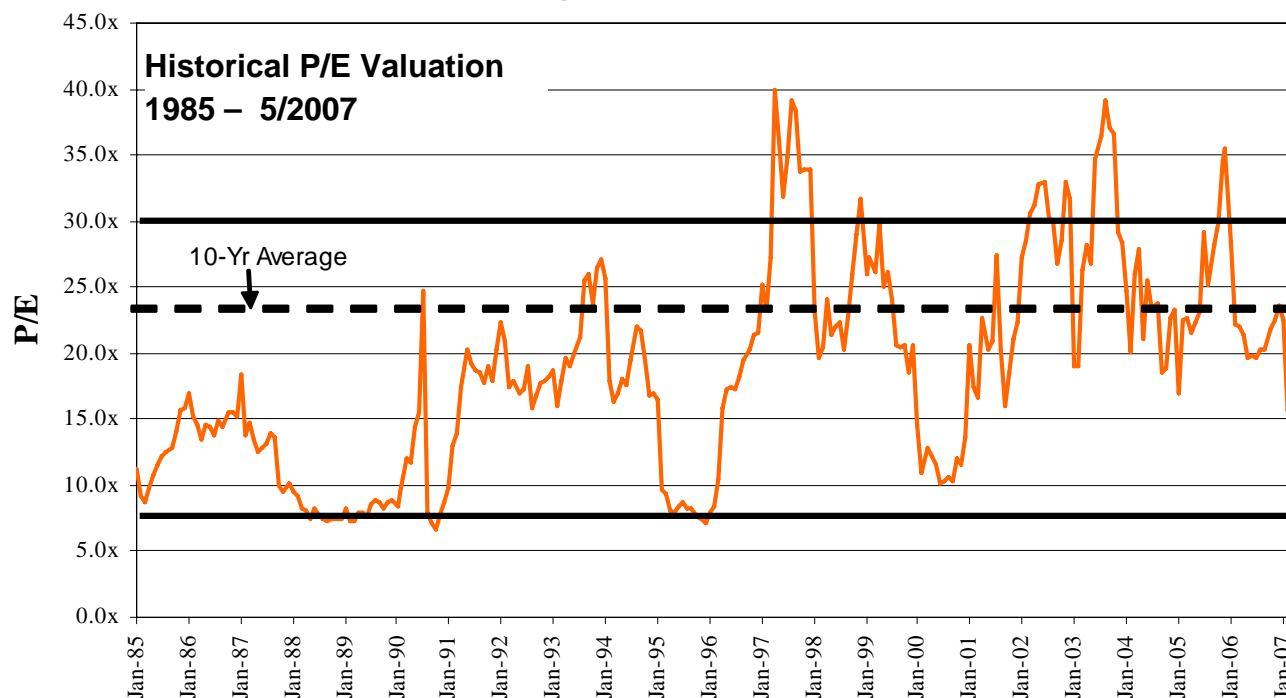
### Deflationary pricing has offset efforts to cut costs



E = Morgan Stanley Research Estimates  
 Source: RISI, Paperloop, AF&PA, Morgan Stanley Research

## How Does Wall Street Value Pulp and Paper Stocks?

- P/E valuations clearly trough during periods of earnings power; cyclical peaks and troughs have been more exaggerated since the 1990s.
- However, the recent trough in multiples has not been as clearly delineated; muted pricing power and hence earnings power during this cycle has caused the stocks to trade between 17x and 25x.
- Current P/E valuations for each stock in the paper and forest products universe are generally trading at the middle of their historical range.



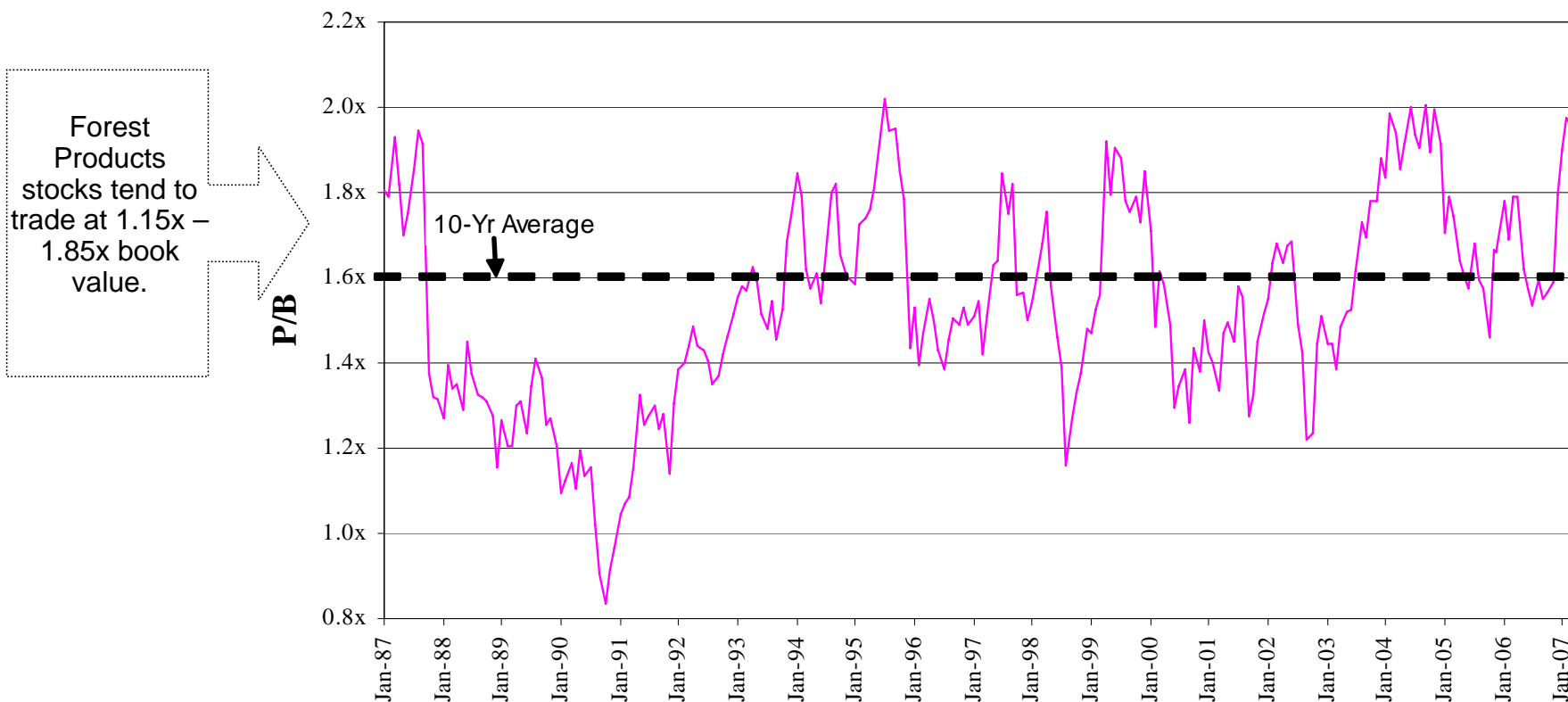
Note: Trailing P/E's shown

Source: FactSet, Morgan Stanley Research

Paper & Forest Products Index: UFS, ABY, LPX, BOW, GP, IP, MWV, PKG, SSCC, TIN and WY

## How Does Wall Street Value Pulp and Paper Stocks?

### North American Paper & Forest Products Stocks – Historical P/B Valuation

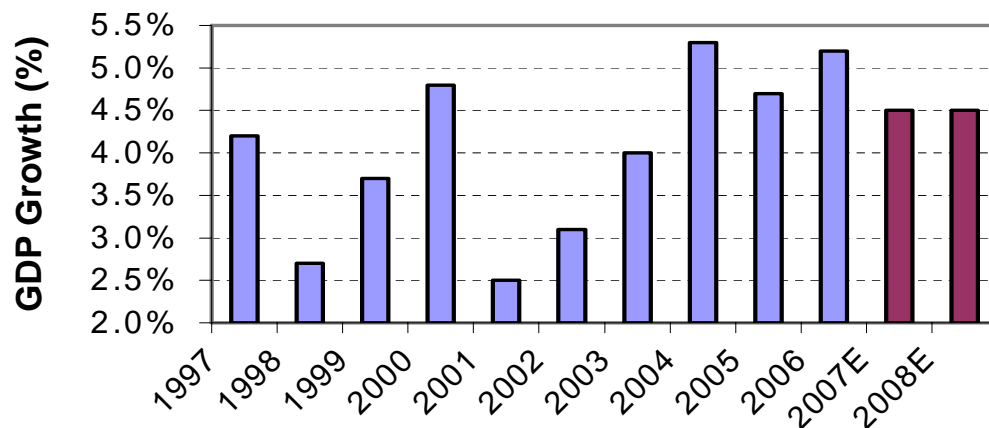


Source: FactSet, Morgan Stanley Research Paper & Forest Products Index: UFS, ABY, LPX, BOW, GP, IP, MWV, PKG, SSCC, TIN and WY

## How Does Wall Street Track the Pulp Industry?

While a slowing U.S. and global economy does pose risks, we see growth picking up after 1Q 2007

### Morgan Stanley Global GDP Forecast



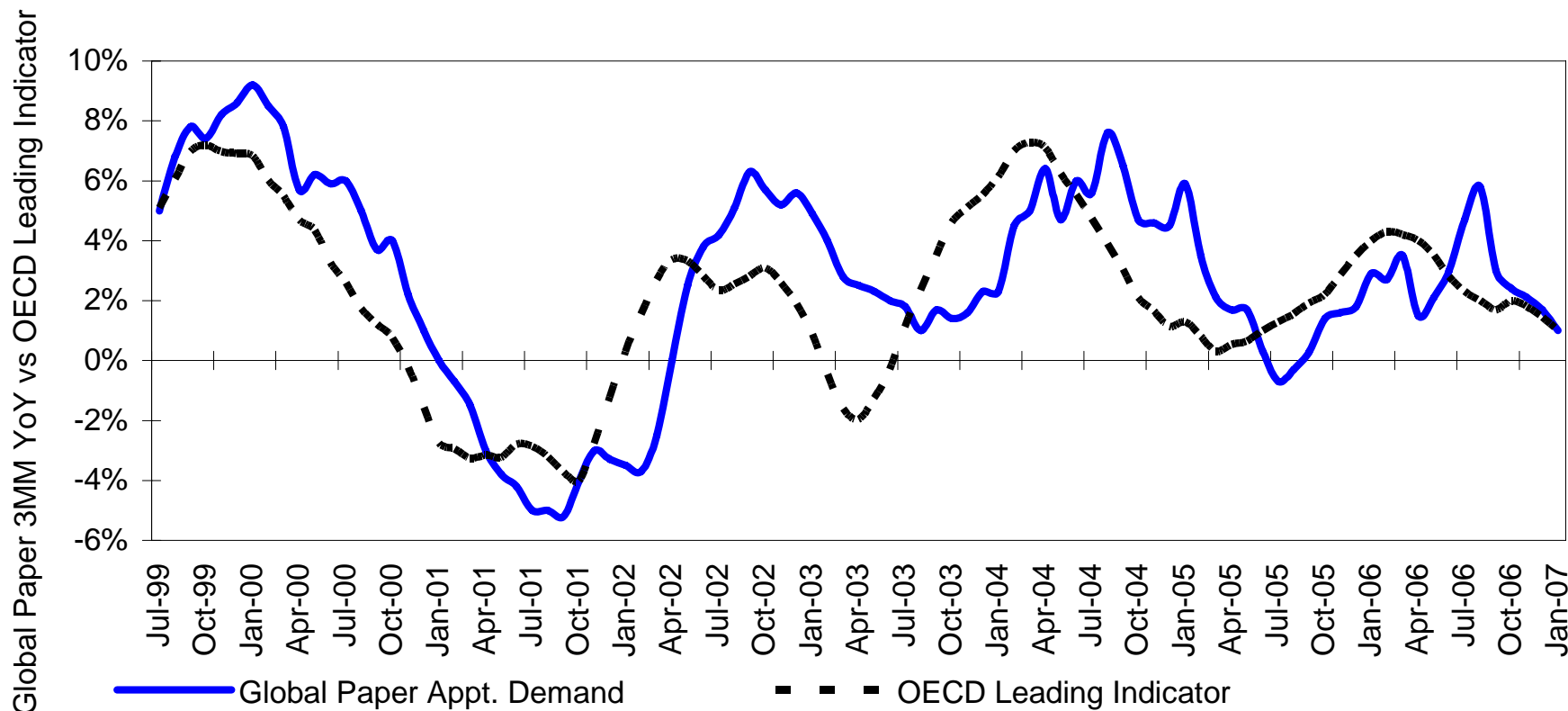
### Morgan Stanley Regional GDP Forecast

|                 | 1Q07e       | 2Q07e       | 3Q07e       | 4Q07e       | 2007e       | 2008e       |
|-----------------|-------------|-------------|-------------|-------------|-------------|-------------|
| US <sup>1</sup> | 2.1%        | 1.9%        | 2.0%        | 2.1%        | 2.0%        | 2.9%        |
| EMU             | 2.9%        | 2.5%        | 2.4%        | 2.1%        | 2.5%        | 2.4%        |
| Emerging Europe | 5.7%        | 5.9%        | 6.2%        | 5.6%        | 6.0%        | 5.7%        |
| Asia            | 8.1%        | 7.2%        | 7.0%        | 7.1%        | 7.3%        | 6.9%        |
| Japan           | 2.8%        | 2.6%        | 2.9%        | 1.9%        | 2.5%        | 2.5%        |
| Latin America   | 4.6%        | 4.1%        | 4.7%        | 4.5%        | 4.5%        | 4.4%        |
| <b>GLOBAL</b>   | <b>4.9%</b> | <b>4.4%</b> | <b>4.5%</b> | <b>4.3%</b> | <b>4.5%</b> | <b>4.5%</b> |

E = Morgan Stanley Research Estimates  
 Source: OECD, Morgan Stanley Research

## How Does Wall Street Track the Pulp Industry?

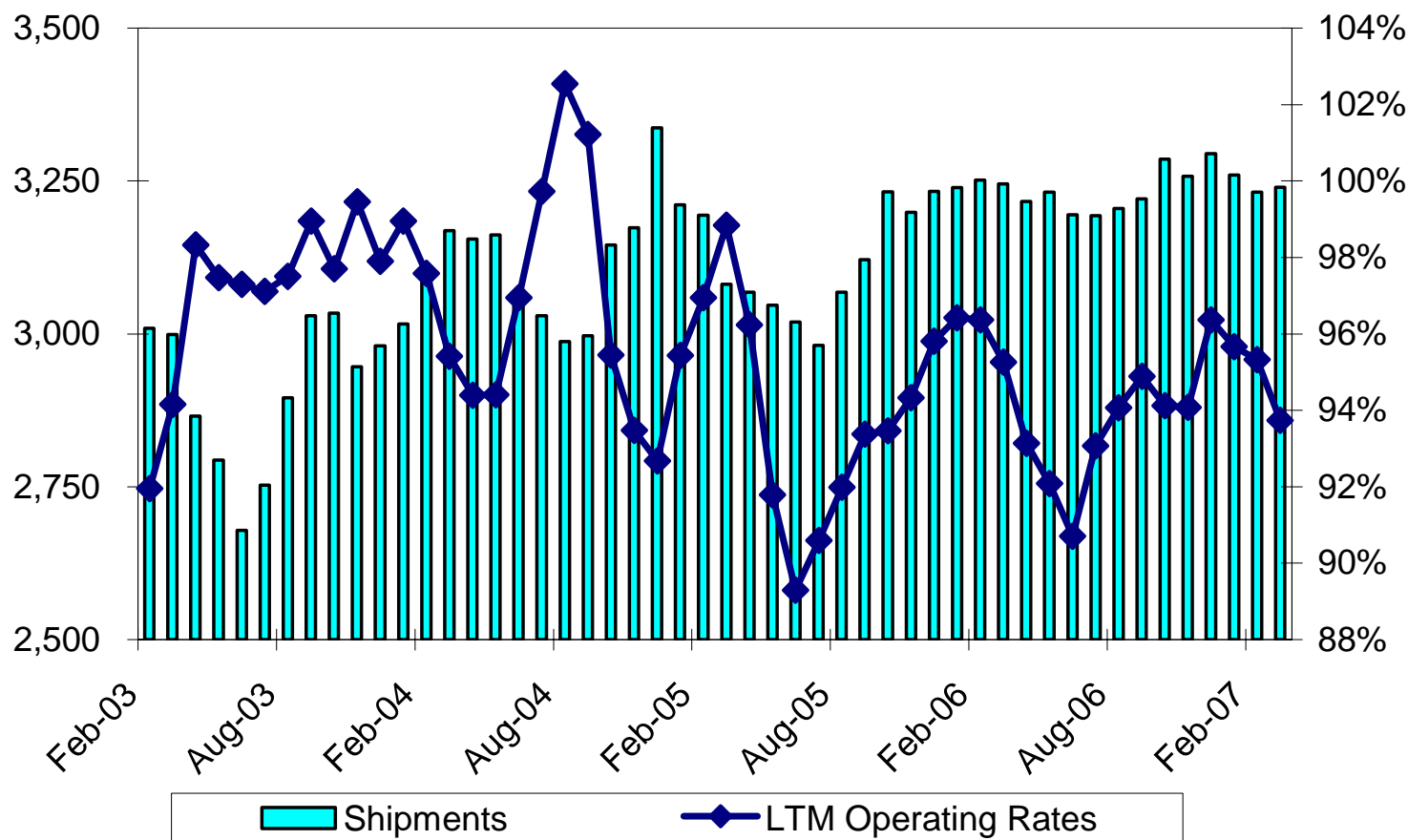
### OECD Leading Paper Indicators Remain Weak



E = Morgan Stanley Research Estimates  
 Source: OECD, Morgan Stanley Research

## How Does Wall Street Track the Pulp Industry?

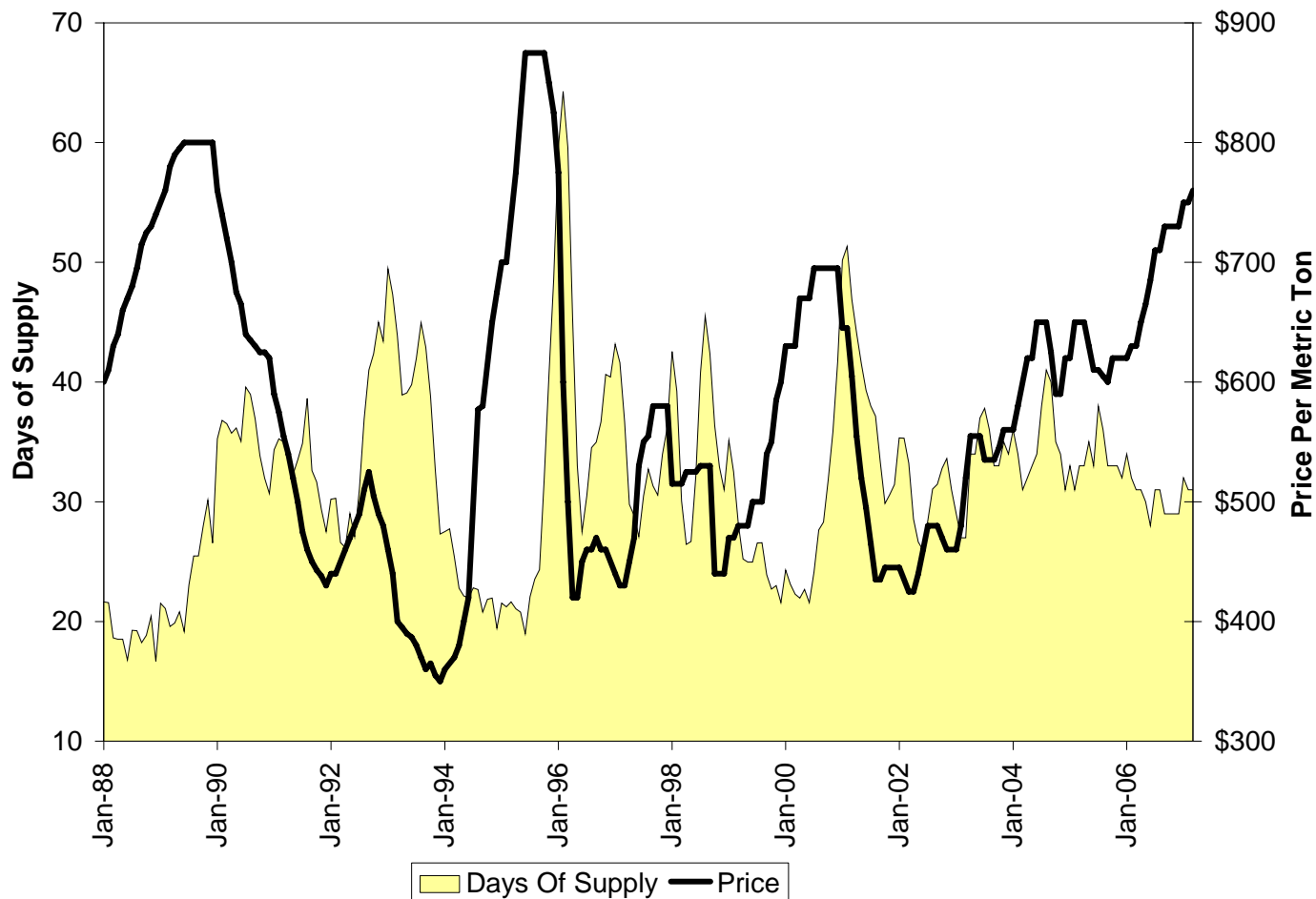
### Monthly Pulp Shipment Data: Shipment Levels and Operating Rates



Source: PPPC

## How Does Wall Street Track the Pulp Industry?

Inventory levels are considered a key indicator of price moves

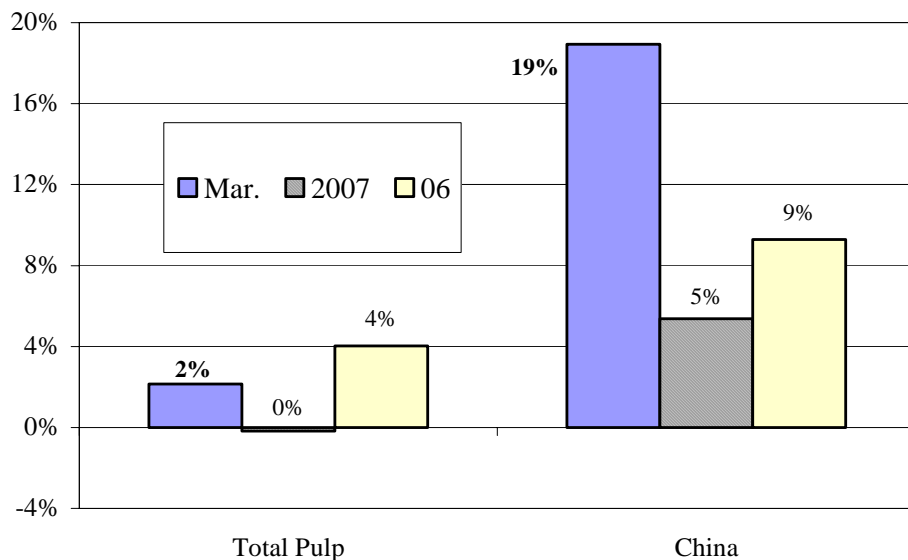


Source: PPPC

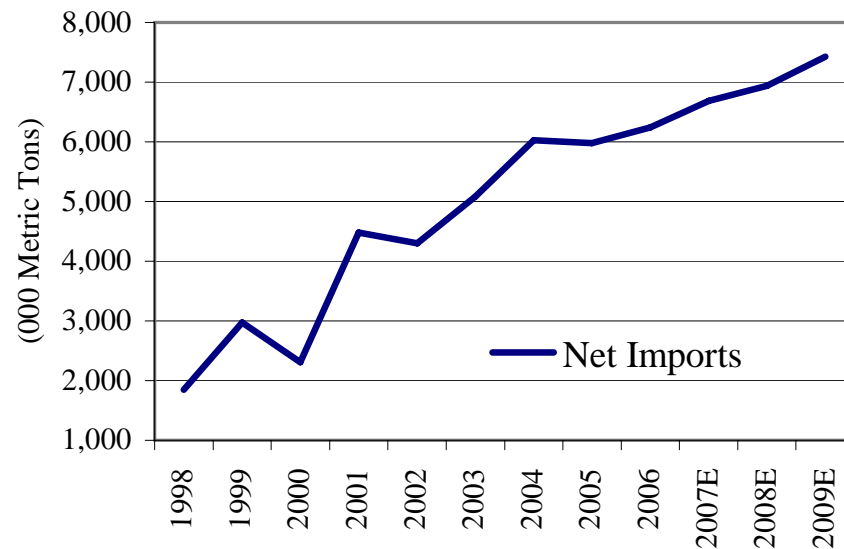
## How Does Wall Street Track the Pulp Industry?

### China is a key point of focus

Change in Pulp Shipments y/y – China vs. World



China Pulp Demand: 1998-2009e

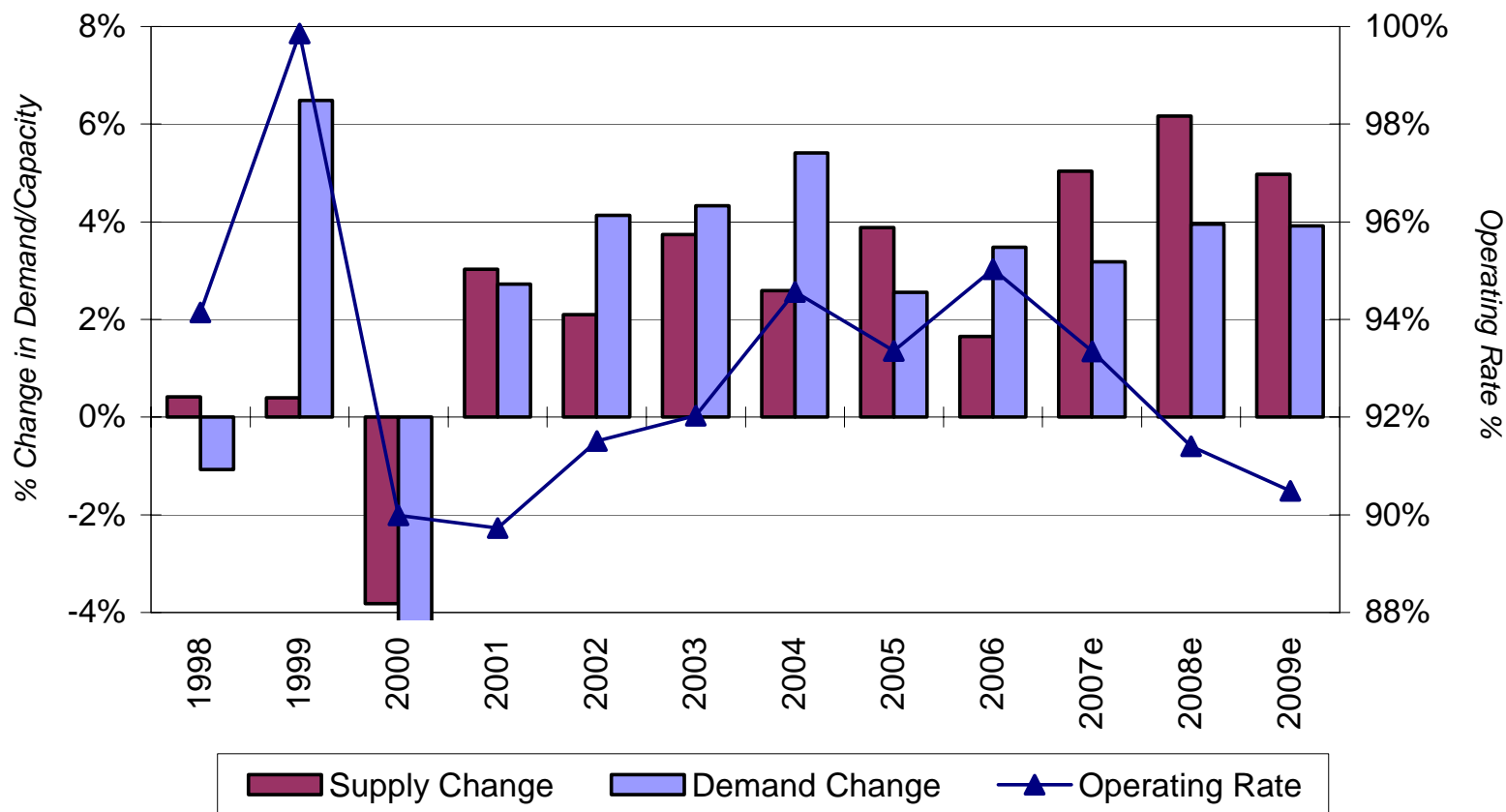


E = Morgan Stanley Research Estimates  
 Source: RISI, PPPC, Morgan Stanley Research

## How Does Wall Street Track the Pulp Industry?

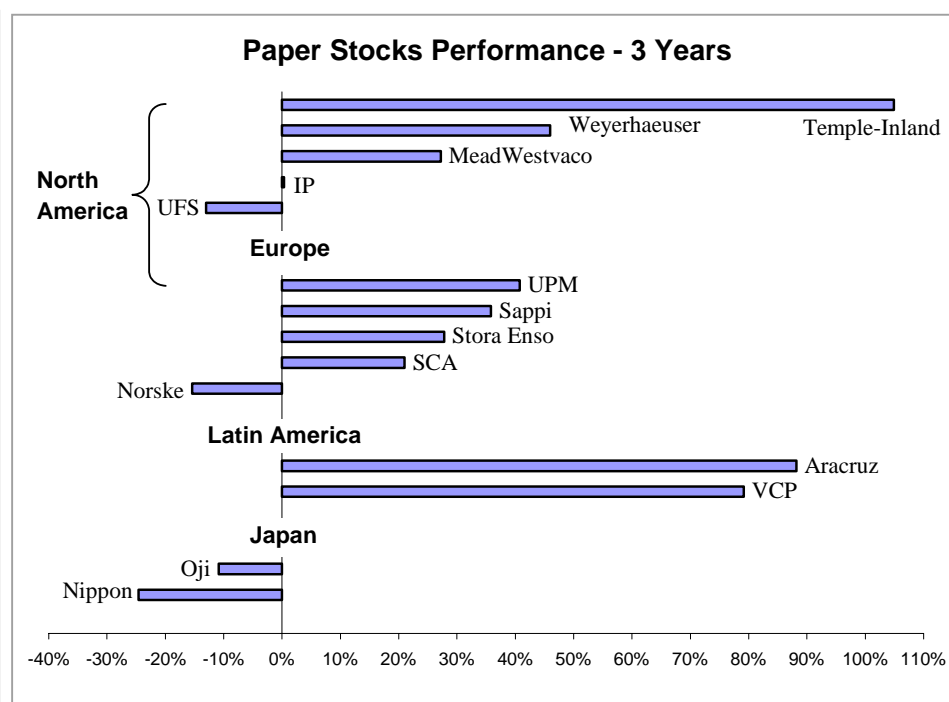
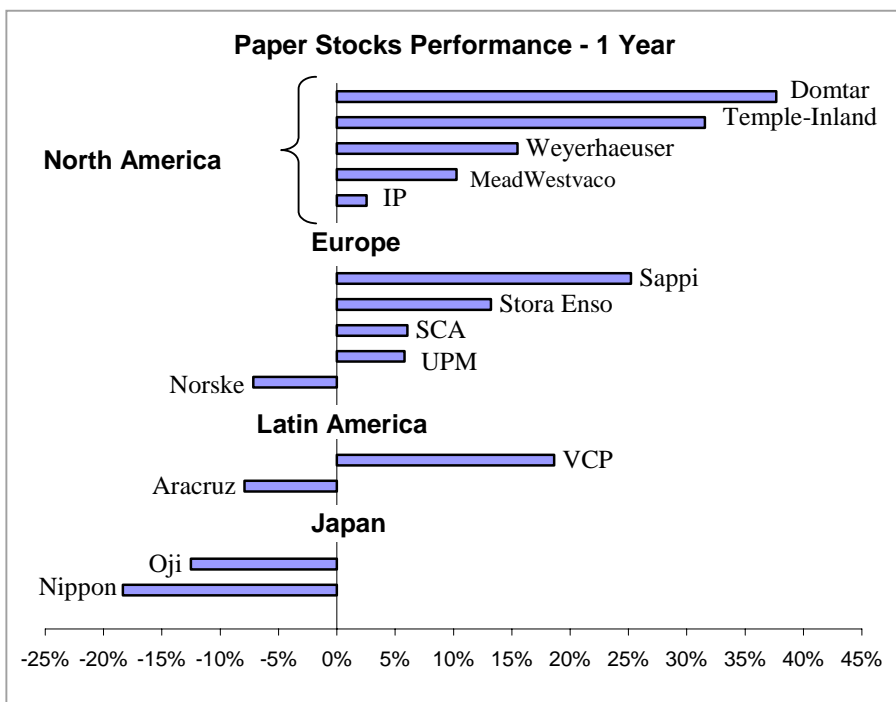
### It's all about supply and demand

#### Global Pulp Shipments and Operating Rates: 1998-2009e



E = Morgan Stanley Research Estimates  
 Source: RISI, PPPC, Morgan Stanley Research

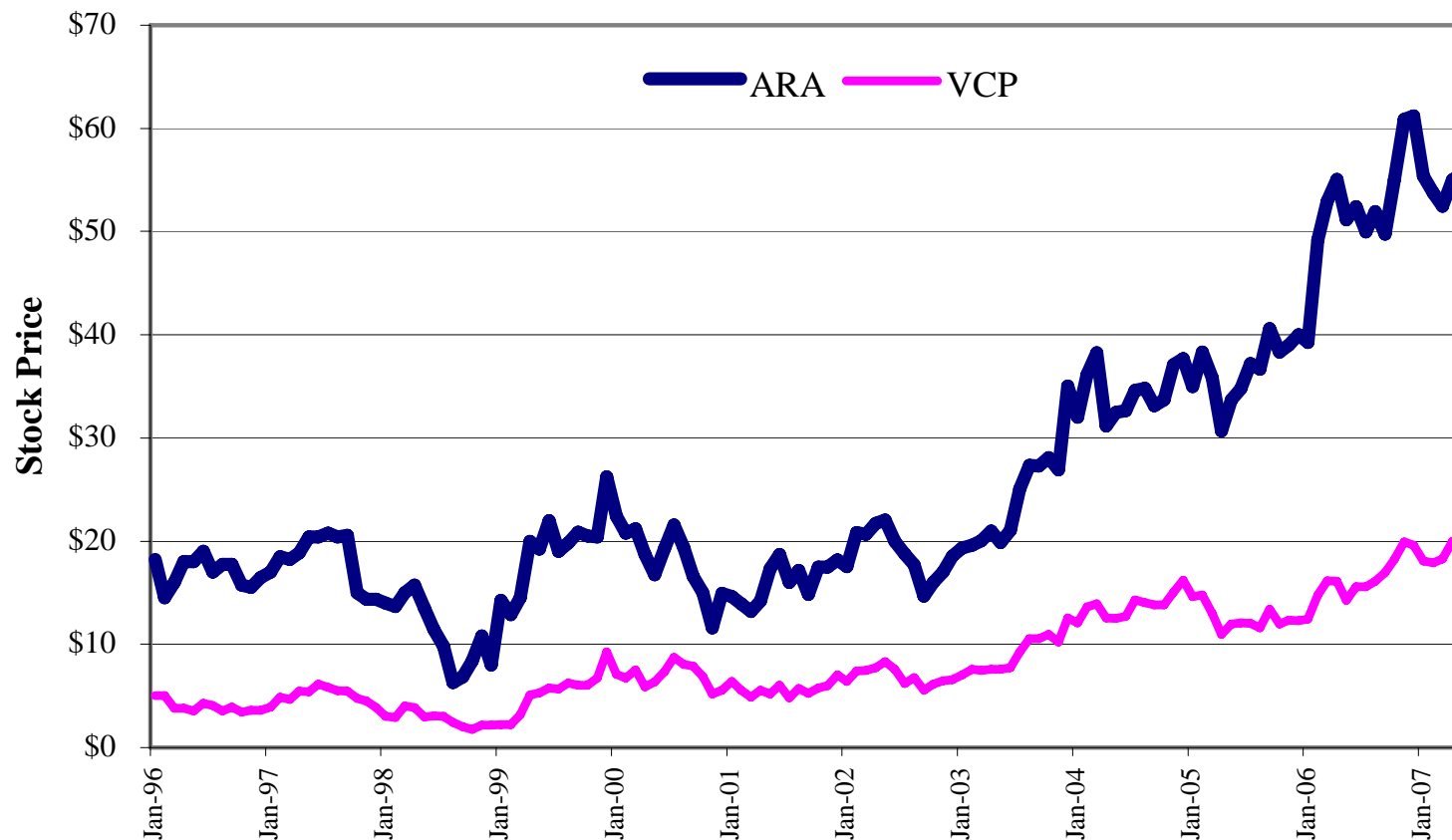
## Not All Stocks Are Created Equal



Source: FactSet, Morgan Stanley Research  
 Note: Local currencies.

## Wall Street Likes Eucalyptus

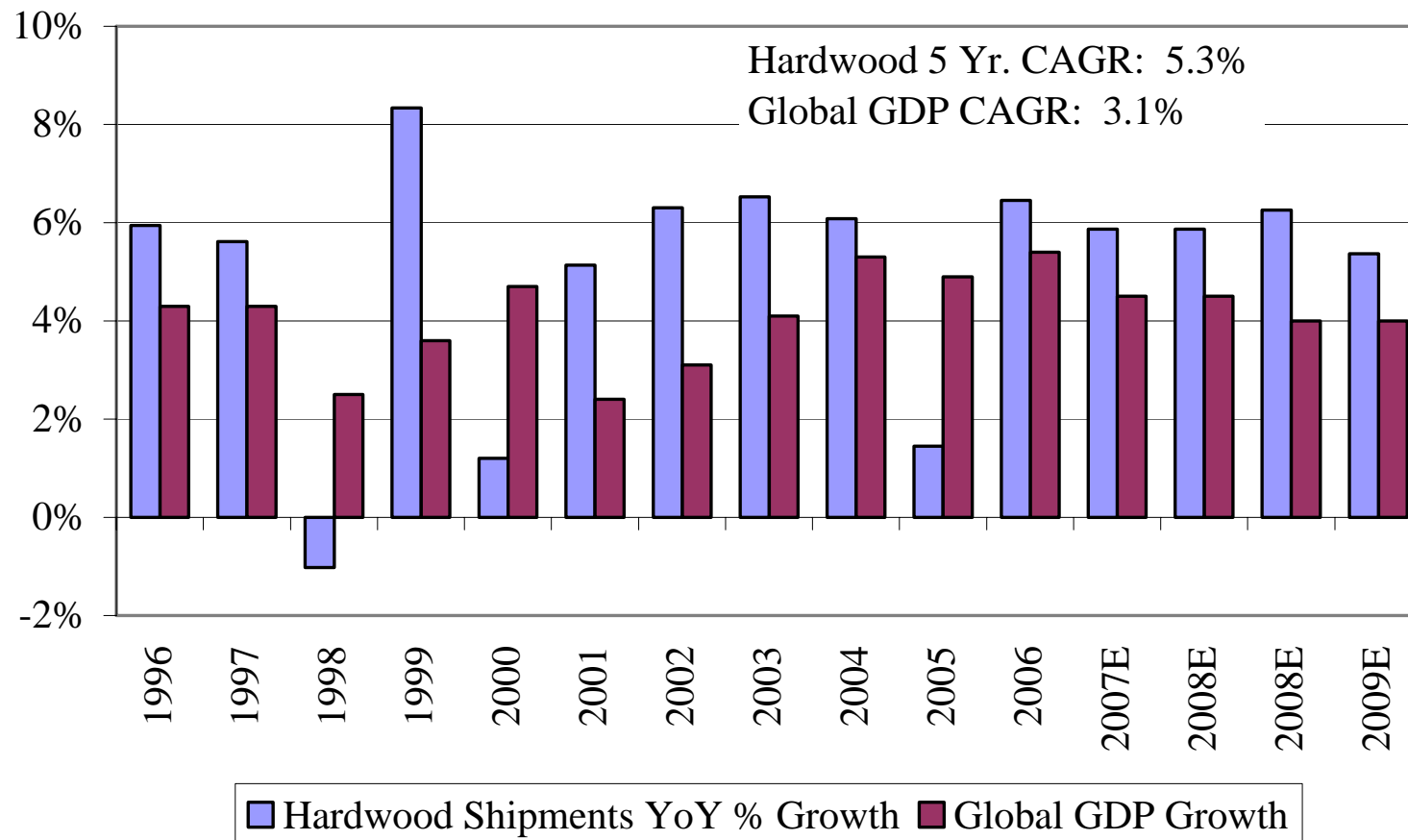
### ARA and VCP Share Price Performance, 1996 – 2007 YTD



Source: FactSet, Morgan Stanley Research

## Wall Street Likes Eucalyptus

### Demand for hardwood is rising faster than GDP

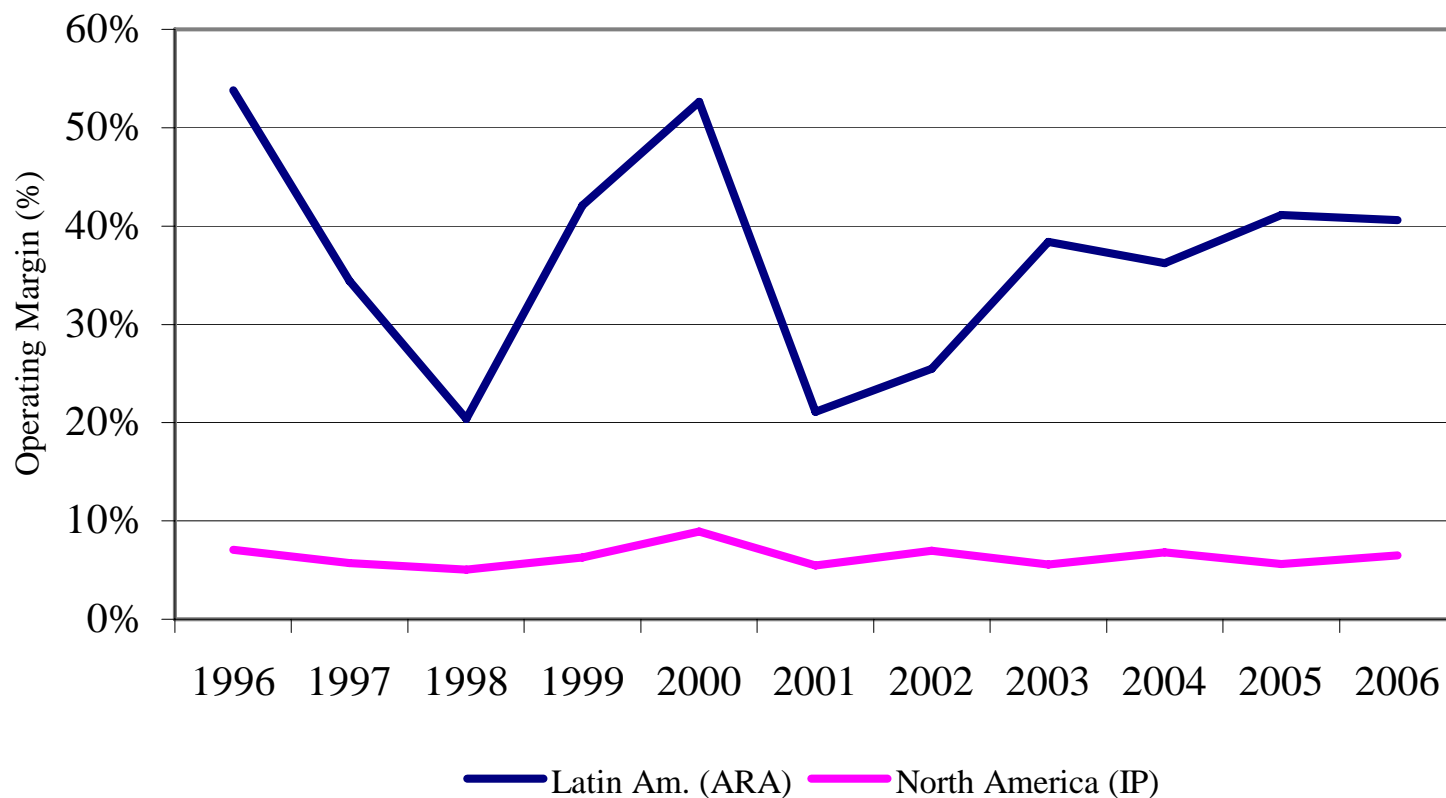


E = Morgan Stanley Research Estimates  
 Source: RISI, PPPC, and Morgan Stanley Research

## Wall Street Likes Eucalyptus

### Low cost producers enjoy high margins even in tough industries

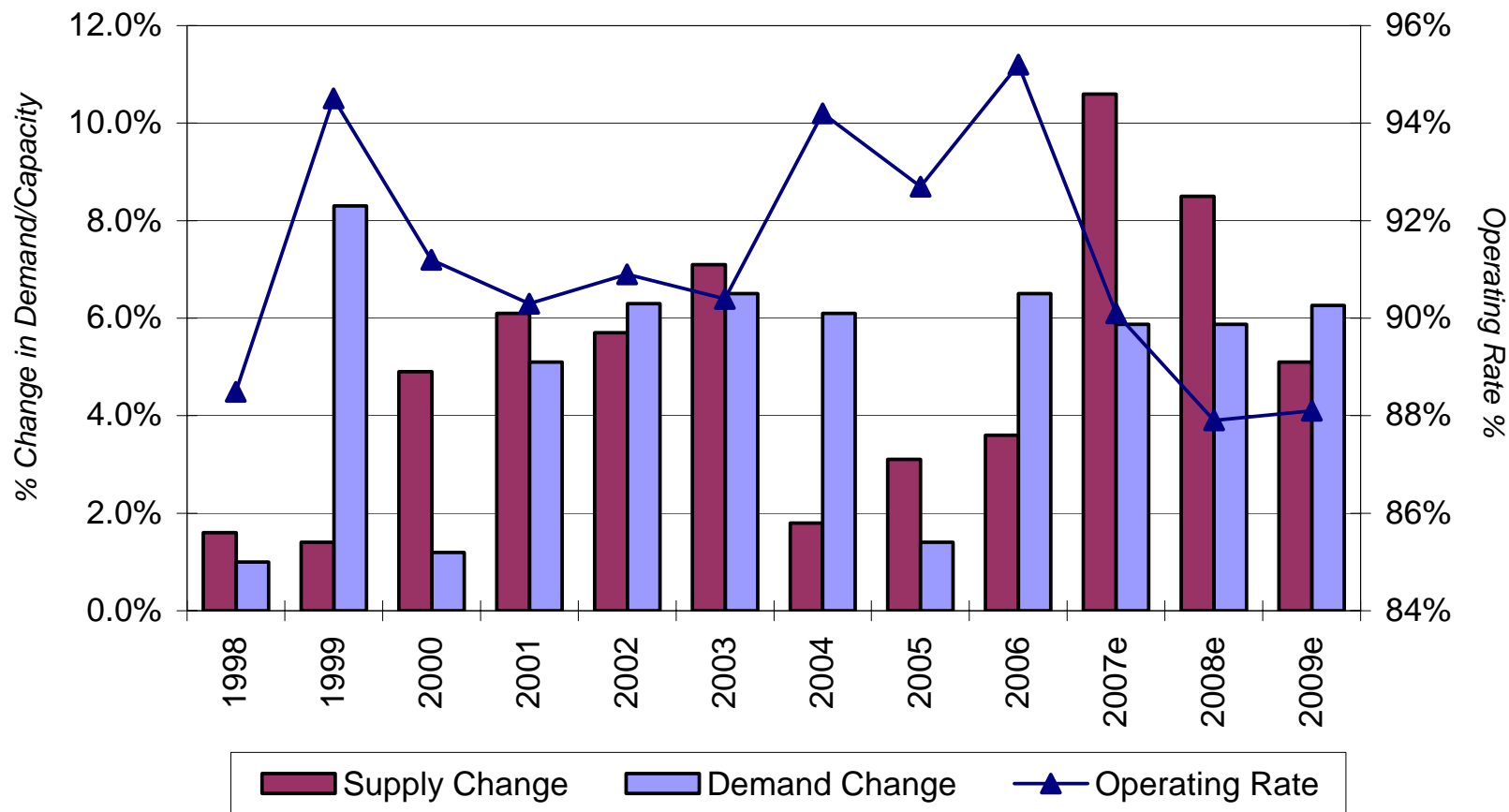
ARA and IP Operating Profit Margin, 1996-2006



Source: FactSet, Company Sources

## Outlook for Eucalyptus is getting Cloudy

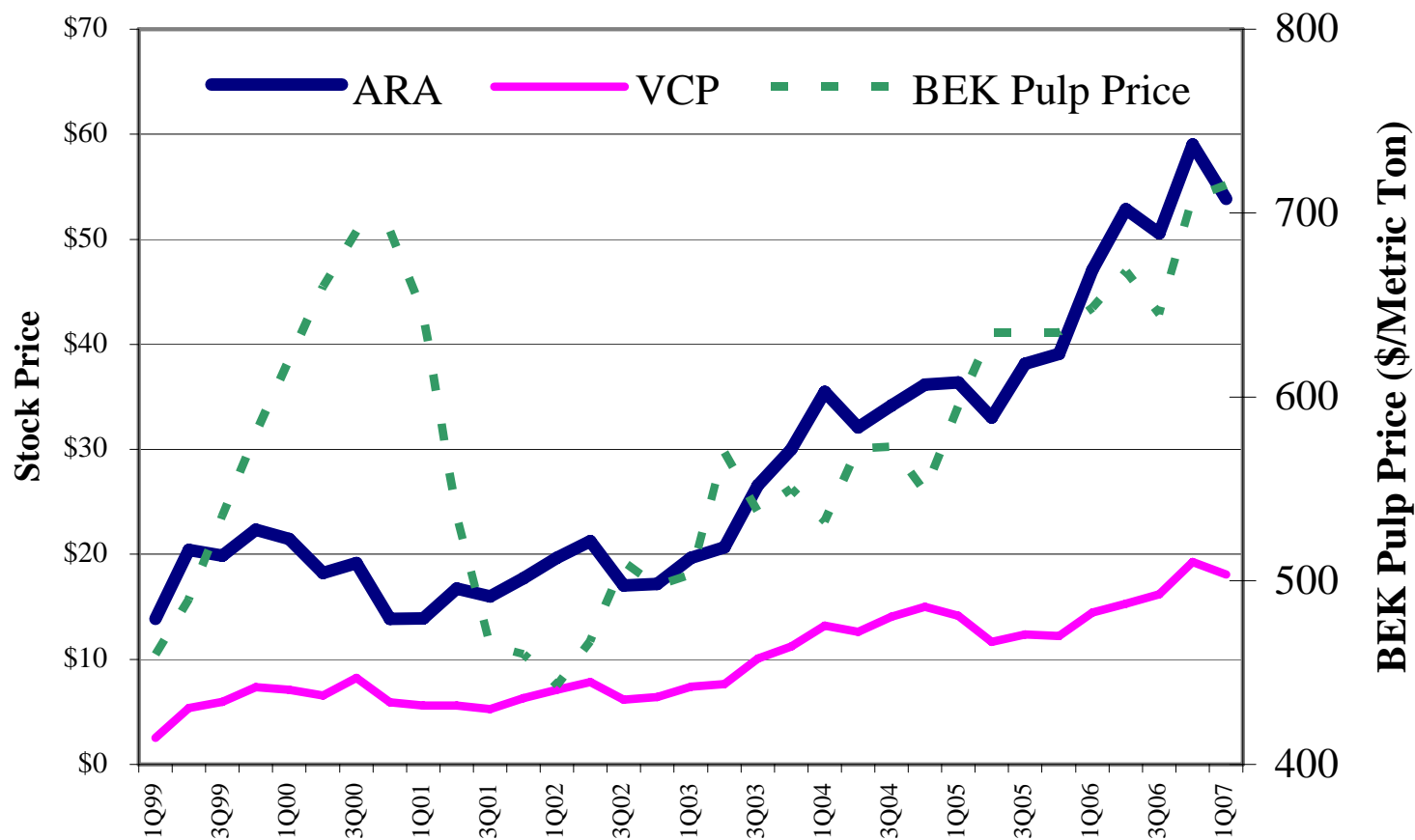
Hardwood supply/demand balance is weakening . . .



E = Morgan Stanley Research Estimates  
 Source: PPPC, RISI, Morgan Stanley Research

## Outlook for Eucalyptus Is getting Cloudy

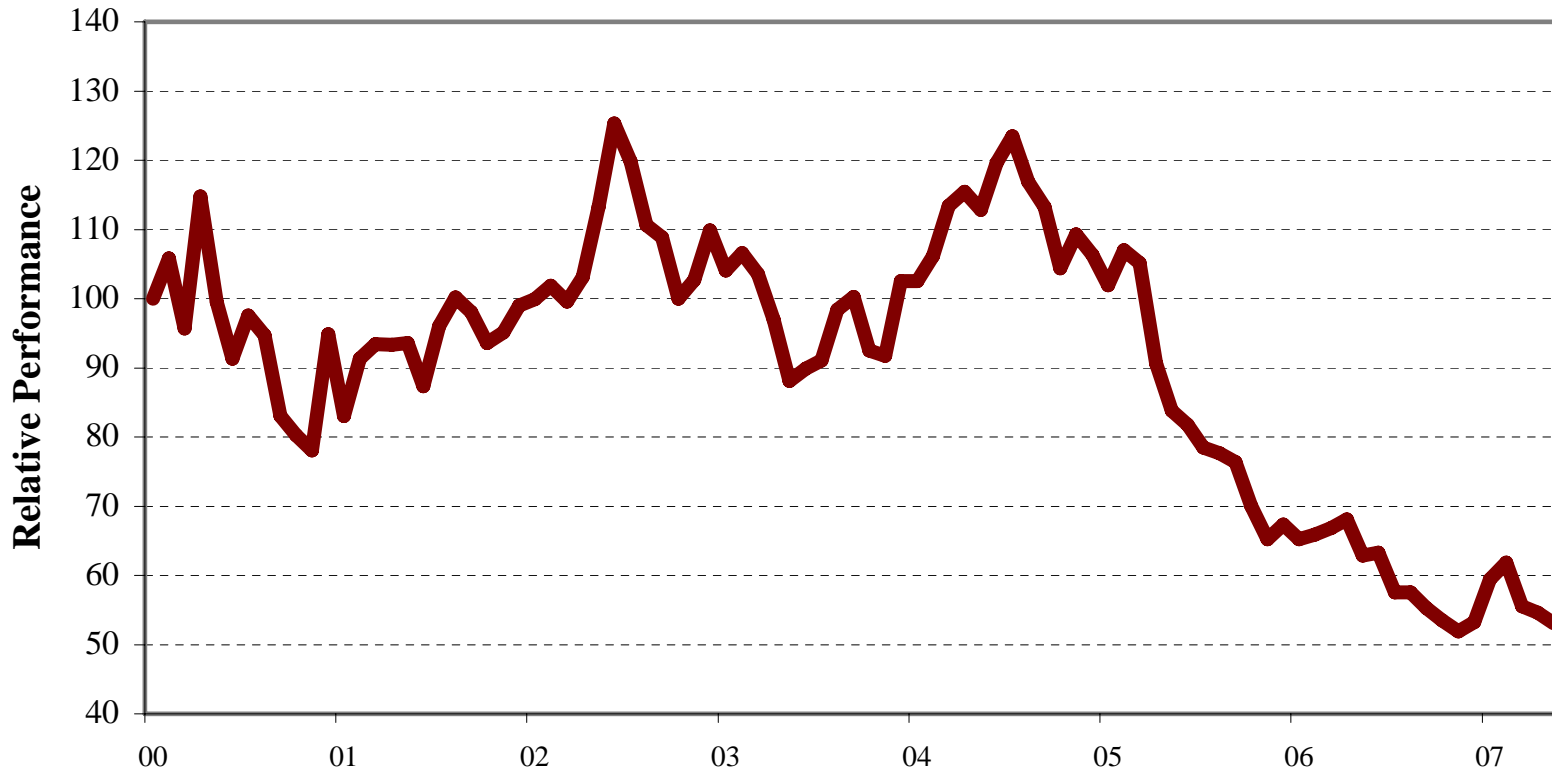
... With negative implications for shares of eucalyptus producers



Source: RISI, FactSet, Morgan Stanley Research

## Other Pulp Producers Have Fared Less Well

Relative Price Performance, 2000-2007 YTD

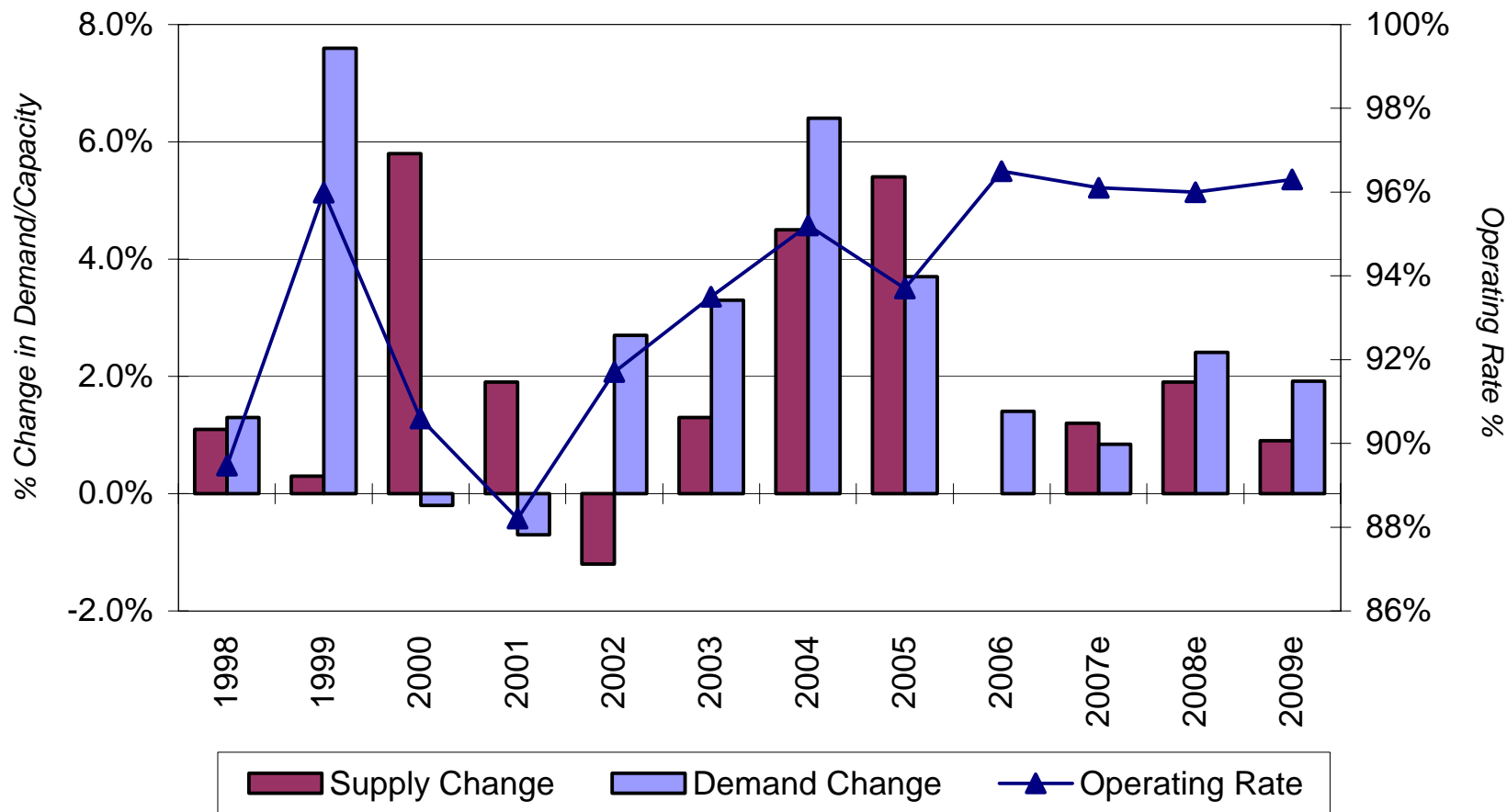


Source: FactSet, Morgan Stanley Research

Average for MERC, POP, TBC-CA, and CFP-TSE

## Outlook for Operating Rates Appears Positive

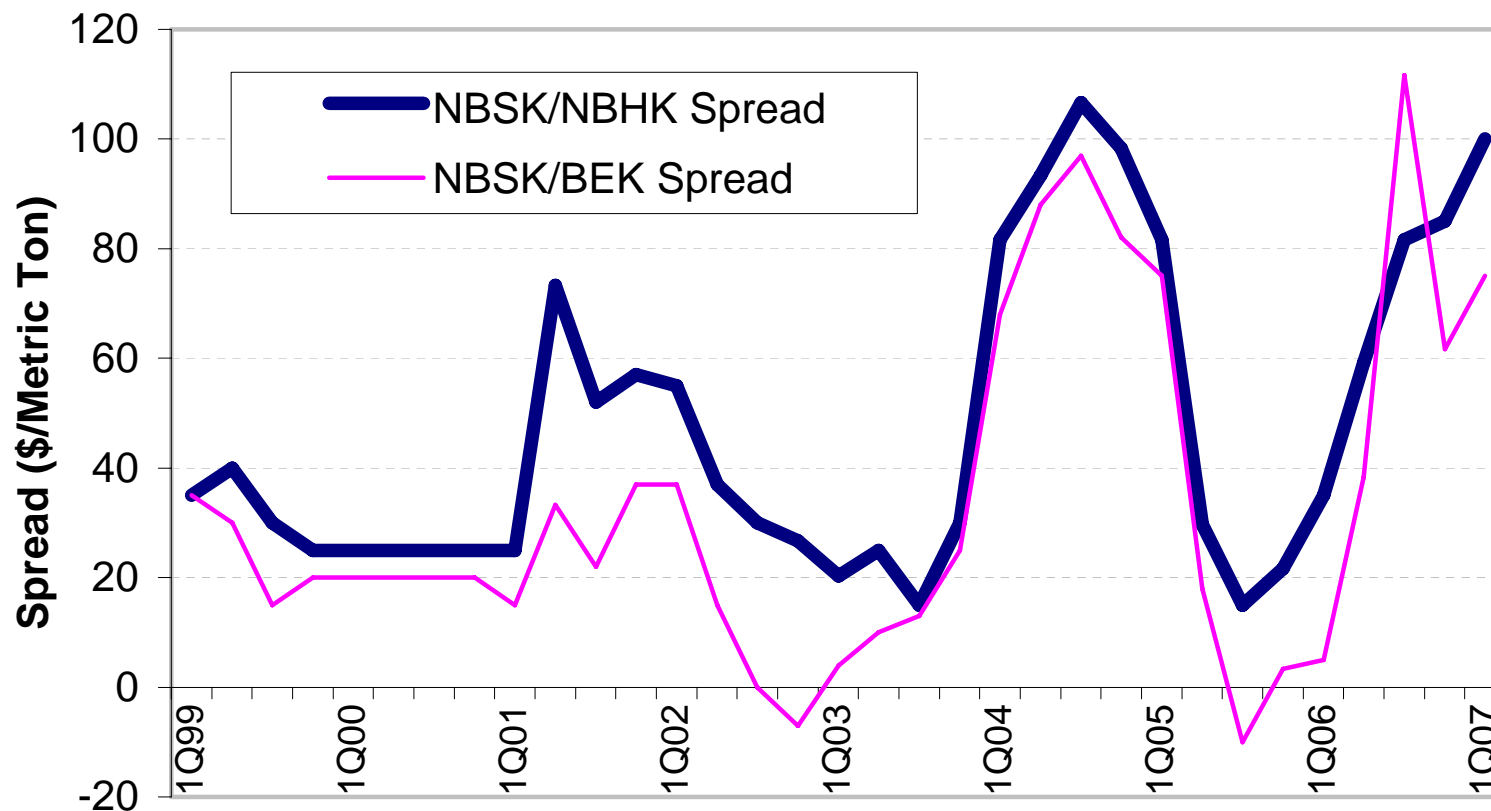
### Softwood Pulp Markets Should Stay Tighter than Hardwood



E = Morgan Stanley Research Estimates  
 Source: RISI, PPPC, Morgan Stanley Research

## Softwood Outlook Brightening

... With positive implications for price spreads



E = Morgan Stanley Research Estimates  
 Source: RISI, Morgan Stanley Research

## What Else Can Be Done to Boost Margins?

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**Wall Street likes structural change:**

- 1) Focus**
- 2) Consolidation**
- 3) Global Reach**

E = Morgan Stanley Research Estimates  
Source: RISI, Morgan Stanley Research

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