



State of the Flexible Packaging Industry Report 2006

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Executive Summary

The impact of the 2005 hurricanes on many industries- including the flexible packaging industry- was significant. They created havoc, disruption and raw-material price increases. The growth in flexible packaging sales and volume, however, did not skip a beat.

Despite continued pressure from major consumer product companies (CPCs) and retailers, inroads by offshore manufacturing and high production costs (beyond the unstable, soaring costs of energy and resins), the industry steadily expands.

INDUSTRY PERFORMANCE

FPA estimates an annual growth rate of 3.6 percent (for 2004-2005), based on information provided by FPA members in the FPA State of the Industry Survey and by non-members in the FAP Industry Wide Converters Survey and FPA's long-term historical model of flexible packaging industry growth. Today the total flexible packaging industry is estimated to be about \$21.8 billion in annual sales.

The focus of this report is on the segment of the industry that adds significant value to the flexible materials, usually by performing multiple processes, and does not include retail shopping bags, consumer storage bags and wraps, or trash bags. The following is a breakdown of the \$21.8 billion in annual sales.

	\$ Billion
"Value-Added"	17.0
Retail Poly Bags	1.5
Poly Storage Bags	0.7
Poly Trash Bags	1.5
Other Poly Bags and Wraps	1.1
TOTAL	21.8

The 'value-added' segment of the industry this report emphasizes is estimated to be \$17.0 billion. Revenues for this segment of the industry have increased over the last 4 years (2002-2005), turning around the downturn the industry experienced in 2001. The combined surveys identified over \$13.5 billion in sales. This \$13.5 billion represents 63% of the estimated \$21.8 billion flexible packaging industry and a solid 79% of the \$17.0 billion value-added segment which is the focus of this report.

The 2002-2005 FPA survey data indicated direct material costs to be steadily increasing from 52 to 56 percent of net sales and operating profit declined from 6 percent of net sales in 2002 to 4 percent in 2005.

Current converter expectations (based on composite FPA member and non-member *Survey* data) are for 2006 sales revenue to increase 3.4 percent to about \$22.5 billion with volume projected to increase at a somewhat higher rate. Looking out 3-5 years, converter expectations are even higher with revenue projected to rise 3 to 5 percent per year and volume to increase 5 to 7 percent per year.

INDUSTRY STRUCTURE

Over the past ten years, flexible packaging industry dynamics have created a more consolidated industry structure where large companies (> \$500 million revenue) account for about half the industry revenue. Small & Mid sized companies share of industry revenue has declined from nearly two-thirds in 1996 to just over half in 2005.

FPA estimates that there are approximately 437 flexible packaging converters in the United States today.

Merger and acquisition activity in the flexible packaging industry for 2005 included 18 domestic transactions completed. This was up significantly from the level of 11 recorded in 2004, and 9 recorded in 2003. However, 2005 was in line with the level of 17 transactions in 2000, but still well below the level of 24 in 1999 and the 22 recorded in 1998. The pace of merger and acquisition activity for 2005 in flexible packaging, while higher, was not as robust as overall global merger and acquisition activity in all industries.

This year's State of the Industry Survey results indicate both Converters and Suppliers expect M&A activity for 2006 to decline slightly from 2005 levels (with changes about the same as in past couple of years), suggesting a dip in the level of flexible packaging M&A activity in 2006.

MATERIALS & PROCESSES

Flexible packaging materials are heavily weighted toward plastics with "plastic resins" and "film & sheet" accounting for over two-thirds (69 percent) of the materials used. Paper accounts for just at 8 percent, inks account for about 6 percent, foil is 4 percent, and coatings & adhesives is only 4 percent.

A composite model was developed to estimate the overall value of printing in the flexible packaging industry which is about \$4.6 billion. Data also showed Converters print from 2 to 10 colors with an overall average of seven colors. The total number of presses was estimated at 3,000 including flexographic, gravure, in-line, offset and other simple presses.

END-USES

Flexible packaging represents a little over 17 percent of the total U.S. packaging industry. Flexible packaging is the second largest packaging segment behind corrugated paper and just ahead of bottles and miscellaneous rigid plastics packaging (other than flexible applications).

End-Use segments for the flexible packaging industry in \$ billions are:

End-Use Segment.....	\$ Billions
Retail Food	10.6
Institutional Food	1.6
Retail Non Food	2.9
Institutional Non Food	0.8
Medical & Pharmaceutical	1.6
Industrial Applications	2.2
Consumer Products	2.1
TOTAL	21.8

Source: FPA 2005 SOI and Industry-Wide Converter Surveys

Food (including both Retail and Institutional) is estimated to be \$12.2 billion for 2005 versus the estimate of \$11.8 billion for 2004. Non-Food (including both Retail and Institutional) represents \$3.7 billion for 2005 compared with the estimate of \$3.9 billion for 2004. It should be noted that the line between retail and institutional is often blurred with many converters not able to make a clear distinction between the two for Food uses and to a lesser extent Non-Food.

ISSUES/ VISIONS

In this year's FPA surveys, raw material (cost & availability) was the number one 2006 issue indicated by Converters (both members and non-members) by a wide margin over the other issues. This is not surprising as 94 percent of participants ranked raw material (cost & availability) among their top five issues for 2006 in the open-ended survey question.

A comparison of the Top Issues for 2006 for Converters (composite member and non-member data) and Suppliers in this year's State of the Industry Survey indicates Material Costs, Competition and Imports are the top three issues for 2006. In total, Converters and Suppliers both rank nine of the same issues among the top ten issues, although not in the same position.

GLOBAL PACKAGING

The packaging industry on a worldwide basis is estimated to be about \$460 billion. Domestic U.S. provides the largest demand for packaging products in the world, accounting for about \$127 billion or 28 percent of the global packaging industry. Paper & board (includes corrugated) and plastics (includes flexible, rigid and other miscellaneous plastics) represent 36 and 35 percent, respectively, of worldwide packaging.

Flexible packaging imports for 2005 (based on the latest data available from the Foreign Trade Division of the Census Bureau) grew 23 percent in 2005 to \$2.9 billion while Exports rose by only 10 percent in 2005 to \$1.2 billion. As a result the industry's trade balance, the difference between exports and imports, increased again in 2005 (up 33 percent) to nearly 1.7 billion dollars for the first time ever. As Converters seek to grow their business, FPA continues to see evidence that exports remains an essential part of most companies' business/growth strategies. The 2005 FPA Survey results indicate that 92 percent of member converters were involved in export activities, up from participation levels for 2001-2004.