DEPARTMENT OF JUSTICE

Antitrust Division

United States v. Abitibi-Consolidated Inc. et al.; Response to Public Comment on the Proposed Final Judgment

Pursuant to the Antitrust Procedures and Penalties Act, 15 U.S.C. 16(b)–(h), the United States hereby publishes the public comment received on the proposed Final Judgment in *United States of America* v. *Abitibi-Consolidated Inc. et al.*, Civil Action No. 1:07–cv–1912 and the response to the comment. On October 23, 2007, the United States filed a Complaint alleging that the merger between Abitibi-Consolidated Inc. (''Abitibi'') and Bowater Inc. (''Bowater'') violated Section 7 of the Clayton Act, 15 U.S.C. 18. The proposed Final Judgment, filed on October 23, 2007, requires the combined company to divest Abitibi's Snowflake, Arizona paper mill. Public comment was invited within the statutory 60-day comment period. Copies of the Complaint, proposed Final Judgment, Competitive Impact Statement, Public Comment and the United States' Response to the Comment and other papers are currently available for inspection in Suite 1010 of the Antitrust Division, Department of Justice, 450 5th Street, NW., Washington, DC 20530, telephone: (202) 514–2481 and the Office of the Clerk of the United States District Court for the District of the District of Columbia, 333 Constitution Ave., NW, Washington, DC 20001. Copies of any of these materials may be obtained upon request and payment of a copying fee.

J. Robert Kramer II,

Director of Operations, Antitrust Division.

In the matter of: United States of America, Plaintiff, v. Abitibi-Consolidated Inc. and Bowater Inc., Defendants.

Case No: [1:07–cv–01912]

Judge: Collyer, Rosemary M.; Deck type: Antitrust.

Response of Plaintiff United States to Public Comments on the Proposed Final Judgment

Pursuant to the requirements of the Antitrust Procedures and Penalties Act (''APPA'' or ''Tunney Act''), 15 U.S.C. 16(b)–(h), the United States hereby files the Comment received from members of the public concerning the proposed Final Judgment in this case and the Response by the United States to the Comment. The United States will move the Court for entry of the proposed Final Judgment after the Comment and this Response have been published in the **Federal Register**, pursuant to 15 U.S.C. 16(d).

The United States filed a civil antitrust Complaint under Section 15 of the Clayton Act, 15 U.S.C. 25, on October 23, 2007, alleging that the merger of Abitibi-Consolidated Incorporated (''Abitibi'') and Bowater Incorporated (''Bowater'') would violate Section 7 of the Clayton Act, 15 U.S.C. 18. Simultaneously with the filing of the Complaint, the United States filed a proposed Final Judgment and an Asset Preservation Stipulation and Order (''Stipulation'') signed by plaintiff and defendants consenting to the entry of the proposed Final Judgment after compliance with the requirements of the Tunney Act. Pursuant to those requirements, the United States filed a Competitive Impact Statement (''CIS'') in this Court on October 23, 2007, published the proposed Final Judgment and CIS in the **Federal Register** on November 8, 2007, see *United States* v. *Abitibi-Consolidated Inc. and Bowater Inc.*, 72 FR 63187 (November 8, 2007); and published summaries of the terms of the proposed Final Judgment and CIS, together with directions for the submission of written comments relating to the proposed Final Judgment, in *The Washington Post* for seven days beginning on November 18, 2007, and ending on November 24, 2007. The 60-day period for public comments ended on January 7, 2008, and one comment was received as described below and attached hereto.

I. Background: The United States' Investigation and the Proposed Resolution

On January 29, 2007, Abitibi and Bowater announced plans to merge into a new company to be called AbitibiBowater Incorporated (''AbitibiBowater''). Over the next nine months, the United States Department of Justice (the ''Department'') conducted an extensive, detailed investigation into the competitive effects of the proposed transaction. As part of this investigation, the Department obtained substantial documents and information from the merging parties and issued 37 Civil Investigative Demands to third parties. In response, the Department received and considered more than 150,000 pages of material. The Department conducted more than 60 interviews with customers, competitors and other individuals with knowledge of the industry. The sole commenter here, the Newspaper Association of America (the ''NAA''), represents newspaper publishers in the United States. During the course of the Department's investigation into the proposed merger, the NAA shared with the investigative staff its concerns about the impact of the proposed merger on competition; the investigative staff carefully analyzed its concerns and submissions, as well as the data, market facts and opinions of other knowledgeable parties.

The Department concluded that the combination of Abitibi and Bowater likely would lessen competition in the North American newsprint market. Newspapers are printed on newsprint, the lowest quality and generally the least expensive grade of groundwood paper. Newspaper publishers, who buy more than 80 percent of all newsprint sold in the United States, have no close substitutes to use for printing newspapers because of newsprint's price and physical characteristics. Because publishers' newsprint presses are optimized to use newsprint, switching to another grade of paper would be costly. A small but significant increase in price likely would not cause customers to switch sufficient newsprint tonnes to other products or otherwise curtail their newsprint usage so as to render the increase unprofitable.

As explained more fully in the Complaint and CIS, the merger of Abitibi and Bowater would substantially increase concentration and lessen competition in the production, distribution and sale of newsprint in North America. After conducting a detailed analysis of the merger, the Department filed its Complaint alleging competitive harm in the newsprint market in North America and sought a remedy that would ensure that such harm is prevented.

The proposed Final Judgment in this case is designed to preserve competition in the production, distribution and sale of newsprint in North America. It requires the divestiture of a newsprint mill that manufactures newsprint for sale in North America. Specifically, the proposed Final Judgment directs a sale of Abitibi's Snowflake, Arizona, newsprint mill (''Snowflake,'' or the ''Snowflake mill'') to a purchaser acceptable to the United States.

In the Department's judgment, divestiture of the Snowflake mill to a qualified purchaser would remedy the violation alleged in the Complaint because the Snowflake mill, located in northeastern Arizona, is one of the most efficient and profitable newsprint mills in North America. Plans to improve the mill's efficiency in coming years with investments in energy and machinery are already underway. Snowflake's size and cost position ensure that its divestiture to a competitor of the merged firm will preserve competition in the North American newsprint market. Although entry of the proposed Final Judgment would terminate this action, the Court would retain jurisdiction to construe, modify, or enforce the provisions of the proposed Final Judgment and punish violations thereof. [1]

II. Standard of Judicial Review

Upon the publication of the Comment and this Response, the United States will have fully complied with the Tunney Act and will move for entry of the proposed Final Judgment as being ''in the public interest.'' 15 U.S.C. 16(e), as amended.

The Tunney Act states that, in making that determination, the Court shall consider:

(A) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration of relief sought, anticipated effects of alternative remedies actually considered, whether its terms are ambiguous, and any other competitive considerations bearing upon the adequacy of such judgment that the court deems necessary to a determination of whether the consent judgment is in the public interest; and

(B) the impact of entry of such judgment upon competition in the relevant market or markets, upon the public generally and individuals alleging specific injury from the violations set forth in the complaint including consideration of the public benefit, if any, to be derived from a determination of the issues at trial.

15 U.S.C. 16(e)(1)(A)–(B); *see generally United States* v. *SBC Commc'ns, Inc.*, 489 F. Supp. 2d 1, 11 (D.D.C. 2007) (concluding that the 2004 amendments ''effected minimal changes'' to scope of review under Tunney Act, leaving review ''sharply proscribed by precedent and the nature of Tunney Act proceedings'').[2]

As the United States Court of Appeals for the District of Columbia Circuit has held, under the APPA a court considers, among other things, the relationship between the remedy secured and the specific allegations set forth in the government's complaint, whether the decree is sufficiently clear, whether enforcement mechanisms are sufficient, and whether the decree may positively harm third parties. *See United States* v. *Microsoft Corp.*, 56 F.3d 1448, 1458–62 (D.C. Cir. 1995). With respect to the adequacy of the relief secured by the decree, a court may not ''engage in an unrestricted evaluation of what relief would best serve the public.'' *United States* v. *BNS, Inc.*, 858 F.2d 456, 462 (9th Cir. 1988) (citing *United States* v. *Bechtel Corp.*, 648 F.2d 660, 666 (9th Cir. 1981)); *see also Microsoft*, 56 F.3d at 1460–62. Courts have held that:

[t]he balancing of competing social and political interests affected by a proposed antitrust consent decree must be left, in the first instance, to the discretion of the Attorney General. The court's role in protecting the public interest is one of insuring that the government has not breached its duty to the public in consenting to the decree. The court is required to determine not whether a particular decree is the one that will best serve society, but whether the settlement is ''*within the reaches of the public interest.*'' More elaborate requirements might undermine the effectiveness of antitrust enforcement by consent decree.

Bechtel, 648 F.2d at 666 (emphasis added) (citations omitted). *Cf. BNS*, 858 F.2d at 464 (holding that the court's ''ultimate authority under the [APPA] is limited to approving or disapproving the consent decree''); *United States* v. *Gillette Co.*, 406 F. Supp. 713, 716 (D. Mass. 1975) (noting that, in this way, the court is constrained to ''look at the overall picture not hypercritically, nor with a microscope, but with an artist's reducing glass''). *See generally Microsoft*, 56 F.3d at 1461 (discussing whether ''the remedies [obtained in the decree are] so inconsonant with the allegations charged as to fall outside of the 'reaches of the public interest' ''). In making its public interest determination, a district court ''must accord deference to the government's predictions about the efficacy of its remedies, and may not require that the remedies perfectly match the alleged violations'' because this may only reflect underlying weakness in the government's case or concessions made during negotiation. *SBC Commc'ns*, 489 F. Supp. 2d at 17; *see also Microsoft*, 56 F.3d at 1461 (noting the need for courts to be ''deferential to the government's predictions as to the effect of the proposed remedies''); *United States* v. *Archer-Daniels-Midland Co.*, 272 F. Supp. 2d 1, 6 (D.D.C. 2003) (noting that the court should grant due respect to the United States' prediction as to the effect of proposed remedies, its perception of the market structure, and its views of the nature of the case).

Court approval of a consent decree requires a standard more flexible and less strict than that appropriate to court adoption of a litigated decree following a finding of liability. ''[A] proposed decree must be approved even if it falls short of the remedy the court would impose on its own, as long as it falls within the range of acceptability or is 'within the reaches of public interest.' '' *United States* v. *Am. Tel. & Tel. Co.*, 552 F. Supp. 131, 151 (D.D.C. 1982) (citations omitted) (quoting *United States* v. *Gillette Co.*, 406 F. Supp. 713, 716 (D. Mass. 1975)), *aff'd sub nom. Maryland* v. *United States*, 460 U.S. 1001 (1983); *see also United States* v. *Alcan Aluminum Ltd.*, 605 F. Supp. 619, 622 (W.D. Ky. 1985) (approving the consent decree even though the court would have imposed a greater remedy). To meet this standard, the United States ''need only provide a factual basis for concluding that the settlements are reasonably adequate remedies for the alleged harms.'' *SBC Commc'ns*, 489 F. Supp. 2d at 17.

Moreover, the Court's role under the APPA is limited to reviewing the remedy in relationship to the violations that the United States has alleged in its complaint, and does not authorize the Court to ''construct [its] own hypothetical case and then evaluate the decree against that case.'' *Microsoft*, 56 F.3d at 1459. Because the ''court's authority to review the decree depends entirely on the government's exercising its prosecutorial discretion by bringing a case in the first place,'' it follows that ''the court is only authorized to review the decree itself,'' and not to ''effectively redraft the complaint'' to inquire into other matters that the United States did not pursue. *Id.* at 1459–60. As this Court recently confirmed in *SBC Communications*, courts ''cannot look beyond the complaint in making the public interest determination unless the complaint is drafted so narrowly as to make a mockery of judicial power.'' *SBC Commc'ns* 489 F. Supp. 2d at 15.

In its 2004 amendments, Congress made clear its intent to preserve the

[1] The merger closed on October 29, 2007. In keeping with the United States' standard practice, neither the Stipulation nor the proposed Final Judgment prohibited closing the merger. See ABA Section of *Antitrust Law, Antitrust Law Developments* 406 (6th ed. 2007) (noting that ''[t]he Federal Trade Commission (as well as the Department of Justice) generally will permit the underlying transaction to close during the notice and comment period''). Such a prohibition could interfere with many time-sensitive deals and prevent or delay the realization of substantial efficiencies. In consent decrees requiring divestitures, it is also standard practice to include a ''preservation of assets'' clause in the decree and to file a stipulation to ensure that the assets to be divested remain competitively viable. That practice was followed here. Proposed Final Judgment § IV(K). In addition, the Stipulation entered by the Court in this case required AbitibiBowater to hold separate the Snowflake newsprint mill, pending the divestiture contemplated by the proposed Final Judgment.

[2] The 2004 amendments substituted ''shall'' for ''may'' in directing relevant factors for court to consider and amended the list of factors to focus on competitive considerations and to address potentially ambiguous judgment terms. Compare 15 U.S.C. 16(e) (2004), with 15 U.S.C. 16(e)(1) (2006).

practical benefits of utilizing consent decrees in antitrust enforcement, adding the unambiguous instruction ''[n]othing in this section shall be construed to require the court to conduct an evidentiary hearing or to require the court to permit anyone to intervene.'' 15 U.S.C. 16(e)(2). The language wrote into the statute what the Congress that enacted the Tunney Act in 1974 intended, as Senator Tunney then explained: ''[t]he court is nowhere compelled to go to trial or to engage in extended proceedings which might have the effect of vitiating the benefits of prompt and less costly settlement through the consent decree process.'' 119 Cong. Rec. 24,598 (1973) (statement of Senator Tunney). Rather, the procedure for the public interest determination is left to the discretion of the court, with the recognition that the court's ''scope of review remains sharply proscribed by precedent and the nature of Tunney Act proceedings.'' *SBC Commc'ns*, 489 F. Supp. 2d at 11.[3]

III. Summary of the Comment and Response

During the 60-day comment period, the United States received one Comment, from the NAA. That Comment is attached to this memo. After reviewing the Comment, the United States continues to believe that the proposed Final Judgment is in the public interest. The Comment includes concerns relating to whether the proposed Final Judgment adequately remedies the harms alleged in the Complaint. The United States addresses these concerns below and explains how the remedy is appropriate.

A. Summary of Comment Submitted by the NAA

The NAA is an association whose members include daily and Sunday newspapers in the United States who purchase a significant proportion of North America's newsprint production. In its Comment of January 2, 2008, the NAA expressed concerns relating to whether the proposed Final Judgment adequately remedies the alleged harms. The NAA argued in its Comment that the Court should not enter the proposed Final Judgment without a hearing for two reasons: (1) the newly merged AbitibiBowater, despite its agreement to divest the Snowflake mill, ''has already begun to exercise the market power created by the merger to anticompetitively raise newsprint prices to North American newsprint customers''; and (2) the United States ''has not provided the Court with any factual or economic analysis to demonstrate that the proposed remedy will eliminate the incentive for AbitibiBowater to reduce industry capacity and raise prices to North American newsprint customers.'' (NAA Comment at 2.)

1. The NAA's Argument That AbitibiBowater Has Already Begun To Exercise Market Power and Anticompetitively Raise Newsprint Prices

The NAA notes that a little more than five weeks following the merger that created AbitibiBowater, the combined firm announced that it would remove 600,000 metric tonnes of newsprint capacity from the North American market and would raise newsprint prices by $60 per metric tonne, to be implemented in three $20 price increases. The NAA further notes that ''[m]ost'' North American newsprint manufacturers not only joined AbitibiBowater's price increase but also implemented a ''previously stalled'' price increase of $25 per metric tonne. The NAA estimated that, taken together, these two price increases constitute a 15 percent price increase as compared to the pre-merger, October 2007, price for newsprint. The NAA also noted that, at the time AbitibiBowater announced the removal of 600,000 metric tonnes of newsprint capacity from the North American market, it also announced that ''more mills could close in Canada later [in 2008].'' (Comment at 7.)

The NAA claims that these post-merger actions by AbitibiBowater demonstrate that the United States ''severely underestimated the risk that the merger posed to competition in the North American newsprint market and severely underestimated the incentive and ability of the merged firm to remove capacity from the market to raise the price of newsprint well above competitive levels.'' (Comment at 7.) Accordingly, the NAA contends that a ''significantly larger divestiture'' than the Snowflake mill is required to prevent ''the substantial anticompetitive price increases that are already occurring and will continue to occur as a result of the merger.'' (Comment at 7.)

2. The NAA's Argument That the United States Has Not Provided Adequate Factual or Legal Analysis Upon Which To Base a Public Interest Determination

The NAA concedes that in the Complaint, the United States ''correctly identifies the competitive harm produced by the merger.'' (Comment at 9.) The NAA argues, however, that the United States has not provided the Court with a factual or legal analysis to demonstrate that the divestiture of the Snowflake mill will ''eliminate the incentive to reduce industry capacity and raise prices to North American newsprint customers,'' and thus has provided the Court with no basis by which to determine if the proposed remedy is in the public interest. (Comment at 9.) Specifically, the NAA argues that, other than noting that Snowflake is ''among the largest and most profitable mills in the United States,'' the United States ''provided no further explanation for its decision that Snowflake was both a sufficient remedy and the best solution, no detail regarding under what 'circumstances' this conclusion was reached, and no scale against which it measured Snowflake as the best alternative.'' (Comment at 17.)

The NAA contends that the proposed Final Judgment should not be entered because the United States has not explained to the Court ''why the remedy it proposes restores or preserves competition.'' (Comment at 19.) In particular, the NAA criticizes the United States for failing to reference in the Complaint or CIS what the NAA describes as historical anticompetitive behavior of Abitibi and Bowater, and it contends that absent such references, it is impossible for the Court to determine if and how much of a factor such conduct played in the United States' evaluation and settlement of the merger. The NAA also criticizes the United States for failing to discuss the anticipated effects of alternative remedies actually considered.

B. Response of the United States to the NAA's Comment

The divestiture of the Snowflake mill adequately remedies the harm alleged in the Complaint. In negotiating this remedy, the United States carefully considered the capabilities and economic viability of the Snowflake mill as well as other assets of the merging parties; the extent of industry excess capacity; the history of declining demand for newsprint, and the forecasts for that decline to continue; the costs of

[3] *See United States* v. *Enova Corp.*, 107 F. Supp. 2d 10, 17 (D.D.C. 2000) (noting that the ''Tunney Act expressly allows the court to make its public interest determination on the basis of the competitive impact statement and response to comments alone''); *United States* v. *Mid-Am. Dairymen, Inc.*, 1977–1 Trade Cas. (CCH) ¶ 61,508, at 71,980 (W.D. Mo. 1977) (''Absent a showing of corrupt failure of the government to discharge its duty, the Court, in making its public interest finding, should * * * carefully consider the explanations of the government in the competitive impact statement and its responses to comments in order to determine whether those explanations are reasonable under the circumstances.''); S. Rep. No. 93–298, 93d Cong., 1st Sess., at 6 (1973) (''Where the public interest can be meaningfully evaluated simply on the basis of briefs and oral arguments, that is the approach that should be utilized.'').

production of all newsprint mills in North America; and the financial viability of the merging parties and their competitors. After considering these issues, the United States analyzed the merger using a comprehensive data set of prices, sales, production volumes and costs, capacities and forecasts of North American newsprint demand. In its analysis, which drew upon non-public information unavailable to the NAA, the United States concluded that the divestiture of the Snowflake mill to a viable qualified purchaser will adequately redress the competitive harm alleged in the Complaint and restore competition to the market for the sale of newsprint in North America.

The United States and the NAA employed the same general economic model to examine the competitive effects of the merger. Accurate data about prices, manufacturing costs, the elasticity of demand and other factors can allow economists to model whether merging firms have an added incentive to exercise market power by reducing capacity after a merger. The United States and the NAA both attempted to determine whether the merger will cause the combined AbitibiBowater to eliminate newsprint capacity earlier than Abitibi and Bowater would have if they had remained independent competitors.

Although the United States and the NAA used a similar framework to model competition, the results differed significantly because of several important differences in the data. First, the United States had more complete and accurate data. Unlike the NAA, the United States was able to use a compulsory process to gather information. See, e.g., 15 U.S.C. 1311–14 (empowering the Antitrust Division to subpoena documents and take oral testimony). In this case, the United States had access to extensive and mill-by-mill data on sales (including exports), production volumes, capacities and costs. The NAA, on the other hand, had to rely on less accurate and publicly available information relating to mill capacities, prices and costs in assessing the profitability of and competitors' likely response to a post-merger price increase. Second, the United States conducted its own analysis of the effect of price changes on the demand for newsprint, using confidential information, in addition to considering estimates provided by others. Based upon its analysis, the United States believes that the estimate used by NAA understates the sensitivity of newsprint consumption to changes in price. In other words, the United States believes that if the price for newsprint rose, customers would purchase less newsprint than the NAA estimates. Third, the United States and the NAA viewed 2007 differently. While the NAA assumed that the newsprint market in 2007 was in equilibrium—which would allow that year's prices to be used as a reference point from which to measure future changes—the United States' investigation revealed that much of 2007 was a period of instability. Unexpectedly large declines in demand for newsprint created excess capacity and caused prices to fall dramatically. The fact that AbitibiBowater and other firms responded to declining demand for newsprint by closing mills that were consistently losing money is discussed in further detail in the following section.

The United States is confident that at the time it negotiated the proposed Final Judgment the divestiture of the Snowflake mill was in the public interest, based upon the best information available at that time. The United States remains confident that the divestiture of the Snowflake mill is in the public interest and adequately remedies the harms alleged in the Complaint.

1. AbitibiBowater's Recently Announced Decision To Reduce Excess Newsprint Capacity, and Industry-Wide Price Increases, Do Not Mean That the Parties Have Exercised Market Power

The NAA's argument, that the Snowflake mill divestiture is insufficient to prevent the combined firm from exercising market power by shutting additional capacity in order to raise prices, assumes that the combined firm's post-merger capacity reductions are the result of the merger. The NAA's suggestions to the contrary events since the filing of the proposed Final Judgment appear to be unrelated to any exercise of market power. The ongoing sharp decline in demand for newsprint in North America, increases in the prices of key inputs into the production of newsprint, and the continued decline in the value of the United States dollar all have disrupted the supply and demand equilibrium for newsprint. Industry observers expect disruptions to continue as North American demand for newsprint declines. Manufacturers will respond by intermittently closing capacity, which will cause the market price to lurch from one equilibrium to another as it adjusts to these shocks to supply. Thus, in a market with declining demand, prices can be expected to fall when the decline in demand creates excess supply and increase when unprofitable capacity is closed in response to that decline in demand. In the remainder of this section, we will discuss the effects of these trends on the newsprint market and show that a careful analysis suggests that the NAA's claims are unfounded.

Demand for newsprint in the North American market ''has declined over the last several years at a rate of approximately 5 to 10 percent per year because of a significant decline in demand for newspapers. * * * This decline in the demand for newsprint is projected to continue, and the resulting excess newsprint capacity will likely lead Defendants and their competitors to close, idle or convert more newsprint mills.'' (Complaint at ¶ 17; *see also* CIS at 5.) As North American demand continues to decline, notwithstanding the merger, all firms, including AbitibiBowater, will eventually have to close inefficient newsprint capacity. In its Comment, the NAA ignores the possibility that AbitibiBowater's post-merger decision to close some of its inefficient capacity was a natural reaction to the continued decline in demand for newsprint and may in fact be perfectly consistent with a competitive market.

The pressure to close inefficient capacity also intensified in 2007 because the prices of key production inputs—specifically, recycled fiber, wood pulp and energy—rose sharply. This increase in input costs has raised the costs of all producers and put upward pressure on the price of newsprint. Further, the United States dollar has lost value relative to the Canadian dollar, which has the effect of raising the costs of Canadian producers of newsprint—the bulk of North American newsprint capacity is located in Canada—and hence the price of newsprint.

Finally, the adjustment of the newsprint market to these disruptive market conditions will not be instantaneous or smooth. Because newsprint mills have very significant fixed costs and relatively smaller incremental costs, newsprint manufacturers may not be able to respond to declining demand by gradually withdrawing capacity. The market therefore can be expected to swing between periods of overcapacity and shortage as companies retire paper machines or entire paper mills. As these swings occur, there will not be smooth changes to the industry's overall capacity or its price levels. For example, while the price of newsprint has risen in the past six months, it is at the time of this filing at or below its lowest level in 2006 when input prices were lower. Further, the United States' investigation has found that the price is so low that many newsprint producers' mills do not cover their costs. Indeed, the three mills that AbitibiBowater closed after the merger were unprofitable.

In summary, the NAA's conclusion that recent newsprint capacity closures and price increases necessarily are anticompetitive actions driven by the merger is misguided and fails to account for significant market facts affecting the supply and demand equilibrium of the North American newsprint market.

2. The United States Has Provided Sufficient Explanation of Why the Proposed Divestiture Is an Adequate Remedy to the Harm Alleged in the Complaint, and Entry of the Proposed Final Judgment Will Be in the Public Interest

The proposed Final Judgment provides an effective and appropriate remedy for the antitrust violation alleged in the Complaint, and its entry, therefore, will be in the public interest. The purpose of Tunney Act review is not for the Court to engage in an ''unrestricted evaluation of what relief would best serve the public,'' *BNS*, 858 F.2d at 462 (citing *Bechtel Corp.*, 648 F.2d at 666) or to determine the relief ''that will best serve society,'' *Bechtel Corp.*, 648 F.2d at 666. Instead, the purpose of Tunney Act review is simply to determine whether the divestiture of the Snowflake mill is within the reaches of the public interest, ''even if it falls short of the remedy the court would impose on its own.'' *AT&T*, 552 F. Supp. at 151. In other words, the purpose of Tunney Act review is to determine whether the divestiture is a ''reasonably adequate'' remedy for the harms alleged in the Complaint. *SBC Commc'ns*, 489 F. Supp. 2d at 17.

Subsections (A) and (B) of 15 U.S.C. 16(e)(1) set forth a number of factors for courts to consider when assessing the competitive impact of proposed final judgments. Many of those factors are not at issue here.[4] Instead, the second argument in the NAA's Comment focuses on the competitive considerations relevant to the proposed Final Judgment, the divestiture it requires and the alternatives the United States considered.

The NAA questions whether the United States has adequately demonstrated to this Court that the divestiture eliminates AbitibiBowater's post-merger incentive to reduce capacity and raise prices to North American newsprint customers. It has. As explained previously, the United States conducted an extensive investigation and compiled comprehensive data on market shares, costs of production, estimations of rest-of-industry newsprint capacity and future reductions in newsprint demand gathered from public and non-public sources. This data was used in an economic model to determine if the merger would cause an anticompetitive increase in newsprint prices.[5] The United States concluded that a merger between Abitibi and Bowater, without a divestiture, would allow the merged firm to ''close its capacity strategically, allowing the merged firm to raise newsprint prices and recoup its lost profits on the combined output.'' (CIS at 8.) But, as the United States concluded in the CIS, ''[d]ivesting Snowflake * * * will reduce the capacity over which the merged firm could profit to a level at which it would not have the ability to close capacity strategically.'' (*Id.*) In other words, the United States' investigation found that without Snowflake, AbitibiBowater did not have enough newsprint capacity to benefit sufficiently from the post-merger price increase to offset the costs associated with shutting down profitable newsprint capacity.

The NAA further contends that the United States ''has left the Court entirely in the dark with absolutely no basis for making a meaningful comparison between a Snowflake-only divestiture and any alternative course of action, including a full trial on the merits.'' (Comment at 18.) This is incorrect; in the CIS the United States addressed both alternatives. (CIS at 10–11.) As the United States noted in the CIS, a full trial on the merits would require significant time and expense, and the outcome would be uncertain. In light of such uncertainty, the United States' decision to take an adequate and available remedy and forgo the risk of trial is well within ''the reaches of the public interest.'' *See SBC Commc'ns*, 489 F. Supp. 2d at 23 (''Success at trial was surely not assured, so pursuit of that alternative may have resulted in no remedy at all. While a trial may have created an even greater evidentiary record, that benefit may not outweigh the possible loss of the settlement remedies. * * *'').

Similarly, the United States need not rehearse every permutation of possible divestiture in order to demonstrate to this Court that the divestiture of Snowflake would adequately address the competitive harm alleged in the Complaint. The competitive harm that the United States alleged—and that the NAA acknowledges—is AbitibiBowater's incentive and ability to raise newsprint prices above competitive levels in the North American market. Any divestiture that removes either the combined firm's incentive or its ability to raise prices above competitive levels would therefore be an adequate remedy. Given AbitibiBowater's ownership of all or part of 19 paper mills in the United States and Canada (*see* Complaint ¶¶ 7 & 8), the United States could have selected different mills, individually or in combination, to remove the merged firm's ability and incentive to raise prices anticompetitively. In this instance, considering all the factors—including the inherent advantages of settlement and avoidance of the risk and uncertainty of litigation[6]—the United States reasonably chose to require the divestiture of one of ''the largest and most profitable newsprint mills in the United States,'' which its analysis determined would deprive the merged firm of the scale needed to recoup its lost profits. (*See* CIS at 6, 11.) As discussed above, given the continuing decline in demand for newsprint, the United States anticipated that AbitibiBowater would continue to close inefficient newsprint capacity. (*See* Complaint at ¶ 17, CIS at 5.) The United States determined that, coupled with the exit from the market of such inefficient capacity, the divestiture of

[4] The NAA does not contest several factors listed for courts to consider under subsection (A). For instance, with respect to ''provisions for enforcement and modification,'' 15 U.S.C. 16(e)(1)(A), the proposed Final Judgment contains the standard provisions that have been effective in numerous other cases brought by the United States. In particular, the proposed Final Judgment provides that the Court retains jurisdiction over this action, and the parties may apply to the Court for any order necessary or appropriate for the modification, interpretation, or enforcement of the Final Judgment. With respect to ''duration of relief sought,'' *id.*, the proposed divestiture is permanent. Finally, with respect to ''whether its terms are ambiguous,'' *id.*, no term in the proposed Final Judgment is ambiguous.

[5] To raise prices above competitive levels, the merged firm must create an artificial shortage by shutting down profitable newsprint mills. The merged firm has the incentive to follow this strategy when the costs of this strategy, which are the profits the merged firm forgoes by prematurely shutting down profitable newsprint mills, are less than its benefits, which are the increased prices the merged firm can expect to recoup across its remaining newsprint capacity. After completing its investigation, the United States concluded that without a divestiture AbitibiBowater would have the incentive to follow this strategy, that is, to create an artificial shortage by shutting down otherwise-profitable newsprint mills.

[6] As noted previously, when making its public interest determination, this Court ''must accord deference to the government's predictions about the efficacy of its remedies, and may not require that the remedies perfectly match the alleged violations because this may only reflect underlying weakness in the government's case or concessions made during negotiation.'' *SBC Commc'ns*, 489 F. Supp. 2d at 17.

the Snowflake mill will be sufficient to prevent AbitibiBowater from engaging in an anticompetitive closure of *efficient* capacity. Abitibi and Bowater, even before the merger, had the incentive to close money-losing mills. The question therefore is whether the merger somehow gave them the incentive to close profitable mills in order to raise prices above competitive levels. The United States determined that AbitibiBowater was not likely to have that incentive once it divested Snowflake.

Finally, the NAA suggests that the proposed Final Judgment should not be entered because Abitibi and Bowater previously had engaged in anticompetitive conduct of the sort alleged in the Complaint, which it alleges the United States did not properly account for in negotiating the proposed Final Judgment. This suggestion is misplaced for two reasons. First, as mentioned earlier, the United States spoke with a number of market participants, including the NAA, and examined historical data on prices and costs in the course of its investigation. The evidence does not support the NAA's claims that the parties' prior behavior was in fact anticompetitive. Second, the NAA's allegations about the parties' prior behavior are irrelevant because the prior behavior does not address whether, after Snowflake is divested, AbitibiBowater will have the incentive and ability to unilaterally raise price above competitive levels. (And as the United States has already explained, the answer to this question is likely to be ''no.'')

Ultimately, in making its public interest determination, the district court ''must accord deference to the government's predictions about the efficacy of its remedies.'' *See SBC Commc'ns*, 489 F. Supp. 2d at 17. As already has been demonstrated, the United States' analysis supports the conclusion that divestiture of the Snowflake mill is an appropriate remedy to the harms alleged in the Complaint.

IV. Conclusion

The issues raised in the NAA's public Comment were among the many considered during the United States' extensive and thorough investigation. The United States has determined that the proposed Final Judgment as drafted provides an effective and appropriate remedy for the antitrust violations alleged in the Complaint, and is therefore in the public interest. The United States will move this Court to enter the proposed Final Judgment after the Comment and Response are published.

Respectfully Submitted,

Dated: April 18, 2008,

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Certificate of Service

I hereby certify that on April 18, 2008, I caused a copy of the foregoing Response of Plaintiff United States to Public Comments on The Proposed Final Judgment in this matter to the following individuals by electronic mail:

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Comments of the Newspaper Association of America Regarding Proposed Final Judgment in United States of America v. Abitibi-Consolidated, Inc. and Bowater, Incorporated

In its Explanation of Consent Decree Procedures, the Justice Department requests the Court to enter the proposed Final Judgment settling *United States of America* v. *Abitibi-Consolidated, Inc. and Bowater, Incorporated* without a hearing ''provided that the Court concludes that the Final Judgment is in the public interest.'' [1] The main provision of the proposed Final Judgment is the requirement that the defendants divest Abitibi-Consolidated's Snowflake, Arizona newsprint mill in order to settle the Justice Department's Complaint [2] enjoining the proposed merger of Abitibi-Consolidated, Inc. (''Abitibi'') and Bowater, Incorporated (''Bowater'').[3] Shortly after the settlement agreement, Abitibi and Bowater completed their merger. The merged firm is named AbitibiBowater.[4]

The Newspaper Association of America (''NAA'') is an association whose membership includes most of the daily and Sunday newspaper publishers in the United States. NAA represents the newsprint customers most significantly affected by the merger of Abitibi and Bowater and the provisions of the proposed Final Judgment.

In its Competitive Impact Statement, the Justice Department asserts that the divestiture of the Snowflake mill ''would adequately address the likelihood that the proposed merger substantially would reduce competition for newsprint in the United States.'' [5] In its filings on this matter, including the Competitive Impact Statement and proposed Final Judgment, the Justice Department provides no information or analysis to the Court to support or justify this assertion.

In these Comments, the NAA makes two separate but related arguments explaining why it believes the Court should reject the Justice Department's request to approve the proposed Final Judgment without a hearing. (1) The newly merged AbitibiBowater, despite its agreement to divest the Snowflake mill, has already begun to exercise the market power created by the merger to anticompetitively raise newsprint prices to North American newsprint customers. This post-settlement exercise of market power by AbitibiBowater shows that the proposed Final Judgment is not in the public interest. (2) Even without the post-settlement evidence of anticompetitive conduct by AbitibiBowater, there would still be ample grounds to reject the proposed remedy. The Justice Department has not provided the Court with any factual or economic analysis to demonstrate that the proposed remedy will eliminate the incentive for AbitibiBowater to reduce industry capacity and raise prices to North American newsprint customers (the injury charged in the Complaint). Each argument, standing on its own, provides sufficient grounds for the

[1] Plaintiff United States' Explanation of Consent Decree Procedures filed with the Court on October 23, 2007 at ¶ 6.

[2] The Complaint and proposed Final Judgment were filed with the Court on October 23, 2007.

[3] Proposed Final Judgment at pages 5–8.

[4] Abitibi and Bowater completed their merger on October 29, 2007. AbitibiBowater press release, October 29, 2007.

[5] Competitive Impact Statement at page 6. The Competitive Impact statement was also filed with the Court on October 23, 2007.

rejection by the Court of the Justice Department's request to enter the proposed Final Judgment without a hearing.

If the proposed Final Judgment is entered without modification, the newly merged AbitibiBowater will have the ability and incentive to unilaterally engage in anticompetitive conduct to raise newsprint prices above competitive levels to U.S. daily newspapers and other North American newsprint customers. The Court should reject the Justice Department's request to enter the proposed Final Judgment and conduct a hearing into this matter to determine a remedy sufficient to prevent the harm to competition and the economic harm to U.S. daily newspapers and other North American newsprint customers that will otherwise result from the merger and from the inadequate divestiture remedy as contained in the proposed Final Judgment.

Analysis of the Competitive Impact of the Merger and the Adequacy of the Divestiture of the Snowflake Mill

On November 8, 2007, the Justice Department published in the **Federal Register** the Proposed Final Judgment resolving a Complaint filed by the United States to enjoin the merger of Abitibi and Bowater. The Complaint describes the acquisition as creating a newsprint producer "three times larger than the next North American newsprint producer" that "will have the incentive and ability to withdraw capacity and raise newsprint prices in the North American newsprint market." [6] Prior to the merger, Abitibi was the largest producer with 25 percent of the North American newsprint capacity.[7] With Bowater's second place share of 16 percent, the combined firm would own "over 40" percent of the North American newsprint capacity.[8] The Complaint seeks to enjoin the transaction because it will "provide the merged firm with an incentive to close capacity sooner than it otherwise would to raise prices and profit from the higher margins on its remaining capacity." [9]

Newspaper publishers do not have alternatives to newsprint to turn to when newsprint prices rise. The Complaint states that "newspaper publishers have no close substitutes to use for printing newspapers," [10] and that "demand for newsprint is highly inelastic to changes in price." [11] Consequently, if North American newsprint manufacturers attempted to exercise market power by raising newsprint prices above competitive levels, U.S. newspaper publishers and other North American newsprint buyers could not successfully resist that exercise of market power.[12] Furthermore, U.S. newspaper publishers and other North American newsprint buyers would not be able to count on other suppliers to produce more newsprint or entry by new suppliers to roll back the price increase. According to the Complaint, "neither supply responses nor entry will defeat the exercise of market power." [13]

In recent years, the U.S. newspaper industry has experienced declining circulation and advertising revenue. As a result, North American demand for newsprint has also declined, leading to excess newsprint capacity. The decline in newsprint demand is projected to continue.[14] In such circumstances, newsprint prices would ordinarily be expected to also decline. According to the Complaint, however, the merger will give the merged firm both the incentive and ability to strategically close enough capacity to raise newsprint prices above competitive levels.[15] The Complaint also concludes that absent the merger, neither Abitibi nor Bowater as separate firms would have the incentive or ability to strategically close capacity to raise newsprint prices.[16] In the words of the Justice Department, the "merger will substantially lessen competition in the production and sales of newsprint," with the result that "prices charged for newsprint in North America likely will increase." [17]

In order to remedy the anticompetitive effects that the Justice Department concluded would otherwise result from the merger, the Department obtained the agreement of Abitibi and Bowater to divest Abitibi's Snowflake, Arizona newsprint mill.[18] In the Competitive Impact Statement, the Justice Department asserts that "[w]ithout Snowflake's capacity, the merged firm would not be of sufficient size to be able to recoup the losses from such strategic closures through increases in prices on its remaining newsprint production. The divestiture of Snowflake would adequately address the likelihood that the proposed merger substantially would reduce competition for newsprint in the United States." [19] The Snowflake mill accounts for about 3 percent of North American newsprint capacity.[20] Thus, the Justice Department is claiming that with a newsprint capacity share of about 40 percent, the merged firm would have the incentive and ability to unilaterally exercise market power to raise newsprint prices above competitive levels but that with a slightly smaller capacity share of 37 percent the merged firm would not have the incentive and ability to unilaterally exercise market power. The Justice Department provides the Court with no data or analysis in support of these assertions.

The Justice Department's prediction that the Snowflake divestiture would be sufficient to eliminate the incentive and ability of the merged firm to exercise market power by strategically removing newsprint capacity from the market to raise the price of newsprint has already been proven wrong. North American newsprint producers, including Abitibi and Bowater, had been trying to implement a $25 per tonne price increase since September of this year. Until November, newspaper publishers were successful in resisting the price increase.[21] On November 29, a little more than five weeks after the agreement to divest the Snowflake mill, the newly combined AbitibiBowater announced that it would remove about 600,000 metric tonnes of newsprint capacity from the North American market, representing about 5 percent of North American newsprint capacity.[22]

[6] Complaint at ¶ 2.

[7] Complaint at ¶ 7, 16.

[8] Complaint at ¶ 8, 16.

[9] Complaint at ¶ 19.

[10] Complaint at ¶ 10.

[11] Complaint at ¶ 11–12.

[12] In Section 0.1 of the Horizontal Merger Guidelines, the Justice Department defines the exercise of market power by a seller or sellers as "the ability profitably to maintain prices above competitive levels for a significant period of time." 1992 Horizontal Merger Guidelines, U.S. Department of Justice and Federal Trade Commission, Issued April 2, 1992 and revised April 8, 1997 ("Horizontal Merger Guidelines" or "Guidelines"). Available at *http://www.usdoj.gov/atr/public/guidelines/hmg.htm*.

[13] Complaint at ¶ 20–26.

[14] Complaint at ¶ 17.

[15] Complaint at ¶ 2–3, 16.

[16] Complaint at ¶ 18.

[17] Complaint at ¶ 3, 16, 28(c).

[18] Proposed Final Judgment at pp. 5–8, Competitive Impact Statement at pp. 8–11.

[19] Competitive Impact Statement at p. 6.

[20] Neither the Proposed Final Judgment nor the Competitive Impact Statement provides the North American newsprint capacity share of the Snowflake mill. At page 2, the Competitive Impact Statement states that the annual newsprint capacity of the Snowflake mill is 375,000 metric tonnes, which would be about 3 percent of current annual North American newsprint capacity of about 11.7 million metric tonnes based on November 2007 newsprint statistics provided by the Pulp and Paper Products Council.

[21] Publisher resistance to $25/tonne North American newsprint increase collapses; producers looking to fast track recovery, 29 Pulp & Paper Week 48 (Dec. 17, 2007) at 1.

[22] AbitibiBowater plans to shut down one million tonnes/yr of capacity in 1Q; expects more closures could follow in 2Q, 29 Pulp & Paper Week 46 (Dec. 3, 2007) at 1. A capacity closure of 600,000 metric tonnes would be about 5 percent of current annual

In conjunction with the capacity closures, AbitibiBowater initiated a newsprint price increase of $60 per metric tonne to be implemented in three $20 per metric tonne monthly increments beginning in January 2008. Most North American newsprint manufacturers quickly joined the $60 per metric tonne price initiated by AbitibiBowater.[23] Also, as a result of AbitibiBowater' s announced newsprint capacity closures of 600,000 metric tonnes, the previously stalled $25 per metric tonne price hike has been successfully implemented by North American newsprint manufacturers. As described in the trade press, ''[p]ublisher resistance to $25/tonne North American newsprint increase collapse[d]'' and the price hike went in ''like a hot knife through butter,'' [24] Combined, these two price increases will raise the price of newsprint by $85 per metric tonne or about 15 percent over the October 2007 price of $560 per metric tonne.[25] As RISI economist Kevin Conley concluded, ''AbitibiBowater's capacity closures will obviously provide the upward pressure for an extended price recovery in 2008, as operating rates soar past the magic 95% threshold generally needed for prices to rise.'' [26]

The combined AbitibiBowater is seeking to ''leverage the North American (newsprint) price up to the price in Europe and not the other way around,'' according to AbitibiBowater President and CEO David Paterson.[27] If AbitibiBowater is successful in ''leveraging'' the North American newsprint price up to the price of newsprint in Europe, that will result in a $200 per metric tonne price increase or about 36 percent over the North American price of $560 per metric tonne in October 2007.[28] At the time AbitibiBowater announced the removal of 600,000 metric tonnes of newsprint capacity from the market, it also announced that ''more mills could close in Canada later [in 2008].'' [29] Based on these statements and other statements by AbitibiBowater executives and past and current actions by AbitibiBowater and its predecessor companies, it is very likely that AbitibiBowater will close additional capacity in 2008 to ''leverage'' the North American newsprint price up to the newsprint price in Europe.

These post-settlement actions by AbitibiBowater show that the Justice Department severely underestimated the risk that the merger posed to competition in the North American newsprint market and severely underestimated the incentive and ability of the merged firm to remove capacity from the market to raise the price of newsprint well above competitive levels. It is evident that a significantly larger divestiture is required to prevent the substantial anticompetitive price increases that are already occurring and will continue to occur as a result of the merger.

NAA Represents the Newsprint Customers Most Significantly Affected by AbitibiBowater's Exercise of Market Power

These comments are timely submitted pursuant to the Antitrust Procedures and Penalties Act, 15 U.S.C. 16(b)–(e) (known as the ''Tunney Act''), on behalf of the Newspaper Association of America (''NAA''). NAA members are the primary purchasers of newsprint. NAA has approximately 2,000 members, representing a broad range of newspaper-related companies ranging from independent, small market, and family owned publishers to the large newspaper chains. These members account for approximately 90 percent of the paid daily and Sunday newspaper circulation in the United States. U.S. daily newspapers are the primary purchasers of newsprint produced by North American newsprint mills and account for about 80 percent of the newsprint consumed in the U.S. and about 70 percent of the newsprint consumed in North America.

Newsprint is an essential and irreplaceable input for newspapers. Because newsprint is second only to labor as a cost for newspapers, higher newsprint prices have a direct impact on the ability of newspaper companies to serve their customers, newspaper readers and newspaper advertisers. When confronted with newsprint price increases, newspapers are forced to restrict their use of newsprint by reducing their circulation, withdrawing from more distant geographic areas, ending editions, and reducing the size and number of pages published. The impact of these changes adversely impacts the interest of the public, with less news available in print to the millions of newspaper readers and less information available in print for the electorate. At price levels equal to the prevailing prices in Europe, $200 per tonne above the pre-settlement October 2007 price, some newspapers will be unprofitable and at risk of failure.

This memorandum and the attached Economic Analysis [30] are submitted as a comment on the Justice Department's Competitive Impact Statement and proposed Final Judgment settling the proposed merger of Abitibi and Bowater. The Economic Analysis addresses, in particular, the inadequacy of the Snowflake divestiture to prevent the competitive harm from the merger that is identified in both the Complaint and Competitive Impact Statement. The attached Economic Analysis references ''An Economic Analysis of Competitive Effects of the Proposed Abitibi-Bowater Merger'' (''White Paper'') and two Supplements to the White Paper, which were provided to the Justice Department during its investigation of the merger. The White Paper and two Supplements, which are attached to the Economic Analysis, address the recent history of anticompetitive conduct by Abitibi and Bowater and explain why a merger of Abitibi and Bowater, if permitted, would lead to a continuation of that anticompetitive conduct. Also cited throughout the Comment are trade press articles relating to post-settlement newsprint capacity removals announced by Abitibi-Bowater and resulting price increases, which are attached to this Comment.[31]

NAA members are the primary victims that the Complaint identifies as suffering competitive injury from the transaction and on whose behalf the Government seeks relief. NAA agrees with the Justice Department that the alleged harm to competition identified in the Complaint is accurate,

North American newsprint capacity of about 11.7 million metric tonnes based on November 2007 newsprint statistics provided by the Pulp and Paper Products Council. In addition to announcing the removal of 600,000 metric tonnes of newsprint capacity from the market, AbitibiBowater also announced the closure of about 400,000 metric tonnes of commercial printing paper capacity.

[23] Most North American newsprint makers join $60/tonne 1Q 2008 hike, 29 Pulp & Paper Week 46 at 2.

[24] 29 Pulp & Paper Week 48 at 1.

[25] Generally, if a merger creates market power resulting in a price increase of 5 percent or more, that price increase is considered to be ''significant.'' In Section 1.11 of its Merger Guidelines, the Justice Department states that in defining the relevant markets affected by a merger in most contexts it ''will use a price increase of five percent lasting for the foreseeable future.'' Horizontal Merger Guidelines at § 1.11. The October 2007 North American newsprint price is from 29 Pulp & Paper Week 45 (Nov. 19, 2007) at 3.

[26] Newsprint giant AbitibiBowater embraces industry leadership, eyes $200/tonne North American newsprint price increase, 29 Pulp & Paper Week 47 at 5.

[27] 29 Pulp & Paper Week 47 at 1.

[28] *Id.* at 1, ''Newsprint prices in Europe were close to $200/tonne higher than in the USA in November.''

[29] 29 Pulp & Paper Week 46 at 1.

[30] See ''An Economic Analysis of the Adequacy of the Snowflake Divestiture in the Settlement of *United States of America* v. *Abitibi-Consolidated, Inc. and Bowater, Incorporated*.''

[31] See Attachment A: Trade Press Articles Relating to Post-Settlement Newsprint Capacity Removals Announced by AbitibiBowater and Resulting Newsprint Price Increases.

demonstrable, and unless adequately remedied, will cause significant economic harm to the U.S. newspaper industry. Indeed, NAA and its members produced documents, economic analyses, and other information to the Justice Department demonstrating the recent anticompetitive pricing and output history of the North American newsprint industry resulting from the joint dominant firm behavior of Abitibi and Bowater and showing how the proposed transaction would permit a merged AbitibiBowater to continue to strategically close capacity to raise newsprint prices well above competitive levels.

But while the Complaint correctly identifies the competitive harm produced by the merger, the remedy in the proposed Final Judgment fails to satisfy even the most deferential standard for Tunney Act review. The Justice Department has not provided the Court with any factual or economic analysis to demonstrate that the proposed remedy will eliminate the incentive to reduce industry capacity and raise prices to North American newsprint customers (the injury charged in the Complaint). Recent events have already proven that the remedy set forth in the proposed Final Judgment is woefully inadequate to prevent the injury charged in the Complaint. Hence, reviewing the remedy ''in relationship to the violations that the United States has alleged in its Complaint,'' [32] and deferring to the Justice Department to whatever extent is required by law, the remedy does not provide any basis to allow the Court to find that it will ameliorate the harm alleged in the Complaint. This is not a case in which there is a debate as to whether the Justice Department inappropriately narrowed the alleged harm. Rather, this is the case in which the economics and recent history of the newsprint industry, along with the Justice Department's conclusions regarding the competitive harm created by the consolidation, compel the conclusion that the remedy is not a ''reasonably adequate remed[y] for the alleged harms.'' [33]

The Proper Standard of Review for the Justice Department's Proposed Remedy for This Merger

''The antitrust laws [* * *] were enacted for the protection of competition, not competitors.'' [34] This means that antitrust remedies are designed to restore competition to the market, not to ensure profits to the competitors in that industry.[35] Since the Supreme Court accepted this notion first proposed by Congress, antitrust law enforcement has been guided by this principle. Since these Supreme Court decisions and Congressional mandates, antitrust law and its regulators have sought to preserve competition ''in the public interest.'' [36] The divestiture of the Snowflake mill is a remedy that fails to preserve competition in the North American newsprint market and is, therefore, not in the public interest.

As is discussed in the attached Economic Analysis, the economic model appropriate to evaluate the current merger as well as prior anticompetitive conduct by Abitibi and Bowater is the dominant firm model.[37] The description of the anticompetitive effects of the merger contained in both the Complaint and the Competitive Impact Statement suggests that the Justice Department applied the dominant firm model in its analysis of the merger.[38] The Merger Guidelines Commentary of the Justice Department and the Federal Trade Commission describes the dominant firm model as follows:

> [The dominant firm] model posits that all competitors but one in an industry act as a ''competitive fringe,'' which can economically satisfy only part of total market demand. The remaining competitor acts as a monopolist with respect to the portion of total industry demand that the competitive fringe does not elect to supply. This model might apply, for example, in a homogeneous product industry in which the fringe competitors are unable to expand output significantly.[39]

In the Competitive Impact Statement, the Justice Department claims that the divestiture of the Snowflake mill will be sufficient to eliminate the incentive for AbitibiBowater to act as a dominant firm.[40] However, the large post-settlement capacity closures accompanied by a large price increase initiated by AbitibiBowater shortly after the Justice Department's settlement demonstrate that AbitibiBowater has the incentive and ability to act as a dominant firm and will likely retain that incentive and ability for future strategic capacity closures.

One consequence of AbitibiBowater's incentive and ability to act as the dominant firm in the North American newsprint market is that the merged firm will likely close at least some capacity that is more efficient than some of the capacity of the fringe firms.[41] The nature of the dominant firm model is that in closing capacity to raise the industry operating rate and newsprint prices, the dominant firm allows the fringe firms to operate at full capacity enjoying the price increasing benefits of AbitibiBowater's dominant firm behavior. Indeed, once they are at full capacity, the fringe firms would have no incentive to do anything other than to follow the price leadership of the dominant firm. Thus, in a declining market, such as the North American newsprint market, it is likely that some inefficient fringe firm capacity is preserved, which, in the absence of dominant firm behavior, would otherwise have to close as the price of newsprint dropped below the cash costs of operating the inefficient fringe capacity.

For instance, Pulp & Paper Week reported that newsprint industry analyst Claudia Shank of JP Morgan believes that AbitibiBowater's announced capacity closures for the first quarter of 2008 ''together with Abitibi-Bowater's

[32] This is the standard the Justice Department claims is ''the Court's role under the APPA.'' Competitive Impact Statement, at Section VII.

[33] This is the standard that the Justice Department contends it must meet for approval of the decree: ''the United States 'need only provide a factual basis for concluding that the settlements are reasonably adequate remedies for the alleged harms.' '' *id.,* citing SBC Commc'ns, 489 F. Supp. 2d at 17.

[34] *Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.,* 429 U.S. 477, 488; 97 S. Ct. 690,712; 50 L. Ed. 2d 701 (1977), citing *Brown Shoe Co.* v. *United States,* 370 U.S. 294, 320 (1962).

[35] See Brunswick, 429 U.S. at 487–88 (In that case, the court would not grant relief to Respondents for profits that the Respondents would have gained had the acquired party exited the industry).

[36] ''In the public interest'' is the standard for entry of proposed Final Judgments under the Tunney Act. 15 U.S.C. § 1 6(e)(1). Congress mandated considerations for determining whether a decree is in the public interest, but never defined the term, ''in the public interest'' itself. NAA believes that it is safe to assume that achieving the goals of the antitrust laws—including preserving competition—is ''in the public interest.''

[37] See Section B.1., ''Unilateral Effects and the Dominant Firm Model,'' and Appendix A, ''Merger Analysis, Unilateral Effects, and the Dominant Firm Model.''

[38] Complaint at ¶ 16–19 and Competitive Impact Statement at pp. 5–6.

[39] Commentary on the Horizontal Merger Guidelines, U.S. Department of Justice and Federal Trade Commission, March 2006 (''Guidelines Commentary''), at p. 25.

[40] Competitive Impact Statement at p. 6.

[41] During the period 2002 to 2006, very little newsprint capacity was removed from the market by fringe firms as Abitibi and Bowater were responsible for the great majority of the North American newsprint capacity closures during this period. See the discussion of Abitibi's and Bowater's prior joint anticompetitive conduct below and in the attached Economic Analysis, Section B.2, ''Abitibi and Bowater Engaged in Joint Dominant Firm Behavior to Raise NA Newsprint Prices Significantly above Competitive Levels 2002 to 2006,'' which also contains references to the relevant portions of the White Paper and the Supplements to the White Paper.

indication that it could cut more capacity in mid-2008, provided second- and third-tier producers some additional 'breathing room' and limit closures from the broader industry before the second half of next year.'' [42] According to RISI economist Kevin Conley, ''[w]ithout AbitibiBowater's bold move [to remove 600,000 metric tonnes of newsprint capacity from the market] operating rates and prices would have continued to languish at low levels until the highest-cost mills could no longer survive, eventually leading to the inevitable closures needed to balance the North American market.'' [43] Even after the competitive ''balancing'' of the North American newsprint market, however, the prevailing newsprint price would be the competitive price, not the much higher anticompetitive prices resulting from AbitibiBowater's current and likely future strategic newsprint capacity closures.

On the other hand, if the Justice Department had successfully blocked this merger, a separate Abitibi and Bowater would likely have considerably less incentive and ability to engage in joint dominant behavior than the current merged AbitibiBowater.[44] The principal effect of the merger is that U.S. newspaper publishers and other North American newsprint customers directly bear the cost of the dominant firm behavior in the form of significantly higher newsprint prices. As a secondary effect of the merger, it is likely some inefficient fringe firm capacity may be preserved by AbitibiBowater's dominant firm behavior. The misallocation of resources that likely results imposes a social cost on the economy that is inconsistent with the goals of the antitrust laws.

The basic premise of the antitrust laws is to protect competition and consumers, not competitors. As interpreted by the courts and by Congress, the antitrust laws are not intended to protect inefficient suppliers to a market. Because the Justice Department is asking the Court to enter a proposed consent decree that would provide no remedy for the customer-victims of AbitibiBowater's dominant firm behavior and that would likely permit the survival of inefficient capacity of fringe firm competitors that would otherwise be forced to close down in a competitive newsprint market, the Justice Department has an obligation to explain the basis for its decision to the Court. By asking the Court to accept with no further analysis or explanation the Department's claim that the Snowflake divestiture will remedy the competitive harms alleged in the Complaint, the Department puts the Court in the position of having no basis upon which to determine if the proposed remedy (a) is adequate to address these competitive problems, (b) is consistent with the Justice Department's own prior positions, or (c) is in accordance with the well established standards of the antitrust laws, all of which are relevant to the determination of ''public interest.''

The Complaint and Competitive Impact Statement Ignore Abitibi's and Bowater's Recent History of Anticompetitive Conduct Prior to Their Merger Announcement

As is discussed above, shortly after Abitibi and Bowater reached their agreement with the Justice Department in October to divest the Snowflake mill and settle the case, the newly merged firm proceeded to announce significant capacity closures and to initiate a substantial price increase. Most other North American newsprint manufacturers quickly matched AbitibiBowater's announced price increase.

During and immediately prior to the period when the merger was being reviewed by the Justice Department,[45] newsprint prices steadily declined from $675 per metric tonne to $560 per metric tonne, a decline of about 17 percent. Also, during this time, Abitibi and Bowater did not take strategic actions to raise the price of newsprint. As discussed immediately below, Abitibi and Bowater had engaged in joint dominant firm behavior to strategically close capacity to raise the price of newsprint well above competitive levels over the period 2002 to 2006. There are two plausible explanations as to why Abitibi and Bowater did not continue their joint dominant firm behavior during and immediately prior to the Department's merger review: (1) Abitibi and Bowater determined, due to the extent of previous capacity closures that occurred between 2002 and 2006, that their ability and incentive to jointly engage in dominant firm behavior had been significantly diminished, thus leading to their decision to merge; and (2) Abitibi and Bowater decided it would be imprudent to attempt to exercise market power during the merger review period as it might adversely affect the outcome of that review.

Between 2002 and 2006, the pricing analysis in the White Paper demonstrates that Abitibi and Bowater jointly acted as a dominant firm, strategically removing newsprint capacity from the market to significantly raise the newsprint industry operating rate, and, thus, increasing the price of newsprint above competitive levels. Due to these strategic capacity closures, the price of newsprint during that period increased by a total of 49 percent despite a steady decline in consumption by North American newsprint customers. The economic White Paper and the two Supplements, presented to the Justice Department during the course of its investigation, extensively document and analyze this joint dominant firm behavior by Abitibi and Bowater.[46] The prior anticompetitive actions of Abitibi and Bowater to close capacity strategically during this four-year period are identical to the anticompetitive strategic behavior alleged in ¶ 2 and ¶ 19 of the Complaint and described on page 6 of the Competitive Impact Statement. Since the Complaint and Competitive Impact Statement contain no references to this prior anticompetitive conduct by Abitibi and Bowater, it is impossible for the Court to determine if and how much of a factor the prior anticompetitive conduct played in the Justice Department's evaluation and settlement of this merger.

Earlier mergers in the North American newsprint industry, especially the Abitibi-Donohue merger in 2000 and the Bowater-Alliance merger in 2001, created both the incentive and ability for Abitibi and Bowater to jointly engage in this anticompetitive conduct. Economic analysis in papers and presentations by representatives of NAA and the U.S. newspaper industry submitted to the Justice Department in 2000 and 2001 forecasted that these two mergers, if not challenged, would have significant anticompetitive results. The Justice Department took no action against either of these two earlier mergers and, as predicted by the economic analyses submitted to the Department, the two mergers enabled Abitibi and Bowater to engage in the anticompetitive conduct that occurred

[42] 29 Pulp & Paper Week 46 at 5.

[43] 29 Pulp & Paper Week 47 at 5.

[44] According to p. 6 of the CIS, ''But for the merger, neither Defendant acting alone would be of sufficient size to profitably increase the price of newsprint by reducing its own output through strategically closing, idling, or converting its capacity.''

[45] Abitibi and Bowater announced their merger on January 29, 2007. Presumably, the Justice Department began their review of the merger shortly after the merger announcement and continued their investigation until the filing of the Complaint, Competitive Impact Statement, and proposed Final Judgment on October 23, 2007.

[46] See Section B.2. of the attached Economic Analysis.

between 2002 and 2006. As a result, U.S. newspapers and other North American newsprint customers incurred significantly higher newsprint prices.

Prior anticompetitive conduct is a highly relevant factor in most merger investigations, according to the Guidelines Commentary:

> Facts showing that rivals in the relevant market have coordinated in the past are probative of whether a market is conducive to coordination. Guidelines § 2.1. Such facts are probative because they demonstrate the feasibility of coordination under past market conditions. Other things being equal, the removal of a firm via merger, in a market in which incumbents already have engaged in coordinated behavior, generally raises the risk that future coordination would be more successful, durable, or complete.[47]

The Complaint, Competitive Impact Statement, and Proposed Final Judgment do not contain any explanation by the Justice Department as to what, if any, consideration was given to the evidence of Abitibi's and Bowater's prior joint anticompetitive conduct. Before determining whether the proposed relief ''is in the public interest,'' the Court is entitled to know whether the Justice Department considered evidence of prior anticompetitive conduct and if not, why not. By failing to provide that evidence in its Court filings, the Justice Department has deprived the Court of information vital to its review of the adequacy of the proposed divestiture.

The Competitive Impact Statement and Proposed Final Judgment Fail To Address the Congressional Mandates of the Tunney Act

As previously noted, the Tunney Act requires that a court determine whether entry of the proposed Final Judgment ''is in the public interest.'' [48] As the Justice Department outlines more thoroughly in its Competitive Impact Statement, the Court is required to consider certain factors in making that determination.[49] Among those considerations mandated by Congress are: (1) ''The competitive impact of such judgment, including * * * anticipated effects of alternative remedies actually considered,'' and (2) the ''impact of entry of such judgment upon competition in the relevant market or markets.'' [50] While evidence of other factors upon which the Court is asked to base its decision are certainly lacking, these two points are noticeably deficient.

The Anticipated Competitive Effects of Alternative Remedies Actually Considered by the Justice Department

The Justice Department lists two alternative remedies to the one it chose: (1) A full trial on the merits, and (2) ''a number of divestiture alternatives.'' [51] After considering other options, the Justice Department ''determined that divestiture of the Snowflake mill, under the circumstances, was the best solution given the size and efficiency of the Snowflake mill.'' [52] Other than noting that Snowflake is ''among the largest and most profitable mills in the United States,'' the Justice Department provided no further explanation for its decision that Snowflake was both a sufficient remedy and the best solution, no detail regarding under what ''circumstances'' this conclusion was reached, and no scale against which it measured Snowflake as the best alternative. The Justice Department leaves the Court entirely in the dark as to what other divestitures it considered and why those were inferior to the divestiture of Snowflake. The Justice Department also failed to note why Snowflake alone—without an additional divestiture—was sufficient. While a detailed rank or scoring of each of the remedies the Justice Department considered may not be necessary, the Justice Department here has left the Court entirely in the dark with absolutely no basis for making a meaningful comparison between a Snowflake-only divestiture and any alternative course of action, including a full trial on the merits.

Critically, the Justice Department also failed to account for the actual ''anticipated effects'' of the alternatives. Determining ''anticipated effects,'' such as whether a transaction will result in one firm having the unilateral power to profitably raise prices or close capacity without being restrained by other competitors in the market, or whether a transaction will result in the market becoming more conducive to competitors coordinating on price, is the essential element of any merger investigation. Yet, here, even though the Court is required to consider it, the Justice Department remains silent. How can the Court determine if the Justice Department chose an acceptable alternative as opposed to one so weak as to provide no meaningful relief? Is the Court expected to take on faith that this alternative is a viable one? The Court is given no support that would assist it in reaching a conclusion that the Justice Department's chosen alternative is in the public interest. If the recent actions by AbitibiBowater are placed on the scale, the Justice Department's silence fails to meet any reasonable burden of proof to establish that its chosen alternative is sufficient to meet the standard that the proposed remedy is ''in the public interest.''

The Impact of the Proposed Final Judgment in the Relevant Market

The divestiture required under the proposed Final Judgment fails to restore the competition lost by the combination of North America's two largest newsprint producers.

The Justice Department has an obligation to explain to the Court why the remedy it proposes restores or preserves competition. The formal policy guidance of the Antitrust Division regarding merger remedies is contained in the Antitrust Division Policy Guide to Merger Remedies.[53] In this policy statement, the Antitrust Division sets forth broad principles that it says guide its decisions to seek remedies to offset potential harms to competition from mergers. A controlling policy principle is that ''restoring competition is the 'key to the whole question of antitrust remedy.' '' [54]

The Horizontal Merger Guidelines ''describe the analytical framework and specific standards normally used by the [Justice Department] in analyzing mergers.'' [55] While the Complaint and Competitive Impact Statement do not directly reference the Guidelines, absent a disclaimer from the Justice Department, the Court can fairly assume the Department followed its own Guidelines in its investigation of this merger.

The Guidelines identify two analytical frameworks for assessing

[47] Guidelines Commentary at p. 22.

[48] 15 U.S.C. § 16(e)(1).

[49] Competitive Impact Statement at VII, citing 15 U.S.C. § 16(e)(1)(A)–(B), *United States* v. *SBC Commc'ns, Inc.*, 489 F. Supp. 2d 1, 11 (D.D.C. 2007).

[50] 15 U.S.C. 16(e)(1)

[51] Competitive Impact Statement at VI.

[52] *Id.*

[53] Antitrust Division Policy Guide to Merger Remedies, U.S. Department of Justice, Antitrust Division, October 2004. Available at *http://www.usdoj.gov/atr/public/guidelines/205108.htm.*

[54] *Id.*, citing *United States* v. *E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 326 (1961). *Ford Motors Co.* v. *United States*, 405 U.S. 562, 573 (1972) (''relief in an antitrust case must be effective to redress the violations and 'to restore competition' * * * '').

[55] 1992 Horizontal Merger Guidelines, U.S. Department of Justice and Federal Trade Commission, Issued April 2, 1992 and revised April 8, 1997 (''Guidelines''). Available at *http://www.usdoj.gov/atr/public/guidelines/hmg.htm.* The Guidelines also say that, ''By stating its policy as simply and clearly as possible, the [Justice Department] hopes to reduce the uncertainty associated with enforcement of the antitrust laws in this area.'' *Id.* The ''unifying theme of the Guidelines,'' like the Merger Remedy Policy noted above, ''is that mergers should not be permitted to create or enhance market power or to facilitate its exercise.'' *Id* at § 0.1.

whether a merger between competing firms may substantially lessen competition. Those frameworks require the Justice Department to ask whether the merger may increase market power by facilitating coordinated interaction among rival firms (''coordinated effects'') and whether the merger may enable the merged firm to raise price unilaterally or otherwise exercise market power (''unilateral effects'').[56] Though the Justice Department provides the Court with no indication of what framework it applied or why, the allegations in the Complaint appear to be consistent with the application of the unilateral effects framework.

A merger may diminish competition because the ''merging firms may find it profitable to alter their behavior unilaterally following the acquisition by elevating price and suppressing output.'' [57] How a merger generates anticompetitive unilateral effects is relatively straightforward: ''The merger provides the merged firm a larger base of sales on which to enjoy the resulting price rise and also eliminates a competitor to which customers otherwise would have diverted their sales.'' [58]

The Complaint states that the combined post-merger share of newsprint held by AbitibiBowater is ''over 40 percent.'' [59] The Complaint also states that ''neither supply responses nor entry will defeat an exercise of market power.'' [60] The Complaint further states that ''[t]he proposed transaction would combine Defendants' large share of newsprint capacity, thereby expanding the quantity of newsprint sales over which the merged firm would benefit from a price increase. This would provide the merged firm with an incentive to close capacity sooner than it otherwise would to raise prices and profit from the higher margins on its remaining capacity.'' [61]

Given these market circumstances, which are highly conducive to the unilateral exercise of market power, the Justice Department fails to explain to the Court why the divestiture of just the Snowflake mill will be sufficient to prevent the merged firm from exercising market power. As noted above, the Snowflake mill represents only 3 percent of North American newsprint capacity. The divestiture of the Snowflake mill would reduce AbitibiBowater's North American newsprint capacity share from about 40 percent to about 37 percent. The Justice Department fails to explain to the Court how reducing AbitibiBowater's capacity share from 40 percent to a slightly smaller share of 37 percent, a difference of 3 percent, will be sufficient to restore the market to competitive conditions. In the absence of a convincing explanation, the Court should reach the conclusion that the Justice Department's assertion that the divestiture of the Snowflake mill will be sufficient to prevent unilateral anticompetitive conduct by AbitibiBowater is simply wrong.

A Previous Application of the Guidelines by the Justice Department to a Comparable Paper Industry Merger Resulted in a Much Larger Divestiture Than the Department Has Proposed for This Merger

In the Justice Department's November 2000 challenge to Georgia-Pacific's proposed acquisition of Fort James Corporation, the two parties were the two largest producers of ''away-from-home'' tissue products. Georgia-Pacific's capacity share of ''away-from-home'' parent tissue rolls was 11 percent and Fort James' capacity share was 25 percent. The combined share of the two companies in the ''away-from-home'' parent tissue roll market would have been 36 percent. The Justice Department challenged the merger using the same basic theory applied here—unilateral effects. The Justice Department's investigation revealed that the industry was operating at nearly full capacity, that the capacity could not be quickly expanded, and that demand for parent rolls was relatively inelastic with respect to price. These factors combined to create the likelihood that, after the merger, Georgia-Pacific would act as a dominant firm by restricting output of parent rolls and thereby forcing up prices for away-from-home tissue products. As a result, the Justice Department settled the case by a consent decree requiring the complete divestiture of Georgia-Pacific's parent tissue roll capacity share of 11 percent.[62]

Nothing in the Competitive Impact Statement for the AbitibiBowater merger explains or even suggests to the Court why a divestiture comparable to that in the Georgia-Pacific/Fort James merger is not required for this merger.[63] AbitibiBowater's post-merger actions have already shown that the divestiture remedy proposed by the Justice Department for this merger will not prevent the exercise of market power.

The Justice Department's action in the Georgia-Pacific/Fort James merger strongly suggests that significantly more capacity needs to be divested by AbitibiBowater to ensure that the merged firm will not have the incentive and ability to unilaterally exercise market power.

Conclusion

U.S. newspaper publishers, the primary victims who will bear the cost of the conduct challenged in the Complaint and the inadequate Snowflake mill divestiture, see the proposed divestiture as ineffective and inadequate. The Justice Department has not provided the Court with sufficient information with which the Court can enter an informed judgment that the remedy proposed by the Justice Department is ''in the public interest.'' Furthermore, events subsequent to the Justice Department's settlement of the Abitibi-Bowater merger have already demonstrated that the proposed Final Judgment does not remedy the public interest harms presented to the Court in the Complaint.

The Court should not enter the proposed Final Judgment. NAA requests that the Court conduct a hearing to determine the amount of divestiture sufficient to prevent the anticompetitive effects that will otherwise result from this merger and the inadequate proposed Final Judgment.

Submitted on behalf of the Newspaper Association of America by Alan L. Marx, King & Ballow, Union Street Plaza 1100, 315 Union Street, Nashville, TN 37201, (615) 259–3456, *amarx@kingballow.com*. January 2, 2008.

[56] Guidelines Commentary at p. 17.

[57] Merger Guidelines at § 2.2.

[58] Merger Guidelines at § 2.22.

[59] Complaint at ¶ 16.

[60] Complaint at ¶ 20–26.

[61] Complaint at ¶ 19.

[62] *See* Competitive Impact Statement describing DOJ's Complaint and settlement of the proposed Georgia-Pacific/Fort James merger at pp. 8–10. For copies of the DOJ's Complaint and Competitive Impact Statement in this matter see the Justice Department Web site at *http://www.usdoj.gov/atr/cases/indx276.htm.*

[63] The complete divestiture of Georgia-Pacific's pre-acquisition capacity share reduced Georgia-Pacific's post-acquisition parent tissue roll capacity share to 25 percent. With respect to the Abitibi-Bowater merger, a comparable divestiture would reduce the combined pre-merger newsprint capacity share of ''over 40 percent'' to 25 percent.

Attachment A—Trade Press Articles Relating to Post-Settlement Newsprint Capacity Removals Announced by AbitibiBowater and Resulting Newsprint Price Increases

Pulp & Paper Week

Dec. 3, 2007 | Vol. 29, No. 46

AbitibiBowater Plans to Shut Down One Million Tonnes/yr of Capacity in 1Q; Expects More Closures Could Follow in 2Q

AbitibiBowater unveiled the first phase of its long-awaited post-merger rationalization plan and announced the closure of four money-losing mills in Canada in the first quarter 2008. A total of 600,000 tonnes/yr of newsprint capacity and 400,000 tonnes/yr of commercial printing papers will be removed.

AbitibiBowater said more mills could close in Canada later next year, and added that it wanted to reopen its Canadian union contracts to ''explore ways to reduce overall labor costs and provide enhanced flexibility in the workplace.'' Salaried employees would also be asked to take cuts.

Under what it called ''phase one of an action plan to address company challenges,'' AbitibiBowater will permanently close its Belgo mill in Shawinigan, QC, and Dalhousie, NB, mill, and indefinitely idle its Donnacona, QC, and Mackenzie, BC, paper mills.

Additionally, the company will permanently close its previously idled Fort William mill in Thunder Bay, ON, and Lufkin, TX, paper mills, as well as paper machine 3 at its Gatineau, QC, mill. The previously idled operations run total capacity of about 650,000 tonnes/yr.

Execution is key. ''(AbitibiBowater) has done what I expect them to do and be really aggressive, but the issue is going to be execution,'' said one newsprint buyer contact with a major U.S. publishing group. ''It is going to be impossible to take out 600,000 tonnes on Jan 1 and people will be looking to see how much comes out in February and March. That will be the test.''

The reaction from Wall Street analysts was broadly favorable. Citibank analyst Chip Dillon said the newsprint capacity reduction figure was double his expectations. JPMorgan's Claudia Shank said that while she believes another 300,000 tonnes/yr would need to come out next year, the closures, together with AbitibiBowater's indication that it could cut more capacity in mid 2008, provided second- and third-tier producers some additional ''breathing room'' and limit closures from the broader industry before the second half of next year.

''AbitibiBowater will probably say 'We've done our part' to get ahead of the curve and gain momentum on the pricing front,'' an analyst in Canada said. ''But the market is looking for a million tonnes (of newsprint reductions) year-over-year so more capacity will have to be taken out if the market is going to be in balance in 2008.''

While AbitibiBowater did not disclose the number of jobs that would be lost by its restructuring, the Communication, Energy and Paperworkers Union of Canada (CEP) estimated at least 1,000 workers could be eliminated in Canada.

CEP wants forestry ''summit.'' The CEP called for an emergency summit of union and industry leaders in the forestry sector.

''Today's 1,000 or more victims in the mills in Dalhousie, Shawinigan, Donnacona, and Mackenzie bring the job losses in the sector to over 20,000 in the past two to three years,'' said CEP pres Dave Coles.

AbitibiBowater pres/CEO David Paterson said management had been very transparent with employees about their mills.

Under phase two of the plan, which starts immediately, AbitibiBowater will continue reviewing all operations.

More Canadian mills at risk. Company chmn John Weaver said several mills in eastern Canada were under particular pressure from high fiber, energy, and labor costs, and the company planned to involve government, communities, and labor to make the mills competitive at dollar parity. Decisions would be taken in the second quarter of 2008 and closures could start by mid-2008, he said.

AbitibiBowater has increased its merger synergies target to $350 million from $250 million. It is also targeting another $500 million in asset sales, which could include overseas mills, non-core facilities, U.S. timberlands, and its Snowflake, AZ, newsprint mill, which it agreed to divest in return for U.S. Dept of Justice approval of the Abitibi-Consolidated/Bowater merger.

Proceeds from the sales will go towards the company's three-year, $1-billion debt-reduction target.

• Citing rising costs and ''difficuit market conditions,'' AbitibiBowater told customers that it would increase prices on its AbiBow high-bright product line by $65/ton effective Jan. 1. The increase applies to all basis weights, calipers, and finishes of Book, Book Cream, Select, Sert, and Form products. Separately, Blue Heron announced a $35/tonne ($31.75/ton) high-bright increase for its reBrite product range, also effective Jan. 1.

Newsprint

Most North American Newsprint Makers Join $60/Tonne 1Q 2008 Hike

U.S. daily newspaper publishers face a New Year's perfect storm, with producers who account for more than 80% of North American production slating $60/tonne first quarter price hikes and AbitibiBowater closing 600,000 tonnes/yr of newsprint capacity, contacts said last week.

The price increases will be phased in monthly increments of $20/tonne in January, February and March.

AbitibiBowater, which with 5.7 million tonnes/yr of capacity accounts for about 45% of all North American newsprint production, initiated the hike.

Among companies that contacts said would keep prices consistent with AbitibiBowater are White Birch, Kruger, SP Newsprint, Catalyst, Tembec, and Blue Heron. Other producers are still considering a price hike, contacts said last week.

In addition to the 1Q 2008 hike almost all North American newsprint producers will seek this month to implement a $25/tonne fall increase that many producers have been trying to apply since September.

Publishers start to panic. ''There is a general panic in the market right now. Supply has tightened up and (producers) are really pushing this December hike. I'm sure there are (publishers) who have been particularly aggressive in the past that are going to get stuck and be told to pay or buy somewhere else,'' said one publisher contact.

One contact with a large supplier said the $25 hike had managed to gain traction in November. ''Things happened in the back half of the month'' buying sources conceded, saying that newsprint producers did have the strength to move November's price ''a little bit.''

Pulp & Paper Week's November Price Watch had showed newsprint prices on U.S. East and West coasts holding flat at $560/tonne.

Suppliers are in dire need for higher prices given the current 10.4% year-to-date decline in North American demand, strong Canadian dollar and high input costs.

''I've never before seen such a confluence of bad things on this side of the business. To save a dollar on production is a Herculean task,'' said one producer contact in Canada.

Sign of modest improvement. According to the latest Pulp and Paper Products Council data, the North American supply-demand balance improved modestly in October, with production falling almost in line with overall demand.

The biggest barometer for newsprint consumption, the U.S. dailies, showed an 11.4% fall. But adjusting for four Sundays in October 2007 compared with five in October last year, the decline was closer to 7–8%.

More significantly, overall inventories fell to 1.13 million tonnes, their lowest level since December 1979, after a two-month 242,000 tonnes or 18% plunge. Exports rose 29.0% in October, but those extra 49,000 tonnes were more than offset by a 69,000 tonnes drop in domestic shipments.

Gloomy economic outlook. With the economy sagging and the outlook for newspaper advertising looking increasingly gloomy, contacts say capacity cuts remain the only answer if mills are going achieve the 95% operating rates that historically lead to higher prices.

RISI economists say that despite higher exports, North American mills will have to shut 800,000 tonnes/yr of capacity by the end of next year (relative to third quarter 2007) if they are to push operating rates above the 95% mark in 2008.

• With plans to eliminate 38,000 tonnes of newsprint production, Catalyst Paper last week extended the shutdown of PM 1 at its Elk Falls newsprint mill in Campbell River, BC, and keep the PM down for the entire first quarter because of a shortage of fiber. PM 1 was shut in September due to a fiber shortage. The company said the mill has been hurt by a coastal fiber strike that recently ended and a weak U.S. lumber market, Canadian Press said. In addition, the mill's kraft pulp line and white-top linerboard PM will also shut 18 days between Dec. 16 and Jan. 2—and could be shut for longer periods depending on fiber availability. PMs 2 and 5 will be shut Dec. 23, and restart Jan. 2 and Jan. 6, respectively.

• Japan's Oji Paper plans to hike the price of newsprint exports by $50/tonne effective with December orders, citing higher energy and raw material prices that will add $460 million to its costs in the current financial year. The company will also hike the price of other export grades, ranging from $30/tonne for coated and uncoated products to $80/tonne for kraft paper.

• Germany's Palm Paper received planning permission to construct a 400,000 tonnes/yr recycled newsprint mill at King's Lynn in eastern England, which would expand Palm's UK production to 550,000 tonnes/yr. Ecco Newsprint, which has plans for a recycled mill of its own at Middlesbrough in the north of the country, also has planning permission but has not yet begun construction. The UK currently imports about 1.2m tonnes of newsprint and exports 1.5m tonnes of waste paper annually.

BILLING CODE 4410–11–M

NEWSPRINT STATISTICS -- OCTOBER 2007

(000 tonnes)

	Current month		Year-to-date	
NORTH AMERICA	2007	% chg. 2007/06	2007	% chg. 2007/06
Operating rate, %	92	91	94	94[1]
Shipments to North America	740	–8.4	7,233	–9.8
Shipments to USA	651	–8.8	6,383	–10.4
Shipments to Canada	90	–5.5	851	–5.4
Overseas exports	220	29.0	2,039	11.9
Imports	6	–43.5	67	–47.1
Total demand	747	–8.9	7,300	–10.4
Mill inventories	391	6.5	—	—
All US users inventories	740	–15.9	—	—
Days of supply -- All US users	34	–8.1	—	—

1. Actual figure, not a percentage change. e=estimate. p=preliminary.
Source: Pulp and Paper Products Council.

US DAILY NEWSPAPER CONSUMPTION, INVENTORY

	Current month			
	2007	% chg. 2007/06	YTD 2007	% chg. 2007/06
US dailies consumption	547	–11.4	5,246	–10.1
US publisher inventories	655	–15.0	—	—
Days of supply - US dailies	36	–2.7	—	—

Source: Newspaper Assn of America.

BILLING CODE 4410–11–C

Dec. 10, 2007 | Vol. 29, No. 47

Newsprint Giant AbitibiBowater Embraces Industry Leadership, Eyes $200/Tonne North American Newsprint Price Increase

Any doubts about AbitibiBowater's determination to regain profitability and retire a billion dollars in debt within three years were dispelled last week when pres/CEO David Paterson told analysts at the Citi Investment Research Basic Materials Symposium: ''Our need is to leverage the North American (newsprint) price up to the price in Europe and not the other way around.''

Newsprint prices in Europe were close to $200/tonne higher than in the USA in November.

AbitibiBowater, the worlds largest newsprint maker, accounts for about 45% of all North American newsprint production capacity.

Paterson said the company's $25/tonne fall price increase was in place, and he anticipated that the company's recently announced $60/tonne first quarter hike would be implemented entirely.

A presentation slide showed the effect of a $25/tonne increase was an additional $126.8 million in operating income.

The benefit to AbitibiBowater's bottom line from shuttering loss-making Canadian newsprint capacity was explained by CFO William Harvey, who said production costs for the entire 600,000 tonnes/yr slated for closure were $60/tonne higher than the company average.

Most North American producers expect the closures to save the struggling North American newsprint industry, and have joined AbitibiBowater's call for a $60/tonne increase in the first quarter of 2008 implemented in three $20/tonne monthly increments.

Upward price pressure. ''AbitibiBowater's capacity closures will obviously provide the upward pressure for an extended price recovery in 2008, as operating rates soar past the magic 95% threshold generally needed for prices to rise,'' said senior RISI economist Kevin Conley. ''Without AbitibiBowater's bold move, operating rates and prices would have continued to languish at low levels until the highest-cost mills could no longer survive, eventually leading to the inevitable closures needed to balance the North American market.''

European producers are also addressing overcapacity, and Europe's largest newsprint producer, Norske Skog, said that it would decide by Feb. 7 how to permanently close 300,000–400,000 tonnes/yr of newsprint capacity.

''We now see 1.4 to 1.5 million tonnes of announced capacity removals in Europe and North America in just the past 10 weeks,'' said Citi analyst Chip Dillon, who told investors in a research note that he expected a recovery in U.S. newsprint prices to close almost all of the gap with European prices over the next 12–18 months.

Dismaying prospect for publishers. What a $60/tonne hike and imminent closure of 5% of North American newsprint capacity portends for U.S. daily newspapers had publishers shaking their heads.

''There is a sense of inevitability that seems to be recognized by most on the publishing side. There's a sense of resignation in their voices that hasn't been there before,'' said one contact with a major metropolitan daily.

''It's a very different world from just a month ago. We certainly did not have these kind of increases in our plans for 2008, so if they are implemented we would have to find ways to use less newsprint,'' said another contact with a major publishing group.

Newspaper publishers have their own business issues which have largely brought about the decline in North American newsprint demand to under nine million tonnes in 2007, from a peak of slightly more than 13 million tonnes in 1999 and more than ten million tonnes as recently as 2005.

Only 2.9% of the 11.4% drop in North American newsprint demand this year is due to lighter basis weights and reduced web widths, according to the Pulp and Paper Products Council. Of the rest, 2.2% is attributed to falling circulation and 6.3% to lost advertising. The bulk of the lost advertising is in real estate and automotive sectors, neither of which show signs of a rebound anytime soon.

2008 a challenging year. ''From a fiscal standpoint 2008 will be a challenging year almost without precedent for publishers. It's an alignment of circumstances and realities that none of us have ever seen before,'' said one publishing source.

But while the domestic market for newsprint is undeniably shrinking, the global market is still growing. Industry consultant Dave Allan told RISI's 2nd annual Latin American Pulp & Paper Outlook Conference in Sao Paulo, Brazil, last week that world demand showed flat growth in 2007 only because of North America's 10% plunge.

Allan said he expected North American demand decline would slow to 2.5% by the end of 2008, and that global demand would see a 2%/yr upturn and grow at close to 1.0 million tonnes/yr in 2008 and 2009.

AbitibiBowater, which like some other North American producers is growing its overseas exports, sees its key destinations as Europe, Latin America and the Middle East and India. Chmn John Weaver said last week that because the company's Canadian export mills were located on ocean ports, the cost of bulk shipments to Europe were comparable with shipments to North American destinations.

• Members of Canada's largest pulp and paper union, the Communications, Energy & Paperworkers union (CEP) want to go to the bargaining table a year earlier than scheduled to tackle the issue of mill closures and job losses. The measure was adopted last week by delegates representing AbitibiBowater paper workers and will go to a conference of eastern Canada union Locals early next year. The CEP opposes reopening negotiated contracts to cut wages and benefits but says there are ways the union could help cut costs that do not involve concessions.

Dec. 17, 2007\Vol. 29, No. 48

Publisher Resistance to $25/Tonne North American Newsprint Increase Collapses; Producers Looking To Fast Track Recovery

Trenchant publisher resistance to a $25/tonne fall newsprint price increase that persisted as late as mid-November vanished toward the end of the month, and the hike went in ''like a hot knife through butter'' in December, sources said last week.

Contacts said the market was tightening and order books filling up due to some newspaper buyers trying to stock up ahead of next year's fresh round of price increases and some commercial printers switching to newsprint because of a shortage of specialty grades.

The price of 30-lb standard newsprint on the U.S. East and West Coasts increased to $585/tonne this month, up $15 from a revised $570/tonne in November, according to Pulp & Paper Week. The revised November level represented a $10/tonne increase. The price of 27.7 lb newsprint was $625/tonne in December, up from $610/tonne in November.

Newspaper publishers' rapid change of heart came after the combination of AbitibiBowater's larger than expected 600,000 tonnes/yr of newsprint capacity cuts along with a $60/tonne first quarter price increase, contacts said. Analysts believe the closures remove sufficient newsprint capacity to match North American market demand—at least temporarily—in the first quarter.

70% 1Q price recovery? AbitibiBowater accounts for about 45% of all North American newsprint capacity, and producers that account for almost all the rest also announced $60/tonne hikes. If these are successfully implemented, by the end of March suppliers will have recovered $85 of the past year's $115/tonne price drop.

''You've got to take your hat off to this guy. He's determined to show value to his shareholders and gained the upper hand very quickly, while we are going to be fighting for our lives,'' remarked one publisher contact, referring to AbitibiBowater CEO David Paterson.

Both buyers and sellers expected that 2008 would bring higher newsprint prices and many contacts believed suppliers would seek a second price hike later in the year.

Three years of increases? ''If you are not building 10% price increases into your budget for the next three years you are foolish. Suppliers are pretty cocky right now and there's no sympathy for publishers,'' commented a buyer contact with a major U.S. newspaper group.

''I think what is going to drive (AbitibiBowater's) decisions is their income statements and balance sheets, and I think they would tell you they have been too deferential to their customers historically—to their own detriment,'' said one contact.

''There's 800,000 tonnes compared to 2007 that will be closed and I'd say the odds are 50–50 or better that we will get north of $700/tonne in 2008, because even with a $150 increase Canadian mills are not going to make money with the dollar at parity,'' said a producer contact in Canada.

Consumption will be key. ''When you start hearing big numbers thrown out, there is a tendency by some publishers to panic, but my concerns are how many tonnes are really coming out and will consumption continue to fall at the same rate we have seen this past year,'' said one big U.S. newsprint buyer. ''Seeing a company like Kruger that rarely takes downtime closing 100,000 tonnes will curl your toes, but how much consumption is going to fall is more important from my point of view.''

Publishers in Canada would be hurt less by higher newsprint prices because the stronger Canadian dollar has shrunk their newsprint costs to the lowest level in almost two decades.

''AbitibiBowater has shown what should be done to get the price up to a level where they can make a dollar or two, but at the same time I don't think U.S. publishers can afford to pay the price,'' said a contact with a major Canadian publisher. ''I am pretty sure they will cut the size (of U.S. newspapers) and at the end of the day demand is going to go down big time—another million tonnes I'm sure.''

Dailies will shrink page size. Supplier sources also said they anticipated consumption cutbacks, but said that given the 6% demand drop in 2006 and near 11% drop in 2007, producers would have difficulty increasing conservation significantly in the first quarter.

''I think it's a given that everybody will go to 44-in. webs as quickly as they can, cut out what they can from editorial, and make the standard U.S. newspaper page 11 inches. That will cut demand 6–8%,'' said one supplier contact.

Still, AbitibiBowater has said it is ready to shutter more mills in eastern Canada if they cannot be made competitive.

''Their goal is to align capacity with demand, and whatever that entails in terms of demand decline they are committed to matching that,'' noted one U.S. publisher source.

But although suppliers are desperate to push prices higher, some producers are wary of them going too high.

AbitibiBowater's weight and the world. ''There has to be an upper limit. At $550/tonne, or even $600 or $625, we don't have any issues with imports. But at $675, $700, or $725 we will see Chinese tonnes here. It's one thing for AbitibiBowater to carry the North American market on its back, but it's another to carry the whole world,'' remarked one producer contact in Canada.

• Europe's Holman Paper intends to close 150,000 tonnes/yr. of standard newsprint capacity at its 795,000 tonnes/yr. Hallsta mill at Hallstavik, Sweden.

• Norway's Norske Skog, the world's second-largest newsprint producer behind AbitibiBowater, may spin off its Asian operations. The company said it has been looking into a separate stock market listing for its South Korean, Chinese, and Thai mills, which run capacity of 1.6 million tonnes/yr. or a quarter of the company's total. Some of Norske's investors want the company to sell its Asian operations to reduce debt, but Norske has ruled out selling the mills outright, saying the price would not reflect their value in a market currently suffering from significant overcapacity, according to a Financial Times report.

Economists Incorporated

An Economic Analysis of the Adequacy of the Snowflake Divestiture in the Settlement of United States of America v. *Abitibi-Consolidated, Inc. and Bowater, Incorporated*

Submitted on Behalf of the NAA

John H. Preston, Kent W. Mikkelsen, PhD, Economists Incorporated, Washington, DC. January 2, 2008.

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Appendix A—Merger Analysis, Unilateral Effects, and the Dominant Firm Model

Attachments

Attachment A Curricula Vitae of John H. Preston and Kent W. Mikkelsen, Ph.D.

Attachment B White Paper by Economists Incorporated, Submitted on Behalf of the NAA to DOJ on April 11, 2007

Attachment C Supplement 1 to the White Paper by Economists Incorporated, Submitted on Behalf of the NAA to DOJ on July 9, 2007

Attachment D Supplement 2 to the White Paper by Economists Incorporated, Submitted on Behalf of the NAA to DOJ on July 20, 2007

A. Introduction

On January 29, 2007, Abitibi-Consolidated, Inc. (''Abitibi'') and Bowater Incorporated (''Bowater'') announced that they had reached an agreement to merge the two companies.[1] Following an investigation of the merger, the U.S. Department of Justice (''DOJ'') filed a civil antitrust complaint (''Complaint'') with the United States District Court for the District of Columbia (''Court'') on October 23, 2007 seeking to enjoin the merger.[2] Paragraphs 2, 3 and 19 of the Complaint explain why DOJ was challenging the proposed merger.

2. Abitibi and Bowater are the two largest newsprint producers in North America. The combination of these two firms will create a newsprint producer three times larger than the next largest North American newsprint producer. After the merger, the combined firm will have the incentive and ability to withdraw capacity and raise newsprint prices in the North American newsprint market.

3. Unless the proposed transaction is enjoined, Defendants' merger will substantially lessen competition in the production and sale of newsprint, in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18.

19. The proposed transaction would combine Defendants' large share of newsprint capacity, thereby expanding the quantity of newsprint sales over which the merged firm would benefit from a price increase. This would provide the merged firm with an incentive to close capacity sooner than it otherwise would to raise prices and profit from the higher margins on its remaining capacity.

At the same time the Complaint was filed, DOJ also filed a proposed Final Judgment (''PFJ'') which, if approved by the Court, would settle DOJ's case against defendants Abitibi and Bowater. As a condition of the settlement, the defendants are required to sell Abitibi's Snowflake, Arizona newsprint mill (''Snowflake mill'') to an acquirer acceptable to DOJ.[3] Following the filing of the Complaint and PFJ, Abitibi and Bowater completed their merger on October 29, 2007.[4] The newly merged company is named AbitibiBowater.

Prior to the completion of the merger, Abitibi's share of North American (''NA'') newsprint capacity was about 25 percent and Bowater's share was about 16 percent.[5] According to the Complaint, the post-merger share of the combined company would be ''over 40 percent.'' The NA newsprint capacity share of the Snowflake mill is about 3 percent.[6] Thus, the divestiture of the Snowflake mill would reduce the combined NA newsprint capacity share of the merged firm from about 40 percent to about 37 percent.

In its Competitive Impact Statement (''CIS''),[7] DOJ explains why it believes the divestiture of the Snowflake mill will be an adequate remedy to prevent anticompetitive conduct by the merged firm.

The combination enhances Defendants' incentives to exercise market power because the merged firm will control a greater base of capacity over which the merged firm would benefit from an increase in newsprint prices after strategically closing, idling, or converting some of its capacity. Without Snowflake's capacity, the merged firm would not be of sufficient size to be able to recoup the losses from such strategic closures through increases in prices on its remaining newsprint production. The divestiture of Snowflake would adequately address the likelihood that the proposed merger substantially would reduce competition for newsprint in the United States.[8]

It is evident that DOJ has concluded that with a capacity share of about 40 percent, the merged firm would have the incentive and ability to unilaterally engage in anticompetitive conduct to raise the price of newsprint but that with a slightly smaller capacity share, about 37 percent, the merged firm would lose that incentive and ability. DOJ provides no information or analysis in the CIS or any other document it filed with the Court to support this claim.

We have been asked by the Newspaper Association of America (''NAA'') and its attorneys to provide an economic antitrust analysis of the Snowflake divestiture to determine whether that divestiture will likely be sufficient to eliminate the anticompetitive effects that would otherwise result from the

[1] At the time of the merger announcement, newsprint accounted for about 48 percent of the value of the combined sales of the two companies. Other products produced by the two companies include coated papers, uncoated papers, market pulp and wood products. Source: The presentation accompanying the merger announcement, ''AbitibiBowater: Creating a Global Leader in Paper and Forest Products,'' January 29, 2007, page 10.

[2] The Complaint is captioned *United States of America* v. *Abitibi-Consolidated, Inc. and Bowater, Incorporated*.

[3] See the PFJ, Section IV.A.

[4] AbitibiBowater press release, October 29, 2007.

[5] See the Complaint, paragraph 16.

[6] The annual newsprint capacity of the Snowflake mill is 375,000 metric tonnes, according to page 2 of the CIS. However, none of the documents filed by DOJ with the court in this case provides the NA newsprint capacity share of the Snowflake mill nor the amount of total NA newsprint capacity that would be necessary to calculate that share. Based on total NA newsprint production and operating rates for November 2007, current total annual NA newsprint capacity is about 11.7 million metric tonnes, which would give the Snowflake mill a NA newsprint capacity share of about 3 percent. Source: The November 2007 North American Newsprint Flash Report (''Flash Report''), published by the Pulp and Paper Products Council (''PPPC''). The members of the PPPC are NA pulp and paper manufacturers, including most if not all NA newsprint manufacturers.

[7] The CIS was also filed with the Court on October 23, 2007.

[8] See the CIS, page 6. The CIS does not specifically define the terms ''strategically closing, idling, or converting some of its capacity'' or ''strategic [capacity] closures.'' However from the context of the paragraph on page 6 of the CIS quoted above, it is evident that a newsprint manufacturer with a relatively large capacity share will, acting by itself, have the incentive and ability to ''strategically'' close capacity if the newsprint manufacturer expects to recoup the losses from the capacity closure through increases in prices on the manufacturer's remaining newsprint production. The larger the newsprint manufacturer's capacity share, the more likely the manufacturer will have the incentive and ability to engage in such unilateral strategic behavior. Newsprint manufacturers with relatively small capacity shares will likely have neither the incentive nor ability to strategically close capacity.

merger. The purpose of this analysis [9] is to assist the Court in its evaluation of the adequacy of the Snowflake divestiture under the Antitrust Procedures and Penalties Act (known as the ''Tunney Act''). During the course of DOJ's investigation of the proposed merger of Abitibi and Bowater, we also submitted to DOJ an economic White Paper and two Supplements to the White Paper on behalf of the NAA. These submissions to DOJ are attached to this analysis.[10]

The NAA is an association whose membership includes newspaper chains of all sizes and independent, small market, and family-owned newspaper publishers. The NAA is headquartered in Arlington, Virginia. NAA members account for nearly 90 percent of the daily newspaper circulation in the U.S.[11] U.S. daily newspapers are the primary purchasers of newsprint produced by NA newsprint mills accounting for about 80 percent of the newsprint consumed in the U.S. and about 70 percent of the newsprint consumed in NA.[12] If the divestiture of the Snowflake mill proves to be inadequate to eliminate the anticompetitive effects of the merger in the NA newsprint market, NAA member newspapers and other purchasers of newsprint in NA will bear the cost of that inadequacy in terms of higher newsprint prices.

As discussed in more detail below, less than six weeks after its agreement to divest the Snowflake mill, AbitibiBowater announced plans to remove a large amount of capacity from the newsprint market and, at about the same time, initiated a significant newsprint price increase. Additional AbitibiBowater capacity closures leading to further price increases appear likely in 2008. The CIS claims that ''[w]ithout Snowflake's capacity, the merged firm would not be of sufficient size to be able to recoup the losses from such strategic closures through increases in prices on its remaining newsprint production.'' [13] This recent unilateral price-increasing action by AbitibiBowater shows that DOJ has seriously misjudged the incentive and ability of the merged firm to engage in strategic behavior to raise the industry operating rate and the price of newsprint. This misjudgment will likely cost U.S. newspapers and other U.S. newsprint customers billions of dollars in coming years.

Even without this recent price-increasing action by AbitibiBowater, there already existed substantial evidence that the merger would likely provide AbitibiBowater with significant market power and that the divestiture of just the Snowflake mill would be unlikely to prevent AbitibiBowater from exercising that market power. As documented and analyzed in the White Paper and in Supplement 1 to the White Paper, Abitibi and Bowater jointly acted as a dominant firm over the period 2002 to 2006 to strategically remove newsprint capacity from the market to raise the price of newsprint, the same type of anticompetitive strategic behavior alleged in Paragraphs 2 and 19 of the Complaint and described on page 6 of the CIS. Neither the Complaint nor the CIS, however, mentions this prior anticompetitive behavior. In our opinion, a history of prior anticompetitive conduct in the market affected by a merger is relevant to merger analysis in two main respects: (1) It provides both support and a justification for the filing of the Complaint; and (2) in cases that are settled with a consent decree, it allows the Court and other interested parties to more accurately evaluate the adequacy of a proposed remedy. By failing to mention the prior anticompetitive conduct of Abitibi and Bowater in the North American newsprint market, DOJ has deprived the Court of information highly relevant to an evaluation of the adequacy of the Snowflake divestiture.

The Complaint and CIS also ignore the significant decline in newsprint prices during the period the proposed merger was under review by DOJ, a period of approximately 9 months. Abitibi and Bowater did not engage in strategic behavior during this period or in the months leading up to their merger announcement. It is plausible that Abitibi and Bowater suspended their strategic capacity closures to maximize the likelihood of a favorable merger review by avoiding conduct that DOJ would likely find anticompetitive. It is also plausible that the incentive and ability of AbitibiBowater to jointly engage in strategic behavior had been significantly weakened by previous capacity closures over the period 2002 to 2006, which led to the decision to merge. The decline in newsprint prices during the merger review period is also information highly relevant to an evaluation of the Snowflake divestiture, information which DOJ did not provide in any of the documents it filed with the Court.

To summarize, from 2002 to 2006, Abitibi and Bowater jointly engaged in strategic dominant firm behavior causing newsprint prices to rise significantly above competitive levels. During DOJ's review of the proposed merger, Abitibi and Bowater suspended their joint strategic dominant firm behavior and, as a result, newsprint prices declined significantly. Shortly after Abitibi and Bowater agreed to divest the Snowflake mill, the newly merged AbitibiBowater resumed the dominant firm behavior by announcing significant newsprint capacity closures and initiating significant newsprint price increases. This resumption of strategic dominant firm behavior was made possible by the merger and was not deterred by the Snowflake divestiture.

B. Economic Analysis

1. Unilateral Effects and the Dominant Firm Model

The type of anticompetitive effect alleged in Paragraphs 2 and 19 of the Complaint and described on page 6 of the CIS is called a ''unilateral effect.'' That is, a unilateral effect results if the merger provides the merged firm with the incentive and ability to unilaterally engage in anticompetitive conduct without the need to coordinate with non-merging firms in the market.

A dominant firm model is a model of unilateral conduct often applied in circumstances where the product is relatively homogeneous and where there is a single dominant firm with a relatively large capacity share and a ''competitive fringe'' consisting of a number of firms with relatively small capacity shares. These characteristics apply to the newsprint industry.

While we have no direct knowledge of the model or models used by DOJ to analyze the competitive effects of the proposed merger of Abitibi and Bowater, the allegations in Paragraphs 2 and 19 of the Complaint and described on page 6 of the CIS are consistent with an application of the dominant firm model. See Appendix A below for additional discussion of merger analysis, unilateral effects, and the dominant firm model.

The method by which AbitibiBowater could unilaterally raise newsprint prices is straightforward. In the newsprint industry, newsprint prices increase at industry operating rates of about 95 percent and above. At industry operating rates below 95 percent, newsprint prices are likely to remain constant or decline.[14] If there is a significant amount of excess capacity, as has recently been the case in the newsprint industry, then newsprint prices are unlikely to increase unless enough capacity is removed from the market to raise the operating rate above 95 percent. Newsprint customers are beneficiaries of the lower prices that result from the excess capacity.

A firm with a sufficiently large capacity share would have the incentive and ability to unilaterally remove capacity from the market to raise the price of newsprint if the increased profit from the price increase on its remaining capacity exceeds the loss in profit from the closed capacity. DOJ's Complaint and CIS are evidently based on the theory that a merger creating a firm with about a 40

[9] The authors of this analysis, John H. Preston and Dr. Kent W. Mikkelsen, are both Senior Vice Presidents at Economists Incorporated, an economic consulting firm headquartered in Washington, DC and specializing in the economic analysis of antitrust and regulation matters for over 25 years. Many economists at Economists Incorporated, including Mr. Preston and Dr. Mikkelsen, worked at DOJ as economists before joining Economists Incorporated. The curricula vitae of Mr. Preston and Dr. Mikkelsen are attached to this analysis as Attachment A.

[10] The White Paper and the two Supplements to the White Paper are attached to this analysis as Attachment B (''White Paper,'' submitted to DOJ on April 11, 2007), Attachment C (''Supplement 1,'' submitted to DOJ on July 9, 2007), and Attachment D (''Supplement 2,'' submitted to DOJ on July 20, 2007.) The White Paper is titled ''An Economic Analysis of the Competitive Effects of the Proposed Abitibi-Bowater Merger,'' Supplement 1 to the White Paper is titled ''Response to Issues Raised at Our Meeting With the DOJ Staff on April 20, 2007,'' and Supplement 2 is titled ''Revision to the July 9, 2007 Response.'' In addition, we met with the DOJ staff on four occasions and participated in a number of conference calls with the DOJ staff, including calls with newsprint buyers for newspapers, to discuss the competitive issues raised by the proposed merger.

[11] Source: NAA Web site.

[12] Source: November 2007 Flash Report. Newsprint is also used in the printing of nondaily newspapers and certain advertising materials such as newspaper inserts and grocery store flyers.

[13] See the CIS, p. 6.

[14] See the White Paper, Section F, pages 83 to 87, and Section 11, pages 94–105, for a discussion and analysis of the relationship between the newsprint operating rate and the price of newsprint.

percent newsprint capacity share would enable that firm to profitably remove capacity from the market in order to raise the industry operating rate to a high enough level to also raise the price of newsprint.

2. Abitibi and Bowater Engaged in Joint Dominant Firm Behavior to Raise NA Newsprint Prices Significantly above Competitive Levels 2002 to 2006

An argument that the merger will provide AbitibiBowater with the incentive and ability to strategically close capacity to raise the price of newsprint is not based solely on a theoretical model. The White Paper and Supplement 1 to the White Paper submitted to DOJ document and analyze prior anticompetitive conduct of Abitibi and Bowater that occurred between the third quarter of 2002 and the third quarter of 2006. See the following sections of the White Paper for this analysis:

Section F: Evidence from Presentations to Investment Analysts and Other Public Information That Abitibi and Bowater Have Used Their Control Over Newsprint Capacity and the Newsprint Industry Operating Rate to Significantly Raise the Price of Newsprint 2002 to 2006 (pp. 73–87)

Section G: An Analysis of Permanent Newsprint Capacity Reductions Between 2002 and 2006 (pp. 88–93)

Section H: Four Articles by Two Newsprint Industry Experts Describing the Abitibi-Bowater Strategy to Raise Prices by Closing Capacity (pp. 94–105)

See also the following section from Supplement 1 to the White Paper:

Section C: Additional Evidence that Abitibi and Bowater Exercised Market Power Over the Period 2002 to 2006 (pp. 16–23)

As explained in these analyses, Abitibi and Bowater jointly acted as a dominant firm to strategically remove newsprint capacity from the NA market to raise the price of newsprint to NA customers significantly above competitive levels during this four-year period. During this four-year period of strategic capacity closures, NA newsprint prices steadily increased by an aggregate of 49 percent between the third quarter of 2002 and the third quarter of 2006 despite a steady decline in the consumption of newsprint by U.S. newspapers. These newsprint price increases were far in excess of the price increases for closely-related uncoated groundwood specialty grades during this period.[15]

Earlier mergers in the NA newsprint industry, especially the Abitibi-Donohue merger in 2000 and the Bowater-Alliance merger in 2001, created both the incentive and ability for Abitibi and Bowater to jointly engage in this anticompetitive conduct. In papers and presentations to the DOJ staff submitted on behalf of the NAA and the U.S. newspaper industry, Economists Incorporated explained in 2000 and 2001 that these two mergers, if not challenged, would have significant anticompetitive results. DOJ took no action against either of these two earlier mergers and, as predicted by Economists Incorporated, the two mergers enabled Abitibi and Bowater to engage in the anticompetitive conduct that occurred between 2002 and 2006.[16] U.S. newspapers and other NA newsprint customers bore the cost of DOJ's inaction in the form of significantly higher newsprint prices.

Despite its obvious relevance to an evaluation of the adequacy of DOJ's settlement with Abitibi and Bowater, this prior history of anticompetitive conduct by Abitibi and Bowater is not mentioned in the CIS, Complaint or PFJ. This is surprising since the documentation of prior anticompetitive conduct would strengthen the grounds for DOJ's challenge of the merger.

The Commentary on the Horizontal Merger Guidelines (''Merger Guidelines Commentary''), jointly published by DOJ and the Federal Trade Commission, explains why evidence of prior anticompetitive effects by finns in a relevant market is probative to the agencies' evaluation of a merger of two firms in that market.

Facts showing that rivals in the relevant market have coordinated in the past are probative of whether a market is conducive to coordination. Guidelines § 2.1. Such facts are probative because they demonstrate the feasibility of coordination under past market conditions. Other things being equal, the removal of a firm via merger, in a market in which incumbents already have engaged in coordinated behavior, generally raises the risk that future coordination would be more successful, durable, or complete.[17]

Two DOJ cases are cited to illustrate the significance of prior anticompetitive conduct in DOJ's merger analysis and, in each of these cases, the anticompetitive conduct was described in the complaint challenging the merger.[18] While these two cases identified in the Merger Guidelines Commentary were challenged on a coordinated interaction theory,[19] evidence of prior anticompetitive conduct should logically also be highly relevant to the agencies' analysis of mergers based on a unilateral effects theory.

3. While the Proposed Merger of Abitibi and Bowater Was Under Review by DOJ, Abitibi and Bowater Suspended Their Dominant Firm Behavior and, as a Result, NA Newsprint Prices Declined Significantly

Abitibi and Bowater began their merger discussions in June 2006, which culminated in their joint merger announcement on January 29, 2007.[20] The four-year run-up in newsprint prices described in the previous section reached a peak of $675 per metric tonne in May 2006. That price prevailed through September 2006. Between September 2006 and December 2006, the NA newsprint price declined slightly to $660 per metric tonne.[21] Between December 2006 and October 2007, the price of newsprint dropped by $100 to $560 per metric tonne, a decline of about 15 percent.[22] The $115 per metric tonne decline in the NA price of newsprint between September 2006 and October 2007 was about 17 percent.

Between September 2006 and October 2007, Abitibi and Bowater did not engage in joint dominant firm behavior despite a decline in NA newsprint prices of about 17 percent. It is plausible that Abitibi and Bowater suspended their joint dominant firm behavior during this period for two reasons: (1) Abitibi and Bowater wanted to maximize their chances of a favorable merger review by DOJ by avoiding conduct that DOJ would likely construe as anticompetitive; and (2) their ability and incentive to jointly engage in strategic capacity closures had been significantly weakened by their previous strategic capacity closures over the period 2002 to 2006. It is also plausible that a weakened incentive and ability to engage in joint dominant firm behavior led to the decision to merge.[23]

From the trade press commentary during the merger review period, it is apparent that newsprint industry analysts and newsprint competitors of Abitibi and Bowater were waiting for the merger to be completed in anticipation that a merged AbitibiBowater would increase NA newsprint prices by shutting down enough newsprint capacity to create a tight market. It is also apparent that these same analysts and competitors believed that Abitibi and Bowater would not take any significant actions to remove capacity from the market until after their merger review was completed.[24]

[15] See the White Paper, Section J: A Comparison of Newsprint Prices with the Prices of Uncoated Groundwood Specialty Grades 3Q 1999 to 4Q 2006 (pp. 109–119).

[16] The implementation of strategic capacity closures by Abitibi and Bowater following their mergers was likely delayed by the U.S. economic recession in 2001 and the economic aftermath of the events of 9/11. During this time, U.S. newspapers suffered a significant decline in the sale of newspapers and newspaper advertising, resulting in a significant decline in the demand for newsprint by U.S. newspapers.

[17] See Merger Guidelines Commentary, p. 22.

[18] The two cited DOJ examples are *Premdor-Masonite* (2001) and *Suiza-Broughton* (1999).

[19] On page 22, the Merger Guidelines Commentary describes an increase in the likelihood of ''coordinated interaction'' that might result from a merger as follows: ''A horizontal merger is likely to lessen competition substantially through coordinated interaction if it creates a likelihood that, after the merger, competitors would coordinate their pricing or other competitive actions, or would coordinate them more completely or successfully than before the merger.'' See Appendix A for additional discussion of the distinctions between unilateral effects theories and coordinated interaction theories.

[20] See Supplement 1 to the White Paper, page 11.

[21] Source: the following editions of Pulp & Paper Week; June 19, 2006, p. 3; September 18, 2006, p. 3; November 20, 2006, p. 3; February 19, 2007, p. 3; and November 19, 2007, page 3.

[22] Between September 2006 and October 2007, the NA price of newsprint dropped $115 per metric tonne, a decline of about 17 percent.

[23] The continued decline in NA newsprint demand likely also contributed to the decision to merge. A continued decline in NA newsprint demand would require continued strategic capacity closures in order to maintain high newsprint industry operating rates and increasing newsprint prices. By merging, Abitibi and Bowater increased their incentive and ability to strategically close capacity in the face of declining demand.

[24] See Section B.3., ''Newsprint Industry Analysts and Competitors of Abitibi and Bowater Do Not Expect Abitibi and Bowater to Take Any Significant Action to Remove Newsprint Capacity from the

Continued

The following quotation is typical of comments that appeared in the trade press during the merger review period. ''No one will close any capacity because they figure AbitibiBowater will do it for them. And Abitibi kind Bowater will figure they can't be too aggressive on pricing or close capacity until their deal closes, said one contact.''[25] For other similar trade press commentary see Supplement 1 to the White Paper, pp. 13–14.

4. AbitibiBowater Resumed the Dominant Firm Behavior in November 2007 Following the October 23, 2007 Settlement Agreement With DOJ to Divest the Snowflake Mill

Less than five weeks after the filing of the Complaint and MFJ, AbitibiBowater announced the removal of about 600,000 metric tonnes of capacity from the NA newsprint market[26] amounting to about a 5 percent reduction in total NA newsprint capacity. These capacity closures will occur during the first quarter of 2008. At approximately the same time, AbitibiBowater initiated a $60 per metric tonne newsprint price increase. This price increase will also take place during the first quarter of 2008. Most other NA newsprint manufacturers quickly joined AbitibiBowater in this $60 price increase.[27]

In addition, AbitibiBowater's announced capacity closures have permitted the successful implementation of a previously announced $25 per metric tonne price increase.[28] Newsprint manufacturers, including Abitibi and Bowater, had previously been unable to successfully implement this price increase, originally scheduled for September 2007, because of excess NA newsprint industry capacity.[29] Combined, these two price increases will raise the price to NA newsprint customers by $85 per metric tonne, which is about a 15 percent price increase over the October 2007 price of $560 per metric tonne.[30]

These post-settlement events are captured in headlines from the trade press newsletter Pulp & Paper Week during the first three weeks of December 2007 following the capacity closure announcement of AbitibiBowater on November 29, 2007 and the $60 per metric tonne newsprint price increase initiated by AbitibiBowater.[31]

''AbitibiBowater plans to shut down one million tonnes/yr of capacity in 1Q; expects more closures could follow in 2Q,'' December 3, 2007, p. 1.[32]

''Most North American newsprint makers join $60/tonne 2008 hike,'' December 3, 2007, p. 2.[33]

''Newsprint giant AbitibiBowater embraces industry leadership, eyes $200/tonne North American newsprint price increase,'' December 10, 2007, p. 1.

''Publisher resistance to $25/tonne North American newsprint increase collapses; producers looking to fast track recovery,'' December 17, 2007, p. 1.

In comments reported in Pulp & Paper Week, RISI economist Kevin Conley explains the cause and effect between AbitibiBowater's capacity closures and the increase in newsprint prices. ''AbitibiBowater's capacity closures will obviously provide the upward pressure for an extended price recovery in 2008, as operating rates soar past the magic 95% threshold generally needed for prices to rise. Without AbitibiBowater's bold move [to remove 600,000 metric tonnes of newsprint capacity from the market] operating rates and prices would have continued to languish at low levels until the highest-cost mills could no longer survive, eventually leading to the inevitable closures needed to balance the North American market.''[34]

The combined AbitibiBowater is seeking to ''leverage the North American (newsprint) price up to the price in Europe and not the other way around,'' according to AbitibiBowater President and CEO David Paterson.[35] If AbitibiBowater is successful in ''leveraging'' the North American newsprint price up to the price of newsprint in Europe, that will result in a $200 per metric tonne price increase or about 36 percent over the North American price of $560 per metric tonne in October 2007.[36] At the time AbitibiBowater announced the removal of 600,000 metric tonnes of newsprint capacity from the market, it also announced that ''more mills could close in Canada later [in 2008].''[37] Based on these statements and other statements by AbitibiBowater executives and past and current actions by AbitibiBowater and its predecessor companies, it is very likely that AbitibiBowater will close additional newsprint capacity in 2008 to ''leverage'' the North American newsprint price up to the newsprint price in Europe.

In the CIS, DOJ asserts that ''[w]ithout Snowflake's capacity, the merged firm would not be of sufficient size to be able to recoup the losses from such strategic closures through increases in prices on its remaining newsprint production.'' These strategic closures announced by AbitibiBowater less than five weeks after the filing of the Complaint, CIS, and PFJ show that DOJ seriously misjudged the incentive and ability of the merged firm to strategically close capacity despite the agreement to divest the Snowflake mill. Furthermore, based on comments by AbitibiBowater, additional strategic capacity closures will likely occur later in 2008.[38] In the absence of a significantly larger divestiture, DOJ's misjudgment will likely cost U.S. newspapers and other U.S. newsprint customers billions of dollars in coming years.[39]

5. DOJ Required a Much More Significant Divestiture To Settle a Comparable Paper Industry Merger in 2000

In August 2000, Georgia-Pacific announced plans to acquire Fort James. At the time of the acquisition Georgia-Pacific was a broadly-based forest products company and Fort James was the largest manufacturer of tissue paper in the United States. Both companies operated paper mills that produced parent tissue rolls used to make tissue products sold to commercial customers (known as ''away-from-home'' tissue products). At the time of the proposed acquisition, Fort James and Georgia-Pacific were the two largest producers of parent tissue rolls in NA. Fort James' share of NA parent tissue role capacity was 25 percent and Georgia-Pacific's share was 11 percent for a combined capacity share of 36 percent.

On November 21, 2000, DOJ filed a complaint challenging the merger in the

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Market Until After They Have Merged,'' in Supplement 1 to the White Paper, pp. 13–15.

[25] ''Market abuzz over merger: concerns center on pricing and customer relationships,'' Pulp & Paper Week, February 5, 2007, p. 11.

[26] Source: Press release on AbitibiBowater Web site, November 29, 2007.

[27] Source: Pulp & Paper Week, Dec. 3, 2007, pp. 1, 2, and 5.

[28] Source: Pulp & Paper Week, Dec. 17, 2007, pp. 1 and 11.

[29] On p. 9 in its October 22, 2007 edition, published the day before DOJ's settlement agreement with Abitibi and Bowater, Pulp & Paper Week reported on the failure of NA newsprint producers to implement the September price increase in an article titled ''North American newsprint hikes lack market traction, price declines $5/tonne more.''

[30] Source for October 2007 newsprint price: Pulp & Paper Week, Nov. 19, 2007, p. 3.

[31] Pulp & Paper Week is published by RISI, which describes itself as ''the leading source of global news for the forest products industry.'' These articles are attached as Attachment A to the Comments of the Newspaper Association of America.

[32] The capacity reduction announced by AbitibiBowater totaled about 600,000 metric tonnes of newsprint capacity and 400,000 metric tonnes of commercial printing papers according to the Pulp & Paper Week article.

[33] The Pulp & Paper Week article states that the $60 per metric tonne increase was initiated by AbitibiBowater.

[34] Source: Pulp & Paper Week, Dec. 10, 2007, p. 5.

[35] Source: Pulp & Paper Week, Dec. 10, 2007, p. 1.

[36] ''Newsprint prices in Europe were close to $200/tonne higher than in the USA in November.'' Source: Pulp & Paper Week, Dec. 10, 2007, p. 1.

[37] Source, Pulp & Paper Week, Dec. 3, 2007, p. 1.

[38] Source: Pulp & Paper Week Dec. 3, 2007, pp. 1 and 5.

[39] Based on the November 2007 Flash Report, current annual U.S. newsprint consumption is about 7.8 million metric tonnes. The $85 per metric tonne price increase resulting from AbitibiBowater's recently announced capacity closures will increase the aggregate cost of newsprint to U.S. newsprint customers by about $663 million per year. If the NA newsprint price rises by a total of $150 per metric tonne due to continued strategic behavior by AbitibiBowter (an increment of $65 per metric tonne over the current price increase of $85 per metric tonne), the cost to U.S. newsprint consumers would be about $1.2 billion on an annual basis. If AbitibiBowater is able to ''leverage the North American (newsprint) price up to the price in Europe,'' as David Paterson, President and CEO of AbitibiBowater, is apparently seeking to do, the annual cost to U.S. newsprint consumers resulting from the $200 per metric tonne price increase (an increment of $115 per metric tonne over the current price increase of $85 per metric tonne) would be about $1.6 billion. These calculations are based on the assumption that the U.S. consumption of newsprint remains at the November 2007 level. In practice, U.S. newsprint consumption will likely continue to decline, as discussed above. Therefore, the magnitudes of the aggregate cost increases to U.S. newsprint customers calculated in this footnote would be reduced somewhat by a continued decline in consumption. Regardless, the aggregate cost increases to U.S. consumers will be substantial.

parent tissue roll market. At the same time, DOJ filed a proposed final judgment requiring the divestiture of all of Georgia-Pacific's parent tissue roll capacity.[40]

As described in the competitive impact statement for the Georgia-Pacific/Fort James merger, the theory DOJ relied upon to challenge the proposed acquisition of Fort James by Georgia-Pacific in the NA tissue parent roll market merger appears to be based on the same basic theory of unilateral anticompetitive conduct DOJ used in its challenge of the Abitibi-Bowater merger.

Georgia-Pacific has approximately 11 percent of North American capacity for the production of AFH tissue, and Fort James has approximately 25 percent. Hence, the acquisition would result in Georgia-Pacific accounting for approximately 36 percent of available North American AFH parent roll capacity. This increase in industry capacity controlled by Georgia-Pacific would give it sufficient capacity to profit from the increase in price caused by a unilateral reduction in output after this merger.[41]

It is evident that DOJ concluded that the combination of firms with a 26 percent capacity share and an 11 percent capacity to create a firm with a 36 percent capacity share would give Georgia-Pacific the incentive and ability to unilaterally exercise market power in the NA parent tissue roll market. It is also evident that DOJ concluded that the divestiture of Georgia-Pacific's entire 11 percent of its NA parent tissue roll capacity share was necessary to eliminate Georgia-Pacific's incentive and ability to engage in unilateral strategic behavior. The divestiture left Georgia-Pacific with a capacity share of 25 percent in the NA parent tissue roll market.

Nothing in the Abitibi-Bowater CIS explains the great disparity between the divestiture required to settle the Abitibi-Bowater merger and the divestiture required to settle the Georgia-Pacific/Fort James merger. The prior recent and well-documented unilateral anticompetitive conduct of Abitibi and Bowater (unacknowledged by DOJ in the Complaint and CIS) makes this disparity all the more puzzling.

If the former Bowater's newsprint capacity, which accounts for 16 percent of NA newsprint capacity according to the Complaint, were divested, the merged firm (AbitibiBowater) would have a NA newsprint capacity share of 25 percent. This divestiture would be comparable to the divestiture DOJ required to settle the Georgia-Pacific/Fort James merger, which left Georgia-Pacific with a 25 percent capacity share in the NA parent roll tissue market.

C. Conclusion

Based on the economic analysis contained in this memorandum and the economic analyses we have previously submitted to DOJ, we conclude that the Snowflake divestiture will not be sufficient to eliminate the anticompetitive effects of the merger and that a substantially larger divestiture is needed to ensure that AbitibiBowater no longer has the incentive and ability to engage in the type of anticompetitive conduct alleged in Paragraphs 2 and 19 of the Complaint and described on page 6 of the CIS.

Appendix A–Merger Analysis, Unilateral Effects, and the Dominant Firm Model

In determining the competitive effects of a merger, DOJ utilizes the analytical framework set out in the U.S. Department of Justice and Federal Trade Commission (''FTC'') Horizontal Merger Guidelines (''Merger Guidelines'').[42] In March 2006, DOJ and the FTC jointly issued a Commentary on the Merger Guidelines (''Merger Guidelines Commentary'') to provide interested parties with a greater understanding of how the agencies apply the Merger Guidelines to the investigation of specific mergers.

Section 2 of the Merger Guidelines describes two general types of anticompetitive effects that potentially could result from a merger: (1) Unilateral effects and (2) coordinated interaction. The Merger Guidelines Commentary describes these anticompetitive effects as follows:

A horizontal merger is likely to lessen competition substantially through coordinated interaction if it creates a likelihood that, after the merger, competitors would coordinate their pricing or other competitive actions, or would coordinate them more completely or successfully than before the merger. A merger is likely to lessen competition substantially through unilateral effects if it creates a likelihood that the merged firm, without any coordination with non-merging rivals, would raise its price or otherwise exercise market power to a greater degree than before the merger.[43]

Paragraph 2 of DOJ's Complaint against Abitibi and Bowater alleges that

After the merger, the combined firm will have the incentive and ability to withdraw capacity and raise newsprint prices in the North American newsprint market.

Paragraph 19 of DOJ's Complaint against Abitibi and Bowater alleges that

The proposed transaction would combine Defendants' large share of newsprint capacity, thereby expanding the quantity of newsprint sales over which the merged firm would benefit from a price increase. This would provide the merged firm with an incentive to close capacity sooner than it otherwise would to raise prices and profit from the higher margins on its remaining capacity.

While DOJ has not disclosed the economic models it used in its investigation of the Abitibi-Bowater merger, these allegations in Paragraphs 2 and 19 of the Complaint are consistent with a unilateral effects theory of competitive harm, specifically a unilateral effects theory of competitive harm based on the application of a dominant firm model. The Merger Guidelines Commentary describes the application of the dominant firm model as follows:

The Agencies' analysis of unilateral competitive effects draws on many models developed by economists. The simplest is the model of monopoly, which applies to a merger involving the only two competitors in the relevant market. One step removed from monopoly is the dominant firm model. That model posits that all competitors but one in an industry act as a ''competitive fringe,'' which can economically satisfy only part of total market demand. The remaining competitor acts as a monopolist with respect to the portion of total industry demand that the competitive fringe does not elect to supply. This model might apply, for example, in a homogeneous product industry in which the fringe competitors are unable to expand output significantly.[44]

In our opinion, a dominant firm model is the appropriate model to assess the competitive effects of the Abitibi-Bowater merger. In our submissions to DOJ, we described our application of the dominant firm model to this merger.[45] Our dominant firm model incorporated the key characteristics of the newsprint industry including the capacity share of the dominant firm (i.e., a combined Abitibi and Bowater), the variable cost of the dominant firm, the industry price elasticity of demand, the industry operating rate, the excess capacity of fringe firms, and prevailing price levels. In our application of the dominant firm model we took into consideration multi-period dynamics, a decline in the NA demand for newsprint, and an increase in the rate of decline in the NA demand for newsprint.

Based on our application of the dominant firm model, we predicted that, under a wide range of dominant firm capacity shares and other assumptions, the merged firm would have both the incentive and ability to remove capacity from the market to raise the price of newsprint. In particular, we were able to show that under a wide range of assumptions the dominant firm would hypothetically be able to close newsprint capacity to raise newsprint prices well above competitive levels at dominant firm capacity shares well below 37 percent.

The results of our application of the dominant firm model are consistent with the observed joint dominant firm behavior of Abitibi and Bowater during the period 2002 to 2006 as discussed in Section B.2. above and with the observed dominant firm behavior of the newly-merged AbibitiBowater as discussed in Section B.4 above.

[40] For an explanation of the allegations in the complaint and the provisions of the proposed final judgment, as well as background information relating to the merger, see the Georgia-Pacific/Fort James competitive impact statement, dated January 25, 2001. DOJ also required the divestiture of certain downstream tissue converting capacity.

[41] Georgia-Pacific/Fort James competitive impact statement, p. 7.

[42] The Merger Guidelines were issued on April 2, 1992 and revised on April 8, 1997.

[43] See the Merger Guidelines Commentary, p. 22.

[44] See Merger Guidelines Commentary, p. 25.

[45] See Section K of the White Paper: Dominant Firm Model (pages 120–124); Attachment K to the White Paper: Technical Appendix to Section K Dominant Firm Model (pages 1–8), and Supplement 1 to the White Paper: Additional Analysis Based on the Dominant Firm Model (DFM) Including a Revision of the DFM Designed to Consider Multi-period Dynamics (pages 24–33).

Attachment A—Curricula Vitae of John H. Preston and Kent W. Mikkelsen, PhD

Curriculum Vitae

John H. Preston

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Home

18505 SE Heritage Oaks Lane, Tequesta, FL 33469, (561) 575–2310, *jhp2004@comcast.net*

Education

A.B. English, Dartmouth College (1966), M. A. Economics, University of Michigan (1972), Candidate in Philosophy in Economics, University of Michigan (1974)

Professional Experience (Consulting)

Senior Vice President, Economists Incorporated (December 1998–Present), Vice President, Economists Incorporated (December 1995–December 1998), Senior Economist, Economists Incorporated (April 1985–December 1995)

Selected Matters

Timberlawn v. *Tenet Healthcare, et al.* Provided affidavit, deposition testimony, and trial testimony on behalf of defendants in the alleged monopolization of psychiatric hospitals in the Dallas area by NME.

Proposed *Abitibi-Consolidated/Donohue newsprint merger.* On behalf of NAA, provided analysis to DOJ concerning the likely anticompetitive effects of the merger.

Proposed *MCI/Sprint Merger.* Provided affidavits to DOJ, FCC, and European Commission analyzing the competitive effects of the proposed merger on behalf of British Telecom and AT&T. Testified before the European Commission on this matter.

Coated Groundwood Paper Anti-Dumping Investigation. Helped prepare response to Antidumping investigation of the ITC on behalf of European groundwood paper manufacturers. Participated in presentation to ITC.

Proposed *SBC/AT&T and Verizon/MCI mergers.* On behalf of BT, analyzed competitive effects of the two telecommunications mergers. Provided affidavits to DOJ, FCC and European Commission and made presentations to DOJ and FCC staffs.

British Telecom/AT&T Global Venture. Provided economic analysis on a wide range of competition issues concerning the global venture, including presentations to the European Commission and DOJ.

PacifiCare/FHP merger. Analysis of the impact of this proposed merger on the provision of Medicare HMO services in California. Made written and oral presentations to the FTC staff and senior management.

WellPoint/HSI merger. Analysis of the competitive effects of this proposed merger of two of the largest HMOs in California and participation in meetings with DOJ.

Sale of General Dynamics' Missile Division to Hughes Aircraft and General Dynamics' Jet Fighter Division to Lockheed. Helped prepare antitrust analysis and participated in presentations to DOJ and FTC on these defense industry mergers.

Professional Experience (Antitrust Division)

Economist (January 1975–April 1985), Economic Policy Office, Antitrust Division, U.S. Department of Justice

Honors

Special Achievement Award for work on *U.S.* v. *Hospital Affiliates International, Inc. and American Health Services, Inc.* (1980)
Outstanding Performance Rating (1980–1981)
Outstanding Performance Rating (1981–1982)
Outstanding Performance Rating (1982–1983)
Outstanding Performance Rating (1983–1984)
Meritorious Award (1983)

Selected Matters Testimony Affidavit

U.S. v. *Hospital Affiliates International, Inc., and American Health Services, Inc.* In 1980, submission of an affidavit to the U.S. District Court in New Orleans analyzing the competitive effects of the proposed merger of three psychiatric hospitals in New Orleans, LA.

Selected Matters Deposition Testimony

U.S. v. *British Columbia Forest Products, et al.* In 1981, deposition testimony on the preparation of the trial exhibits for the challenge of an acquisition of a coated groundwood paper plant by a firm partially owned by two other manufacturers of coated groundwood paper.

U.S. v. *State Board of Certified Public Accountants of Louisiana.* In 1984, deposition testimony on product and geographic market definition and competitive effects of restrictions on advertising and solicitation by the Louisiana board of accountants.

Grand Jury Testimony

U.S. v. *Gary L. McAliley et al.* In 1980, testimony before a grand jury in Alabama on the effects of an alleged agreement between attorneys in Coffee County, Alabama to raise fees for real estate closings.

Other Filed Cases

U.S. v. *National Medical Enterprises, et al.* Hospital merger case.

U.S. v. *American Consulting Engineers Council.* Prohibitions on free designs and on participation in design competitions.

U.S. v. *Alaska Board of Registration for Architects, Engineers and Land Surveyors.* Competitive bidding ban.

U.S. v. *First Multiple Listing Service.* Alleged exclusion of competitors by owners of an essential facility.

Investigations

Georgia-PacifIc Acquisition of Hudson Pulp & Paper. This merger was investigated by DOJ for antitrust implications in a number of paper and paperboard product lines.

Acquisition of Hospital Affiliates International by Hospital Corporation of America (1981). Merger of two major hospital management companies.

South Florida Physicians' Boycott (1983). Boycott by physicians to place pressure on the legislature to enact malpractice insurance legislation favorable to physicians.

Stanislaus Preferred Provider Organization (SPPO) (1984). Agreement by physician members of SPPO not to contract with any other PPOs allegedly in order to forestall the development of PPO competition in Stanislaus County.

Policy Matters

The Division's position on the Health Care Cost Containment Act of 1983 (1984). This position was delivered in testimony by Charles F. Rule, Deputy Assistant Attorney General, to a Senate Subcommittee.

Letter to the Health Care Financing Administration (HCFA) (1984). This letter expressed the Division's views on certain proposals which would restrict the dissemination of information collected by Professional Review Organizations.

The Division's policy toward the health care sector in general and preferred provider organizations (PPOs) in particular (1985). This policy was expressed in a paper presented by J. Paul McGrath, Assistant Attorney General, to the National Health Lawyers Association and the ABA.

Business Review commenting on plans by the Southwest Michigan Health Systems Agency (HSA) (1982). The HSA wanted to publish rates charged by hospitals within the HSA.

Business Review commenting on a proposal by the Maryland Health Care Coalition (1982). The Coalition wanted to collect and disseminate information concerning the incentive effects of different types of insurance policies.

Letters to the ABA and State Supreme Courts (1982–1984). These letters expressed the Division's views on restrictions on advertising and solicitation contained in the ABA's Model Rules.

Publications

''An antitrust analysis of the *Alliant* decision and defense industry mergers,'' *International Merger Law,* April 1993 (w/ Philip B. Nelson) [Note: a shorter version appeared in *Economists Ink* (Winter 1993), a newsletter published by Economists Incorporated.]

''Coated Groundwood Paper Anti-Dumping Investigation,'' *Economists Ink* (Winter 1993).

Curriculum Vitae

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Background

Born: September 20, 1954, married, 3 children

Education

Ph.D., Economics, Yale University, 1984
M.Phil., Economics, Yale University, 1981
M.A., Economics, Yale University, 1980
B.A., Economics, Brigham Young University, 1978, *summa cum laude*

Fellowships, Honors and Awards

College Valedictorian, Brigham Young University, 1978
H. B. Earhart Fellow, 1978–1979
University Fellow, Yale University, 1978–1980
Richard Bernhard Fellow, 1980–1981
Research Scholar, International Rice Research Institute, 1981

Fields of Concentration

Industrial Organization, Economic Development

Professional Experience

1986–present: Senior Vice President, Economists Incorporated
1984–1986: Economist, Economic Analysis Group, Antitrust Division, U.S. Department of Justice
1983–1984: Visiting Assistant Professor, University of Michigan
1982: Acting Instructor, Yale University
1981–1982: Teaching Fellow, Yale University
1979–1983: Research Fellow, Yale University

Testimony

Expert witness for Government in *United States* v. *Calmar Inc. and Realex Corp.,* United States District Court, District of New Jersey, Civil Action No. 84–5271.

Expert witness for Defendant in *Sunbelt Television, Inc.* v. *Jones Intercable, Inc.,* United States District Court, Central District of California, Case No. CV–91–3506 WDK (Kx).

Expert witness for Defendant in *Stag-Parkway, Inc.* v. *The Dometic Corporation,* United States District Court, Northern District of Georgia, Case No. 1–91–CV–2579–JOF.

Expert witness for Plaintiff in *Thomas L. Hopkins (Commonwealth of Virginia)* v. *Smithfield Foods, Inc.,* Virginia Circuit Court, Isle of Wight County, No. 96–125.

Expert witness for Defendant in *Elpizo Limited Partnership* v. *Marriott International, Inc.* and *Host Marriott Corporation* v. *Maryland Hospitality, Inc.,* Court of Common Pleas for Philadelphia County, Pennsylvania, October Term, 1994, No. 607.

Expert witness for Plaintiff in *Thomas L. Hopkins (Commonwealth of Virginia)* v. *Smithfield Foods, Inc.,* Virginia Circuit Court, Isle of Wight County, No. 97–80.

Expert witness for Defendant in *Consumer Health Foundation* v. *Humana Group Health Plan, Inc., et al.*, United States District Court, District of Columbia, Case No. 1:98CV02920 (GK).

Expert witness for Defendant in *United States* v. *Broadcast Music, Inc.* United States District Court, Southern District, New York, 64 Cir. 3787 (LLS).

Expert witness for Defendants Advance Stores Company, Inc. and Discount Auto Parts, Inc. in *Coalition for a Level Playing Field LLC et al.* v. *AutoZone, Inc., et al.*, United States District Court, Eastern District of New York, No. CV 00 0953 (LDW) (ETB).

Expert witness for Defendant in *United States* v. *Broadcast Music, Inc.* United States District Court, Southern District, New York, 64 Cir. 3787 (LLS), remand proceeding.

Expert witness for Defendants in *Ramallo Bros. Printing, Inc.* v. *El Dia, Inc. et al.*, United States District Court, District of Puerto Rico, Civil No. 02–2400 (JAF).

Expert witness for Defendant in *Marco Island Cable, Inc.* v. *Comcast Cablevision of the South, Inc.,* United States District Court, Middle District of Florida, Case No. 2:04cv–26–FtM–29–DNF.

Testimony, *Federal Communications Commission En Banc Hearing Regarding Local Television Ownership Rules,* February 12, 1999.

Testimony, *United States Senate Committee on Commerce, Science, and Transportation, Hearing on Media Ownership,* May 22, 2003.

Selected Consulting Matters

Detroit Free Press and Detroit News Joint Operating Agreement (JOA)—Prepared economic and business analysis used in hearing before Administrative Law Judge.

Soft Drink Price Fixing—Analysis of evidence of price fixing and estimation of damages in Department of Justice investigations and private damage suits against various CocaCola bottlers.

Federal Communications Commission Inquiry into Cable Television—Supervised and wrote up research projects regarding cable rates and vertical market structure submitted with briefs filed by TCI.

GenCorp acquisition from Goodyear, Department of Justice review—Analyzed demand and supply-side substitution for vinyl laminates.

York acquisition of Hyster, Federal Trade Commission review—Analyzed geographic market definition in forklift trucks.

Stag-Parkway v. *Dometic*—For defendant, testified regarding lack of injury and damages due to price discrimination in sales to distributors.

Sunbelt Television v. *Jones Intercable*—For defendant, testified regarding market definition and monopoly power in local advertising and critiqued plaintiff's damage study.

Kiwifruit antidumping investigation by International Trade Commission—Coordinated preparation of economic analysis for New Zealand respondents.

State of Virginia v. *Smithfield Foods*—For plaintiff, evaluated the economic gain defendant received through non-compliance with environmental laws.

Federal Communications Commission Inquiries into Broadcast Television—For three broadcast networks, prepared comments on the economic effects of prime-time access rules and station ownership rules.

Elpizo Ltd Partnership v. *Marriott*—For defendant, analyzed plaintiff's damages model and testified regarding inappropriateness of plaintiff's damages model.

Media Ownership Rules—Researched and submitted three separate papers to FCC on behalf of ABC, CBS and Newspaper Association of America.

Cable & Wireless Optus acquisition of AAPT—Presented analysis of multiple telecommunications markets to Australian Competition and Consumer Commission.

TeleCell Cellular, Inc. et al. v. *GTE Mobilnet of South Texas Limited Partnership*—For defendant, analyzed damages claims of plaintiffs for compensation allegedly less favorable than another cellular agent.

Kesmai Corp. et al. v. *America Online*—For defendant, analyzed plaintiff's claim of damages to Internet games business.

Federal Communications Commission En Banc Hearing—Presented testimony on FCC local television ownership rules.

Consumer Health Foundation v. *Humana*—For defendant, evaluated damages from alleged delay in releasing payment.

API v. *Granite*—Advisor to court-appointed special master making findings on below-cost pricing in road construction.

Hearst Acquisition of San Francisco Chronicle—For Hearst, prepared analysis showing prospects for competition by San Francisco Examiner outside the JOA and incremental contribution of Examiner to JOA profits.

Denver Post-Denver Rocky Mountain News JOA—For applicants, analyzed probable failure and incremental unprofitability of the News.

United States v. *BMI*—For defendants, testified about a reasonable royalty rate for a music performing right blanket license.

Vitamin Price Fixing Case—Submitted expert reports finding no incentive for two vitamin producers to participate in conspiracies involving vitamins they did not manufacture.

Newspaper-Broadcast Cross-Ownership Rule—For the Newspaper Association of America, submitted a paper to the FCC on structural change since 1975 and potential benefits of joint ownership.

Advance-Discount Robinson-Patman Case—For defendants, testified about drawing cost inferences from pricing data.

U.S. Senate Commerce Committee Hearing—Presented testimony supporting elimination of three FCC rules governing ownership of broadcast stations.

IPSCO v. *Mannesmann Steel Mill Case*—For defendant, analyzed damages from deficiencies of a steel mill.

TRICO v. *NKK et al. Steel Mill Case*—For plaintiff, analyzed damages from deficiencies of a steel mill.

FCC ''Omnibus'' Broadcast Ownership Proceeding—For CBS, Fox and NBC, analyzed station ownership, news broadcast and diversity issues.

FCC Cable Bundling and Retransmission—For Disney, submitted analysis of proposals to mandate a la carte cable programming and value of cable retransmission rights for ABC stations.

Heavy-Duty Trucks—For defendant Mack Trucks, submitted expert report discussing market definition, market power, alleged anticompetitive practices and damages.

Printing Monopolization—For defendant El Dia, testified on market definition, dangerous probability, and alleged anticompetitive practices including predatory pricing.

Dissolution of Birmingham JOA—For Birmingham News Post-Herald and Birmingham Post-Herald, presented to DOJ an analysis of the incremental unprofitability of the Post Herald.

Cable Monopolization—For defendant Comcast, testified on alleged monopolization and anticompetitive practices including exclusive contracts and on damages.

Regulatory Impact—For a consortium of telecommunications firms in Bermuda, analyzed the impact of proposed regulatory changes.

Attachment B—White Paper by Economists Incorporated, Submitted on Behalf of the NAA to DOJ on April 11, 2007

Economists Incorporated

An Economic Analysis of the Competitive Effects of the Proposed Abitibi-Bowater Merger

Submitted to DOJ on Behalf of NAA

John H. Preston, Kent W. Mikkelsen, PhD, Economists Incorporated, Washington, DC, April 11, 2007.

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4. Projected NA Newsprint Demand 2006–2008.
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3. Presentation by David Paterson, President and CEO of Bowater, at the Citigroup Conference in December 2006.
4. Presentation by John Weaver, President and CEO of Abitibi, at the Credit Suisse First Boston Investment Analysts Conference in March 2004.
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2. Article by Harold M. Cody Titled ''New Paradigm: Newsprint Demand Falls, Prices Soar.''
3. Three Articles by RISI Senior Economist Andrew Battista Analyzing the Strategy of Abitibi and Bowater to Shut Down Capacity to Maintain High Operating Rates and Increasing Prices.

Section I. Abitibi's Newsprint Capacity Closures 1999 to 2001

Section J. A Comparison of Newsprint Prices With the Prices of Uncoated Groundwood Specialty Grades 3Q 1999 to 4Q 2006

1. Introduction.
2. The Adverse Impact of the Increases in Input Prices and the Appreciation of the Canadian Dollar Has Fallen More Heavily on Producers of Uncoated Groundwood Specialty Grades Than on Producers of Newsprint.
3. Comparing Quarterly Prices tbr Newsprint and Uncoated Groundwood Grades from 3Q 1999 Though 4Q 2006.
4. Abitibi's Variable Costs to Produce Newsprint and Uncoated Groundwood Specialty Grades Have Been Relatively Constant for the Period 2001–2005.
5. Applying the Percentage Price Changes for the Uncoated Groundwood Specialty Grades to the 3Q 1999 Price of Newsprint to Determine the Effect on Newsprint Revenues from Sales to NA Customers.

Section K. Dominant Firm Model

Section L. Conclusions

Attachments

Attachment A Links to Newsprint-Related Web Sites
Attachment B Additional Analysis of Uncoated Groundwood Specialty Grades and Tables B1 to B7 for Section B
Attachment C Tables C1 to C3 for Section C
Attachment D Tables D1 to D4 for Section D
Attachment K Technical Appendix to Section K Dominant Firm Model

Section A. Overview of the White Paper

1. Introduction

Economists Incorporated has been asked by the Newspaper Association of America (''NAA''), an association of U.S. daily newspapers, to prepare an economic analysis of the likely competitive effects of the proposed Abitibi-Bowater merger in the North American (''NA'') newsprint market (''White Paper'') with the intent to provide that analysis to the U.S. Department of Justice to assist the department in its investigation of the proposed merger.

The objective of this White Paper is to analyze the economic effects of the proposed merger of Abitibi and Bowater and to identify any anticompetitive consequences of the proposed merger.

In Section A below, we summarize our analysis and main conclusions of each section. Sections A, B, C, D, and K have attachments containing data and analysis related to the analysis in the section.

The last subsection of Section A contains a table of contents to the White Paper. Attachment A to Section A provides a list of the Internet addresses of newsprint manufacturers and other Web sites most frequently cited in the White Paper.

2. Summary of Our Analysis and Our Main Conclusions

a. Introduction

This section provides a summary of our analysis and our main conclusions reached in Sections B through L.

b. Section B. Market Definition

In Section B, we conclude that the relevant product market is newsprint and that the relevant geographic market is NA. We also provide some evidence that East of the Rockies may be a relevant geographic market.

Our analysis shows that new Chinese capacity is likely to be largely if not entirely absorbed in Asia over the next couple of years and will not have a significant impact on the NA market. That is also the expectation of Abitibi, Bowater, and the PPPC. If there is an effect on the NA newsprint market from the new Chinese capacity, it is likely to be indirect. Some NA mills may be displaced from some Asian accounts by the new Chinese capacity. However, the effect on the NA newsprint market of any displacement is not likely to be significant. Abitibi and Bowater, who combined account for about 70% of exports from North America, expect strong export growth in 2007. Abitibi expects its exports from NA to grow by 10% in 2007 and Bowater expects its exports from NA to grow by 5% to 6% in 2007.

Attachment B to Section B provides additional analysis of the relation between uncoated groundwood specialty grades and newsprint. One analysis compares prices of four uncoated groundwood grades with the price of newsprint. A second analysis shows the estimated combined Bowater and Abitibi capacity share of several uncoated groundwood specialty segments.

c. Section C. Analysis of the Increase in Concentration That Would Result From the Proposed Merger

In Section C, we identify all of the suppliers to the NA newsprint market and estimate their 2006 newsprint capacity by mill. Based on estimated 2006 capacity, we show that the combined Abitibi-Bowater would have a capacity share of 45.0%. The premerger HHI is 1,380, the change in the HHI that would result from the merger is 962 and the post-merger HHI is 2,342. According to § 1.51(c) of the Merger Guidelines, markets with post-merger HHIs above 1,800 are highly concentrated and that HHIs of this magnitude create the presumption that the merger would be ''likely to create or enhance market power or facilitate its exercise.''

Based on estimated 2006 capacity, we also calculate capacity shares and HHIs for a possible East of the Rockies relevant newsprint market. We show that the combined Abitibi-Bowater would have a capacity share of 54.3%. The pre-merger HHI is 1,876, the change in the HHI that would result from the merger is 1,445 and the post-merger HHI is 3,321.

Attachment C to Section C contains tables showing 2006 estimated capacity by NA mill and the capacity share and HHI calculations for the NA newsprint market and the East of the Rockies market.

d. Section D. Analysis of the Increase in Concentration and Decrease in Capacity in the NA Newsprint Market 1995–2006

Due primarily to acquisitions by Abitibi and Bowater between 1995 and 2001, the NA newsprint market was transformed from an unconcentrated market in 1995 to a highly concentrated market in 2000 with Abitibi's acquisition of Donohue in April 2000. Bowater's acquisition of Alliance in 2001 and Norske Skog's acquisition of Pacifica, also in 2001, further increased concentration in an already highly concentrated market. This section analyzes the mergers and increase in concentration that occurred between 1995 and 2006.

Both John Weaver, President and CEO of Abitibi, and David Paterson, President and CEO of Bowater, have made presentations to investment analyst conferences describing the significant consolidation in the NA newsprint market and the roles of Abitibi and Bowater in achieving that consolidation. Slides from their presentations illustrating the increase in consolidation are included in this section.

This section also shows that there has been a 20.7% reduction in NA newsprint capacity between 1995 and 2006. Most of that reduction has occurred since 2002. Of the 16 firms that remain in the NA newsprint market today, Abitibi and Bowater combined account for 83.6% of that capacity reduction and Catalyst accounts for 15.9%. The other 13 firms account for 0.5%.

Attachment D to Section D contains tables showing how Abitibi and Bowater significantly increased their shares of newsprint capacity between 1995 and 2001 and tables showing that Abitibi and Bowater account for most of the reduction in NA newsprint capacity between 1995 and 2006, which primarily occurred after 2002.

e. Section E. NA Newsprint Demand and Supply

This section provides charts showing annual and quarterly data concerning NA newsprint demand and supply from 1999 through 2006. Almost all of the data are from standard industry sources PPPC and RISI. Chart E7 in Section E shows a steady decline in quarterly NA newsprint demand (quantity purchased) between 1999 and 2006. The chart also shows quarterly newsprint prices (30 lb., Eastern U.S.) over that same period. Chart E7 shows that while NA newsprint demand (quantity purchased) fell 18.0% between the third quarter of 2002 and the third quarter of 2006, the price of news print increased an aggregate of 49.0% over that same period.

Section E also analyzes the causes of the decline in newsprint consumption over time by U.S. daily newspapers. We conclude that the primary causes are declining newspaper circulation, declining advertising lineage, and newspaper efforts to reduce the consumption of newsprint by reducing the width of newspaper pages, by switching to lower basis weight paper, and by moving some content to the newspaper Web site. Declining circulation and advertising lineage should be regarded as exogenously shifting the newspapers' demand curve for newsprint downward. These declines are unrelated to the price of newsprint. While newspaper efforts to conserve on newsprint are largely in reaction to increasing newsprint prices, they should be regarded as efforts to permanently shift the demand curve for newsprint downward. If the price of newsprint drops significantly, it is improbable that newspapers will respond by increasing the width of newspaper pages or return content to the newspaper that was placed on Web sites. As long as the relative prices for higher and lower basis weight paper remain approximately the same, as seems likely, newspapers will have no incentive to switch back to higher basis weight paper.

f. Section F. Evidence From Presentations to Investment Analysts and Other Public Information That Abitibi and Bowater Have Used Their Control Over Newsprint Capacity and the Newsprint Industry Operating Rate To Significantly Raise the Price of Newsprint 2002 to 2006

As noted above, the price of newsprint increased 49.0% from the third quarter of 2002 to the third quarter of 2006 while the demand for newsprint (quantity demanded) declined 18.0%. Since the reductions in newsprint demand were largely caused by exogenous factors, the price of newsprint would be expected to decline holding the supply curve constant. However, the supply was not held constant during this period. Abitibi and Bowater responded to continual downward shifts in the demand curve by indefinitely idling and permanently closing their own capacity. Each downward shift in the demand curve was met with an upward shift in the supply curve sufficient to maintain maximum practical NA newsprint industry operating rates. At maximum practical operating rates price increases can successfully be imposed as they were throughout this four-year period by Abitibi and Bowater. The remaining firms in the industry generally followed the announced price increases of Abitibi and Bowater within a month or two.

John Weaver, President and CEO of Abitibi, has been describing this strategy in slide show presentations at investment analyst conferences since 2003. David Paterson, who became President and CEO of Bowater in April 2006, discussed this strategy at an investment analysts' conference in December 2006. Section F documents the AbitibiBowater strategy to use their control of capacity to raise the price of newsprint through an analysis of relevant slides presented and described by Weaver and Paterson at investment analyst conferences. This section also contains excerpts from an interview of Weaver that relate to this strategy.

g. Section G. An Analysis of Permanent Newsprint Capacity Reductions Between 2002 and 2006

Section G contains an analysis of permanent newsprint capacity reduction in NA between 2002 and 2006. The analysis shows that 18.0% of NA newsprint capacity was removed from the market between the end of 2000 and the end of 2006. Abitibi and Bowater combined were responsible for 80.0% of the permanent capacity removals and Catalyst was responsible for 7.3%. Of manufacturers that remain in the market today, Abitibi and Bowater combined account for 89.4% of the total capacity removals and Catalyst accounts for 8.1%. The other 13 remaining firms account for 2.5% of the capacity removals.

Through these permanent capacity removals, Abitibi reduced its own capacity by 30.7% and Bowater reduced its own capacity by 24.0%. Catalyst also reduced its newsprint capacity by a significant proportion—22.7%. The other 13 newsprint manufacturers that remain in the market today reduced their capacity by a combined 1.0%.

h. Section H. Four Articles by Two Newsprint Industry Experts Describing the Abitibi-Bowater Strategy to Raise Price by Closing Capacity

The Abitibi-Bowater strategy to use their control of capacity to raise newsprint prices is well known within the newsprint industry. Every newspaper newsprint buyer that we talked to described the Abitibi-Bowater strategy. This section analyzes four articles by two newsprint experts. These articles accurately describe the Abitibi-Bowater strategy. The titles of the articles are ''(1) New Paradigm: Newsprint Demand Falls, Prices Soar,'' (2) ''Will operating rates climb high enough in 2003 to support rising newsprint prices in the U.S.?,'' (3) ''Is rising newsprint demand necessary to support higher prices in 2004?,'' and (4) ''Newsprint producers must rely on supply reductions to support rising prices.''

i. Section I. Abitibi's Newsprint Capacity Closures 1999 to 2001

Between the third quarter of 1999 and the second quarter of 2001, newsprint prices increased 30.2% as shown in Section E6. Abitibi's permanent capacity removals immediately before and during that period were a significant cause of the price increases. Abitibi removed 450,000 metric tonnes of newsprint capacity from the market in 1999 or almost 3% of NA capacity. In conjunction with its acquisition of Donohue in April 2000, Abitibi announced that it would remove an additional 400,000 metric tonnes of newsprint capacity from the market during 2000 and 2001. Section I documents Abitibi's permanent newsprint capacity removals between 1999 and 2001.

j. Section J. A Comparison of Newsprint Prices With the Prices of Uncoated Groundwood Specialty Grades 3Q 1999 to 4Q 2006

Over the last four years there have been significant increases in energy, fiber, and transportation costs faced by NA newsprint manufacturers. Newsprint mills in Eastern Canada have been especially hard hit. In addition, the appreciation of the Canadian dollar relative to the U.S. dollar has effectively raised the cost of Canadian newsprint mills while lowering the cost of U.S. newsprint mills.

In this section, we compare the price of newsprint from the third quarter of 1999 to the second quarter of 2006 with the prices of four uncoated groundwood specialty grades. We find that the quarterly prices for newsprint as a percentage of its price in 3Q 1999 were significantly higher than the quarterly prices for three of the four uncoated groundwood specialty grades over the period 4Q 1999 to 2Q 2006. Based on these results, it is implausible that the increases in newsprint prices were caused by the increases in input prices. We find that the price trend of one uncoated groundwood specialty grade was similar to that of newsprint. It appears that Abitibi and Bowater are the dominant providers of that grade as well.

Section J presents a slide from an Abitibi presentation showing that Abitibi's variable cost of newsprint production has been virtually flat between 2001 and 2005. Since all or nearly all of the newsprint price increases over the period 2002 to 2006 were led by Abitibi, it seems unlikely that increases in Abitibi's input costs are a plausible justification for the price increases.

In Section J, we also calculate quarterly newsprint revenues over the period 3Q 1999 to 2Q 2006 based on actual NA newsprint consumption and actual newsprint prices. We then apply the quarter to quarter percentage price changes for each of the four uncoated groundwood specialty grades to the 3Q 1999 newsprint price and multiply the resulting adjusted newsprint prices by actual NA demand. For the three grades with percentage changes in prices significantly below the percentage changes in newsprint prices, total revenues over the period are reduced by $4.7 billion to $7.4 billion.

k. Section K. Dominant Firm Model

Based on our analysis in Sections B through J, we conclude that Abitibi and Bowater have acted as a joint dominant firm since at least the end of 2002 and perhaps since 2000. Abitibi and Bowater have jointly used capacity closures to raise the price of newsprint well above competitive levels. By removing capacity from the newsprint market in a timely way Abitibi and Bowater have been able to maintain maximum practical operating rates for the newsprint industry which has directly led to the price increases.

Section K presents a theoretical dominant firm model which formally explains the joint behavior of Abitibi and Bowater. Using current data, we use the dominant firm model to predict whether it would be profitable for a merged Abitibi-Bowater to further increase the price of newsprint through additional capacity closures. We show that it would be profitable for the merged firm to close additional capacity to achieve a 5% price increase.

Attachment K of Section K is a technical appendix in which the equations of the dominant firm model are formally derived.

l. Section L. Conclusions

Based on our analysis in Sections B through J, we conclude that the joint strategy of Abitibi and Bowater to close NA newsprint capacity to raise the price of newsprint is anticompetitive and has caused significant economic harm to U.S. daily newspapers and other NA purchasers of newsprint.

We predict that if the proposed merger is allowed to proceed, the ability of the merged entity to pursue the Abitibi-Bowater strategy of closing capacity to raise the price of newsprint will be strengthened. The market power of the merged firm will be more effectively employed than Abitibi and Bowater were able to do as separate but coordinating firms. The possibility that one of the two firms would stop coordinating, resulting in a price decrease, will be eliminated once the two firms are merged. The merged entity will have an increased incentive and ability to use its control over capacity to raise the price of newsprint significantly above competitive levels. Newsprint consumers, whom the antitrust laws are designed to protect, will suffer additional significant competitive harm.

3. A Note on Our Sources

In conducting our analysis of the competitive effects of the proposed AbitibiBowater merger, we relied on a wide variety of newsprint industry sources. Amongst the most important sources for data and other information concerning the NA newsprint industry are RISI and the Pulp and Paper Products Council (''PPPC''). RISI is the leading source of information about the pulp, paper, and forest products industries in NA and worldwide. The PPPC is a private organization that compiles demand and supply data and conducts forecasts for North American producers of pulp and paper products, including manufacturers of newsprint. We also relied on information that Abitibi and Bowater make publicly available on their Web sites as well as similar information on the Web sites of other newsprint manufacturers. We interviewed a number of U.S. newspaper newsprint buyers who gave us their perspective on the NA newsprint market and the likely competitive effects of the proposed merger. The NAA also provided us with data.

B. Product and Geographic Market Definition

1. Introduction

The principles of product and geographic market definition are set out in the U.S. Department of Justice (''DOJ'') and Federal Trade Commission (''FTC'') Horizontal Merger Guidelines (''Merger Guidelines'').[1] Following the Merger Guidelines methodology, product and geographic markets are defined from the perspective of consumers of the products of the merging firms. With respect to the proposed merger of Abitibi and Bowater, the two companies manufacture newsprint, uncoated groundwood specialty grades, and other pulp, paper, and forest products which they sell in NA and, in some cases, in other regions of the world. We have been asked to determine likely competitive effects of an Abitibi-Bowater merger on the sale of newsprint in NA. Our provisional product market is newsprint and our provisional geographic market is NA.[2]

2. A Description of Newsprint and Uncoated Groundwood Specialty Grades

a. Introduction

The main focus of this analysis is on the production and sale of newsprint in NA, but in applying the methodology of the Merger Guidelines to a provisional newsprint product market, it is necessary to consider demand and supply substitution possibilities regarding closely related uncoated groundwood specialty grades. While we do not reach any firm conclusions on relevant product markets within the uncoated groundwood specialty grade segment, we provide considerable information about the grade structure of that segment and the manufacturers of uncoated groundwood specialty grades in this section.

b. Newsprint

Newsprint is used to print newspapers, inserts, flyers and other advertising materials. In the U.S., the main purchasers of newsprint are newspaper publishers (both daily and non-daily) and commercial printers. In 2006, U.S. daily newspapers accounted for 80.0% of the U.S. consumption of newsprint.[3] U.S. demand for newsprint accounted for 88.9%

[1] The Merger Guidelines were issued on April 2, 1992 and revised on April 8, 1997.

[2] In Section B2 in Attachment B and Section J below, we provide some evidence that suggests that the proposed merger of Abitibi and Bowater may have an adverse competitive effect concerning at least one uncoated groundwood specialty grade.

[3] Source: December 2006 PPPC Flash Report.

of total NA demand for newsprint in 2006.[4] The PPPC estimated 2006 NA newsprint capacity at 12,625,000 metric tonnes.[5]

Newsprint is the lowest quality and least expensive uncoated groundwood paper. The main ingredient of newsprint is groundwood pulp, also known as mechanical pulp, recycled fiber (old newspapers (ONP) and old magazines (OMG)), or a combination of groundwood pulp and recycled fiber. Chemical pulp is usually added to the pulp furnish to improve runnability on printing presses.

Although newsprint must meet the exacting standards of modem printing presses, it is a commodity grade. About half the newsprint sold in NA today has a basis weight of 30 lb. (48.8 grams per square inch) and about half has a basis weight of 27.7 lb. (45.0 grams per square inch). Over the last four or five years newspapers have been gradually switching from the heavier basis weight newsprint to the lighter basis weight newsprint.[6]

c. Uncoated Groundwood Specialty Grades

(1). The Similarities and Differences Between Newsprint and Uncoated Groundwood Specialty Grades

To evaluate demand and supply substitution possibilities in a provisional newsprint market, it is necessary to describe in some detail the similarities and differences between newsprint and higher quality and higher value uncoated groundwood specialty grades. See Attachment B for (a) a comparison of the price of newsprint with the prices of four uncoated groundwood specialty grades and (b) Abitibi-Bowater HHIs based on estimated 2006 capacity and capacity shares by manufacturer for uncoated groundwood specialty grade segments.

Newsprint is a type of uncoated groundwood paper, but to distinguish newsprint from other uncoated groundwood grades, the paper industry refers to the other uncoated groundwood grades as uncoated groundwood specialty grades or higher value uncoated groundwood grades. Uncoated groundwood paper is also referred to as uncoated mechanical paper.

RISI estimated the 2006 NA capacity of uncoated groundwood specialty grades as 6,915,000 metric tonnes or somewhat more than half of 2006 NA newsprint capacity.[7] Some uncoated groundwood specialty grades are produced on machines that never produced newsprint, some uncoated groundwood specialty grades are produced on machines that have been converted from newsprint production, and some uncoated groundwood grades are produced on machines that also produce newsprint. Machines that produce both newsprint and uncoated groundwood specialty grades are called ''swing'' machines.

There are significant similarities in the production process for newsprint and the production processes for uncoated groundwood specialty grades. Indeed, many machines that currently produce uncoated groundwood specialty grades were formerly newsprint machines. The main ingredient of newsprint and uncoated groundwood specialty grades is pulp produced from some combination of groundwood pulp, recycled fiber, and chemical pulp. The grades vary by brightness, gloss, basis weight, opacity, and strength. Generally, newsprint has the lowest value combination of these characteristics. Higher value uncoated groundwood specialty grades are glossier and brighter than newsprint.

Slide 13 below, which is from Abitibi's presentation of financial results for Q1 2006 in June 2006, shows uncoated and coated printing paper grades.[8]

A graph appearing in this comment is not able to be reprinted here. Copies of the comment with the graph are available at the Department of Justice Antitrust Division Web site, *http://www.usdoj.gov/atr,* at the Antitrust Documents Group of the Department of Justice Antitrust Division, 450 Fifth Street, NW., Suite 1010, Washington, DC 20530, (202) 514–2481, and at the Office of the Clerk of the United States District Court for the District of Columbia, 333 Constitution Avenue, NW., Washington, DC 20001.

The slide is titled ''Paper Spectrum'' and states that ''Two key properties, brightness and gloss, define paper grade groups.'' The blue ovals in Slide 13 represent printing paper products produced by Abitibi. The blue ovals also identify the main uncoated groundwood specialty grades. The white ovals identify coated groundwood grades (all of coated #5 and some of coated #4) and coated free sheet grades (some of coated #4 and all of coated #3).[9] These coated grades are not produced by Abitibi. However, Bowater does produce #3, #4, and #5 coated paper.

The uncoated groundwood specialty grades can be divided into two categories: Glossy and non-glossy. The glossy grades are distinguished primarily by their degree of glossiness. The non-glossy grades are distinguished primarily by their degree of brightness. These distinctions are apparent in Slide 13.

Newsprint is a non-glossy grade. Newsprint is the least bright and, with the exception of the bulky book grade (ABIbook), the least smooth of the non-glossy grades. In terms of smoothness and brightness, the bulky book grade is closest to newsprint followed by the directory grade and the Hi-Brite grade (ABIbrite). Bulky book paper is typically used for paperback books and coloring books. Directory paper is somewhat brighter and smoother than newsprint and is also lighter (basis weight typically 22.1 lb. vs. 30 lb. or 27.1 lb. for newsprint) and is used primarily for the printing of telephone directories. The typical brightness of newsprint is 58. The brightness of Hi-Brite grades ranges from 65 to 75. Hi-Brite grades are used for printing inserts and flyers and in other similar commercial printing applications. The brightness of Super Hi-Brite grades (Abitibi grades EO, IO, and AO) ranges from 75 to 85.[10] Abitibi's Super Hi-Brite Grades compete with uncoated free sheet for the printing of books and may also be used in commercial printing applications.

The glossy uncoated groundwood specialty grades are supercalendered (SC) and soft nip calendered (SNC) grades. The gloss in SC and SNC grades is produced by adding clay fillers to the pulp furnish. After the SC paper roll comes off of the paper machine, gloss and smoothness are imparted to the paper by running the paper through a series of rolls called supercalenders. The gloss of SNC paper is typically achieved by an on-machine soft-nip calender. Slide 13 shows several SC grades (SCA, SCB+, SCB) which vary primarily by the degree of glossiness. SC and SCN grades are used in printing inserts, flyers, and catalogs. SC grades are also used in printing magazines.[11] The New York

[4] Source: December 2006 PPPC Flash Report. The PPPC Flash Report does not provide data on Canadian consumption of newsprint nor does it provide data on purchases of newsprint by Canadian daily newspapers. The difference between annual demand and annual consumption is the change in inventories from the prior December.

[5] See PPPC's March 29, 2006 NA Mechanical Printing Papers Forecast.

[6] There is a financial gain for a newspaper from switching to the lower basis weight paper, but it is not a large gain. The switch to the lower basis weight reduces a newspaper's consumption of newsprint by 8.5% holding the square footage of newsprint purchased constant, but the gain to the newspaper from the reduced consumption is mostly offset by the higher price that the newspaper must pay for the lower basis weight paper. Based on February newsprint prices, the net gain to a newspaper from switching would be a cost saving per metric tonne of about 2.7% or $16.94.

[7] See the 2006 RISI Fact and Price Book, p. 163. The PPPC forecast 2006 NA capacity for uncoated groundwood specialty grades as 6,360,000 metric tonnes. See the PPPC March 2006 forecast. We can account for some but not all of the difference between the RISI estimate and the PPPC forecast.

[8] This presentation is available on Abitibi's Web site under Investor Relations/Presentations & Webcasts.

[9] There are two additional coated free sheet grades not shown in Slide 13, coated #1 and coated #2.

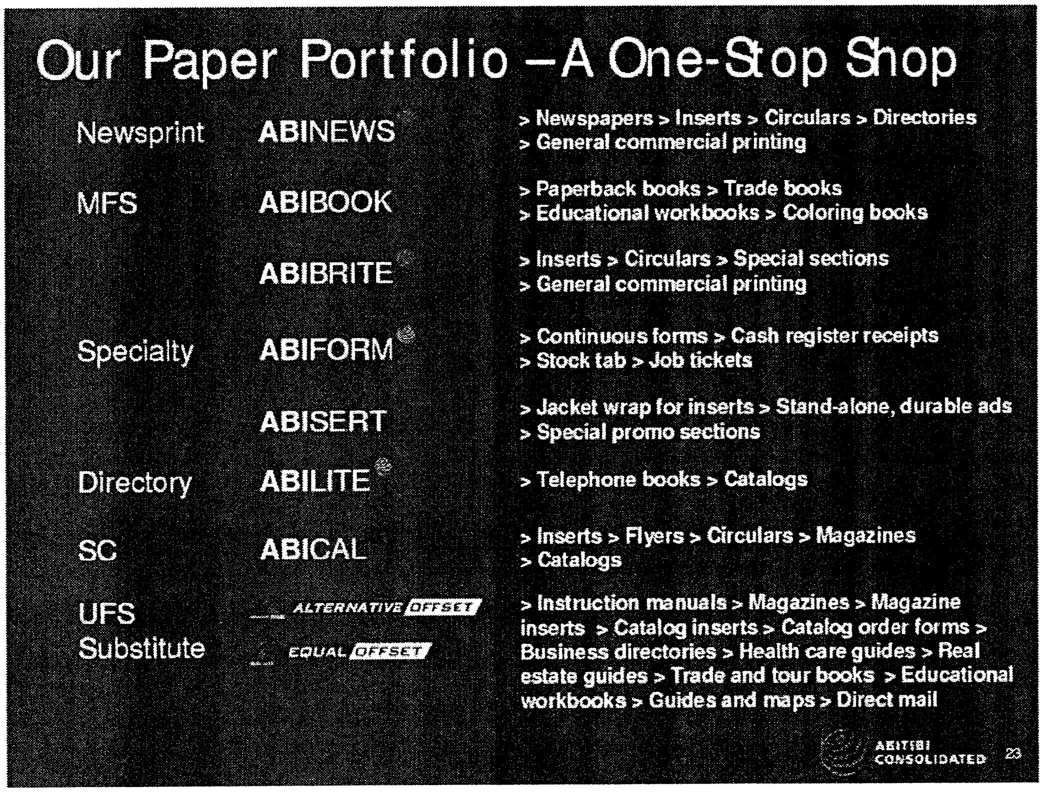
[10] We follow two practices of Abitibi in terminology and brightness ranges. Abitibi calls the Highbright and Super-bright grades Hi-Brites and Super Hi-Brites, respectively. Abitibi sells Hi-Brites in the brightness range 65–75 and Super Hi-Brites in the brightness range 75 and over. The PPPC categorization limits High-brights to the brightness range ≥65 to less than 75. Super-brights, according to the PPPC have a brightness level ≥75.

[11] The PPPC classifies uncoated groundwood specialty grades into three categories: High-Gloss, Standard, and Lightweight. The High-Gloss category includes all grades with a gloss ≥26, a smoothness ≤2.5 (the lower the smoothness measure, the smoother the surface of the paper), and a brightness ≥65. The grades included in this category ranked from highest to lowest gloss, highest to lowest smoothness, and highest to lowest brightness are SCA+, SCA, SCB, and SNC+. The low gloss SNC and SCC grades have a gloss ≥20 but less than 26, a smoothness measure greater than 2.5 and a brightness measure ≥60 ISO. The PPPC places these latter two grades in the Standard Category even though the other Standard Category grades are non-glossy. The Standard Category is defined primarily in terms of brightness and is not defined in terms of smoothness or gloss except for the SNC and SCC grades. The other grades in the Standard Category are Superbright (brightness ≥75 ISO), High-bright (brightness ≥65 but less than 75 ISO), Bulky book (brightness ≤60 ISO), and Other (no brightness requirement). All High-Gloss and Standard grades have a basis weight ≥40 grams per square meter. The Lightweight category contains one grade: Directory paper. Directory paper has a basis weight of less than 40 grams per square meter.

Times Sunday Magazine is printed on SC paper.

Slide 23 below is from the presentation of John Weaver, President and CEO of Abitibi, to a Credit Suisse First Boston Global Basics investment analysts conference on March 4, 2004.[12] This slide provides additional information on the relation between uncoated groundwood grade categories, the brand names of Abitibi products in each category, and the end uses served by each category.[13]

Slide 23: Abitibi Credit Suisse Presentation 3/4/04



Slide 12 below is from the presentation at the announcement of the AbitibiBowater merger.[14] Compared to Slide 13 discussed above, it provides a somewhat different perspective on the relation between the quality and value of uncoated and coated printing paper grades. It shows that newsprint is the lowest valued and lowest quality grade. The qualities indicated in the slide are brightness, opacity, paper gloss, print gloss, basis weight, and strength. Slide 12 shows that the two closest grades to newsprint in terms of value and quality are the Bulky Book and Hi-Brite grades.[15]

A graph appearing in this comment is not able to be reprinted here. Copies of the comment with the graph are available at the Department of Justice Antitrust Division Web site, *http://www.usdoj.gov/atr*, at the Antitrust Documents Group of the Department of Justice Antitrust Division, 450 Fifth Street, NW., Suite 1010, Washington, DC 20530, (202) 514–2481, and at the Office of the Clerk of the United States District Court for the District of Columbia, 333 Constitution Avenue, NW., Washington, DC 20001.

3. Product Market Definition

a. Likely Demand Substitution Responses by NA Newsprint Customers

Assuming a hypothetical monopolist of newsprint imposed ''a 'small but significant and nontransitory' increase in price'', would current newsprint customers switch in sufficient numbers to other paper grades to defeat the attempted price increase?[16] There are four pieces of evidence that suggest current newsprint customers are unlikely to switch to other grades of paper in sufficient numbers to defeat such an attempted price increase.

(1) Newsprint is the lowest quality and least expensive uncoated groundwood grade. Newsprint is designed to run on the printing presses of daily newspapers. We are unaware of any daily newspaper that has responded to increases in the price of newsprint in the past by switching to a higher quality and higher priced uncoated groundwood specialty grade. We believe it is implausible that in the future newspapers will switch to any higher quality and higher priced uncoated groundwood specialty grade if there is a relative increase in the price of newsprint. Every newspaper newsprint buyer we talked to said that if the price of newsprint rose 5% to 10% following the proposed merger they would have no alternative but to pay the increased price. They said they could not switch to other types of paper nor could they turn to suppliers outside of NA for any significant quantity of newsprint.

(2) Estimates of the elasticity of demand for newsprint have consistently been quite low (i.e., consistently quite inelastic). A 2004 study estimated that the U.S. demand

[12] This presentation is available on Abitibi's Web site under Investor Relations/Presentations & Webcasts.

[13] MFS means machine-finished surface. Hi-Brite and Bulky Book grades are MFS grades. All finishing to the surface of the paper is accomplished on the paper machine. In contrast, the surface finishing to SC grades is usually accomplished on off-machine supercalenders. The Abitibi Alternative Offset and Equal Offset grades are primarily sold as a substitute for uncoated free sheet (UFS) grades for the printing of books. The Alternative Offset and Equal Offset grades as well as the Innovative Offset grade (not shown in Slide 23) are also MFS grades.

[14] See the AbitibiBowater merger announcement presentation, ''Creating a Global Leader in Paper and Forest Products,'' January 29, 2007. This presentation is available on Abitibi's Web site under Investor Relations/Presentations & Webcasts.

[15] Directory paper is not shown in Slide 12. If it were included in Slide 12, it would probably be placed between the Bulky Book and Hi-Brite grades as is indicated in Slide 13.

[16] See the Merger Guidelines, § 1.1 Product Market Definition.

[17] While we have not attempted to estimate the demand elasticity for the NA newsprint market, we

elasticity for newsprint was 0.36.[17] A hypothetical monopolist could profitably raise the price 5% to 10% and considerably more in a market with a demand elasticity of 0.36.

(3) Over the period 2002 to 2006, average annual newsprint prices rose a total of 42.6%. Over that same period the consumption by U.S. daily newspapers declined by 13.6%. The ratio of the percentage decline in newsprint consumption by U.S. daily newspapers to the percentage increase in the price of newsprint was 0.32.[18] Daily newspapers account for 80% of U.S. newsprint consumption and non-daily newspapers and commercial printers account for the remaining 20%. Over the four-year period 2002–2006, newsprint consumption for this latter category of newsprint customers declined 15.2%. The absolute ratio of the percentage decline in newsprint consumption by U.S. non-daily newspapers and commercial printers to the percentage increase in the price of newsprint was 0.36. When total U.S. newsprint consumption is considered, the percentage decline over the four-year period was 13.9% and the absolute ratio of the percentage decline in newsprint consumption to the percentage increase in the price of newsprint was 0.33. These results are consistent with the estimated U.S. newsprint demand elasticity of 0.36 discussed immediately above.

(4) As shown in Table B1 in Attachment B, the prices of three major uncoated groundwood specialty grades are significantly above the price of newsprint even before the reduction in printing surface due to the switch to a heavier basis weight is taken into account. Taking the reduction in printing surface into account, as a newsprint customer rationally would, a buyer of 30.0 lb. newsprint who switched to 35 lb. SCB, Hi-Brite 65, or SCA, would face an equivalent price increase per metric tonne of 30.0 lb. newsprint ranging from 34.0% to 47.0% based on February 2007 prices.[19] Table B1 in Attachment B does show a financial gain to a newsprint buyer of 27.7 lb. from switching to 22.1 lb. directory paper. However, the information provided to us by newsprint buyers leads us to conclude that the lower basis weight and thinner directory paper would not be suitable for use in a newspaper or for running on newspaper printing presses. The lowest basis weight newsprint that we are aware of that is being used to print newspapers is 26.4 lb. (43.0 g/m^2) newsprint. Our understanding is that 26.4 lb. newsprint is used primarily if not entirely on flexographic printing presses and not on the predominant offset printing presses.[20]

b. Identifying Participants in the NA Newsprint Market

(1) Introduction

In Section C below we identify NA capacity to produce newsprint by manufacturer mill. This capacity participates in the NA newsprint market. According to the Merger Guidelines, it is also necessary to identify those firms that could participate in the NA newsprint market through a supply response.

The antitrust agencies' methodology for determining whether such capacity should be included is described in ''§ 1.32 Firms That Participate Through Supply Response'' of the Merger Guidelines. § 1.32 notes that the agencies ''will identify other firms [or capacity] not currently producing or selling the relevant product in the relevant area as participating in the relevant market if their inclusion would more accurately reflect probable supply responses. These firms are termed 'uncommitted entrants.' These supply responses must be likely to occur within one year and without the expenditure of significant sunk costs of entry and exit, in response to a 'small but significant and nontransitory' price increase.'' § 1.32 further notes that ''[i]f a firm [or capacity] has the technological capability to achieve such an uncommitted supply response, but likely would not (e.g., production would render such a response unprofitable), that firm [or capacity] will not be considered to be a market participant.''

The most likely type capacity for inclusion as a participant in the newsprint market would be uncoated groundwood specialty grades produced on so-called ''swing'' machines. The next most likely type of capacity would be newsprint machines that have been converted to the exclusive production of groundwood specialty grades without the expenditure of capital funds to rebuild the machine, to add or reconfigure pulping capability, or add off-machine finishing equipment. In cases where the conversion of a newsprint machine to an uncoated groundwood specialty grade has required a significant expenditure of capital funds, it is the least likely that that capacity should be included as a participant in the newsprint market. Similar analytical considerations apply to uncoated groundwood specialty machines that have never produced newsprint.

(2) Swing Machines

A certain amount of newsprint is produced on so-called ''swing'' machines. That is, the same machine is used to produce both newsprint and one or more higher quality and higher priced uncoated groundwood specialty grades. For example, some manufacturers may be able to produce Hi-Brite grades and Directory paper on the same machine as newsprint. It is likely that Bulky Book paper can also be produced on the same machine as newsprint. The Catalyst 2006 annual report, p. 9, states that ''Capacities in the above table can vary as the Company is able to switch production between products, particularly newsprint, directory, and machine-finished [i.e., Hi-Brite] uncoated grades.''

Bowater's 2005 Annual Report states on p. 4 that it has newsprint and uncoated groundwood swing machines at the following mills: Calhoun, TN, Thunder Bay, ON, Gatineau, QC, and Dalhousie, NB. Abitibi's 2005 Annual Report, p. 10, indicates that Abitibi may have swing newsprint machines at its Belgo, QC, Iroquois Falls, ON, and Grand Falls, NL mills. Since the annual report does not provide a capacity breakdown by machine, it cannot be determined from the table on p. 10 which, if any, of the machines at these mills are producing both newsprint and uncoated groundwood paper. The annual report also indicates that Abitibi's Fort William mill in Thunder Bay, ON has a newsprint and uncoated groundwood swing machine. The mill's only paper machine is shown with a capacity of 107,000 metric tonnes for newsprint and 38,000 metric tonnes for uncoated groundwood grades.

The PPPC 2003 NA Newsprint Capacity Survey (March 3, 2003) states on p. 2 that at the time of the survey there were 17 machines in NA that were classified as ''swing'' machines. The PPPC noted that the

note that an article in 2004 reported on an analysis that estimated the elasticity of the U.S. demand for newsprint at 0.36 taking into account structural changes in U.S. demand. See Jari Kuuluvainen, ''Structural Change in U.S. Newsprint Demand: GDP and Price Elasticities,'' University of Helsinki, Department of Forest Economics, Reports #34, 2004, p. 8. A demand elasticity of 0.36 is in the same range as demand elasticities reported in earlier articles. An article in 1997 reported the demand elasticity in NA at 0.22. Other estimates cited in this article have been about twice as large. Estimates of demand elasticity vary from 0.22 to 0.44. These estimates all indicate a fairly inelastic demand curve for newsprint. See Ylbing Zhang and Joseph Buongiorno, ''Communication Media and Demand for Printing and Publishing Papers in the United States,'' Forest Science 43(3) (August) 1997, p. 372. The results of our analysis of the proposed Abitibi-Bowater merger are consistent with an inelastic demand curve.

[18] The ratio is expressed as an absolute number. Sources: PPPC NA Monthly Newsprint Bulletins and PPPC Flash Reports. As discussed in Section E below, much of the decline in the demand of U.S. daily newspapers has not been caused by the rise in newsprint prices.

[19] RISI Pulp & Paper Week does not publish prices for the lowest quality uncoated groundwood specialty glossy grades, SNC and SCC. Abitibi-Bowater Slide 12 above, which plots quality against the value of uncoated groundwood grades, placed SNC and SCC in between SCB and Hi-Brite in terms of value and quality. In Table B1 in Attachment B, 35 lb. SCB is priced 8.8% below the price of 35 lb. SCA. If 35. lb. SNC and SCC grades were priced 8.8% below the price of 35 lb. SCB, their prices would still be 22.1% above the price of 30 lb. newsprint.

[20] According to RISI 2006 Fact and Price Book, p. 145, offset presses account for 85% of the presses at U.S. daily newspapers, letterpress presses account for 10%, and flexographic presses account for 5%.

[1] The Merger Guidelines were issued on April 2, 1992 and revised on April 8, 1997.

[19] RISI Pulp & Paper Week does not publish prices for the lowest quality uncoated groundwood specialty glossy grades, SNC and SCC. Abitibi-Bowater Slide 12 above, which plots quality against the value of uncoated groundwood grades, placed SNC and SCC in between SCB and Hi-Brite in terms of value and quality. In Table B1 in Attachment B, 35 lb. SCB is priced 8.8% below the price of 35 lb. SCA. If 35. lb. SNC and SCC grades were priced 8.8% below the price of 35 lb. SCB, their prices would still be 22.1% above the price of 30 lb. newsprint.

[20] According to RISI 2006 Fact and Price Book, p. 145, offset presses account for 85% of the presses at U.S. daily newspapers, letterpress presses account for 10%, and flexographic presses account for 5%.

number of swing machines had been declining due to increased machine specialization and the conversion of newsprint machines to other grades. We do not know the total current capacity of NA ''swing'' machines by NA mill, but believe that the newsprint capacity of each swing machine is reported by manufacturers to the PPPC in proportion to the actual or anticipated production of newsprint on the machine.

As the Merger Guidelines suggest, it would be necessary to determine if it would be profitable to switch the capacity on swing machines used to make uncoated groundwood specialty grades to newsprint production in the event of an increase in the price of newsprint. If it would be profitable, then the capacity of the swing machine used to make uncoated groundwood specialty grades should be included as participating in the newsprint market through a supply response. If it would not be profitable, then that capacity would not be included. We are aware of no publicly-available information that could be used to address this issue.

(3) Machines That Have Been Converted From Newsprint Production

In contrast to the use of swing machines to produce both newsprint and uncoated groundwood specialty grades, some newsprint manufacturers have converted newsprint machines to the production of higher quality and higher priced uncoated groundwood grades (e.g., SC grades). That is, these machines are no longer used to manufacture newsprint. In some cases, these machine conversions required significant investment expenditures and non-trivial down times. To the extent that it would not be profitable to produce newsprint on a converted newsprint machine ''in response to a 'small but significant and nontransitory' price increase,'' the capacity of that machine should not be regarded as participating in the market (supply response within one year) or as en entrant (entry within two years). See § 1.32 as discussed above and ''§ 3 Entry Analysis'' of the Merger Guidelines. In some cases, however, it may be profitable to produce newsprint on a converted newsprint machine ''in response to a 'small but significant and nontransitory' price increase.'' This analysis can also be applied to machines that have never produced newsprint but are used to produce closely related uncoated groundwood specialty grades.

Below we provide two examples of recent conversions by Abitibi from newsprint to uncoated groundwood specialty grades. In 2005, Abitibi removed about 118,000 metric tonnes of newsprint capacity by converting a newsprint machine at its Shawinigan (Belgo). QC mill to Hi-Brite production. The conversion consisted of an increase in bleaching capacity at the Belgo mill. The cost was about C$15 million.[21] It seems likely that the Belgo machine could still technically produce newsprint. Hi-Brites are essentially brighter newsprint, once called improved newsprint. If the Belgo mill were owned by a firm that could not influence the price of newsprint through the removal of capacity from the market, that firm potentially might have the incentive to switch some of the capacity of the converted machine back to newsprint in response to a relative increase in the price of newsprint. To determine whether that incentive exists requires knowledge of alternative profitability scenarios involving different mixes of Hi-Brite and newsprint production. Abitibi is quite unlikely to use the Belgo machine to produce newsprint in the event of an increase in the price of newsprint since part of Abitibi's objective in converting the machine to Hi-Brites was likely to remove newsprint capacity from the newsprint market in order to raise the price of newsprint.

In 2003 and 2004, Abitibi converted about 170,000 metric tonnes of newsprint capacity at its Alma, QC mill to the production of Super Hi-Brites. The total cost of the conversion exceeded C$200 million. The conversion likely included an expansion of bleaching capacity and a rebuild of the paper machine. It seems unlikely that this machine would be used to produce newsprint under any foreseeable circumstances.

In 2002, Great Northern Paper rebuilt its No. 11 uncoated groundwood specialty machine at its Millinocket, ME at a cost of $103 million. After the mill was sold to Katahdin in 2003, the new owners made additional improvements to the machine to enable it to produce high quality SCA and SCA+ paper for magazines and catalogs. The machine was down 17 months before being restarted in 2004. Part of this downtime was due to the bankruptcy of Great Northern.[22] We do not know if the investment and lost downtime required to convert the Katahdin machine to SC paper is representative nor do we know if SC machines are technically capable of producing newsprint. Assuming SC machines are technically capable of producing newsprint, it seems unlikely to us that owners of SC capacity would find it profitable to divert part of their SC capacity to the production of newsprint in the absence of a substantial increase in the relative price of newsprint.[23]

Referring to Slide 13 in Section B.2.b.(1) above, the most likely capacity to be converted to the production of newsprint in the event of a relative increase in the price of newsprint would be Directory, Bulky Book, and Hi-Brite. The machines used to produce these grades are technically closest to the machines used to produce newsprint. As discussed above, the machines used to produce SC grades and Super Hi-Brite grades have been significantly upgraded from newsprint machines or from lower quality uncoated groundwood grades. It seems unlikely that it would be profitable to use these machines to produce newsprint even if the price of newsprint were increased significantly.

Directory paper is sold under one- to three-year contracts that specify both price and volume. About 80% to 90% of directory paper is sold under contract. The other 10% to 20% is sold on the spot market. The main buyers of Directory paper are RBOCs and independent publishers of telephone directories. The demand for Directory paper has shown strong growth since 2004 and contract price increases of 10% are expected in 2007.[24] It seems unlikely to us that owners of Directory capacity could divert Directory capacity that is being sold under contract. To the extent that some owners of Directory capacity have excess capacity, they might use that capacity to produce newsprint in the event of a relative increase in the price of newsprint. However, with a growing demand for Directory paper, the use of that capacity to produce newsprint is likely to be short-lived.

As shown in Table B–7 in Attachment B, Abitibi and Bowater control 76.5% of the NA Hi-Brite capacity and 100% of the Hi-Brite capacity East of the Rockies. Abitibi and Bowater also appear to control most of the Bulky Book capacity although we were not able to obtain a Bulky Book capacity figure for Bowater.

(4) Machines Producing Uncoated Groundwood Specialty Grades That Have Never Produced Newsprint

There are at least three machines producing uncoated groundwood specialty grades that have been designed specifically to produce those grades. These are high-speed, high-capacity machines use to produce high-quality SC paper. These machines are owned by Stora Enso and Madison paper. It is highly unlikely that these machines would ever be used to produce newsprint under any conceivable circumstances.

c. Conclusions Regarding Product Market Definition

(1) Newsprint Market

Based on our analysis in Section B.3.a. above of the likelihood of demand substitution in the event of a relative increase in the price of newsprint, we conclude that the relevant product market is no larger than newsprint.

(2) Participating Manufacturers in the NA Newsprint Market

Current newsprint suppliers are participants in the NA newsprint market.[25] Based on our analysis in Section B.3.b., we considered whether it was likely that capacity used to manufacture uncoated groundwood grades could be considered likely participants through a supply response following the Merger Guidelines

[21] Sources: Abitibi 2005 Annual Report p. 28, Abitibi 2004 Annual Report, p. 42, and Abitibi-Bowater Merger Announcement Presentation, p. 17.

[22] Source: ''Katahdin Paper, The Maine Chance,'' Manufacturing in Action, September 2004. While, strictly speaking, this machine was not converted from newsprint to SC grades, it seems likely that prior to the conversion the machine was producing paper close to the quality of newsprint.

[23] SNC grades are typically made on former newsprint machines with an on-machine soft-nip calendar added to the paper machine. SNC grades are comparable to SCB and SCC grades as discussed above. While technically they likely could produce newsprint, it seems unlikely that an SNC machine that has switched away from newsprint production would switch back to newsprint production in the event of a 5% to 10% increase in the price of newsprint relative to the price of SNC grades. Both Abitibi and Bowater manufacture SNC grades.

[24] RISI Fact & Price Book, pp. 168–169.

[25] In Section B.4 below, we consider whether the geographic market is narrower or broader than NA.

methodology. Our conclusion is that there is undoubtedly some swing capacity that should be included as likely participants in the NA newsprint market. There are no public data available to quantify the amount of swing capacity that should be included but a significant portion of that swing capacity is likely controlled by Abitibi and Bowater.

Abitibi and Bowater also control a very large portion of Bulky Book and Hi-Brite, the next most likely capacity to participate in the NA newsprint market, and control virtually all of that capacity East of the Rockies.[26]

Several of the newspaper newsprint buyers we interviewed said that they were unaware of any newsprint machine that had been converted to production of uncoated groundwood specialty grades that had subsequently been converted back to the production of newsprint. Given the steady decline in the NA demand for newsprint since at least 1999 this is not a surprising result. As shown in Section E2 below, NA demand (quantity purchased) for newsprint has declined every year from 1999 to 2006 for a total decline of 25.5% over that period.[27]

We conclude that the participants in the NA newsprint market are the current NA newsprint producers. These 16 NA newsprint producers are identified in Tables C1 and C2 attached to Section C1.

4. Geographic Market Definition

a. Introduction

The methodology for geographic market definition is described in § 1.2 of the Merger Guidelines. The methodology is similar to the methodology used to define relevant product markets.

Absent price discrimination, the Agency will delineate the geographic market to be a region such that a hypothetical monopolist that was the only present or future producer of the relevant product at locations in that region would profitably impose at least a ''small but significant and nontransitory'' increase in price, holding constant the terms of sale for all products produced elsewhere. That is, assuming that buyers likely would respond to a price increase on products produced within the tentatively identified region only by shifting to products produced at locations of production outside the region, what would happen? [28]

In this section we consider whether the relevant geographic market is narrower or broader than our provisional geographic market of NA.

b. Is the Relevant Geographic Market Narrower Than NA?

There is evidence that the relevant market may be narrower than NA. Based on interviews with buyers of newsprint for newspaper publishers, newsprint mills located West of the Rockies rarely ship to customers located East of the Rockies and vice versa.[29] According to these buyers, the high cost to transport newsprint from West Coast newsprint mill locations to customers located East of the Rockies makes newsprint produced in West Coast mills non-competitive with newsprint manufactured at mills located East of the Rockies. Even if there were a relative 5% to 10% increase in the price of newsprint sold East of the Rockies, these buyers believe that it would not be profitable for West Coast mills to begin shipping newsprint in significant quantities to customers located East of the Rockies.

We do not have the information necessary to determine if newsprint sold to customers located East of the Rockies is a relevant geographic market for the purposes of assessing the competitive effects of the merger. Primary sources of information on whether such a geographic market can be properly defined would include West Coast newsprint mills and customers located East of the Rockies. An analysis of comparative freight rates from West Coast mills and mills located East of the Rockies to East of the Rockies newsprint customers would also be useful in determining whether there is a relevant East of the Rockies market. For the purposes of calculating capacity shares and HHIs in Section C below, it is assumed that East of the Rockies is a relevant geographic market.

c. Is the Relevant Geographic Market Broader Than NA?

(1) Introduction

There has been considerable speculation in the trade press concerning the likely impact of new Chinese newsprint capacity on NA purchasers of newsprint and NA newsprint mills. While some buyers of newsprint have shown an interest in newsprint from China, it appears from press reports that the only newsprint that they have bought from Chinese mills is for test runs. There is no current indication that they intend to buy significant amounts of newsprint from China within the next one to two years. To the extent that there are imports of newsprint from China in the near-term, it is likely that the phenomena will be short-lived.

If there is an effect of the new Chinese capacity on NA newsprint mills, it will likely be on the displacement of export sales from NA mills to current customers located in Asia. It is likely that the new Chinese newsprint capacity will be largely absorbed in Asia over the next several years.

(2) Current and Past NA Import Levels

Imports of newsprint into NA have not been a significant source of supply for NA newspaper publishers and other NA purchasers of newsprint. In 1999, imports accounted for only 3.3% of NA newsprint purchases.[30] Since 1999, imports have accounted for 2.0% or less of NA purchases. See Section E2 below. Imports have been falling since 2004 both in absolute quantities and as a percentage of NA demand. In 2006, imports accounted for just 1.5% of NA newsprint purchases. For the first two months of 2007, imports have fallen 56.1% compared to the first two months of 2006. Imports accounted for 0.7% of NA newsprint purchases for the first two months of 2007.[31]

In the latter part of the 1990s, there was an increase in NA imports to about 555,000 metric tonnes in 1998 (about 4.3% of NA consumption).[32] Almost all of the increase was due to imports from South Korea and Russia.

There were a number of unique circumstances that accounted for the increase in imports from South Korea to NA. These include (1) significant new efficient capacity coming on line in South Korea; (2) a very steep devaluation of the South Korean won relative to the U.S. dollar; (3) a significant recession in South Korea and Asia which reduced Asian demand for newsprint; and (4) strikes at newsprint mills in British Columbia which removed about 1 million metric tonnes of annual newsprint capacity from the NA market.[33] As the South Korean and Asian economies began to recover, as the South Korean won began to appreciate against the U.S. dollar, and as the strikes at the British Columbia mills were settled, the new South Korean capacity was largely absorbed in Asia. NA publishers, however, have continued to import some newsprint from South Korea, although at significantly reduced amounts from the 1998 peak. NA imports from all sources, including South Korea and Russia, declined from the 1998 peak of 555,000 metric tonnes to about 221,000 metric tonnes in 2000. NA imports have remained at the 2000 level or slightly below until declining to 142,000 metric tonnes in 2006.

Imports from Russia also increased during the latter part of the 1990's though not as significantly as imports from South Korea. Newspaper publishers found that newsprint from Russian mills was unreliable both in terms of quality and delivery. As a consequence, imports from Russia declined to a low level by 2000.

[26] As explained in Section B.3.b.(3) above, it is unlikely that manufacturers of Directory paper would divert more than a small amount of Directory capacity to the production of newsprint and that diversion is likely to be short-lived.

[27] The last de novo entry into the NA American newsprint market was in 1990 by Atlantic Newsprint and Alberta Newsprint. Inland Empire installed a small newsprint machine in 2001 to replace an old newsprint machine. That machine is the only new newsprint machine installed in NA since 1991. Source: ''Newsprint: A Pulp & Paper Market Focus Book (1999), pp. 19–20. These facts and the 25.5% decline in NA consumption since 1999 indicate that de novo entry into this high capital cost industry is unlikely for the foreseeable future.

[28] See the Merger Guidelines, § 1.21 General Standards.

[29] This evidence also implies that newsprint sold to customers West of the Rockies may also be a relevant market. Since Bowater is not a majority owner of any mill on the West Coast the merger would not have a competitive effect in a West of the Rockies newsprint market. Bowater does have a 40% minority interest in the Ponderay Newsprint mill, which is located in Usk, WA. Abitibi does own two newsprint mills West of the Rockies. These mills are located in Snowflake, AZ and Mackenzie, BC.

[30] Sources: December 2006 and December 2005 PPPC NA Newsprint Statistics-Flash Report (''Flash Report'') and December 2001–2004 PPPC NA Newsprint Statistics Monthly Bulletin (''PPPC Monthly Bulletin'').

[31] Source: February 2007 Flash Report.

[32] Sources: RISI 2006 Fact and Price Book, p. 142, and Pulp & Paper 2000 NA Factbook, p. 190.

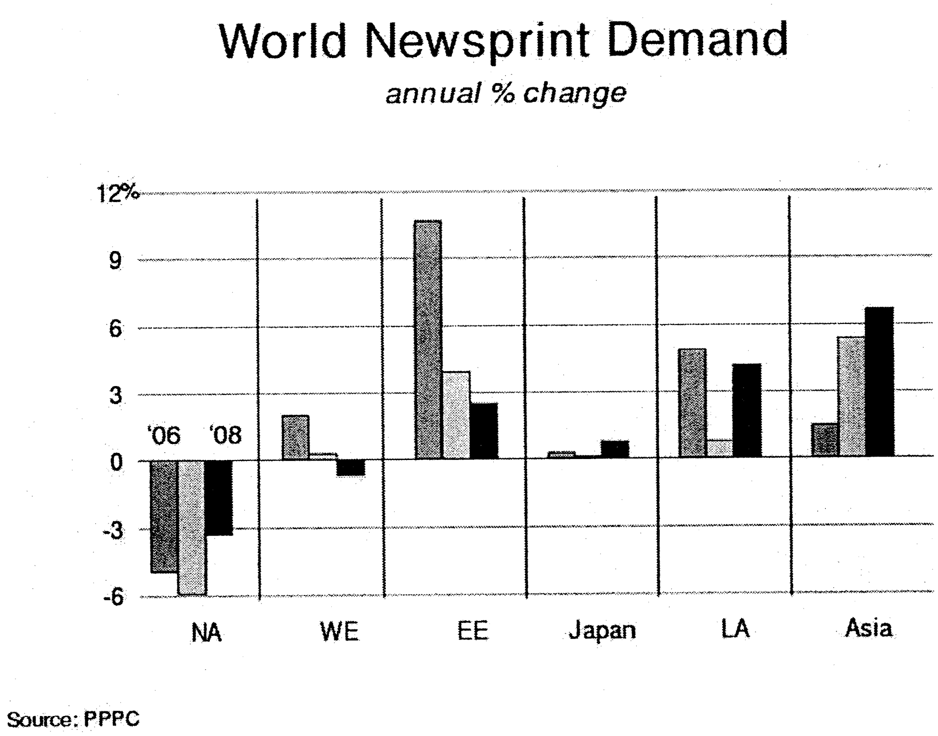
[33] See Economists Incorporated's submission to DOJ concerning the proposed acquisition of Alliance by Bowater, dated May 7, 2001, pp. 15–18.

(3) The Likelihood of Imports From China

(a) Projected Growth in Global Newsprint Demand

Martine Hamel, head of market research for the PPPC, estimates growth in newsprint demand for all regions of the world over the period 2006 to 2008.[34] See Slide 39 below. The slide shows negative growth for NA for all three years. Western Europe is expected to have positive growth in 2006 and 2007 before experiencing negative growth in 2008. All other regions are shown with positive growth for all three years.

Slide 39: PPPC 2006 NPA/NAA Presentation

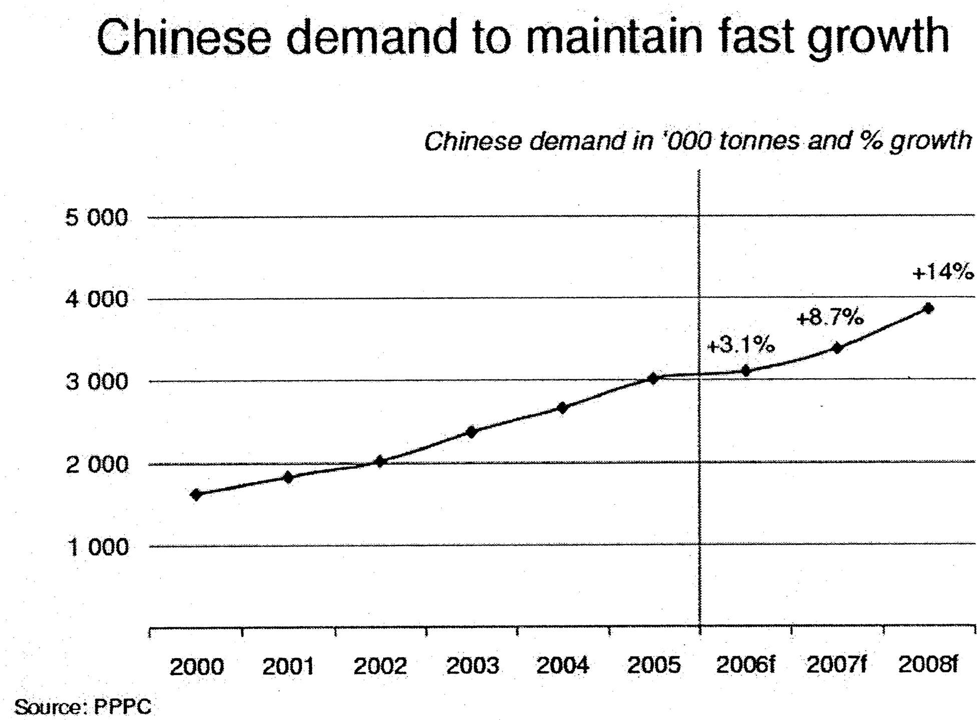


(b) Projected Growth in Chinese and Other Asian Newsprint Demand

Slide 36 below from Martine Hamel's presentation shows the forecast growth of Chinese demand for newsprint. Chinese newsprint demand is projected to increase by 3.1% in 2006, 8.7% in 2007, and 14.0% in 2008.

[34] Source: At the November 2, 2006 joint NPA/NAA Newsprint Conference, Martine Hamel, VP, COO and head of market research for the PPPC, presented a report titled ''Review and Forecast of Newsprint Demand and Supply'' (''PPPC 2006 NPA/NAA Presentation''). The Presentation reviews global demand and supply of newsprint for the first nine months of 2006 and earlier years and forecasts global demand and supply of newsprint for the period 2006–2008.

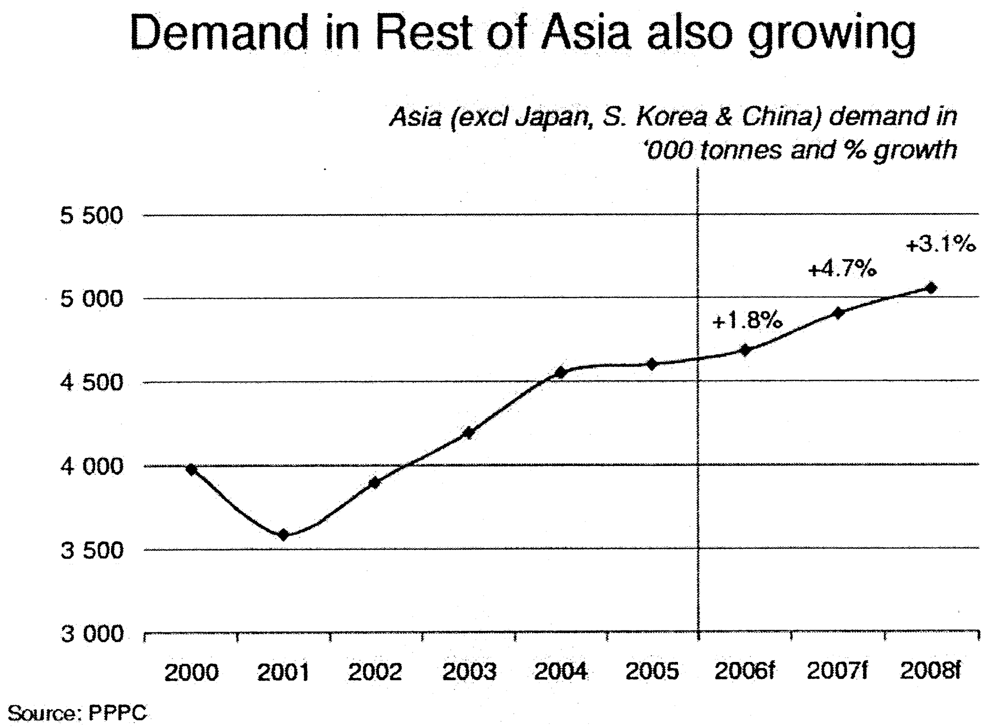
Slide 36: PPPC 2006 NPA/NAA Presentation



Slide 37 shows growing demand in the rest of Asia (excludes Japan, South Korea, and China). The projected demand growth in China and the rest of Asia [35] was likely the primary reason for the installation of the new newsprint capacity in China.

[35] We assume that the growth projections in Slides 36, 37, and 39 above correspond to similar projections that were available to Chinese officials responsible for investments in new newsprint capacity.

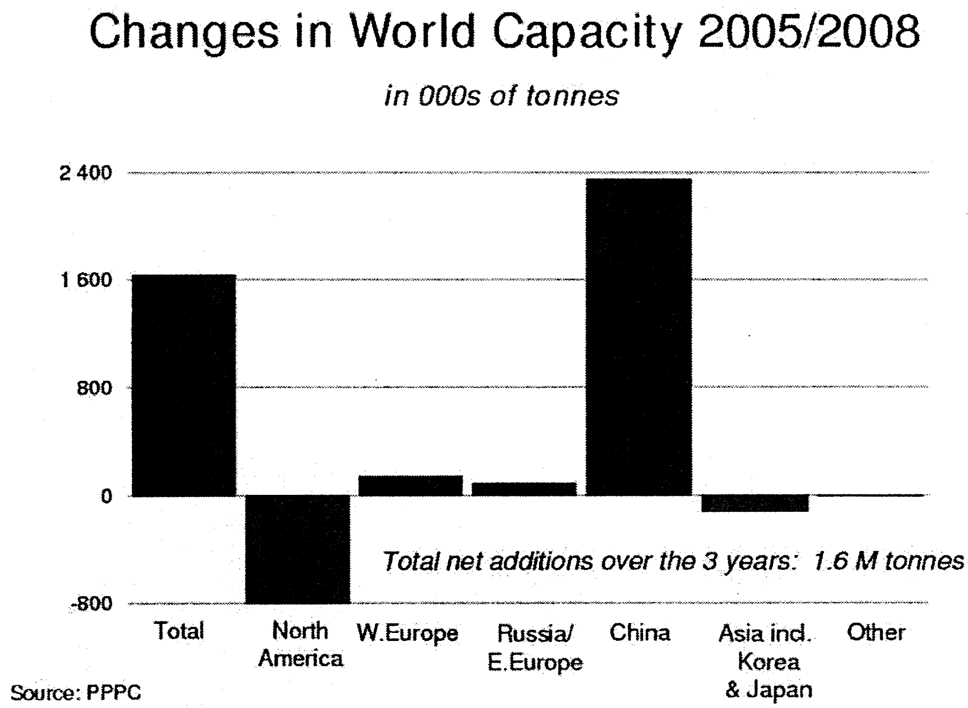
Slide 37: PPPC 2006 NPA/NAA Presentation



(c) Projected Growth in Global Newsprint Supply

Slide 42 below from Martine Hamel's presentation shows that virtually all of the growth in global newsprint capacity over the period 2005–2008, is expected to come from the installation of new Chinese capacity. This growth in Chinese newsprint capacity is partially offset by reductions in NA newsprint capacity.

Slide 37: PPPC 2006 NPA/NAA Presentation

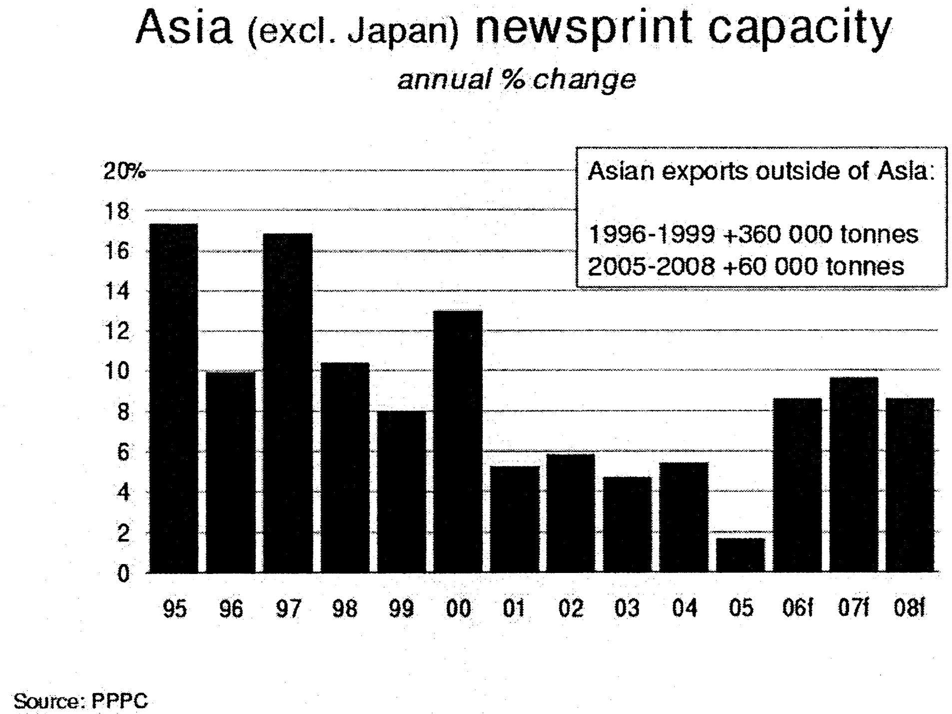


(d) Evidence From the PPPC 2006 NPA/NAA Presentation That the New Chinese Newsprint Capacity Is Expected To Be Mostly Absorbed in Asia Over the Next Several Years

Martine Hamel of the PPPC also estimates that exports from Asia to other regions of the world will total 60,000 metric tonnes per year over the period 2005 to 2008.[36] See Slide 49 below. The slide shows that despite the significant increase in Chinese newsprint capacity, exports from Asia to other regions of the world are not expected to be significant.

[36] While Slide 49 does not specify whether the 60,000 metric tonnes of exports from Asia is per year or for the entire four-year period, we conservatively assume that the figure is an annual average estimate.

Slide 49: PPPC 2006 NPA/NAA Presentation



We expect that many of these exports from Asia would be to regions other than NA since, as shown in Slide 39 above, demand in those regions is growing while demand in NA is decreasing significantly. To the extent there were exports from Asia in 2005 and 2006, these exports did not have a significant impact on the NA newsprint market since imports into NA in 2005 and 2006 actually declined each year from the prior year.

Slide 49 also shows exports from Asia during the period 1996 to 1999 at a rate of 360,000 metric tonnes per year. For five of the six years 1995 to 2000, Asian newsprint capacity increased by a greater percentage than is projected for the three years 2006 to 2008. As was discussed above, this capacity came on line at the same time that the Asian region was undergoing a steep economic decline and steep decline in the demand for newsprint. The new Chinese capacity is coming on line at a time of significant growth in demand for newsprint in China and in the rest of Asia. See Slides 36 and 37 above. This significant projected growth in newsprint demand increases the likelihood that the new Chinese capacity will be absorbed in Asia over the next several years. This projected growth was undoubtedly a major factor in the PPPC's forecast of 60,000 metric tonnes of exports per year from Asia for the period 2005–2008, compared to the much higher export total of 360,000 metric tonnes per year from Asia that occurred over the period 1996–1999.

(e) Evidence From the Heads of Abitibi and Bowater That the New Chinese Newsprint Capacity Is Expected To Be Mostly Absorbed in Asia Over the Next Several Years

The heads of Abitibi and Bowater also expect that the new Chinese capacity will be absorbed in Asia over the next several years.

John Weaver, President and CEO of Abitibi, gave a presentation to Citigroup's 11th Annual Global Pulp & Forest Products Conference on December 7, 2006 (''Citigroup Conference''). During the Q&A that followed his slide show presentation, Weaver was asked about the impact of the new Chinese newsprint capacity on the global and NA newsprint markets.[37]

Weaver begins his response by saying that ''There will be a trend in the international market in [2007] but it won't be China.'' He said that he does not know of any deal that a publisher has signed that is not a trial. He said that there had been only 242 tonnes of imports from China so far in 2006.

''So I don't really expect to see any significant imports of Chinese paper to North America [in 2007],'' he said. He also said that based on most of the calculations he has seen, including those by Abitibi, ''it's hard to see the economic benefit of the Chinese coming.''[38]

He said that he does expect there will be some Chinese exports. He specifically mentions that Abitibi has seen Chinese exports in India. He said, ''I really feel that the phenomena of Chinese oversupply may be short-lived.'' He gives several reasons. He mentions 1.7% growth in global newsprint demand. He also says that the Chinese government recently announced that they would close their smaller polluting newsprint mills in 2007 and 2008, which would reduce the amount of Chinese newsprint capacity.

David Paterson, President and CEO of Bowater, also gave a presentation at the 2006 Citigroup Conference. Paterson addressed the issue of new Chinese capacity during his slide show presentation (Slides 14 and 15).[39]

[37] We have provided DOJ with a copy of the audio recording of Weaver's remarks at the Citigroup Conference. The copy is a .wma file and can be played on Windows Media Player (''WMP''). If the copy is played on WMP, the time expressed as minutes and seconds is shown as the recording proceeds. Weaver's discussion of the possibility of imports from the new Chinese capacity begins at 24:04 into the recording. We have also provided DOJ with a copy of the slide show that Weaver presented to the Citigroup Conference. The slide show of Weaver's presentation is available under Investor Relations/Presentations & Webcasts on Abitibi's Web site. According to Abitibi's Web site, the audio recording of Weaver's remarks at the Citigroup Conference is no longer available on the Web site.

[38] While he does not elaborate further on this statement, he appears to be saying that it would be more profitable for the Chinese mills to sell their newsprint closer to home rather than to incur the additional freight costs to ship newsprint to NA.

[39] We have provided DOJ with a copy of the audio recording of Paterson's remarks at the Citigroup Conference. The copy is a .wma file and can be played on Windows Media Player (''WMP''). If the copy is played on WMP, the time expressed as minutes and seconds is shown as the recording proceeds. Paterson's discussion of the possibility of imports resulting from the new Chinese capacity begins at 11:59 into the recording. We have also provided DOJ with a copy of the slide show that Paterson presented to the Citigroup Conference. The slide show of Paterson's presentation is available under Investor Relations/Presentations on Bowater's Web site. According to Bowater's Web site, the audio recording of Paterson's remarks at

He notes the strong growth in demand globally for newsprint except in the U.S. He also notes the strong growth in the demand for newsprint in China.

He asks, ''Where will those Chinese tonnes go as they start up and come into the market?'' Paterson said Bowater believes they will flow into Asia and that there will be some coming into NA. He said that U.S. newspapers were talking openly about importing newsprint from China into the east coast and the west coast of the U.S. But, he said, ''Having said that, I think most of the tonnes will show up in places like Singapore, Malaysia, India, Brazil. These are all high growth markets.'' He said that newsprint consumption in India was up 17% so far this year. He said that Bowater sees the Chinese in India and that Chinese newsprint sales are growing.

He said, ''There is room for those tonnes to go. It will be a difficult 12 to 18 months as they find a home.'' He said there were also other forces affecting Chinese tonnage, primarily Chinese demand as well as the change in their tariff system. He said if the government does what it said it is going to do and eliminates tariff protection for exports, then high-cost Chinese capacity will start shutting down.[40]

In their audio remarks, both Weaver and Paterson, emphasized the export opportunities for NA newsprint manufacturers created by the global growth in the demand for newsprint. Abitibi and Bowater foresee a healthy increase in overseas shipments in 2007 due to the projected growth in newsprint demand in other regions. Abitibi and Bowater account for about 70% of total exports from NA to overseas locations. In a news report, Weaver said he expected Abitibi to increase its offshore shipments by 10% in 2007 and Paterson anticipated a 5% to 6% increase in offshore shipments from NA.[41]

(f) Evidence That Buyers of Newsprint for U.S. Daily Newspapers Generally Do Not Have Plans To Buy Newsprint From China Within the Next Several Years

Several of the newspaper newsprint buyers we talked to indicated that they had tested Chinese newsprint but that they had no immediate plans to purchase newsprint from Chinese mills. Factors that they cited were an unknown track record, the lack of a relationship, the need to assure reliability of delivery and quality, and the need to assure service. While price is an extremely important factor to a newsprint buyer, another important factor is the need to assure an adequate and reliable supply of newsprint at all times since newspapers print on a daily basis.[42]

The buyers emphasized the need to develop a very close relationship with their suppliers. Buyers emphasized that it would take several years of low-volume purchases to establish the trust and track record needed to increase their level of purchases.

Several buyers believed that if Chinese newsprint were shipped to the U.S., it would only be economically feasible to ship the paper to west coast ports to supply newspaper printing plants located close to the docks.

d. Conclusions Regarding Geographic Market Definition

(1) Relevant Geographic Market

We conclude that the geographic market is no larger than NA. It is possible that the relevant geographic market may be narrower than NA. Some evidence suggests that there may be a relevant East of the Rockies geographic market. To conclude that there is a relevant East of the Rockies market it would be necessary to determine if West of the Rockies newsprint mills could profitably ship newsprint to East of the Rockies customer locations in response to a ''small but significant and nontransitory'' increase in price in sufficient quantities to make the price increase unprofitable.

(2) The Likely Effect of New Chinese Newsprint Capacity on the NA Newsprint Market

While there is new Chinese newsprint capacity that has come on line recently, it appears that that capacity will be largely absorbed in Asia over the next couple of years. There may be some limited sales to U.S. publishers by Chinese mills over the next couple of years. Most publishers we talked to showed little interest in buying newsprint from Chinese mills. They placed great emphasis on trust, reliability and a close relationship with their newsprint suppliers. Currently they have no relationship with any of the Chinese mills and believe that establishing the trust and reliability necessary to buy more than nominal amounts of newsprint would take at least a couple of years if not longer.

If there is to be an effect on the NA newsprint market from the new Chinese newsprint capacity, it would likely be an indirect one. It is possible that some NA suppliers who currently export to Asia will be displaced from some of their customers by the new Chinese capacity. If so, that would create excess capacity at their NA mills used to supply the Asian market. As discussed above, however, Abitibi and Bowater expect newsprint exports from NA to increase, not decrease. The export growth opportunities that Abitibi and Bowater expect to be able to take advantage of should be available to other NA mills that export newsprint, including those that may be displaced from Asian customers by the new Chinese capacity.

C. Analysis of the Increase in Concentration That Would Result From the Proposed Merger

1. Analysis of the Increase in Concentration in the NA Newsprint Market Based on Estimated 2006 Capacity

According to § 1.51(b) of the DOJ/FTC Horizontal Merger Guidelines (''merger guidelines'') the NA newsprint market is currently moderately concentrated. Based on estimated 2006 NA newsprint capacity, the pre-merger HHI is 1,380. If the merger is consummated, the change in the HHI would be 962 and the post-merger HHI would be 2,342.[43] See Chart CI below.

the Citigroup Conference is no longer available on the Web site.

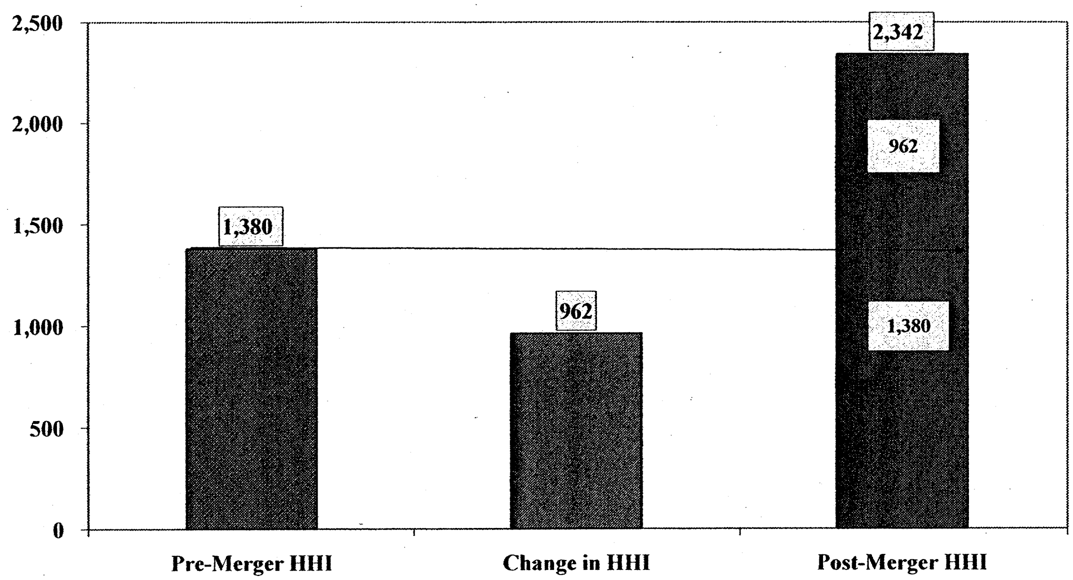
[40] Paterson appears to referring to a 13% rebate to Chinese newsprint exporters on a 17% import tax that newsprint mills must pay on imported raw materials. If this rebate has been eliminated, the cost of newsprint exports has been increased, especially exports made from recycled paper (ONP). Chinese newsprint mills are major importers of recycled paper. The two newest Chinese newsprint machines are recycled paper machines. The price of ONP has nearly doubled since last fall to $180 per tonne. This will make the new Chinese newsprint capacity and other Chinese capacity that relies on ONP less competitive against Abitibi and Bowater who rely primarily on wood fiber for their pulp needs. See ''Paper Chase,'' by Andrew Bary, Barron's On-Line, April 5, 2007.

[41] See ''Abitibi, Bowater turning to export markets to counter declines in NA,'' RISI, February 12, 2007.

[42] Two newspaper publishers, Gannett and the Tribune Co., have been publicly identified as conducting test runs using Chinese newsprint. See ''Tribune's Second Test of Chinese Newsprint a Success,'' by Jim Rosenberg, Editor & Publisher, December 11, 2006. According to the article, Gannett and the Tribune Co. said the results of the tests were successful. According to the article, a Gannett executive said last year that Gannett expects to buy Chinese newsprint but would not specify the quantity it planned to purchase or when purchases might commence. The Tribune Co. continues to run tests on Chinese newsprint for its Los Angeles Times printing operation. After the Tribune's first successful test run in November 2006 at its Orlando (FL) Sentinel printing plant. John Cannizzo, Tribune's senior manager of group operations, is quoted as saying '''If it turns out we can get, say, 1,000 tons shipped in a reasonable time and on a consistent basis, (buying Chinese newsprint) might be a viable option in 2007'. [* * *] We're not in a great hurry. We just want to see if this might work.'' ''Tribune marks 'successful' test of Chinese mill's newsprint,'' by Chuck Moozakis, Newspapers & Technology, December 2006. The newsprint tested in Orlando was originally intended for a test at the Los Angeles Times plant. However, the paper's cores and chucks were not compatible with the Chinese rolls, according to the article. That problem has since been solved. It seems unlikely that it would be profitable to ship newsprint from China through the Panama Canal to an east coast location, given the much greater shipping costs.

[43] Table C1 in Attachment C identifies the owner, location and capacity for each NA newsprint mill. Table C1 also provides detailed information on the methods and sources relied upon for the estimate of the market shares. Table C2 in Attachment C shows the calculation of the capacity shares and HHIs by manufacturer based on the mill-level data contained in Table C1. Table C2 is the source for both Charts C1 and C2.

Chart C1: Abitibi-Bowater Merger: Pre-Merger HHI, Change in HHI, and Post-Merger HHI Based on Estimated 2006 NA Newsprint Capacity

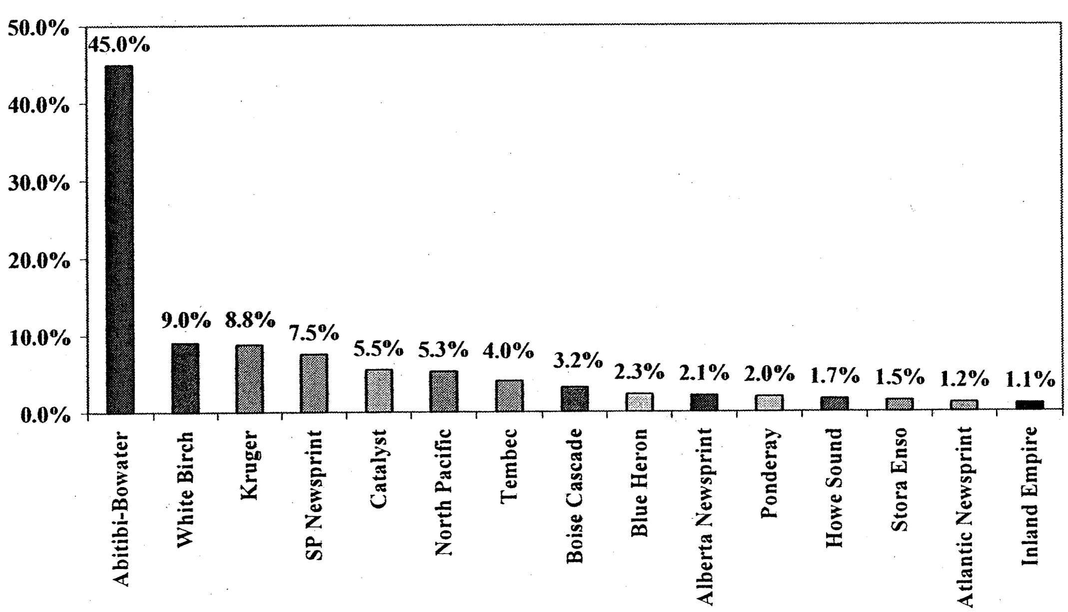


According to § 1.51(c) of the merger guidelines, markets with post-merger HHIs above 1,800 are highly concentrated and HHIs of the magnitude shown in Chart C1 create the presumption that the merger would be "likely to create or enhance market power or facilitate its exercise." This section of the merger guidelines states in part that:

Where the post-merger HHI exceeds 1800, it will be presumed that mergers producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise. The presumption may be overcome by a showing that factors set forth in Sections 25 of the Guidelines make it unlikely that the merger will create or enhance market power or facilitate its exercise, in light of market concentration and market shares.

Pre-merger, Abitibi has a 27.4% market share based on estimated 2006 capacity and Bowater has a 17.5% share. Following the merger Abitibi-Bowater would have a combined share of 45.0%. The next largest newsprint manufacturer, White Birch would have a 9.0% share. See Chart C2 below.

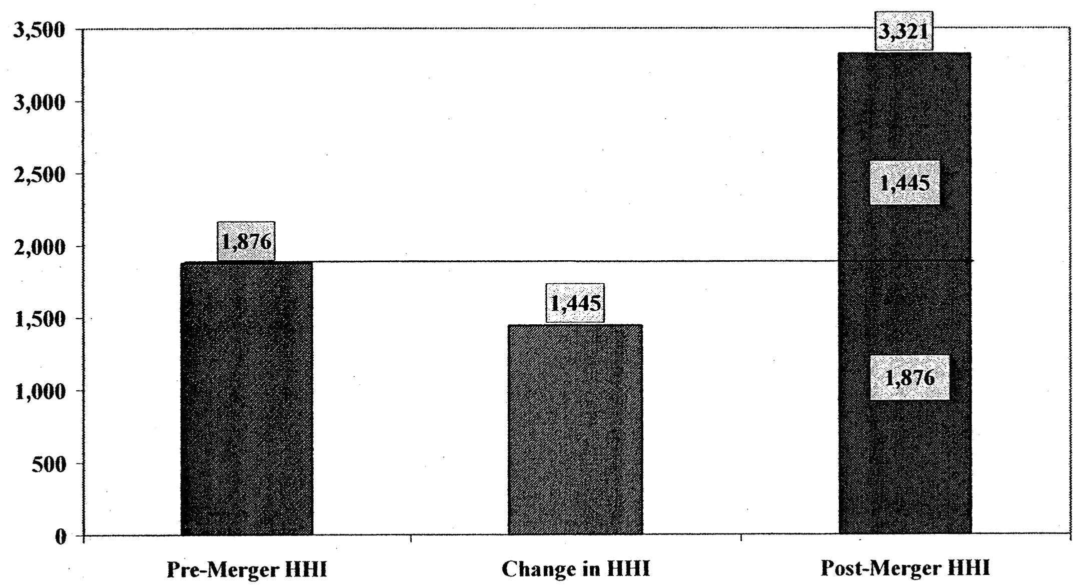
Chart C2: Abitibi-Bowater Merger: Post-Merger Market Shares Based on Estimated 2006 NA Newsprint Capacity



2. Analysis of the Increase in Concentration in the East of the Rockies Newsprint Market Based on Estimated 2006 Capacity

Based on estimated 2006 east of the Rockies newsprint capacity, the pre-merger HHI is 1,876. If the merger is consummated, the change in the HHI would be 1,445 and the post-merger HHI would be 3,321. See Chart C3 below.[44] In terms of pre-merger and post-merger HHIs, an east of the Rockies newsprint market would be more concentrated than a NA newsprint market.

Chart C3: Abitibi-Bowater Merger: Pre-Merger HHI, Change in HHI, and Post-Merger HHI Based on Estimated 2006 East of the Rockies Newsprint Capacity

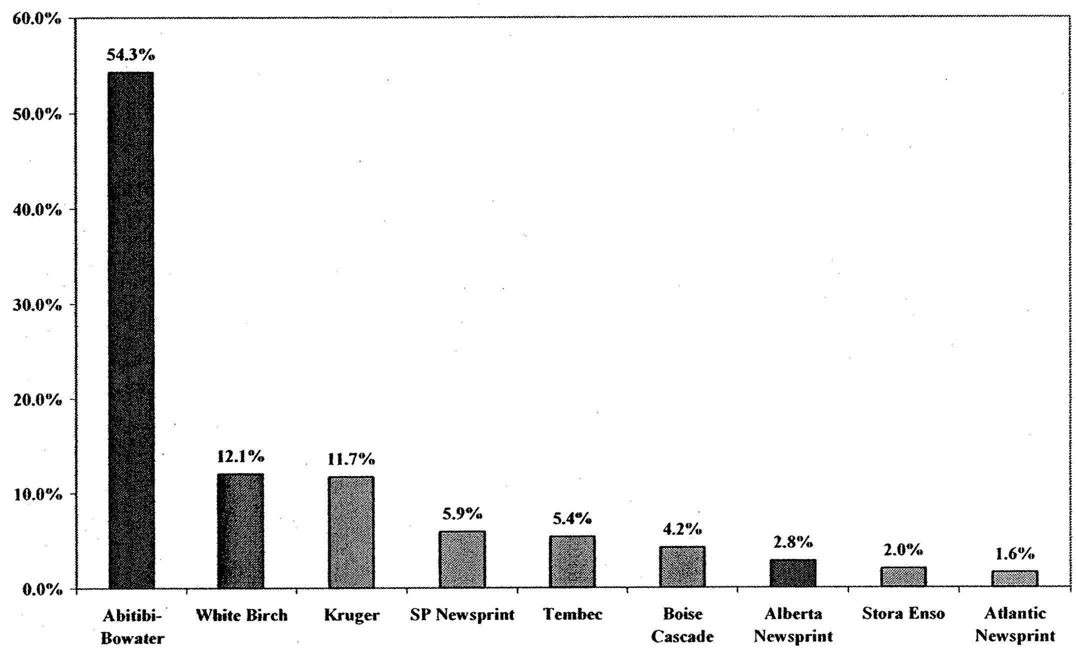


Abitibi has only two west of the Rockies mills (Mackenzie, BC and Snowflake, AZ) and, as noted above, Bowater does not own a majority interest in any west of the Rockies newsprint mill. Virtually all of their combined capacity is located east of the Rockies. Pre-merger, Abitibi has a 30.8% market share based on estimated 2006 east of the Rockies capacity and Bowater has a 23.4% share. Following the merger, AbitibiBowater would have a combined share of 54.3%. The next largest newsprint manufacturer, White Birch, would have a 12.1% share. See Chart C4 below.[45]

[44] The source for Charts 3 and 4 is Table C3 in Attachment C.

[45] The following North America newsprint manufacturers have all of their newsprint capacity in mills located west of the Rockies: Catalyst, North Pacific, Blue Heron, Ponderay, Howe Sound, and Inland Empire. In addition, the following NA newsprint manufacturers have some but not all of their newsprint capacity in mills located west of the Rockies: Abitibi (561,000 metric tonnes) and SP Newsprint (395,000 metric tonnes).

Chart C4: Abitibi-Bowater Merger: Post-Merger Market Shares Based on Estimated 2006 East of the Rockies Newsprint Capacity



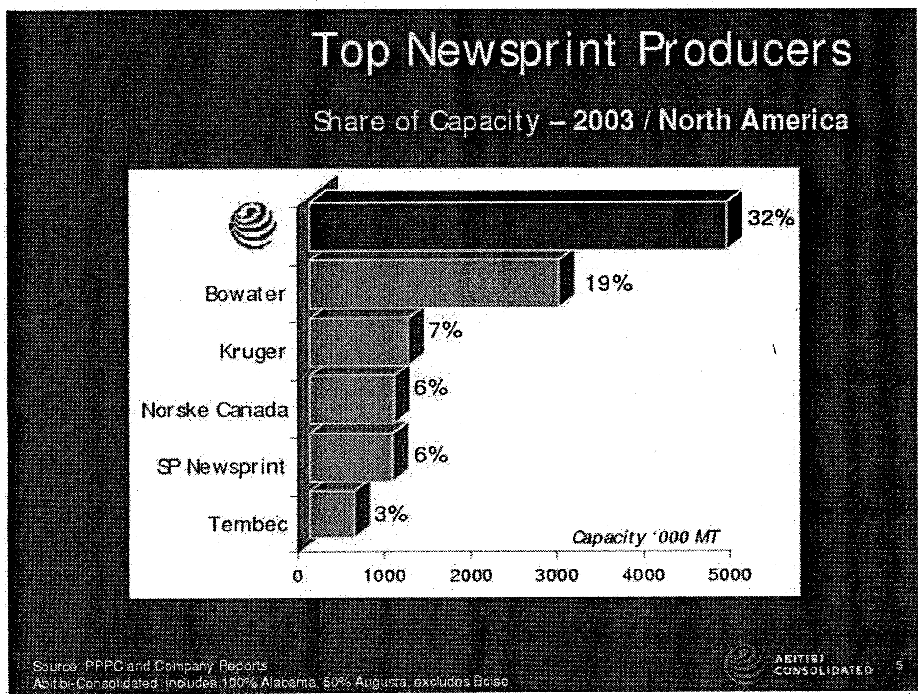
D. Analysis of the Increase in Concentration and Decrease in Capacity in the NA Newsprint Market 1995–2006

1. The Increase in Concentration in the NA Newsprint Market 1995–2005 as Described by Abitibi and Bowater

a. Description of the Increase in Concentration by John Weaver, President and CEO of Abitibi

John Weaver, the President and CEO of Abitibi, has discussed the increase in consolidation in the NA newsprint market in a number of presentations to investment analysts. Slide 5 below is from a presentation that Weaver made at the UBS Global Paper and Forest Products Conference on September 18, 2003. The presentation was titled ''Is the Industry Positioned to Reap the Benefits of Its Restructuring?'' and is available on the Abitibi Web site. Slide 5 shows Abitibi with a 32% capacity share and Bowater with a 19% capacity share in NA.

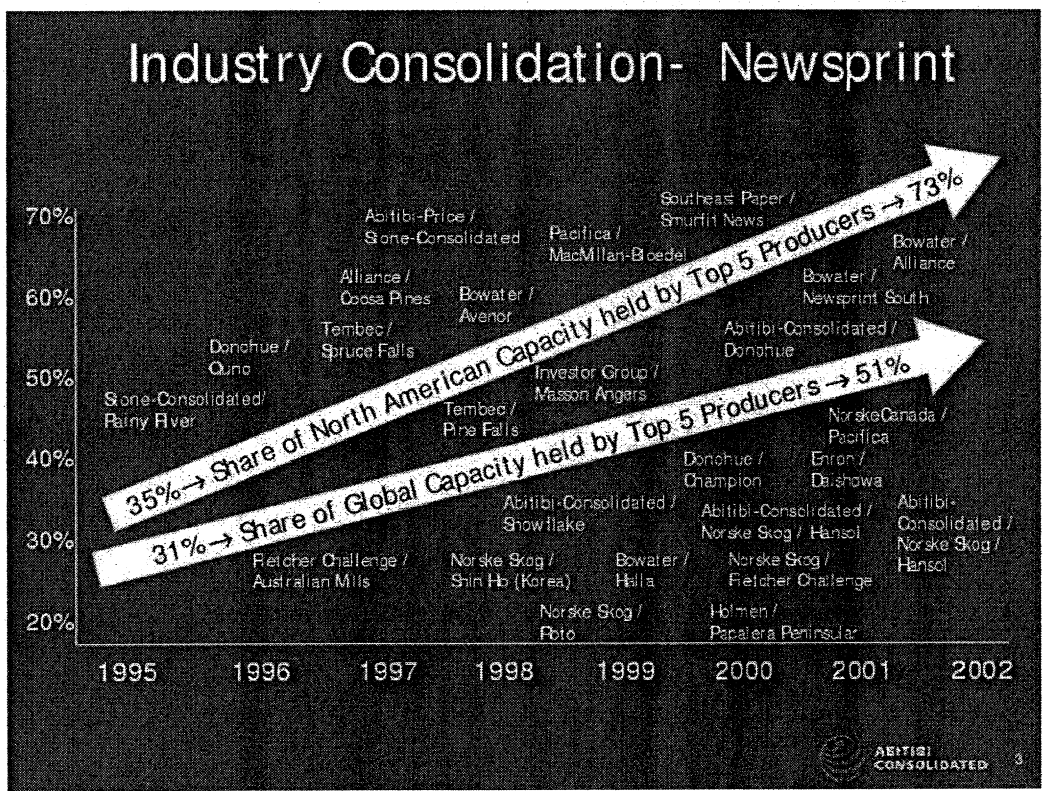
Slide 5: Abitibi UBS Conference 9/18/03



Slide 3 below from Abitibi's UBS presentation states that the capacity share of the top 5 NA newsprint producers more than doubled from 35% in 1995 to 73% in 2002. Slide 3 also identifies the acquisitions and mergers that occurred over the period 1995 to 2002 that enabled the share of the top 5 newsprint producers in North America to rise from 35% to 73%.[46] Some of these mergers involved companies that Abitibi and Bowater eventually acquired.

[46] Seven mergers identified in the lower right hand corner of the slide involve overseas transactions. In 2003, Abitibi was a 50% owner of PanAsia, a large Asian newsprint producer. In 2005, Abitibi sold its interest in PanAsia to the other 50% owner, Norske Skog, in order to reduce its debt, part of which was incurred in the Donohue acquisition in 2000. See Abitibi presentation "Divesting PanAsia: A Good Price at the Right Time," September 2005, pp. 5–6. This presentation is available on the Abitibi Web site.

Slide 3: Abitibi UBS Conference 9/18/03



Slide 4 below from Abitibi's UBS presentation shows the acquisitions that enabled Abitibi to increase its NA newsprint capacity share from 11.2% in 1995 [47] to 32% in 2003. All of these acquisitions occurred between 1995 and 2000.

[47] Source: ''Newsprint: A Pulp & Paper Market Focus Book,'' p. 113, 1999.

Slide 4: Abitibi UBS Conference 9/18/03

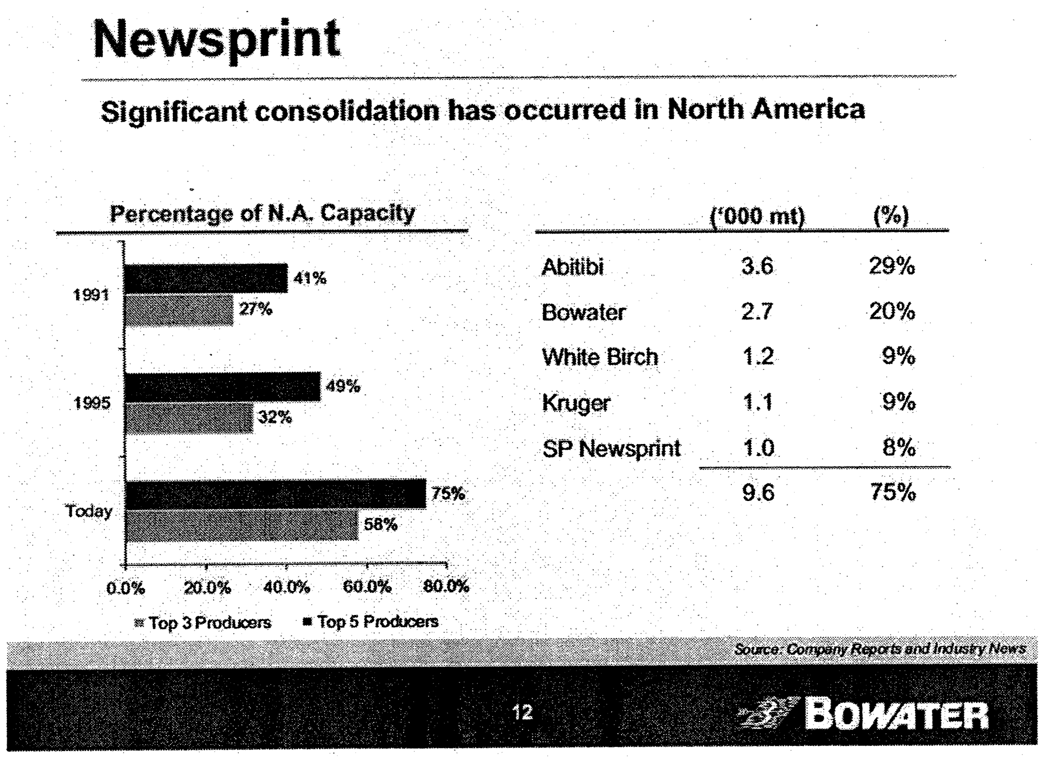
b. Description of the Increase in Concentration by David Paterson, President and CEO of Bowater

In a slide show presentation at the Annual Citigroup Paper and Forest Products Conference on December 7, 2006, David Paterson, President and CEO of Bowater, spoke to investment analysts about Bowater's product lines, efforts to reduce costs, and financial results. Referring to Slide 12,[48] Paterson noted that there had been significant consolidation in the newsprint industry and that he expected that consolidation would continue. See Slide 12 below. Slide 12 shows that in 1995 the top 5 producers had a combined share of 49%.[49] If the Abitibi-Bowater merger is allowed to be completed, the chart shows that the merged entity will have a share equal to the 49% share of the top 5 firms in 1995. The chart also shows the pre-merger share of the top 5 firms increased from 49% in 1995 to 75% in 2006.

[48] The slide show is titled ''Bowater: Citigroup Global Paper and Forest Products Conference, December 2006'' (''Paterson 2006 Citigroup slide show''). Both the slide show and an audio recording of Paterson's remarks are available on the Bowater Web site.

[49] Slide 3 in the Weaver UBS presentation discussed above shows the top 5 NA newsprint producers with a 35% capacity share in 1995, 14% lower than the capacity share shown in the Paterson presentation. Page 113 of ''Newsprint: A Pulp & Paper Market Focus Book'' (1999) shows the top 5 newsprint producers with a 42.5% capacity share.

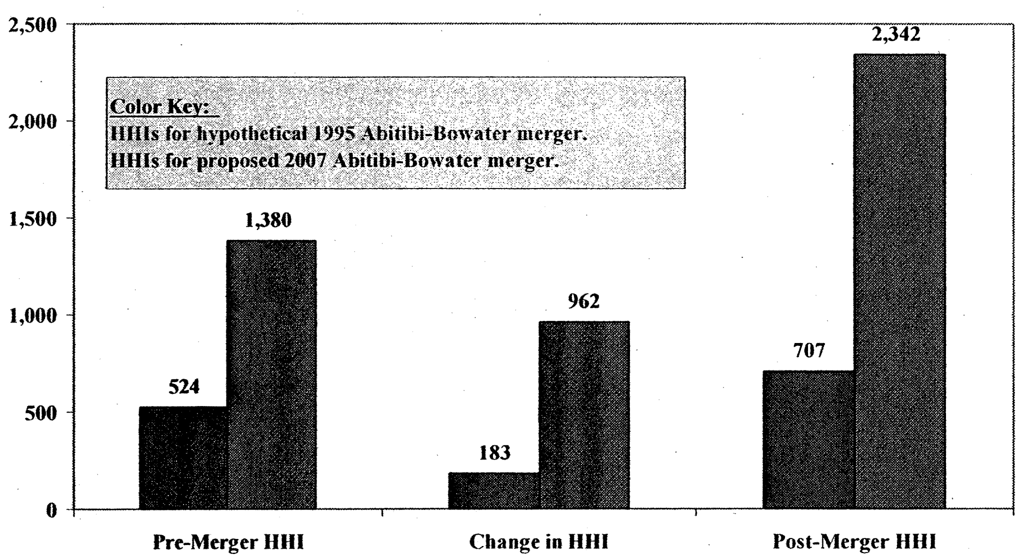
Slide 12: Bowater Citigroup Conference 12/7/06



2. Concentration in the NA Newsprint Market in 1995

In 1995, Abitibi Price was the largest newsprint manufacturer with a capacity share of 11.2% and Bowater was the third largest firm with a capacity share of 8.1%. Their combined share was 19.4%. If Abitibi-Price and Bowater had merged in 1995, the pre-merger HHI would have been 545, the change in the HHI would have been 183 and the post-merger HHI would have been 728. According to § 1.51(a) of the Merger Guidelines, markets with post-merger HHIs below 1,000 are unconcentrated. See Chart D1 below which includes both the HHIs for the 1995 hypothetical AbitibiBowater merger and the HHIs for the proposed 2007 AbitibiBowater merger.[50]

Chart D1: A Comparison of HHIs Between a Hypothetical Abitibi-Bowater Merger in 1995 and the Proposed Abitibi-Bowater Merger in 2007 Based on 1995 and 2006 Capacity Shares for NA Newsprint Manufacturers



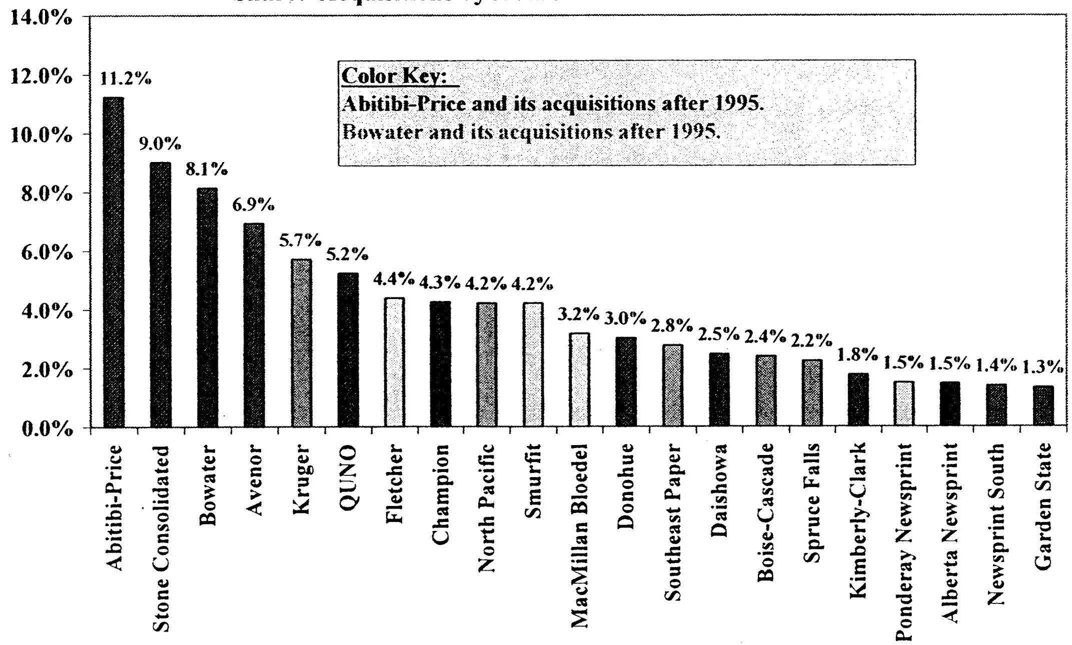
[50] The sources for Chart D1 are Table D1 (1995 capacity shares) in Attachment D and Table C2 (2006 capacity shares) in Attachment C.

3. Acquisitions and Exits of NA Newsprint Manufacturers Since 1995

See Table D1 in Attachment D for capacity shares and HHIs for all 33 NA manufacturers of newsprint in 1995. Based on Table D1, Table D2 in Attachment D identifies all acquisitions and exits in the NA newsprint market since 1995.

See Chart D2 below, which shows capacity shares for the top 20 newsprint manufacturers in 1995.[51]

Chart D2: Top 20 NA Newsprint Manufacturers in 1995 Ranked by Capacity Share: Acquisitions by Abitibi and Bowater After 1995



The chart also shows which of the top 20 newsprint manufacturers in 1995 were acquired directly and indirectly by Abitibi and Bowater after 1995.[52] As Table D2 shows, Abitibi also indirectly acquired Finley Forest Industries, the 27th largest newsprint manufacturer in 1995 with a capacity share of 1.2%. Bowater also directly acquired Alliance, the 24th largest manufacturer in 1995 with a capacity share of 1.3%.

4. Analysis of the Reduction of Newsprint Capacity in North America 1995 to 2006

In 1995, there were 16,093,000 metric tonnes of NA newsprint capacity. In 2006, there were an estimated 12,760,000 metric tonnes of NA newsprint capacity, a reduction of 20.7%, most of it occurring since 2002.[53] Utilizing the data and other information in Table C2 in Attachment C and Tables D1 and D2 in Attachment D, it is possible to identify the sources for the reduction of newsprint capacity in North America since 1995. This is a two-step process. The first step is to adjust the 1995 capacities and shares shown in Table D1 to account for subsequent acquisitions while eliminating the acquired firms from the list of manufacturers, See Table D3 in Attachment D. As shown in Table D2, there were 34 manufacturers of newsprint in North America. After all acquisitions since 1995 are accounted for, 21 manufacturers remain. There has been a reduction of 14 newsprint manufacturers through acquisition since 1995.[54] Through direct and indirect acquisitions, Abitibi accounted for five of those newsprint manufacturer reductions and Bowater four. Table D3 shows that Abitibi also accounted for 46.8% of the acquired capacity and Bowater 21.2% for a combined total of 68.0%. Through these acquisitions, Abitibi increased its capacity share by 22.7% from 11.2% to 34.0% and Bowater increased its capacity share by 10.3% from 8.1% to 18.4%. Abitibi and Bowater increased their combined capacity share by 33.0% from 19.4% to 52.4%. The second step is to subtract estimated 2006 newsprint capacity from adjusted 2005 newsprint capacity. See Table D4 in Attachment D. Table D4 shows that the total net reduction in capacity between 1995 and 2006 was 3,333,000 metric tonnes. Table D5 below summarizes the results in Table D4.

[51] The source for Chart 2 is Table D1 in Attachment D. The source for Table D1 is ''Newsprint: A Pulp & Paper Market Focus Book,'' (1999), p. 113. In 1995 Avenor was a 40% minority owner of Ponderay Newsprint. For the purposes of this analysis, Ponderay is listed as a separate firm. Bowater acquired its current 40% interest in Ponderay when it acquired Avenor in 1998. In 1998, Ponderay had a capacity of 240,000 metric tonnes (1998 Bowater Annual Report, p. 3).

[52] An example of a direct acquisition is Abitibi's acquisition of Donahue in 2000. Donahue had acquired QUNO in 1996. When Abitibi acquired Donahue in 2000, it also indirectly acquired QUNO.

[53] Sources: See Table DI in Attachment D and Table C2 in Attachment C.

[54] The net reduction in firms is 13 because a new firm was added to the NA newsprint market in 1999 when Bowater sold its East Millinocket, ME newsprint mill to Great Northern Paper. Following Great Northern's subsequent bankruptcy, Katahdin acquired the East Millinocket mill in 2003 and produced newsprint until it converted its newsprint capacity to uncoated groundwood specialty grades in 2005–2006. In 1998, the newsprint capacity of the East Millinocket mill was $168,000 metric tonnes (1998 Bowater Annual Report, p. 4).

TABLE D5.—SUMMARY OF THE NET CAPACITY REDUCTION IN NA NEWSPRINT CAPACITY 1995–2006

	Net capacity changes 1995–2006	Percent of total net capacity changes 1995–2006	Percent of net capacity reductions 1995–2006 for 5 firms that remain in the market
Abitibi	(1,964)	58.9	60.9
Bowater	(731)	21.9	22.7
Catalyst	(514)	15.4	15.9
Tembec	(15)	0.5	0.5
North Pacific	(2)	0.1	0.1
Net Capacity Reductions for 5 Firms That Remain in the NA Newsprint Market Today	(3,226)	96.8	100.0
Net Capacity Additions or No Capacity Change for 11 Firms That Remain in the NA Newsprint Market Today	630	(18.9)	
Net Capacity Reduction of the 16 Firms That Remain in the NA Newsprint Market Today	(2,596)	77.9	
5 Firms That Exited from the NA Newsprint Market Between 1995 and 2006	(737)	22.1	
Total Net Capacity Reduction 1995–2006	(3,333)	100.0	

The firms in Table D5 can be divided into three categories: (1) Firms remaining today in the NA newsprint market that had a net reduction in capacity over the period 1995 to 2006; (2) firms remaining today in the NA newsprint market that had a net addition in capacity over the period 1995 to 2006; and (3) firms who exited from the NA newsprint market between 1995 and 2006.[55] As Table D5 shows, there are 5 firms in the first category, 11 firms in the second category, and 5 firms in the third category.

The first and third categories total 3,963,000 metric tonnes in net capacity reductions. These net capacity reductions are partially offset by 630,000 metric tonnes in net capacity additions by 10 of the 16 firms that remain in the market today.[56] After this offset is taken into account, the total net reduction in NA newsprint capacity is 3,333,000 metric tonnes.

The first category in Table D5 shows that the reductions by Abitibi, Bowater, and Catalyst account for 99.5% of NA capacity reductions by firms that (a) had net capacity reductions between 1995 and 2006 and (b) remain in the market today.[57] Abitibi accounts for 60.9% of the net capacity reduction, Bowater for 22.7% of the net capacity reduction, and Catalyst for 15.9% of the net capacity reduction.[58] Combined, Abitibi and Bowater account for 83.6% of the net reduction in NA newsprint capacity since 1995 shown in the first category. See Chart D3 below.

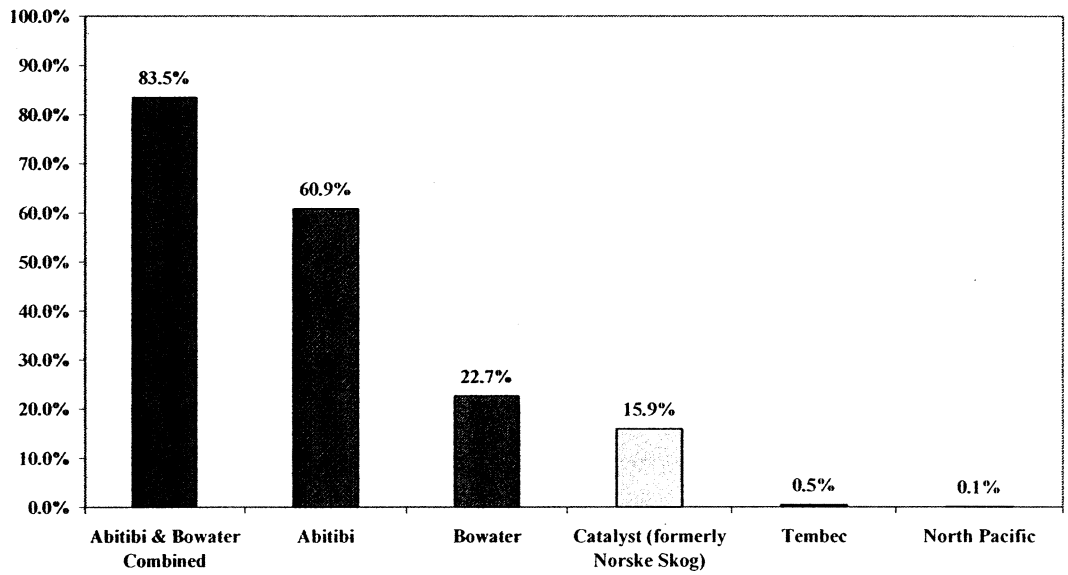
[55] Of the five firms that exited from the NA newsprint market, four of those firms converted their newsprint capacity to other groundwood grades. Only Garden State exited by permanently closing its newsprint mill.

[56] One of the remaining firms had no change in capacity. There could be several reasons for the net increases in capacity. These may include speed-ups and other improvements to existing newsprint capacity and switching capacity from the production of uncoated groundwood grades to newsprint. The increase for Inland Empire is due to the installation of a new newsprint machine in 2001 and the permanent closure of the machine it replaced. There were no other installations of new newsprint machines in North America between 1995 and 2006. Some of the additions may not be real (e.g., they may result from methodological differences in reporting or estimating capacity in 1995 and 2006 or they may result from errors).

[57] The net capacity reduction shown for North Pacific is not meaningful. In 2004, Tembec permanently closed one newsprint machine at its mill in Kapuskasing, ON.

[58] It should be noted that some of the net capacity reduction for Abitibi, Bowater, and Catalyst occurred in acquired firms after 1995 but prior to their acquisitions by Abitibi, Bowater, or Catalyst. The most significant such capacity reduction is the closure of a 184,000 metric tonne capacity newsprint machine by MacMillan Bloedel in 1996. MacMillan Bloedel was subsequently acquired by Pacifica which was subsequently acquired by Norske Canada (later renamed Catalyst). This machine closure accounts for 35.8% of Catalyst's total net capacity reduction shown in Table D5 and Chart D3. Capacity reductions after 1995 by firms before they were acquired by Abitibi or Bowater make up a much smaller percentage of their respective net capacity reductions. Taking into account these prior capacity reductions for the three acquiring firms, Abitibi's share of the net capacity reduction of firms that remain in the market would increase to 66.2%, Bowater's share would increase to 21.8% and Catalyst's share would decrease to 11.4%. Source: ''Newsprint: A Pulp & Paper Market Focus Book,'' p. 20 (1999).

Chart D3: Percentage of Total Net Reduction of NA Newsprint Capacity from 1995 (1995 Adjusted Capacity) to 2006 by Firms That (1) Reduced Net Capacity and (2) Remain in the Market Today



As Table D4 indicates, Abitibi lost 6.5% in capacity share. Bowater lost 0.9% in capacity share, and Catalyst lost 2.1% in capacity share between 1995 (adjusted 1995 capacity) and 2006 due to their net capacity reductions. Combined, the three firms lost 9.5% in newsprint capacity share. The 5 firms that exited the NA newsprint market lost a combined 4.6% in newsprint capacity share.

E. NA Newsprint Demand and Supply

1. Introduction

The demand for newsprint by daily newspapers is derived from the demand for newspapers by readers and advertisers. Demand, as used in this sense, means the demand curve for newsprint and the demand curve for newspapers. If the demand for newspapers declines independent of the price of newsprint, the demand curve for newspapers will shift downward causing the newspaper's derived demand curve for newsprint to also shift downward.

Chart E2 below shows the total NA average quarterly demand for newsprint 1999 to 2006.[59] Demand, as used in this sense, means the quantity of newsprint purchased during a quarter. The same is true with respect to Chart E1 below, except that the period over which quantity is purchased is a year. Chart E2 shows that while there were quarters where demand increased from the prior quarter the overall trend is declining in demand. Demand in Q4 2006 was 24.5% lower than demand in Q1 1999. Chart E2 cannot explain the causes of this decline in demand (i.e., quantity purchased); it can only show that demand (i.e., quantity purchased) did generally decline over the 32 quarters.

Chart E6 shows quarterly prices for newsprint. Prices declined from the Q1 1999 to Q3 1999, generally increased from Q3 1999 to Q2 2001, declined significantly from Q2 2001 before bottoming out in Q2 and Q3 2002, and generally increasing from Q3 2002 to Q3 2006 before declining somewhat in Q4 2006. Just considering the period from Q3 2005 to Q3 2006 the price of newsprint increased by an aggregate of $222 or 49.0% while demand (quantity purchased) declined by an aggregate of 521,000 metric tonnes or 18.0%.

This section, as well as Sections D and F, explores the likely causes of the significant and sustained increase in newsprint prices over the two periods described above while newsprint demand (quantity purchased) was either flat or steadily declining. See Chart 7 below, which combines Chart 2 and Chart 6. In seeking the explanation for the likely causes, we make three main observations:

(1) The decline in demand (quantity purchased) over the period 1999 to 2006 was due primarily by downward shifts in the demand curve for newspapers caused by declining circulation and advertising lineage independent of increases in the price of newsprint. The downward shifts in the demand curve for newspapers caused downward shifts in the derived newsprint demand curve.

(2) Holding the newsprint supply curve constant, downward shifts in the newsprint demand curve would be expected to lead to lower newsprint prices. That has not happened. The steady rise in newsprint prices over the two periods was primarily caused by the strategic and coordinated removals of newsprint capacity from the market by Abitibi and Bowater in response to the downward shifts in the newsprint demand curve, These upward shifts of the supply curve maintained maximum operating rates and increased newsprint prices. Both Abitibi and Bowater pursued the approach of reducing capacity, which was highly successful in achieving a steady increase in the price of newsprint.

(3) It is not plausible that increases in the price of inputs used to manufacture newsprint or the appreciating Canadian dollar are a significant cause of the price increases.

The reduction in newsprint capacity by Abitibi and Bowater and its relationship to the maintenance of high operating rates and rising prices was recognized as a strategic move by newsprint producers, newsprint buyers, and newsprint industry analysts, as this passage from The Global Pulp & Paper Fact Book 2006[60] on p. 152 indicates.

Even though demand continued to decline during the 2003–2006 period, newsprint producers have steadily raised prices during the past several years. Through a policy of closing mills and either shutting newsprint machines or converting them to added-value grades, newsprint producers have kept supply and demand relatively balanced, and operating rates high enough to support the progression of supply-driven price increases. By third quarter of 2006 the market average stood at $675/tonne with another $20/tonne increase proposed by some producers for August 1 and by others for September 1.

The Global Pulp & Paper Fact Book 2006 does not identify any newsprint manufacturers but noted that unnamed newsprint manufacturers had a "*policy* of closing mills and either shutting newsprint machines or converting them to added-value grades" in order to keep "supply and demand relatively balanced, and operating rates high enough to support the progression of supply-driven price increases." (Emphasis

[59] Annual demand equals annual consumption plus the change in inventories held by customers from the prior December.

[60] The Global Pulp & Paper Fact Book 2006 is published by RISI.

added) The identification of those newsprint manufacturers will be the subject of Section F.

2. NA Demand (Quantity Purchased) 1999–2006

NA annual newsprint demand (quantity purchased) has fallen 25.5% on an annual basis between 1999 and 2006. See Chart E1 below.[61] In 1999, imports accounted for 3.3% of NA demand. Since 1999, imports have accounted for 2.0% or less of NA purchases. As Chart E1 shows, imports of newsprint into North America have not been a significant source of supply for NA newspaper publishers and other NA purchasers of newsprint. In 2006, imports supplied just 1.5% of NA newsprint consumption. For the first two months of 2007, imports have fallen 56.1% compared to the first two months of 2006.[62]

Chart E1. NA Demand (Quantity Purchased), Shipments to NA from NA Mills and Imports from Overseas 1999 to 2006

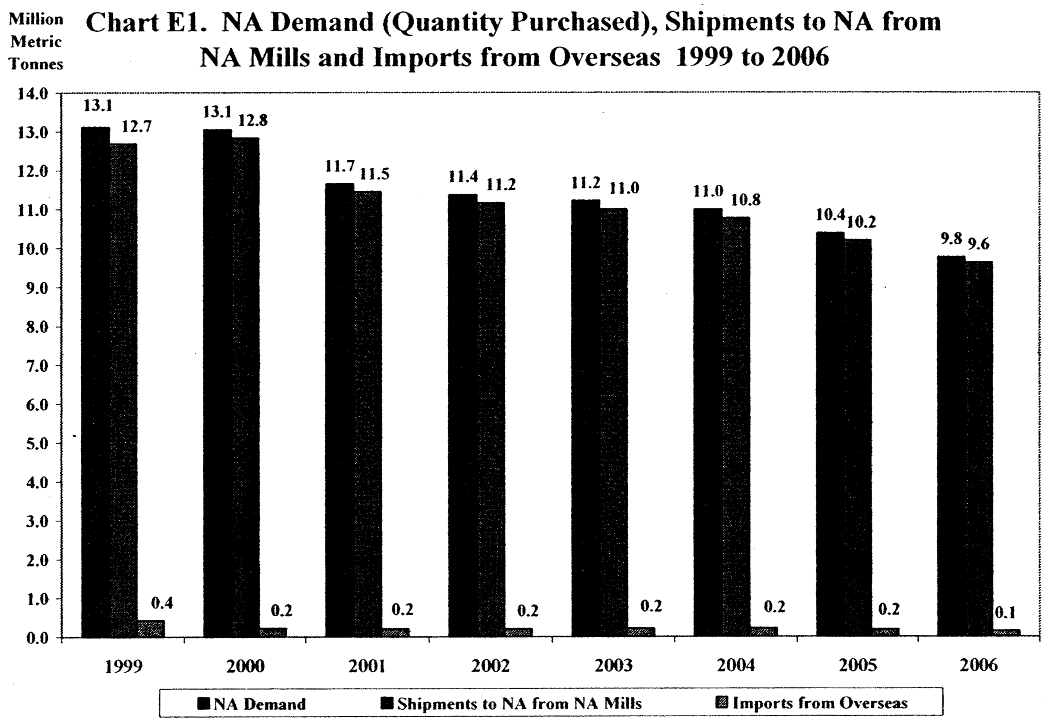
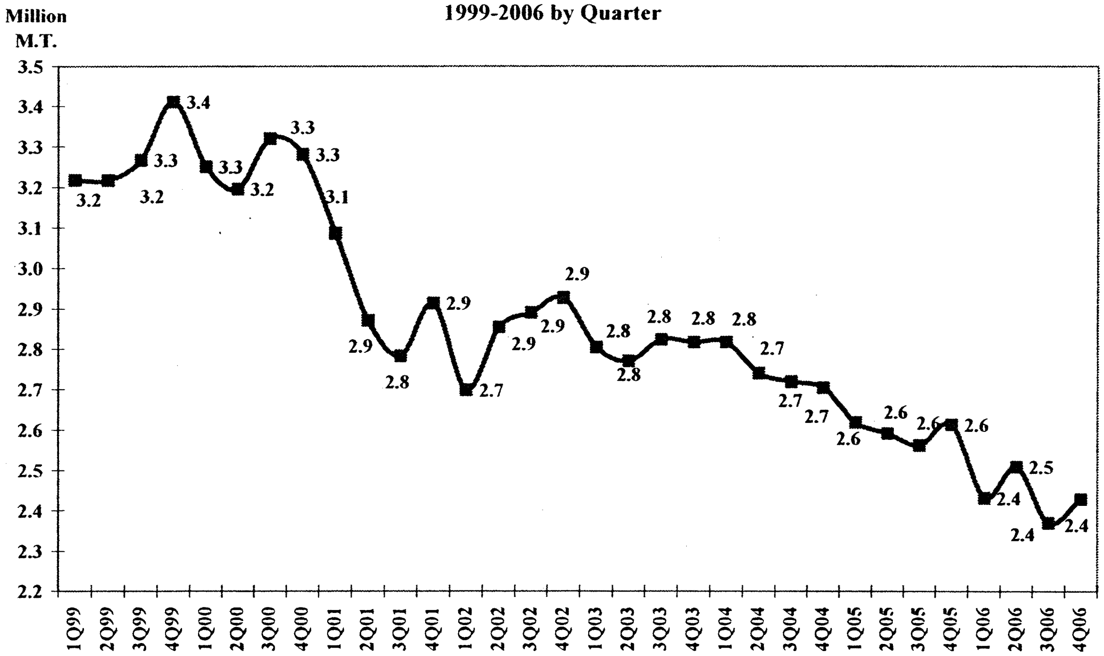


Chart E2 below shows NA demand (quantity purchased) by quarter from Q1 1999 to Q4 2006. Quarterly NA demand (quantity purchased) has decreased from Q4 1999 to Q4 2006 by 28.8%

[61] Sources: December 2006 and December 2005 PPPC NA Newsprint Statistics-Flash Report (''Flash Report''). and December 2001–2004 PPPC NA Newsprint Statistics Monthly Bulletin (''PPPC Monthly Bulletin'').

[62] Source: February 2007 Flash Report.

Chart E2. The NA Demand (Quantity Purchased) for Newsprint (Million Metric Tonnes) 1999-2006 by Quarter



3. Causes of the Decline in NA Newsprint Demand 1999–2006

a. Estimates of the Causes of the Decline in NA Newsprint Demand by the PPPC

There are three main causes of the decline in NA newsprint demand over the period 1999–2006: (a) Declining newspaper circulation; (b) declining newspaper ad linage; and (c) newspaper efforts to conserve on the consumption of newsprint.[63] These conservation efforts include reducing the width of newspapers, switching to lighter basis weight paper (i.e., thinner paper), and eliminating certain sections of the newspaper and placing them on the newspaper's Web site (e.g., stock tables and TV listings).

In the March 2007 edition of Pulp & Paper Magazine, Bill Moore of Moore & Associates, a recycled paper consulting firm, states that ''[t]he decline in newsprint consumption in North America is structural and very little can be done at this point to change the situation.'' [64]

Mr. Moore described how the decline in newspapers has led to the decline in the production of newsprint.

The reasons for this decline in NA newsprint production have been well documented and are related to a series of factors in the decline of newspapers:

• Newspaper readership in the U.S. has been steadily declining for a number of years and the downward trend has accelerated in the last few years.

• Many newspapers have moved to smaller formats, tighter margins, and also the use of a lower basis weight sheet.

• More advertising and classifieds have moved to the web.

• Stock pages, and even the classical in-depth reporting that newspapers were known for, have been eliminated from many papers. The recent Wall Street Journal changes resulted in a 15% reduction in the use of newsprint [by that newspaper]!

Martine Hamel, head of market research for the PPPC, has estimated the relative size of each of these effects [65] on the consumption of newsprint by U.S. daily newspapers.[66] Slide 17 of the 2005 PPPC Presentation below shows that for the first nine months of 2005 compared to the first nine months of 2004, consumption by U.S. daily newspapers declined 4.9%. Declines in ad linage and circulation accounted for about 63% of the consumption decline and switching to lower basis weight paper (i.e., grammage reduction) accounted for about 31% of the consumption decline. Other (presumably other conservation methods including width reductions) accounted for 6%.

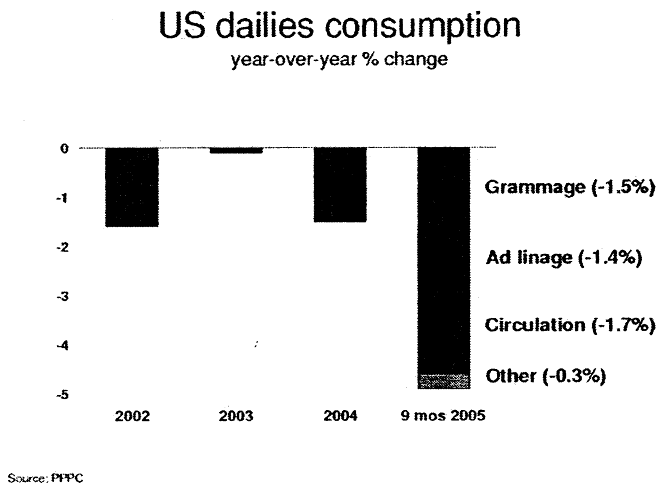
[63] In 2006, U.S. daily newspapers accounted for 71.3% ofNA newsprint demand and 80.2% of US. newsprint demand and U.S. newsprint demand accounted for 88.7% of NA newsprint demand. Source: December 2006 Flash Report.

[64] ''Another side of the decline of newspapers.'' Mr. Moore believes that local governments should put more effort into encouraging citizens in their communities to recycle old newspapers.

[65] See the presentations to the November 2005 and 2006 Joint NPA/NAA Newsprint Conference titled ''Review and Forecast of Newsprint Demand and Supply'' (''PPPC 2005 and 2006 NPA/NAA Presentations''). NPA is the Newsprint Producers Association.

[66] Annual NA demand equals shipments to North America by NA mills plus imports from overseas. Annual newsprint consumption by NA customers equals NA demand minus the change in newsprint inventories from the prior December. In 2006, the change in inventories at U.S. daily newspapers was a decline of 58,000 metric tonnes or 0.8% (absolute) of NA consumption and demand. The PPPC publishes inventory data for U.S. newsprint customers but not Canadian newsprint customers.

Slide 17: PPPC 2005 NPA/NAA Presentation



Slide 8 of the PPPC 2006 NPA/NAA Presentation shows a 7.8% decline in U.S. daily newsprint consumption for the first nine months of 2006 compared to the first nine months of 2005.[67] The decline in ad linage and circulation account for about 55% to 60% of the decline and grammage reduction and other conservation methods such as width reductions account for 40% to 45% of the decline.

Slide 8: PPPC 2006 NPA/NAA Presentation

Main factors explaining the 7.8% decline in US dailies consumption

- Grammage reduction (20%)
- Decline in advertising volumes (20-25%)
- Decline in circulation (35%)
- Conservation measures (20-25%)

Source: PPPC

b. Distinguishing Between Shifts in the Newsprint Demand Curve and Movements Along the Newsprint Demand Curve

If the newsprint supply curve shifts upward and to the left due, say, to the permanent closure of newsprint capacity, a new equilibrium price and quantity will be established. The new price will be higher than the old price and the new quantity purchased will be lower than the old quantity purchased. This can be described as a movement along the demand curve caused by the shift of the supply curve upward and to the left. The effect of the supply curve shift on equilibrium price and quantity will depend upon the price elasticity of demand. If the demand curve is highly inelastic in the region of the supply curve shift,[68] then price

[67] U.S. daily newspapers accounted for 83.7% of the decline in NA demand between 2005 and 2006. Other US. newsprint customers accounted for 14.1% of the decline and Canadian customers accounted for 23% of the decline.

[68] While we have not attempted to estimate the demand elasticity for the NA newsprint market, we note that an article in 2004 reported on an analysis that estimated the elasticity of the U.S. demand for newsprint at 0.36 taking into account structural changes in U.S. demand. See Jari Kuuluvainen, "Structural Change in U.S. Newsprint Demand: GDP and Price Elasticities," University of Helsinki, Department of Forest Economics, Reports #34, 2004, p. 8. A demand elasticity of 0.36 is in the same range as demand elasticities reported in earlier articles. An article in 1997 reported the demand elasticity in North America at 0.22. Other estimates cited in this article have been about twice as large. Estimates of demand elasticity vary from 0.22 to 044. These estimates all indicate a fairly inelastic demand curve for newsprint. See Ylbing Zhang and Joseph Buongiorno, "Communication Media and Demand for Printing and Publishing Papers in the United States," Forest Science 43(3) (August) 1997, p. 372. The results of our analysis of the proposed Abitibi-Bowater merger are consistent with an inelastic demand curve.

would likely rise significantly and quantity of newsprint purchased would be little reduced from the previous level. If demand were elastic in the region of the supply curve shift, then, compared to an inelastic demand curve, the resulting equilibrium price would be lower and the resulting quantity reduction would be greater.

Newspapers, of course, buy newsprint to help meet the demands of their customers, the readers and advertisers. Their demands for newspapers are exogenous to the newspapers' demand for newsprint. That is, their demand for newspapers is shaped by factors completely independent of the market for newsprint.[69] If the demand for newspapers declines because, say, readers and advertisers are moving from newspapers to the Internet, this movement will result in the newspaper demand curve for newsprint shifting downward and to the left. As a result of the shift of the demand curve down the supply curve, both price and quantity purchased will decline.

When newspapers narrow the width of the page or buy lower basis weight newsprint or move stock tables from the newspaper to their web sites, they are permanently removing newsprint demand from the market. In so doing, they are shifting the demand curve downward and to the left. While the conservation efforts are no doubt largely in response to the four years of newsprint price increases, they do not indicate movements along the demand curve. They indicate shifts in the demand curve. If newsprint prices declined by 10 percent, it is implausible that newspapers would go back to wider webs or start running stock tables in the newspaper again. As long as the relative prices for higher and lower basis weight paper remain approximately the same, as seems likely, newspapers will have no incentive to switch back to higher basis weight paper.

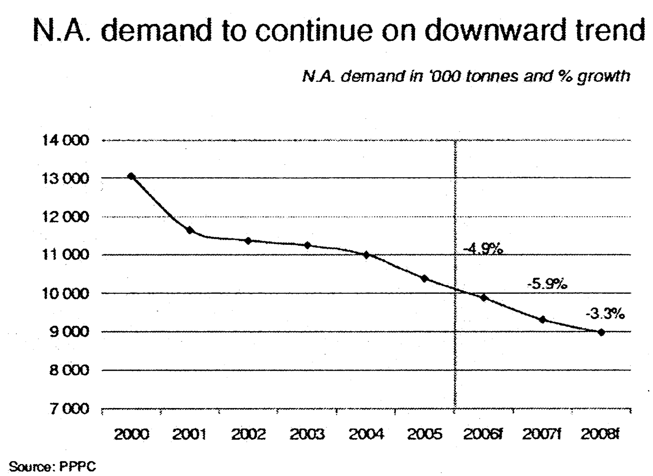
The demand removal through conservation efforts is directly analogous to the capacity removal that has been taking place in the NA newsprint market, particularly since 2002. The capacity removals shift the supply curve upward and to the right. The demand removals shift the demand curve downward and to the left. The major difference between the two is that the capacity removals occur more quickly and have a much greater impact on price than the demand removals. The narrowing of the width of newspapers from 50 inches to 48 inches would be the equivalent of a 4 percent reduction in price. The move from 30 lb. newsprint to 27.7 lb. newsprint[70] will only save a newspaper an equivalent of a 2.7% reduction in the price of 30 lb. newsprint.[71] If the price of 30 lb. newsprint were $630 per metric tonne (as it was in February 2007), a 2.7% net savings in newsprint purchases would be equivalent to a $16.94 reduction per metric tonne in the price of 30 lb. newsprint.

Slide 5 of the 2006 PPPC presentation shows that in 2006, about half of the newsprint shipped by NA mills to NA customers was 27.7 lb. newsprint. That implies that only half of the 2.7% or $16.94 cost savings potentially available to newsprint customers had been realized even though prices had steadily risen over the prior four years. Slide 6 in the same presentation also shows that conservation efforts on the part of newsprint customers take years to accomplish in the aggregate and even then, some and perhaps many customers will never convert. The same general comments can be made with respect to the reduction of page widths to 48 inches from 50 inches. Finally, newsprint buyers have said that the low-hanging fruit has been picked and that the opportunities for cost savings from future efforts to conserve on newsprint are reaching the point of diminishing returns.

4. Projected NA Newsprint Demand 2006–2008

The PPPC forecasts a 5.9% decline in NA newsprint demand in 2007 and an additional 3.3% decline in NA newsprint demand in 2008.[72] See Slide 10 below.[73]

Slide 10: PPPC 2006 NPA/NAA Presentation



Assuming the PPPC forecast is reasonably accurate, NA demand will fall by a total of 879,000 metric tonnes over the two-year period. Assuming no change in overseas shipments from NA mills or in imports by NA customers from 2006 levels, NA manufacturers would have to temporarily idle or permanently shut down 1,055,000 metric tonnes of capacity during 2007 and

[69] While it is certainly possible that some newspapers have been able to pass some portion of the last four years' of newsprint price increases on to newspaper customers, we are unaware of any such examples. To the extent there are such examples, they are likely to be insignificant in comparison to the aggregate magnitude of the newsprint price increases.

[70] Basis weight correlates with the thickness of the newsprint sheet. The higher the basis weight, the thicker the newsprint sheet and vice-versa. Most newsprint in North America is sold in two basis weights 30 lb. and 27.7 lb. Many of the largest newspapers and newspaper chains in the U.S. have switched from 30 lb. basis weight to 27.7 lb. basis weight newsprint in the last several years.

[71] Holding constant the square footage of printing surface purchased, the move to 27.7 lb. newsprint by the customer will reduce the tonnage needed by 8.5%. However, the newspaper will be paying more per metric tonne for the reduced amount of newsprint. According to Pulp & Paper Week, the February 2007 price of 30 lb. newsprint delivered in the eastern U.S. was $630 per metric tonne and the price of 27.7 lb. newsprint was $670 per metric tonne. At these prices, the cost per tonne purchased will increase by 6.3%. When these two effects are combined, the newspaper will save 2.7% or $16.94. per metric tonne. Whether the newsprint manufacturer will financially benefit from the switch depends on the relationship between the manufacturer's variable costs to produce the lower basis weight paper and the higher basis weight paper. If the manufacturer's variable cost to produce the lower basis weight paper is not too far above the variable cost to product the higher basis weight paper, the profits of the manufacturer could actually increase as a result of the switch.

[72] While Slide 10 forecasts a 4.9% decline in NA demand for 2006, the actual decline was 6.0%. Source: December 2006 PPPC Flash Report.

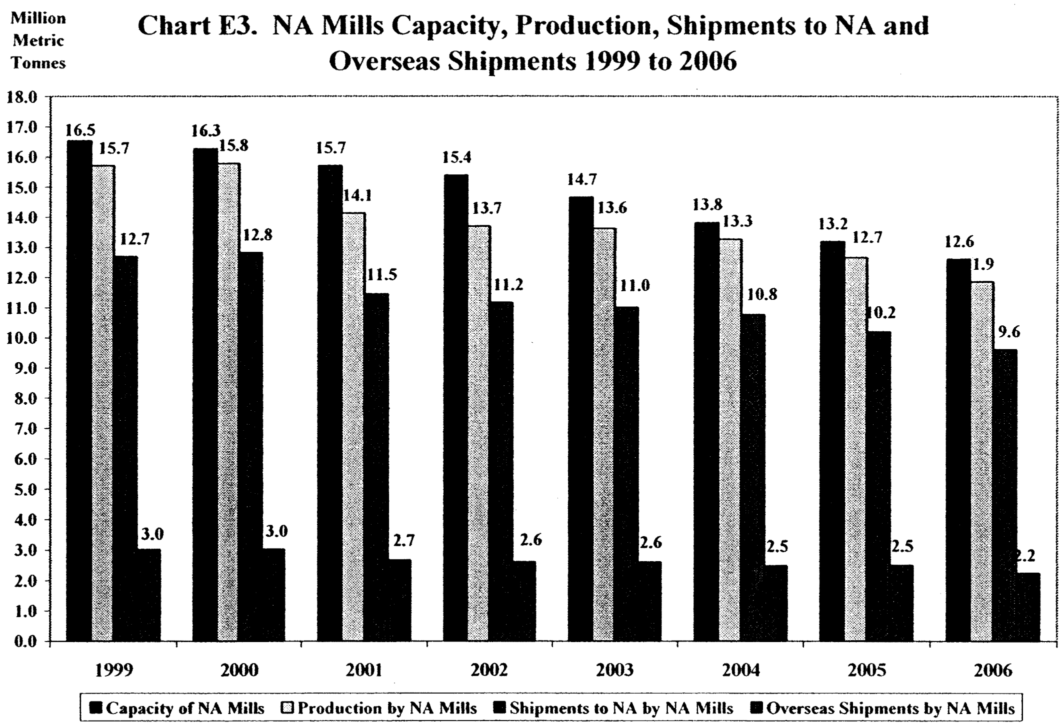
[73] Source: 2006 NPA/NAA Presentation.

2008 in order to maintain a 95% industry operating rate.[74] That amount of capacity reduction would represent 8.4% of current NA capacity and 19.1% of the current combined Abitibi-Bowater capacity.

5. Production, Shipments, and Operating Rates of NA Newsprint Mills 1999–2006

Shipments by NA mills to NA customers and overseas customers declined significantly over the period 1999 to 2006. See Chart E3 below.[75] Shipments to NA customers declined by 24.1% and shipments to overseas customers declined by 25.8%.

Chart E3. NA Mills Capacity, Production, Shipments to NA and Overseas Shipments 1999 to 2006



As a result of the decline in shipments to NA and overseas customers, NA newsprint production declined by 24.5% between 1999 and 2006. Due to newsprint mill closures, newsprint machine shut downs, and newsprint machine conversions to other grades, NA newsprint capacity has declined by 23.7% during the same period.

Chart E4 below shows capacity and production by quarter over the period 1999 to 2006. The chart shows that both capacity and production have declined steadily from the beginning of 2001 through the end of 2006.

[74] The industry operating rate for 1996 was 94% down 2% from a 96% operating rate in 2005 and 2004. Source: December 2005 and 2006 PPPC Flash Reports.

[75] Sources: December 2005 and 2006 PPPC Flash Reports and December 2001–2004 PPPC NA Newsprint Statistics Monthly Bulletin (''PPPC Monthly Bulletin'').

Chart E4. Capacity and Production by NA Newsprint Mills 1999-2006 by Quarter

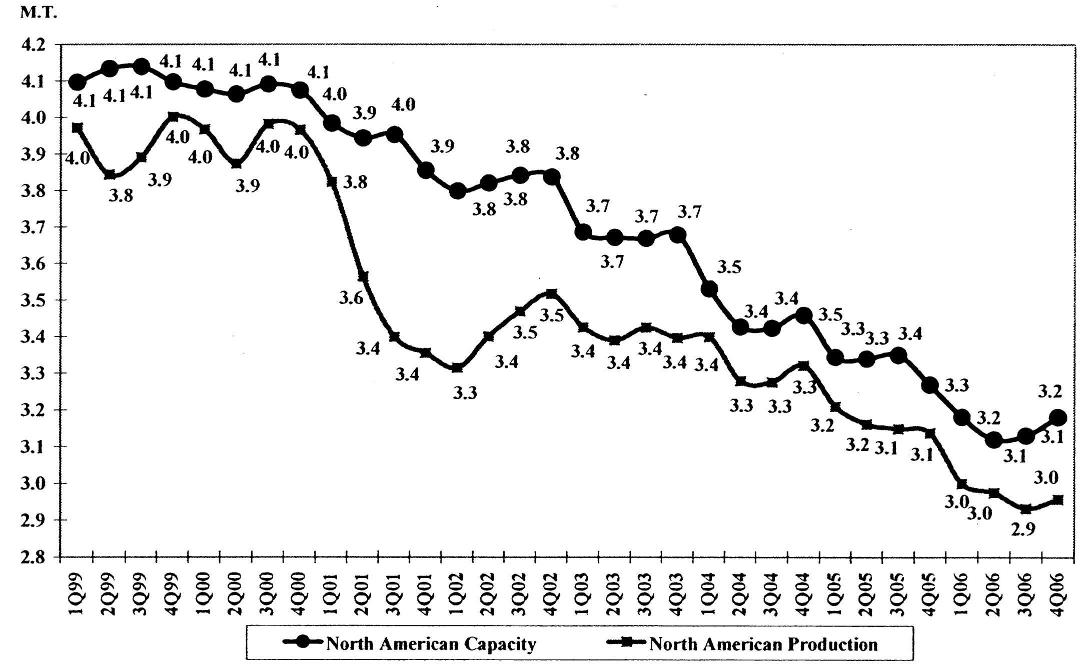
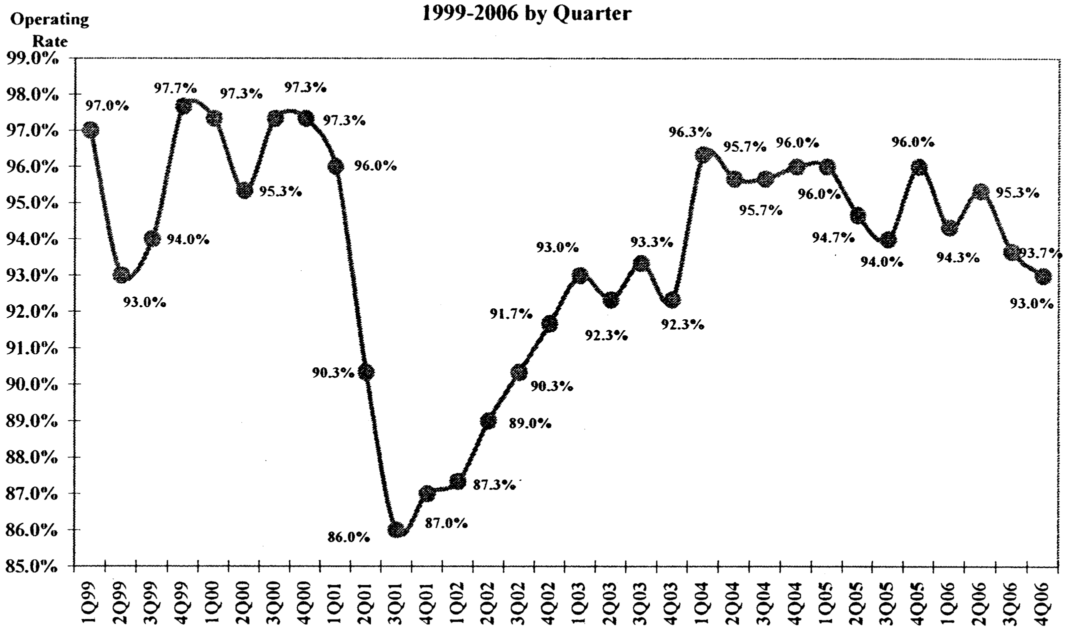


Chart E5 below shows the quarterly operating rates[76] of NA newsprint mills for the period 1999–2006. After the operating rate reached 97.3% in the third and fourth quarters of 2000, the operating rate dropped slightly to 96.0% in the first quarter of 2001 and then plunged sharply for the rest of 2001 reaching a low of 86.0% in the third quarter of 2001. This plunge corresponds to the widening gap between capacity and production shown in Chart E4 over the same period. The sharp decline in the operating rate was caused by the 18.7% decline in the NA demand for newsprint that occurred between the third quarter of 1999 and the first quarter of 2002. The decline in newsprint demand followed the significant slowing of the U.S. economy that began in the first quarter of 2001 and which was exacerbated by the economic disruption caused by the attacks of September 11, 2001.[77] After the third quarter of 2001, the operating rate increased fairly steadily reaching 96.3% in the first quarter of 2004 and remaining at about 96% for the next two years. The operating rate then mostly declined throughout 2006 falling to 93.0% in the fourth quarter of 2006.

Chart E5. The Operating Rates of NA Newsprint Mills 1999-2006 by Quarter



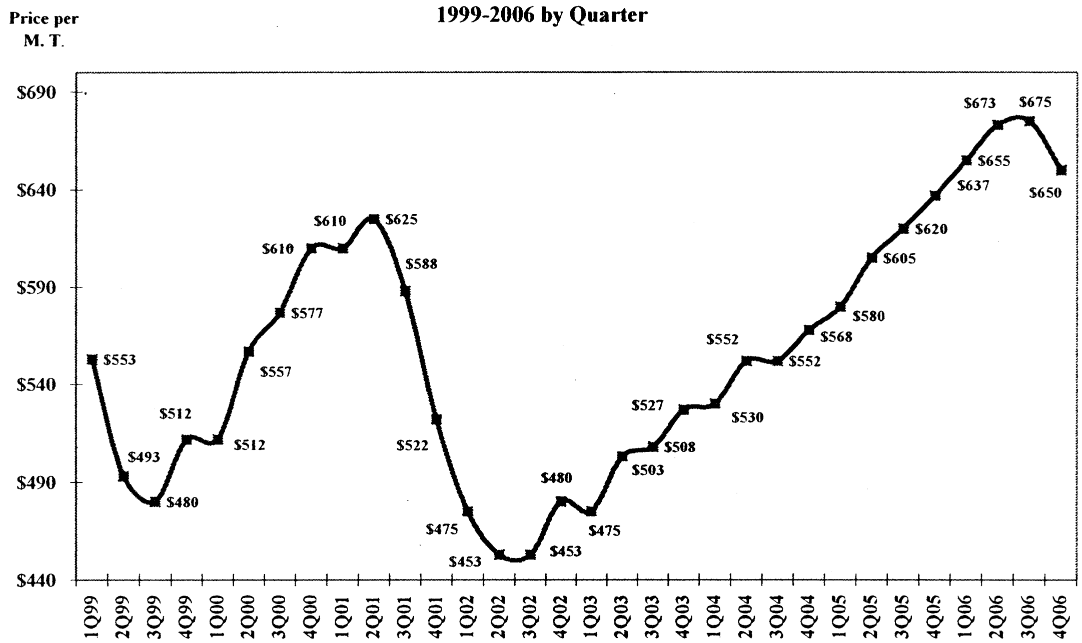
[76] The operating rate is production as a percentage of capacity.

[77] From the fourth quarter of 2000, the U.S. Real Gross Domestic Product declined for three consecutive quarters before increasing in the fourth quarter of 2001. Source: Economic Report of the President, February 2003, Table B.2—Real Gross Domestic Product 1959–2002, p. 278.

6. The Price of Newsprint per Metric Tonne (Eastern U.S., 30 lb.) 1999 to 2006 by Quarter

Chart E6 below shows the price of newsprint per metric tonne by quarter for the period 1999 to 2006.[78] The price is the delivered price per metric tonne in the eastern United States for 30 lb. basis weight newsprint.

Chart E6. The Price of Newsprint per Metric Tonne (Eastern U.S., 30 lb.) 1999-2006 by Quarter



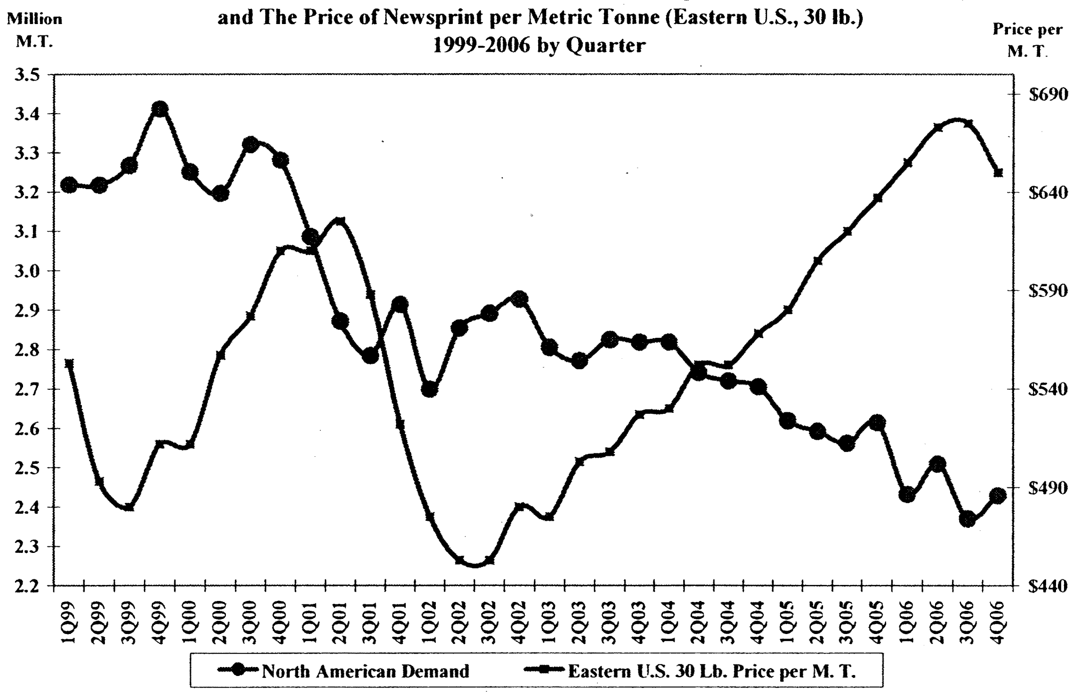
The price of newsprint increased $145 or 30.2% from the third quarter of 1999 to the second quarter of 2001 before falling by $172 or 27.5% through the second quarter of 2002. As Chart E6 shows, price increased in 5 of the 7 quarters during the period of the price rise. In the other two quarters, price was unchanged.

After the bottom was reached in the second and third quarters of 2002, the price of newsprint steadily increased over the next four years from $453 to $675 in the third quarter of 2006. This was an increase of $222 or 49.0%. As Chart E6 shows, price increased in 14 of the 16 quarters over this four-year period. In one quarter, the price was unchanged and in one quarter the price declined by $5. In the fourth quarter of 2006, price decreased slightly to $660.

Combining Chart E2 and Chart E6, shows the two sustained price increases from the end of 1999 to the beginning of 2001 and from the end of 2002 to the end of 2006. During the first period demand was more or less flat and during the second period demand was steadily trending downward. See Chart E7 below.

[78] The source for the quarterly prices is RISI. RISI calculates quarterly prices based on monthly prices that appear in the RISI publication Pulp & Paper Week.

Chart E7. The NA Demand (Quantity Purchased) for Newsprint (Million Metric Tonnes) and The Price of Newsprint per Metric Tonne (Eastern U.S., 30 lb.) 1999-2006 by Quarter



F. Evidence From Presentations to Investment Analysts and Other Public Information That Abitibi and Bowater Have Used Their Control Over Newsprint Capacity and the Newsprint Industry Operating Rate To Significantly Raise the Price of Newsprint 2002 to 2006

1. Introduction

In Section D above, the significant increase in concentration in the NA newsprint industry between 1995 and 2006 and the significant decrease in newsprint capacity over that same period were analyzed. Due primarily to acquisitions by Abitibi and Bowater between 1995 and 2001, the NA newsprint market was transformed from an unconcentrated market in 1995 to a highly concentrated market in 2000 with Abitibi's acquisition of Donohue in April 2000. Bowater's acquisition of Alliance in 2001 and Norske Skog's acquisition of Pacifica, also in 2001, further increased concentration in an already highly concentrated market.

The key to increasing newsprint prices is maintaining high newsprint industry operating rates. Before 1995 no newsprint producer had a market share large enough to cause an increase in the market price. Without the acquisitions of newsprint capacity that they made between 1995 and 2001 (described in Section D above), Abitibi and Bowater could not have profitably pursued a strategy to increase the market price even through coordinated interaction. With the increased capacity under their control, Abitibi and Bowater gained that power and have jointly used it to play the role of a dominant firm. Publicly available information shows that Abitibi and Bowater have acted in a coordinated manner to strategically idle and shut down newsprint capacity sufficient to maintain high industry operating rates and increase the price of newsprint. With the possible exception of Catalyst,[79] the remaining firms in the market have played the role of fringe firms. As fringe firms, they have been generally allowed to operate at full capacity while Abitibi and Bowater determine the amount of their own capacity to idle and shut down as needed to maintain high operating rates for the NA newsprint industry.

Since the end of 2002, Abitibi and Bowater have used their dominant control over NA newsprint capacity to raise operating rates and the price of NA newsprint significantly above competitive levels. Between the third quarter of 2002 and the third quarter of 2006, the price of newsprint has increased by an aggregate of 49.0 percent even though the demand for newsprint declined 16.5 percent over that same period.[80]

John Weaver, the President and CEO of Abitibi, and David Paterson, the President and CEO of Bowater, made separate presentations at the 11th Annual Citigroup Global Paper and Forest Products Conference on December 7, 2006 ("Citigroup Conference"). These presentations are discussed in more detail in Sections F.2. and F.3. below. Weaver emphasized the importance of maintaining a "balance" in the demand and supply of newsprint. Weaver introduced a slide which shows the positive relationship between the level of the newsprint industry operating rate and the percentage change in the list price of newsprint.[81] He said that industry demand and supply had been in "balance" since 2003 and that manufacturers had been able to improve pricing significantly since 2003. He also said that the industry was currently operating at full capacity.

Paterson of Bowater stated that the "industry" had "responded fairly aggressively" to declines in demand and that Bowater was "taking action" to remove capacity from the market. He described the removal of more than 10% of Bowater's newsprint capacity from the market during 2006. During the Q&A, he said that to maintain cash flow and dividend payments, Bowater needed to stay ahead of the demand curve to maintain an operating rate that would give Bowater "pricing leverage". He said "I can do that" by shutting down Bowater's high cost assets hopefully before price erosion has set in with any significance. From these remarks, it is clear that that the control of capacity is used by Abitibi and Bowater not only to raise newsprint prices but to prevent prices from falling from current levels.

This section discusses information primarily from Abitibi and Bowater presentations to investment analysts. This evidence is consistent with and supportive of our hypothesis that Abitibi and Bowater acted as a joint dominant firm to raise the price of newsprint significantly above competitive levels from the end of 2002 through 2006. Section I below discusses

[79] If there is a West of the Rockies relevant market (as well as an East of the Rockies relevant market), it seems possible that Catalyst has played the role of a dominant finn in that market in much the same way that Abitibi and Bowater have played that role in the NA newsprint market or in an East of the Rockies relevant market should such a market exist. Catalyst's newsprint mills are located entirely within British Columbia. Evidence relating to the possibility of Catalyst acting as a dominant firm in a West of the Rockies market is discussed at the end of Section G.5.

[80] As analyzed in Section E above, the decline in newspaper demand for newsprint was due mostly to downward shifts of the demand curve for NA newsprint and does not indicate a movement up the demand curve in response to upward shifts of the supply curve.

[81] The percentage change shown in the slide is the percentage change of a price in a given month from the June 2000 price of newsprint.

Abitibi's closures of newsprint capacity over the period 1999 to 2001 and the relation of those closures to increases in the operating rate and increases in newsprint prices.

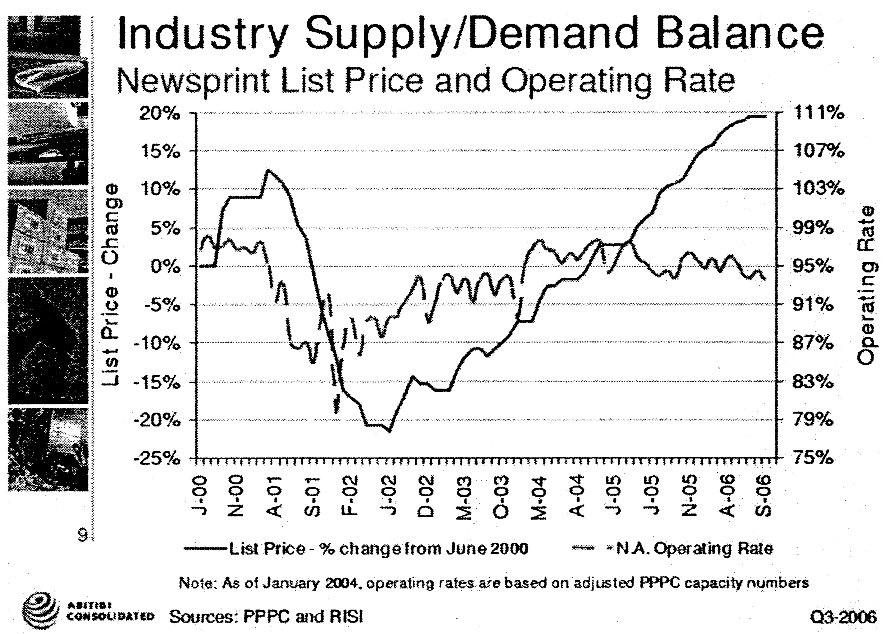
This section provides evidence of Abitibi's and Bowater's anticompetitive conduct for the period 2002–2006, based on (a) John Weaver's presentation at the December 2006 Citigroup Conference (Section F.2.); (b) David Paterson's presentation at the same Citigroup Conference (Section F.3.); (c) John Weaver's presentation to the Credit Suisse First Boston investment analysts conference in March 2004 (Section F.4.); and (d) an interview of John Weaver by paperloop.com in February 2004 (Section F.5.).

2. Presentation by John Weaver, President and CEO of Abitibi, at the Citigroup Conference in December 2006

John Weaver, president and CEO of Abitibi, spoke for about 30 minutes at the December 2006 Citigroup Conference. His presentation consisted of commentary on slides prepared by Abitibi [82] and a follow-up Q&A session with investment analysts.[83]

Slide 9 of Weaver's presentation shows the relation between the level of the newsprint operating rate and percentage change in the list price of newsprint between July 2000 and September 2006.[84] The list price is expressed as a percentage of the June 2000 list price. List prices are based on RISI data and operating rates are based on PPPC data. See Slide 9 below. This slide with some variations has been presented by Abitibi to investment analyst groups since June 5, 2003. These presentations are archived on the Abitibi Web site.

Slide 9: Abitibi Citigroup 12/7/06



Slide 9 and Slide 10, which follow are titled ''Industry Supply/Demand Balance.'' Slide 9 is sub-titled ''Newsprint List Price and Operating Rate.'' Slide 9 shows that beginning in September of 2000, price rose about 12% above the June 2000 price by April 2001. As the U.S. economy went into negative growth in 2001, price plunged by 33% (from 12% above the June 2000 price to 21% below the June 2000 price) reaching the bottom in July 2002. Price then rose in a fairly uninterrupted path from 21% below the June 2000 price to 20% above the June 2000 price by September 2006.

The operating rate bottomed out at the end of 2001, about 6 months before the bottoming out of price. The operating rate then rose in fits and starts to above 95% by early 2004. Price rose accordingly, lagging the increase in the operating rate by several months. As will be discussed below, Weaver describes a 95% operating rate as a full capacity rate for the industry.

Weaver said that demand and supply have more or less been in balance since 2003.[85] He said that manufacturers have been able to improve pricing significantly over this period [as is clearly depicted in Slide 9].

Weaver said that the industry had been at a 95%+ operating rate for past 2 years and since mill inventories were declining, a 95% operating rate is ''for all intents and purposes the full operating rate.[86] We can't really make

[82] The 27 page slide show is titled ''Our Story on Paper.''

[83] The slide show is available on Abitibi's Web site under Investor Relations/Presentations and Web casts. According to Abitibi's Web site, the audio recording of Weaver's comments at the Citigroup Conference is no longer available on the Web site.

[84] John Weaver's presentation to the June 5, 2003 Scotia Capital Materials Conference appears to be the first presentation where Abitibi provided a slide (Slide 15) showing the relation between the newsprint operating rate and the price of newsprint. See the investment analyst presentations on the Abitibi Web site. As discussed in Section H.3.a. below, Slides 9 and 15 may have been inspired by a similar figure published in an article by a RISI senior economist in *paperloop.com* on February 20, 2003. While there are obvious differences between Slides 9 and 15 and the figure that appeared in the RISI economist's article, the differences are superficial. The fundamental economic relationships that are illustrated in Slide 9 and in the figure in RISI economist's article are identical.

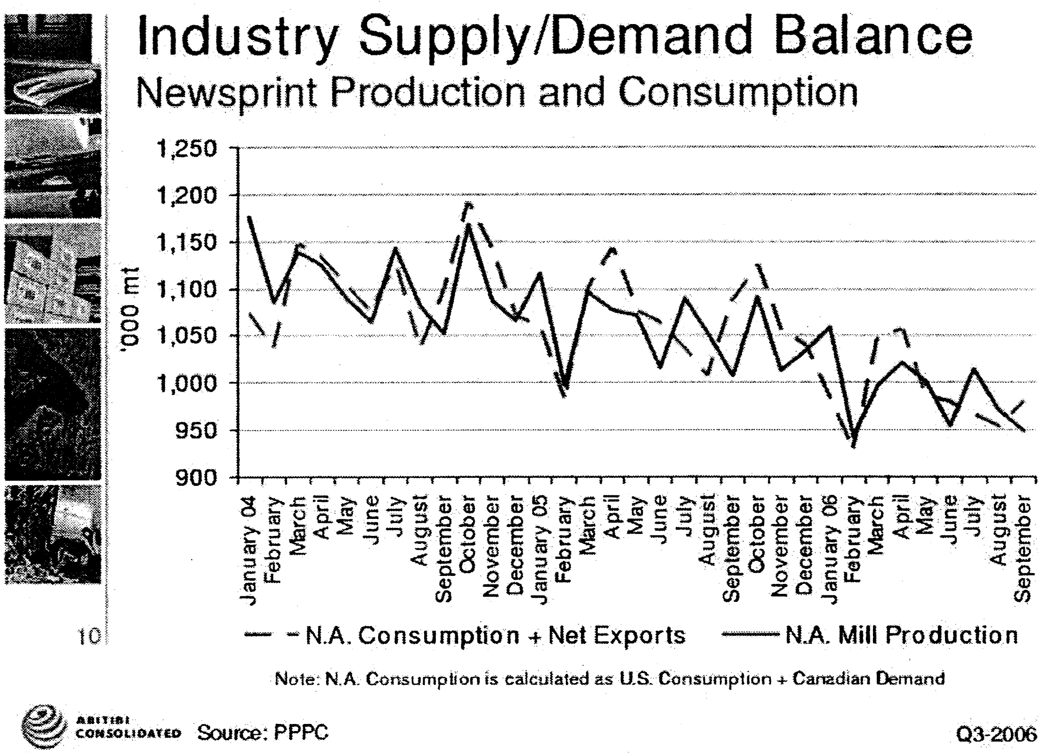
[85] Weaver's remarks on Slides 9 and 10 begin at about 5:31 into the copy of the audio recording that we have provided to DOJ.

[86] Full operating capacity is usually considered to be 98% of theoretical full capacity. How can 95% be full operating capacity as Weaver stated? Newsprint operating rates are calculated by the PPPC. If Abitibi indefinitely idles a machine in order to maintain the maximum practical industry operating rate, that machine is still counted as available capacity by the PPPC even though the machine has been strategically idled. If the Abitibi newsprint machine remains idled for a long enough period of time the PPPC will eventually remove that capacity from its capacity forecasts and Flash Reports. At the time Weaver spoke to the Citigroup Conference in December 2006, Abitibi and Bowater had each indefinitely idled one newsprint machine. In addition, Stora Enso's newsprint machine had been shut down for almost a year due to labor and energy problems. If the capacity of these three machines were not included in the calculation of industry operating rates, the industry would be operating at 98% of total capacity. The Stora Enso machine was re-started at about the time Weaver was giving his presentation at the December 2006 Citigroup Conference.

There is also a distinction between market-related downtime and the strategic idling of capacity. If a relatively small newsprint producer takes market-related downtime, it is because the producer does not have enough orders to keep operating. It is any more tonnes than we are making now. I am talking about the industry there.''

Slide 10 below shows the newsprint industry supply/demand balance from January 2004 through September 2006.

Slide 10: Abitibi Citigroup 12/7/06



Demand (quantity purchased) is defined as NA consumption plus net exports. Referring to Slide 10, Weaver said ''month after month production is equal to consumption'' and since mill inventories are flat or trending down, ''there is no excess capacity in the marketplace today. It [i.e., production] is all being consumed.''

3. Presentation by David Paterson, President and CEO of Bowater, at the Citigroup Conference in December 2006

David Paterson of Bowater, also made a presentation at the Citigroup Conference on December 7, 2006. The format was similar to Weaver's presentation.[87]

The note at the bottom of Slide 13 of Paterson's presentation says ''Balanced newsprint capacity & demand.'' See Slide 13 below. The slide plots the quantity of NA demand and supply over the period 2000 to 2006. The slide shows similar downward slopes over time for both demand and supply. Paterson said ''North American demand. That's not the slope you want clearly but the industry has responded fairly aggressively.''[88] He said that ''I think that the real challenge is that if that slope continues at the rate it is in the fourth quarter, clearly actions will need to be taken.'' He said that Bowater has removed 300,000 metric tonnes of newsprint capacity (or more than 10% of Bowater's total capacity) in 2006 from the NA market. The capacity removals were accomplished by a machine conversion at Bowater's Calhoun, TN mill to uncoated groundwood specialty grades (150,000 metric tonnes) and by a shut down of PM #4 at Bowater's Thunder Bay, ON mill (150,000 metric tonnes). He said that Bowater also took significant downtime on PM #5 at Thunder Bay in the fall.[89] ''We are taking action,'' he said.

likely that the producer intends to restart the machine as soon as it can book enough orders, perhaps through offers of discounts. With Abitibi and Bowater, the motivation is generally, though not always, different. [Both Abitibi and Bowater have taken market-related downtime since 2002.] Their goal is maximum operating rates. They are using the indefinite idling of capacity as a lever to raise prices.

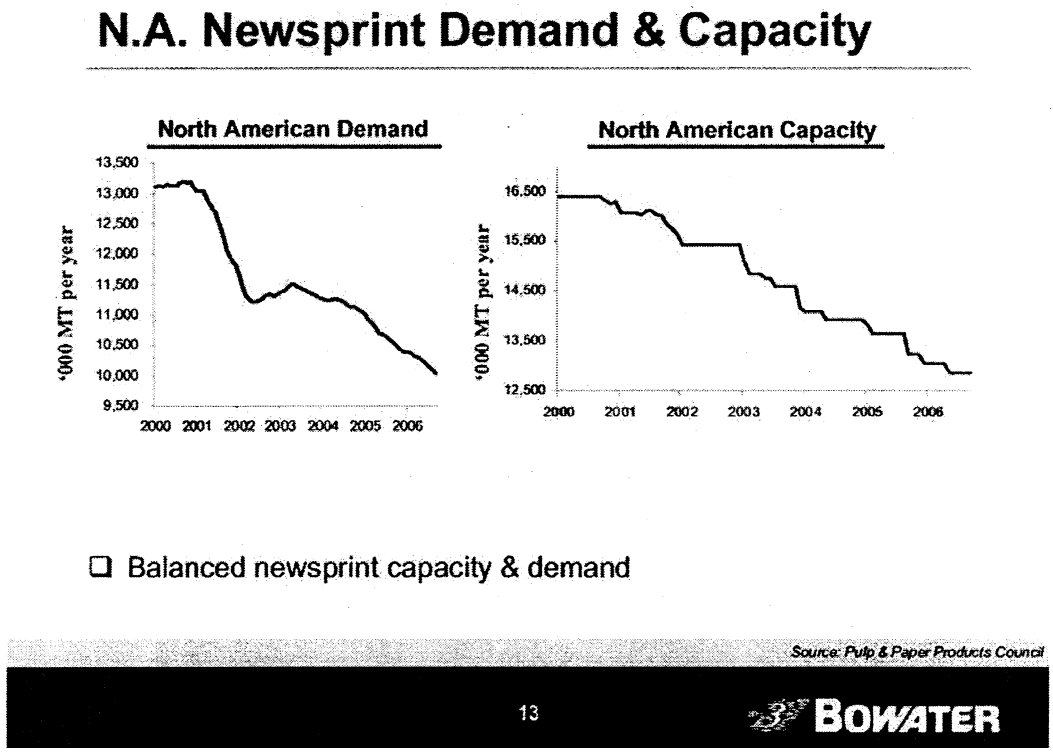
We are unaware of any Abitibi or Bowater indefinitely idled newsprint capacity that has been restarted. The capacity has either been shut down or has remained indefinitely idled. The subject of determining the ''real'' operating rate as opposed to the PPPC official operating rate is discussed further in Section H.3.c. below.

[87] The slide show is available on Bowater's Web site under Investor Relations/Presentations. According to Bowater's Web site, the audio recording of Paterson's comments at the Citigroup Conference is no longer available on the Web site.

[88] Paterson's remarks on Slide 13 begin at about 10:44 of the copy of the audio recording we have provided to DOJ.

[89] PM #5 at Thunder Bay was only temporarily idled and has been restarted. PM #4 at Thunder Bay has been indefinitely idle. If it is restarted it is unlikely that it will be producing newsprint according to news reports.

Slide 13: Bowater Citigroup 12/7/06



During the Q&A that followed the slide show, Paterson was asked about maintaining cash flow and dividend payments. Paterson said that in the near term, newsprint pricing is stable but that any significant decline in prices would cause another round of closures, primarily Canadian assets.[90] Paterson said that Bowater's U.S. mills are more efficient than Bowater's Canadian mills. He said if Bowater just had U.S. mills, the newsprint business would be pretty good at today's prices. But in Canada, due to energy and currency issues, age of equipment and other reasons, ''there is not a lot of margin left in the Canadian assets.''

Paterson said he thinks about near-term cash management as using two tools to sustain cash flow.—''One is newsprint pricing and the ability to manage that and that's critical. I've got two and a half million tonnes [of capacity], so the math is pretty compelling. Every $10 bucks, with a company our size, that's $25 million in revenue that I've got to protect. So that's number one.''

Paterson then elaborated on the second tool that Bowater uses to sustain near-term cash flow:

''Number two is we have to stay ahead of that curve, that demand curve that you mentioned to sustain cash flow. So my belief [* * *] is that we have to move faster to stay ahead of that [demand] curve to maintain an operating rate that gives us some pricing leverage in the market and I can do that. We know which our high cost assets are and we will shut them down hopefully before rather than after price erosion with any significance. So that's the second tool. Now what does that do? My spread between best and worst assets is quite significant. So without doing anything else, I can lower my total manufacturing costs pretty significantly. I've got to balance that against—you know these assets are generating cash and we need to pay down debt and do other things.''

He said that the Bowater Board of Directors is committed to paying dividends and that the board challenges management to generate operating cash flow on a sustainable basis to pay dividends and interest payments.

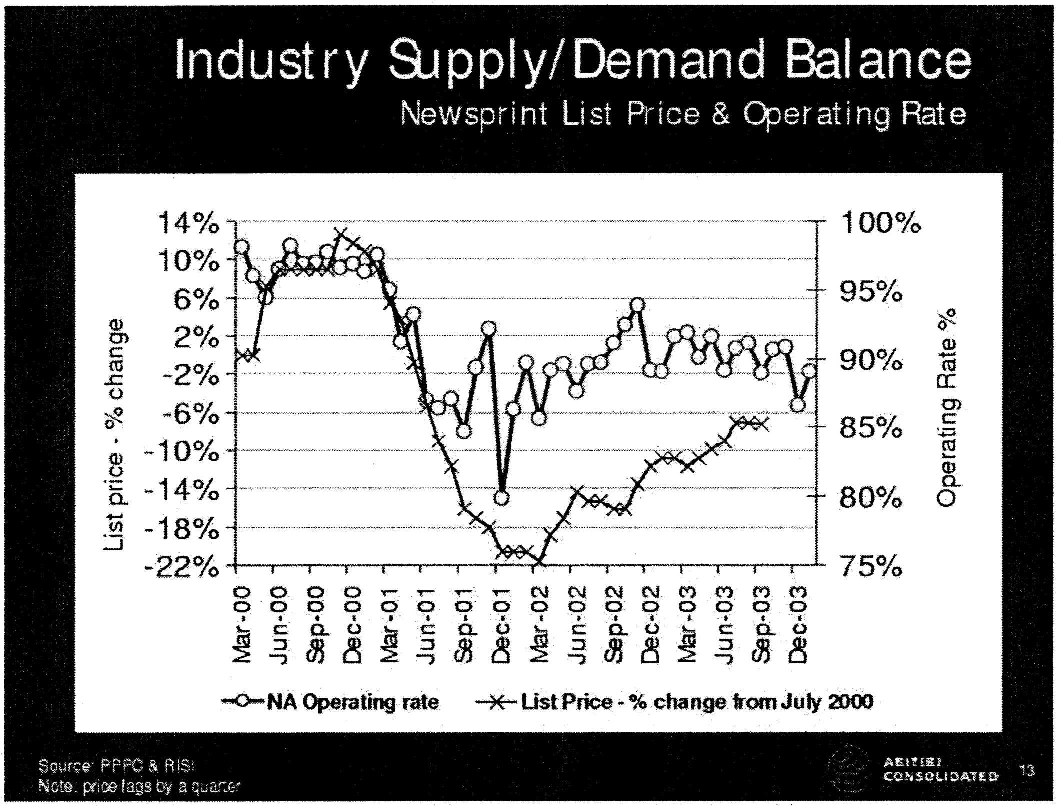
4. Presentation by John Weaver, President and CEO of Abitibi, at the Credit Suisse First Boston Investment Analysts Conference in March 2004

John Weaver gave a presentation at the Credit Suisse First Boston Credit Global Basics Conference on March 3, 2004 (''Credit Suisse Conference''). Three consecutive slides presented by Weaver relate to the closure of Abitibi's capacity in order to raise industry operating rates and prices.

Slide 13 below is an earlier version of Slide 9 that Weaver presented at the December 2006 Citigroup Conference. Slide 13 shows that the price of newsprint lags the NA operating rate by about a quarter. When the operating rate begins to fall, the newsprint price will begin to fall several months later. Similarly, when the operating rate begins to rise, the newsprint price will begin to rise several months later.

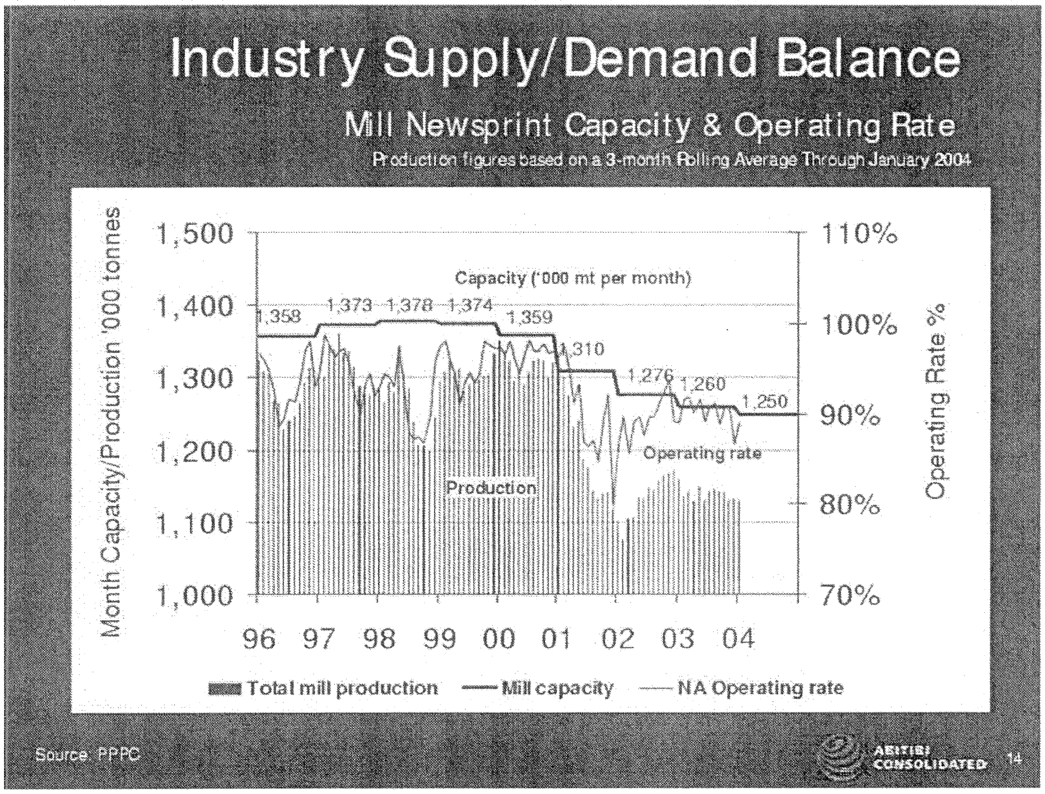
[90] Paterson's response to the question on how Bowater will sustain its cash flow begins at about 27:35 of the copy of the audio recording we have provided to DOJ.

Slide 13: Abitibi Credit Suisse 3/3/04



Slide 14 below shows NA monthly newsprint production, capacity and operating rate from mid-1996 through January 2004.

Slide 14: Abitibi Credit Suisse 3/3/04



Note that capacity hit a monthly high of 1,378 metric tonnes in 1998. Between 1998 and 2001, capacity declined by about 5%. Abitibi began removing newsprint capacity from the newsprint market in 1999 and announced additional newsprint capacity removals in conjunction with its acquisition of Donohue in April 2000. These capacity closures are discussed in Section I below. Between the end of 2001 and the end of 2003, an additional 7% of capacity, compared to the 1998 peak, was removed from the market. Some of this capacity removal was due to the closure of the Garden State mill at the end of 2001. In addition, several other manufacturers converted small newsprint machines to other groundwood grades as is discussed in Sections D.3. and D.4. above. Slide 14 projects additional capacity reduction in 2004 to bring the total reduction as a percentage of the 1998 peak to 12.8%. Between the 1998 peak through projected 2004, Abitibi and Bowater accounted for almost 80% of the total reduction.

Slide 15 below shows that Abitibi removed 977,000 metric tonnes of capacity from the NA newsprint market in 2003. About 43% of the removal was due to temporary rotating downtime (i.e., market related downtime). The remaining 57% of the 2003 capacity removal was due to the indefinite idling of capacity. Abitibi calculated the 2003 industry operating rate at 87%. This calculation excludes Abitibi's indefinitely idled capacity from total NA newsprint capacity (i.e., the denominator of the operating rate calculation). The exclusion of Abitibi's indefinitely idled capacity from total NA capacity indicates that the capacity was withheld from the market for the strategic purpose of raising the industry operating rate and increasing the price of newsprint.

Slide 15: Abitibi Credit Suisse 3/3/04

Newsprint Capacity Closures

Abitibi-Consolidated - North America

In metric tonnes	2003	2004
Indefinitely Idled	558,000	760,000
Converted	0	(50% of Alma) 85,000
Permanently Closed	0	230,000
Rotating Downtime	419,000	0
Total Capacity removed	977,000	1,075,000
NA Capacity (ex indefinite idling)	4,272,000	3,774,000
Operating Rate (based on 2003 sales : ex indefinite idling)	87%	99%

For complete details, see Q4-2003 MD&A, table 3

ABITIBI CONSOLIDATED 15

Slide 15 also shows Abitibi's projected 2004 capacity removals. In 2004, Abitibi was projected to remove 1,075,000 metric tonnes of newsprint capacity from the NA market. Rotating downtime was not expected to account for any of the capacity removal in 2004. Abitibi projected that it would achieve its capacity removal in 2004 by increasing indefinitely idled capacity by 202,000 metric tonnes, by permanently closing 230,000 metric tonnes of capacity, and by converting 85,000 metric tonnes of capacity to uncoated groundwood specialty grades. Slide 15 also shows projected 2004 NA capacity (excluding indefinitely idled capacity) declining by 498,000 metric tonnes from 2003. Abitibi's projected increase in capacity removal in 2004 accounts for all of the projected reduction in total NA newsprint capacity from 2003.[91] The 2004 industry operating rate was projected to rise from 87% in 2003 to 99% in 2004. This calculation does not include Abitibi's indefinitely idled capacity in NA capacity. Slide 15 illustrates numerically the key role that Abitibi's indefinitely idled capacity played in achieving the projected maximum industry newsprint operating rate in 2004.

5. Interview of John Weaver Titled "Tighter Supply/Demand Balance Boosts Newsprint Hike Prospects Says Abitibi's Weaver"

John Weaver, President and CEO of Abitibi, was interviewed by Will Mies, Editorial Director, Paperloop Information Products. The interview was published on *paperloop.com* on February 11, 2004.

The article describes Abitibi's aggressive "focused downtime" strategy. While the term "focused downtime" strategy is not explicitly defined in the article, it clearly means that the newsprint machine or newsprint mill has been indefinitely idled. It should be noted that none of the mills mentioned in the article subject to Abitibi's "focused downtime" strategy in December 2003 have re-opened. The Port-Alfred, QC and Sheldon, TX mills have been permanently closed. The Lufkin, TX mill remains indefinitely idled.

Abitibi-Consolidated has been aggressively pursuing a "focused downtime" strategy. On Dec. 14 the company indefinitely idled its Lufkin, Texas, and Port-Alfred, Que., newsprint mills, extended downtime at its Sheldon, Texas, mill and permanently shut two machines at the latter two mills with 230,000 tonnes/yr. of capacity. As a result, the company began the year with one million tonnes of newsprint capacity removed from the market—and this excludes the conversion of the company's Alma, Que., to Equal Offset paper production later this year. Last year the company took 977,000 tonnes of newsprint downtime and 887,000 tonnes in 2002.

As used by Abitibi, "focused downtime" or the indefinite idling of capacity means that this capacity has been removed from the market to maintain high newsprint industry operating rates. The capacity would not be restarted if the effect would be to lower the operating rate from its current and, presumably, high level. However, it seems plausible that indefinitely idled capacity would be restarted if there were sufficient increases in newsprint demand that the restart would not adversely affect the industry operating rate. Since demand has been consistently declining in recent years, none of Abitibi's indefinitely idled machines has been restarted. As noted above, most have been permanently closed. "Focused downtime" or the indefinite idling of capacity should not he confused with market related downtime. As discussed in Section F.4 above market related downtime, called "rotating downtime" in Slide 15, was a temporary idling of capacity that would be brought back on line as demand rebounds to expected levels.

When asked about Abitibi's pricing goal, "Weaver said that AbitibiConsolidated's goal is to 'return newsprint prices back to their trend line level' which would eventually bring prices on standard newsprint up to around $585–595/tonne level."

Weaver was asked if consolidation is working (i.e., Abitibi's acquisitions of Stone-Consolidated and Donohue that occurred in 1997 and 2000). His reply was included in the quote below.

The acquisition of Donohue followed the 1997 merger with Stone-Consolidated; both events were followed by significant capacity shutdowns, downtime and rationalization. Has all of the money spent on the vision of consolidation begun to pay off for shareholders? "There have been a number of signs that consolidation is working, such as the inventory control we have seen over the past several years and *several supply-driven price increases over the last two years,*" Weaver said.

[91] In fact, Abitibi's projected increase in capacity removals between 2003 and 2004 exceeds the projected decline in industry capacity by 19,000 metric tonnes.

"All of the consolidators have taken out significant cost by closing their high cost capacity and reconfiguring their companies,"[92] he said. But none of the acquiring companies could foresee at the time of their acquisitions that they would have to carry the debt through a three-year economic downcycle, he added. "When the economy recovers, we will see the real returns from consolidation." (Emphasis added)

G. An Analysis of Permanent Newsprint Capacity Reductions Between 2002 and 2006

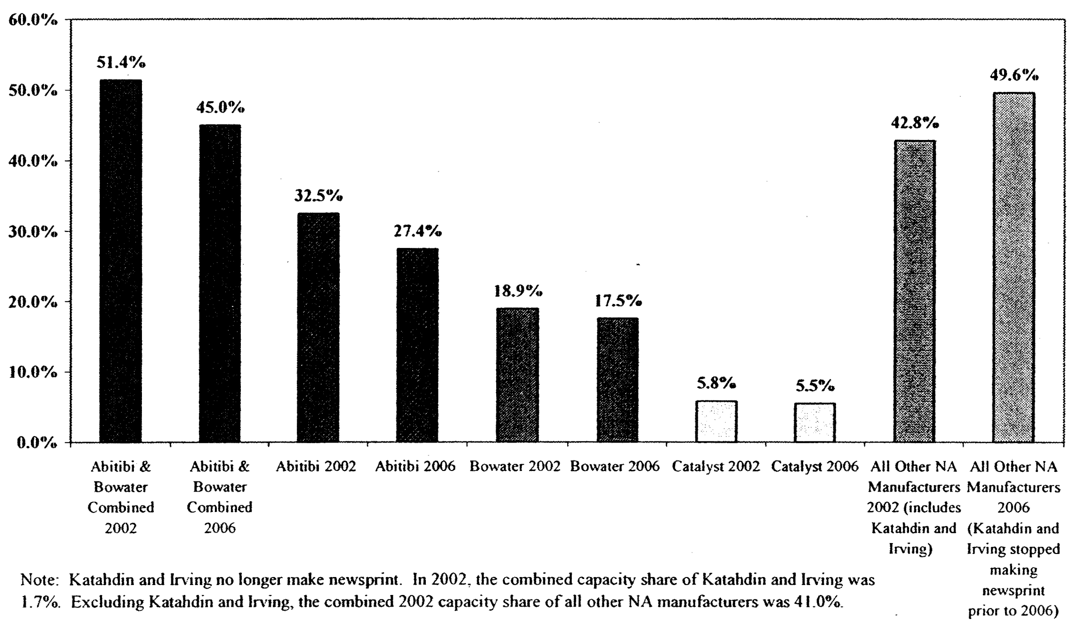
1. Introduction

Section D.4. above analyzed the permanent capacity reductions that occurred in the NA newsprint industry between 1995 and 2006. The analysis showed that of the firms that (a) had net capacity reductions between 1995 and 2006 and (b) remain in the market today, Abitibi and Bowater combined accounted for 83.6% of those permanent capacity reductions. Catalyst accounted for most of the remaining permanent capacity reductions. The analysis in this section focuses on permanent newsprint capacity reductions in North America between 2002 and 2006. As documented in Section E.6., newsprint prices rose an aggregate of 49.0% between the third quarter of 2002 and the third quarter of 2006. Of the newsprint manufacturers that remain in the market today, Abitibi and Bowater combined accounted for 89.4% of the permanent reductions of NA newsprint capacity between the end of 2002 and the end of 2006. Charts G1 to G4 provide an analysis of the NA permanent capacity reductions during this period.

2. Chart G1: Shares of NA Newsprint Capacity by Manufacturer 2002 and 2006

Chart G1 below shows the shares of NA newsprint capacity by manufacturer for 2002 and 2006.[93] At the end of 2002, NA newsprint capacity was 15,555,000 metric tonnes and at the end of 2006, estimated NA newsprint capacity was 12,760,000 metric tonnes.

Chart G1: Shares of NA Newsprint Capacity by Manufacturer 2002 and 2006



Note: Katahdin and Irving no longer make newsprint. In 2002, the combined capacity share of Katahdin and Irving was 1.7%. Excluding Katahdin and Irving, the combined 2002 capacity share of all other NA manufacturers was 41.0%.

Chart G1 shows that the combined Abitibi and Bowater NA capacity share declined from 51.4% to 45.0% between the end of 2002 and the end of 2006 and that Catalyst's share declined by 0.3%. Including Katahdin and Irving, the shares of all other NA newsprint manufacturers increased from 42.8% to 49.6%.[94] Katahdin and Irving converted their newsprint capacity to the production of uncoated groundwood specialty grades in 2005–2006. Excluding Katahdin and Irving, the shares of all other NA newsprint manufacturers increased from 41.0% to 49.6% from the end of 2002 to 2006.

3. Chart G2: Permanent Reduction of NA Newsprint Capacity by Manufacturer During the Period 2002–2006

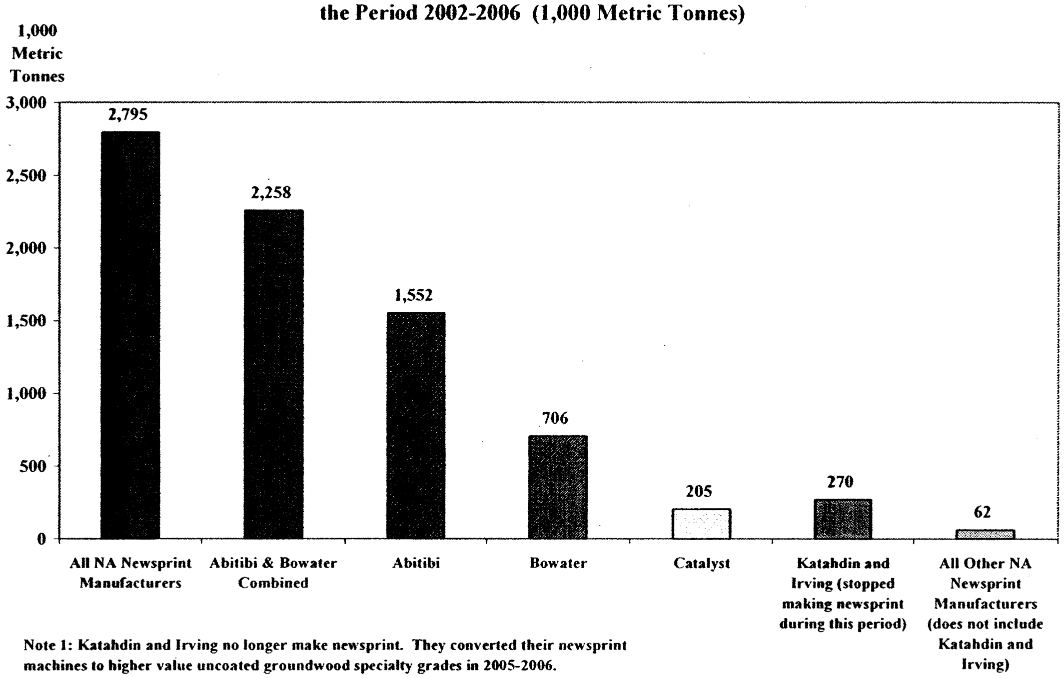
Chart G2 below shows the permanent reduction of NA newsprint capacity by manufacturer during the period 2002 to 2006.

[92] This statement can only apply to Abitibi, Bowater and Catalyst.

[93] The Sources for Charts G1 to G4 are as follows: (I) For estimated 2006 NA newsprint capacity, see Tables C1 and C2 in Attachment C. (2) The sources for 2002 newsprint capacity are as follows: (a) Abitibi 2002 Annual Report, p. 28; (b) Bowater 2002 Annual Report, p. 6; (c) for Catalyst, Katahdin Paper, and Irving Paper, see 2003 capacity shown in PPPC's July 9, 2004 "Update of North American Mechanical Printing Papers Capacity Forecast"; (d) for total 2002 NA newsprint capacity, see "North American Newsprint Capacity: Results of PPPC's 2003 Capacity Survey," March 3, 2003. The Abitibi and Bowater annual reports are available on their respective Web sites. The two PPPC capacity surveys are available on the PPPC Web site under Press Releases.

[94] At the end of 2006 there were 16 newsprint manufacturers operating in North America. This total includes the Ponderay newsprint mill in which Bowater has a 40% ownership-interest. The category "All Other NA Manufacturers 2006" includes 13 firms. See Tables C1 and C2 in Attachment C for more details.

Chart G2: Permanent Reduction of NA Newsprint Capacity by Manufacturer During the Period 2002-2006 (1,000 Metric Tonnes)



Note 1: Katahdin and Irving no longer make newsprint. They converted their newsprint machines to higher value uncoated groundwood specialty grades in 2005-2006.

There were 2,795,000 metric tonnes of capacity permanently removed from the NA newsprint market from the end of 2002 to the end of 2006. Abitibi and Bowater combined accounted for 2,258,000 metric tonnes that were permanently removed [95] and Catalyst accounted for 205,000 metric tonnes. The conversion of the Katahdin and Irving newsprint capacity to uncoated groundwood specialty grades accounted for 270,000 metric tonnes of capacity removal. All other NA newsprint manufacturers accounted for 62,000 metric tonnes of capacity removal.

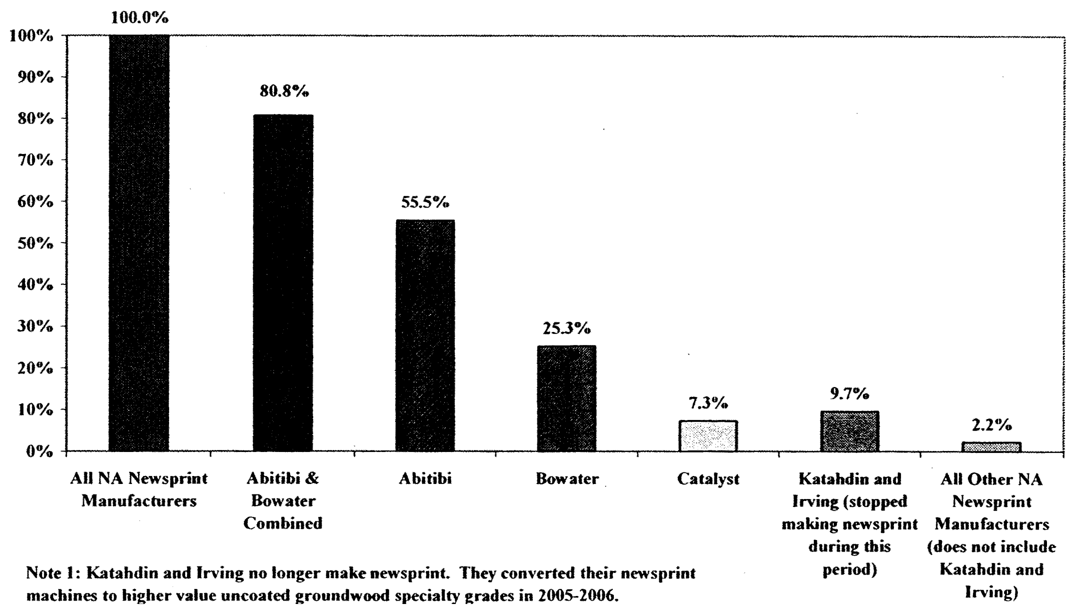
Tembec's closure of a 35,000 metric tonne capacity newsprint machine at its Kapuskasing, ON mill accounted for more than half of this total.

4. Chart G3: Percentage of Total NA Permanent Newsprint Capacity Reduction by Manufacturer During the Period 2002–2006

Chart G3 below shows the percentage of total NA permanent newsprint capacity reduction by manufacturer during the period 2002 to 2006.

[95] The capacity reduction totals for Abitibi and Bowater do not include the capacity of their newsprint machines that are currently indefinitely idled. Abitibi has two indefinitely idled newsprint machines. One machine (PM 2) is at its indefinitely idled Lufkin, TX mill. It has a capacity of 150,000 metric tonnes and has been idled since December 2003. The other machine (PM 7) is at Abitibi's Grand Falls, NL mill. It has a capacity of 60,000 metric tonnes and has been indefinitely idled since the end of 2005. Bowater's #4 paper machine at its Thunder Bay, ON mill has been indefinitely idled since September 2006. It has a capacity of 146,000 metric tonnes.

Chart G3: Percentage of Total NA Permanent Newsprint Capacity Reduction by Manufacturer During the Period 2002-2006



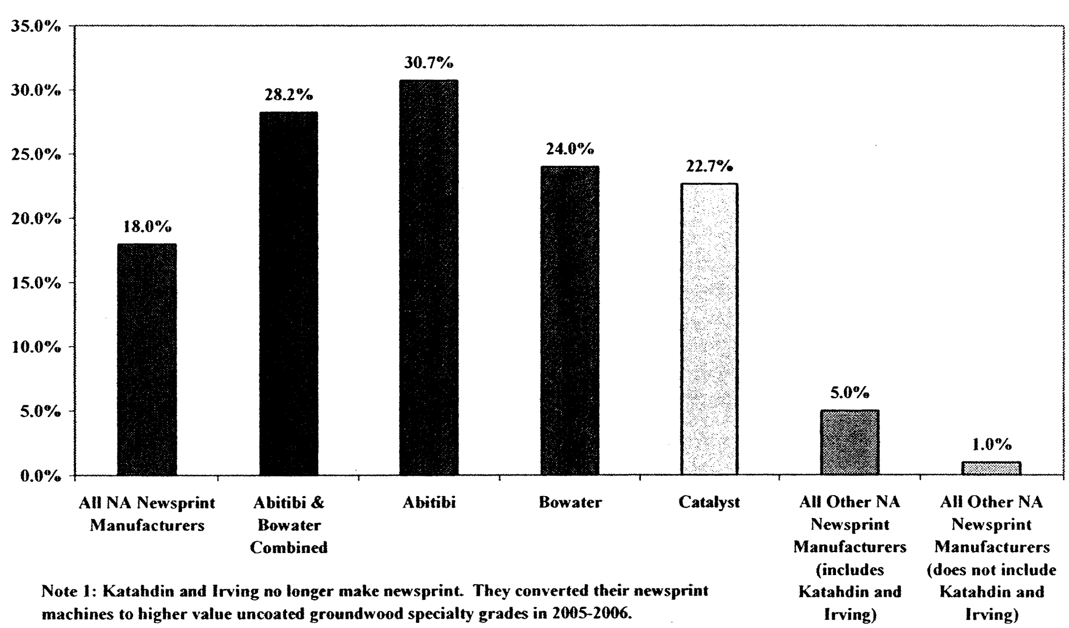
Note 1: Katahdin and Irving no longer make newsprint. They converted their newsprint machines to higher value uncoated groundwood specialty grades in 2005-2006.

The percentage calculations are based on the capacity reduction figures shown above in Chart G3. Combined, Abitibi and Bowater accounted for 80.8% of the permanent capacity removals over this period and Catalyst accounted for 7.3%. Of manufacturers that remain in the market today, Abitibi and Bowater combined account for 89.4% of the total capacity removals and Catalyst accounts for 8.1%. The two manufacturers who converted their newsprint capacity to uncoated groundwood specialty grades accounted for 9.7% of the total permanent capacity reduction. All other NA newsprint manufacturers accounted for 2.2% of the total capacity removals and 2.5% of the capacity removals by the manufacturers that remain in the market today.

5. Chart G4. Permanent Reduction of Newsprint Capacity Over the Period 2002–2006 as a Percentage of Own 2002 NA Capacity by Manufacturer

Chart G4 below shows the permanent reduction of NA newsprint capacity over the period 2002 to 2006 as a percentage of each manufacturer's own capacity at the end of 2002.

Chart G4. Permanent Reduction of Newsprint Capacity Over the Period 2002-2006 as a Percentage of Own 2002 NA Capacity by Manufacturer



Note 1: Katahdin and Irving no longer make newsprint. They converted their newsprint machines to higher value uncoated groundwood specialty grades in 2005-2006.

Between the end of 2002 and the end of 2006, NA newsprint capacity was reduced by 18.0%. Through permanent capacity removals, Abitibi reduced its own capacity by 30.7% and Bowater reduced its own capacity by 24.0%. Catalyst also reduced its newsprint capacity by a significant proportion—22.7%. The other 13 newsprint manufacturers that remain in the market today reduced their capacity by a combined 1.0%.

Catalyst is the largest newsprint manufacturer West of the Rockies. Catalyst's removal of a significant amount of its own newsprint capacity from the market suggests the possibility of a relevant West of the Rockies newsprint market and a relevant East of the Rockies newsprint market. Norske Skog's acquisition of Pacifica in 2001 may have given it the incentive and ability to shut down capacity to raise the industry operating rate and increase prices in a West of the Rockies market.[96] If there is a West of the Rockies relevant newsprint market, Catalyst may have been playing the same role in a West of the Rockies market as Abitibi and Bowater were playing in an East of the Rockies market (i.e., shut down capacity to raise the industry operating rate and increase prices). All of Abitibi's and Bowater's capacity reductions have occurred in mills located East of the Rockies. Bowater has no mills West of the Rockies and Abitibi has only a limited newsprint manufacturing presence West of the Rockies.

H. Four Articles by Two Newsprint Industry Experts Describing the AbitibiBowater Strategy to Raise Price by Closing Capacity

1. Introduction

Four articles by two newsprint industry experts are cited in this section describing the strategy of Abitibi and Bowater to raise the price of newsprint through the closure of capacity. The first article does not specifically identify Abitibi and Bowater, but the events described can only apply to Abitibi, Bowater and, possibly, Catalyst. The four articles are evidence that the Abitibi-Bowater strategy is well understood throughout the newsprint industry by buyers and sellers alike. The four articles also provide confirmation of our analysis in this White Paper.

2. Article by Harold M. Cody Titled ''New Paradigm: Newsprint Demand Falls, Prices Soar.''

Harold M. Cody, Contributing Editor to Paper Age, published an article in the May/June 2006 edition of Paper Age titled ''New Paradigm: Newsprint Demand Falls, Prices Soar.'' The following passage confirms how newsprint industry consolidation has permitted unnamed manufacturers to strategically shut down capacity to raise newsprint prices despite a ''steady five year decline in demand.''

North American newsprint consumption continued its steady five-year decline last year and newspaper publishers faced similar difficulties. *In early 2006, demand continued to drop at an accelerating rate. But producers continue to fight the fight as evidenced by the almost hard-to-believe fact that prices are now reaching the highest levels in five years in spite of all this.*

Continuing the boxing parallel, these prolonged tribulations clearly illustrate just how adept U.S. and Canadian newsprint producers really are at fighting. *They have been able to quickly and decisively cut supply in response to these challenging conditions, masterfully reducing capacity via either shutdowns or conversions to other grades.*

The closure of 3.5 million metric tpy of newsprint capacity since 2001 has kept operating rates for the most part above 95%, fueling the steady increase in prices from a bottom of about $475/mton in 2002 to more than $650/mton or higher on lightweight grades by early 2006. Consolidation has also had an impact, as the top five newsprint producers control nearly 75% of capacity, and maybe even more importantly, the top three hold more than 50%. (Emphasis added.)

Cody notes that, despite the continual decline in newsprint demand, ''[t]hey have been able to quickly and decisively cut supply in response to these challenging conditions, masterfully reducing capacity via either shutdowns or conversions to other grades.'' Cody does not identify who ''they'' are, but his description of events can only apply to Abitibi, Bowater, and, possibly, Catalyst. He says that the capacity reductions have ''kept operating rates for the most part above 95%, fueling the steady increase in prices.''

3. Three Articles by RISI Senior Economist Andrew Battista Analyzing the Strategy of Abitibi and Bowater to Shut Down Capacity to Maintain High Operating Rates and Increasing Prices

a. ''Will operating rates climb high enough in 2003 to support rising newsprint prices in the U.S.?'' (February 20, 2003)

Andrew Battista, senior economist at RISI, published an article[97] in February 2003 titled ''Will operating rates climb high enough in 2003 to support rising newsprint prices in the U.S.'' This was the first of three articles Battista wrote over a two year period analyzing the unfolding AbitibiBowater strategy to use their control over capacity to raise the price of newsprint.

At the time Battista wrote this article, newsprint prices were just starting to increase after the 28% decline in newsprint prices between the second quarter of 2001 and the second and third quarters of 2002, caused primarily by the U.S. recession that began in late 2000/early 2001 and the economic aftermath of 9/11.

Producers finally got the ball moving in the other direction with a $35/tonne rise (of the proposed $50/tonne) last autumn. Newsprint manufacturers hope to capitalize on this momentum and push hard for the next $50/tonne increase announced for March 1.

Battista describes the economic relationships between production costs, operating rates and the price of newsprint.

There are two predominant drivers of product prices: Production costs and operating rates. Both are highly and positively correlated with newsprint prices through mechanisms that are well understood. When production costs inflate, newsprint profit margins fall. Buyers may balk at paying more for newsprint when ONP [recycled old newspapers] gets more expensive, but as cost pressure mounts, the least competitive mills edge closer to shutdown unless newsprint prices also rise.

The closure of a mill will result in higher operating rates. Likewise, a rise in demand usually leads to a tighter market (higher operating rates) in which paper becomes increasingly scarce, and hence, more valuable.

* * * * *

Rising costs support higher prices, but do not guarantee them in the short term. We still need to forecast the supply/demand balance in order to get a handle on pricing.

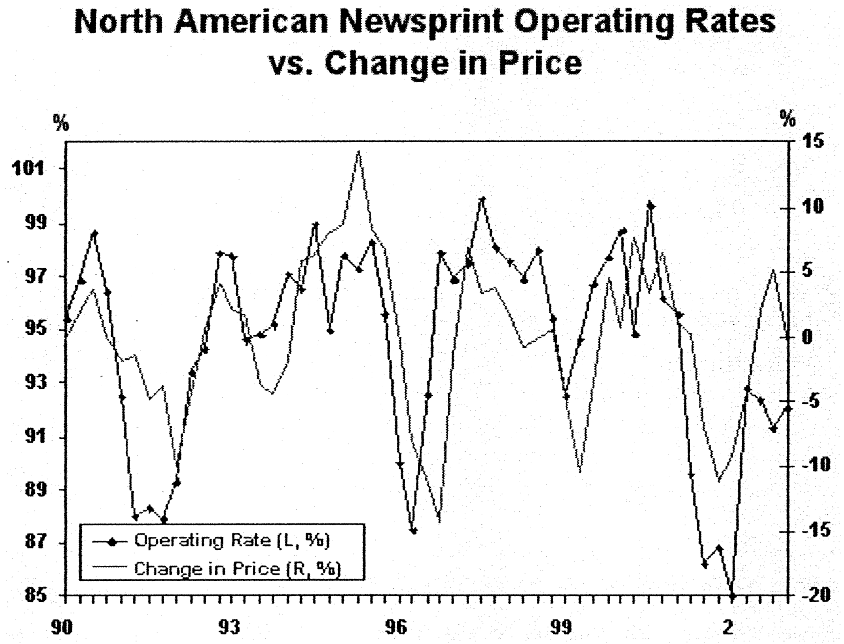
Battista provides an analysis of the relationship between operating rates and changes in newsprint prices.

When we plot operating rates against the (quarter-to-quarter) percent change in prices (as in Figure 1), we clearly see a high degree of correlation between the two series.[98]

[96] See Section D.1. above for more details. The Norske Skog and Pacifica newsprint mills were all located in British Columbia. Norske Skog's Canadian newsprint assets were renamed Norske Canada after the Pacifica acquisition and then renamed Catalyst in 2005. Norske Skog sold its interest in Catalyst in 2006.

[97] Source: *paperloop.com,* February 20, 2003. RISI is the major NA and global source of data, information, news, and analysis on the pulp, paper, and forest products industries.

[98] Note that Slide 9 contained in John Weaver's presentation to the Citigroup Conference in December 7, 2006 is a close variation of Battista's Figure 1. In presentations to investment analyst conferences by John Weaver and Pierre Rougeau, a close variation of the Battista figure is included in all or almost all such presentations beginning with Weaver's presentation to the June 5, 2003 Scotia Capital Materials Conference. The Scotia investment analysts conference was held a little bit more than three months after the Battista article was published. A similar slide is included in the most recent Abitibi presentation on March 20, 2007, which was by Rougeau, who is Abitibi's Senior Vice-President for Corporate Development and CFO.



Furthermore, we observe that the goodness of fit in this relationship is best with a one-quarter lag on operating rates. This fact reinforces the hypothesis of a causal relationship; higher operating rates lead to higher prices. In other words, a tight market in the summer tends to yield higher prices in the autumn. But how tight is ''tight''?

Closer examination of Figure 1 shows us that sustained operating rates in excess of 95% are typically required to lift newsprint prices.

Battista then analyzes the newsprint price increase that had occurred since the market hit bottom in mid-2002 and the prospects for further price increases in 2003 and 2004.

Last autumn's increase stands as an exception to that rule [that sustained operating rates in excess of 95% are required to lift newsprint prices]. The oddly timed price hike led publishers to complain that the market fundamentals did not justify an increase and forced producers to argue that they needed a rise just to stay alive.

But the massive market downtime taken by producers held inventory levels in check and led to a compromise increase (buyers accepted $35/tonne of the proposed $50/tonne). And although market recovery seems to be on hold during the winter months, with operating rates hovering between 92% and 93%, signs point to a tighter market in 2003. Abitibi-Consolidated Inc. and Bowater Inc. recently announced plans to withdraw 270,000 tonnes of combined capacity at Alma, Que., and Calhoun, Tenn.

In addition, ad lineage will likely continue along a gradual growth path and support a steady rise in newsprint demand. These factors should push operating rates above 94% this spring and summer before cresting [at] 95% toward the end of 2003.

Therefore, rising ONP costs and the threat of additional mill shutdowns may spur some positive pricing momentum this spring and once again, a portion of the $50/tonne sought on March 1 may be accepted. Continued market discipline through downtime will support prices a bit by keeping mill inventories low, but downtime does not affect the market as powerfully as the permanent removal of capacity.

North American newsprint producers will struggle to get prices to crest [at] $500/tonne by the fourth quarter of this year because operating rates will struggle to get above the 95% threshold in time to have much impact.

No new capacity will come online in North America in 2004, and we forecast newspaper advertising lineage growth to accelerate. Operating rates will likely top 97% for the year next year, and cost pressure probably will not subside. [Emphasis added]

b. ''Is rising newsprint demand necessary to support higher prices in 2004?'' (December 11, 2003)

Battista followed up his February 2003 article with an article [99] published in December 2003 titled ''Is rising newsprint demand necessary to support higher prices in 2004?'' His answer is that capacity closures will be sufficient to cause rising prices. He describes the removal of significant amounts of newsprint capacity from the market. The only capacity closures and conversions he describes are by Abitibi and Bowater. Like Weaver and Paterson in Section F above, Battista describes industry efforts to restore ''balance'' between supply and demand and forecasts the likelihood of a price increase, as the following excerpt indicates.

Just yesterday, Abitibi-Consolidated announced its intention to idle, or keep idle, its mills at Sheldon, Lufkin, and Port-Alfred. Over 750,000 metric tonnes per year (mtpy) will be indefinitely removed from the market. Perhaps more importantly, though, the company will permanently shut down two machines, one in Port-Alfred and one in Sheldon. This latter action will remove 230,000 mtpy from the North American newsprint market, permanently. Furthermore, closures and conversions at Abitibi-Consolidated's mill at Alma and Bowater's mills at Calhoun and Catawba in addition to any market-related downtime taken next year by anyone will further exacerbate the 7-year downward trend in North American newsprint supply. *The point is that producers' efforts to reconcile supply with demand have come a long way toward restoring balance in the market.* A strong rebound in demand next year would undoubtedly spark a sharp rise in newsprint prices, but *as capacity continues to fall, prices could jump even without a recovery in newsprint consumption.* (Emphasis added)

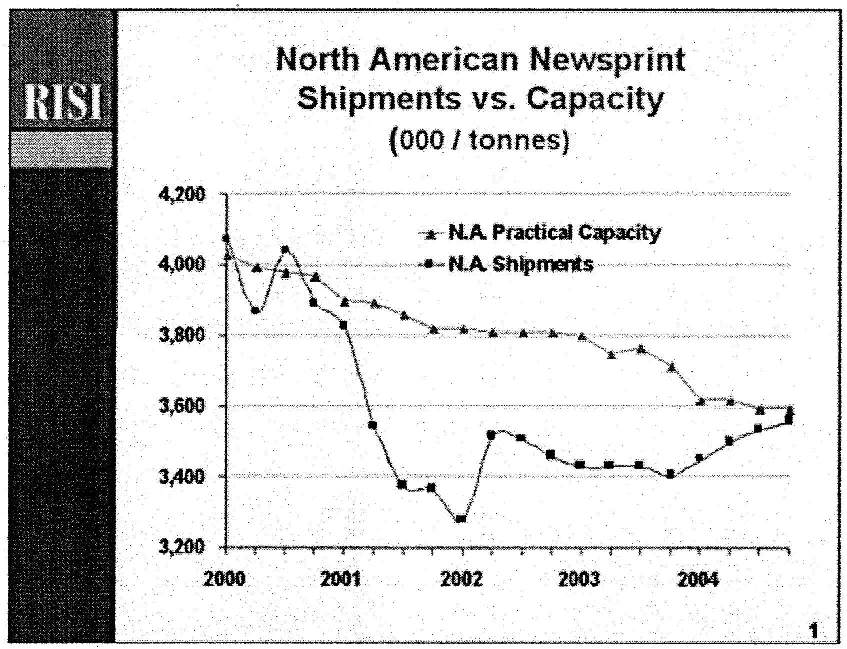
The extremely tight market for newsprint in 2000 pushed the average transaction price over $600/tonne by the end of the year. Several successive years of approximately 2% annual gains in demand against virtually flat supply led to extraordinarily high operating rates (near 100%) in the autumn of 2000. However, the turnaround in 2001 proved to be bitterly sharp for newspapers and newsprint manufacturers, alike. In the three years since, flailing newspaper advertising lineage pulled North American newsprint demand down by over 12% or approximately 1.4 million tonnes on an annual basis.

Mills struggled and eventually succeeded in matching the declines in demand with permanent closures and downtime. True operating rates (which count temporarily idled capacity as if it were available capacity) stayed below 90% throughout 2003, and we further know that production corresponded with demand during 2002–2003 because producer inventories remained low. This producer discipline had its first impact last summer when it effectively stopped the year-and-a-half long slide in prices, and has since permitted three partially successful increases (thanks also to rising production costs and the Canadian dollar).

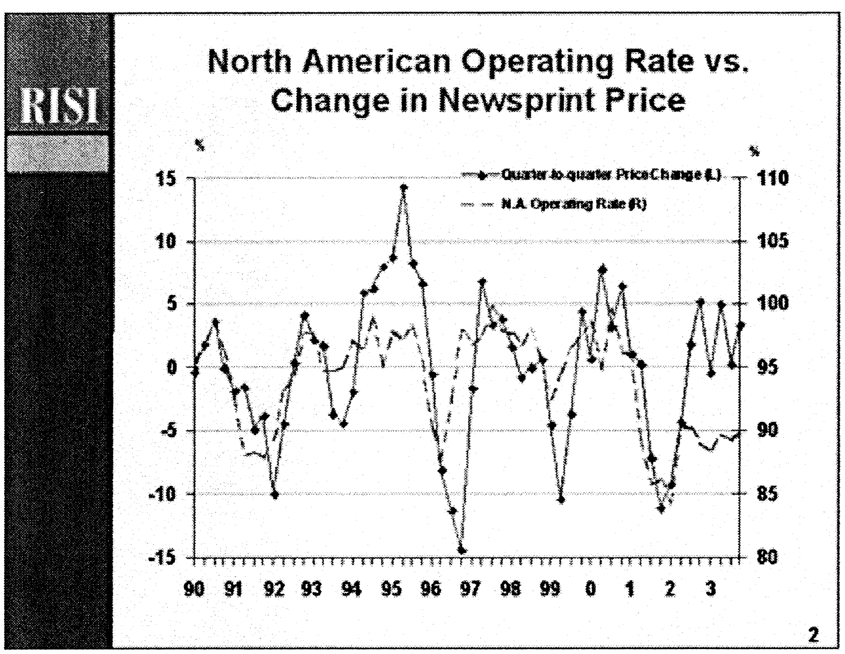
If we now include Abitibi-Consolidated's latest permanent cuts to the announced list of newsprint capacity withdrawals, we see that the drop in North American newsprint

[99] Source: *paperloop.com*, December 11, 2003.

supply over the last three years amounts to nearly 1.3 million mtpy. This reduction nearly matches the aforementioned (1.4 million tonne) drop in domestic demand over the same period. If domestic shipments or exports improve at all next year over the four levels endured during the second half of 2003, the industry operating rate will move to between 93% and 95% for the year. We predict that a moderate rise in both demand and exports will cause the gap between shipments and practical capacity (98% of theoretical capacity) to vanish, just as it did during the tight market of 2000 (see Figure 1). Thus, operating rates could top 97% in late 2004 not adjusting for any ongoing downtime.



What then will happen to newsprint prices in 2004? Given that, in all likelihood, the North American operating rate in newsprint will climb above 95% sometime in 2004 perhaps as early as the spring—prices will surely rise. When we plot operating rates against the (quarter-to-quarter) percent change in prices (as in Figure 2), we clearly see a high degree of correlation between the two series. Furthermore, we observe that the goodness-of-fit in this relationship is best with a one-quarter lag on operating rates. This fact reinforces the hypothesis of a causal relationship; higher operating rates lead to higher prices. In other words, a tight market in the summer tends to yield higher prices in the autumn. But how tight is ''tight''?



Closer examination of Figure 2 shows us that sustained operating rates in excess of 95% are typically required to lift newsprint prices. The half-successful increases since last summer provide a very noteworthy exception, but are attributable to the massive downtime and rising production costs borne by North American newsprint mills over the period. *Therefore, should downtime continue to be taken through 2004 as the true industry operating rate crests 95%, paper will be extremely scarce even though demand may be not much higher than during 2003. The average transaction price for newsprint might not get above $600/tonne next year, but this latest move by Abitibi-Consolidated brings the supply-and-demand balance much closer to where it stood 3 years ago, when newsprint last topped $600/tonne*. (Emphasis added)

c. ''Newsprint producers must rely on supply reductions to support rising prices'' (October 14, 2004)

In October 2004, Battista wrote a third article on the use of reductions and downtime of newsprint capacity to raise the price of newsprint.[100] The article was titled ''Newsprint producers must rely on supply reductions to support rising prices.'' By this time it had become clear to Battista that increases in demand were likely to be anemic at best, and that higher newsprint prices would come about as a result of the manufacturers' ''zeal'' in further reducing capacity.

Last year, in the RISI Viewpoint, I wrote that rising newsprint demand would not be necessary to support higher North American newsprint prices in 2004. Over the first eight months of the year, U.S. demand is off 0.8%, and Canadian demand is down 2.0% from 2003. And yet, average prices climbed $30/tonne higher this spring and are in the midst of another bitterly fought $50/tonne hike that could take them above $575/tonne before the end of the year.

After three consecutive years of declines in newsprint demand, seasonally adjusted U.S. consumption among all users is finally showing marginal improvement on a quarterly basis. The year-over-year figures will probably show some growth in the current quarter if only because the market during 4Q03 was so weak. And even though we expect to see solid, 3%, expansion in North American GDP in 2005, print advertising and newspaper circulation will likely continue to underperform and, at best, yield a meager 0.8% gain in domestic newsprint consumption. Nevertheless, we foresee U.S. newsprint prices climbing above $600/tonne in 2005 owing to producers' ongoing zeal to match the declining market with supply reductions.

Battista then discusses the removal of idled Abitibi and Bowater newsprint capacity from the official PPPC total. His discussion illustrates why it is misleading to rely on official PPPC capacity numbers to calculate operating rates. Based on these misleading capacity numbers, the official PPPC newsprint operating rate was 92%. In reality, the ''real'' operating rates were 98% to 99% which explains the sustained rise in newsprint prices from the end of 2002 through the time the article was written. According to Battista, the capacity the PPPC had removed from its official total a few weeks before his article was published raised the official operating rate to over 95% but still below the ''real'' operating rate of 98% to 99%. Battista anticipated that the PPPC would remove additional capacity from the official total in the first quarter of 2005, which would then align the official operating rate with the ''true'' operating rate. Note that with one minor exception,[101] Abitibi and Bowater account for all of the capacity removals in 2004 and 2005 that are discussed by Battista.

Several weeks ago, the PPPC officially removed some idled capacity that had been inoperative for more than one year: Bowater's PM3 at Thunder Bay, and Abitibi's PM5 and PM7 at Sheldon. The move suddenly took 480,000 tpy from the North American capacity base and lifted operating rates by more than 3% to over 95%. Furthermore, over the next two to three months, several more idled machines will have to come out of the official numbers. Abitibi's remaining machines at La Baie (Port Alfred) and PM2 at Lufkin were officially idled last December and account for approximately 430,000 tonnes of annual capacity. Also, accounting for Tembec's idled PM1 at Kapuskasing will pull an additional 35,000 tpy in early 2005.

The supply reductions in 2005 could run deeper still. Abitibi may soon announce the conversion of yet another newsprint machine to Alternative Offset/Equal Offset. The company has high expectations for this growing market. Such a conversion would probably be in addition to possible permanent closures at Sheldon and La Baie. (The PPPC reporting change temporarily removes those machines from the books, but Abitibi is rumored to be considering permanent shutdowns at these sites.) Bowater is also expected to make aggressive moves out of newsprint in the year ahead, although no details have yet been made public.

The forthcoming PPPC cuts will effectively boost the North American newsprint operating rate to 98%–99% in the first quarter of 2005. If another machine or two were to stop manufacturing newsprint, the market would be as tight as the white-hot market in 2000 and paper would be extremely hard to find. Prices next year will almost certainly rise even if demand fails to show any improvement at all.

Battista next discusses, as he did in his two previous articles, the relation between operating rates and price changes and he forecasts high operating rates for 2005. Also, as he did before, he includes a figure plotting NA newsprint operating rates against changes in price with one adjustment. In the figure below, Battista adjusts the operating rate for ''downtime,'' presumably to reflect the ''true'' operating rate rather than the PPPC official operating rate. The comparable figure that was included in his December 2003 article above reflects the PPPC official operating rate. The figure shows the PPPC official operating rate bottoming out at 84% at the end of 2001 and then rising to about 90% by the third quarter of 2002 before leveling out at or slightly below 90% through the third quarter of 2003. The figure below, which adjusts for downtime, shows the ''real'' operating rate bottoming out at perhaps 89% at the end of 2001 and then rising very quickly to above 95% by mid-2002 and generally remaining at that level or above through the third quarter of 2004.[102]

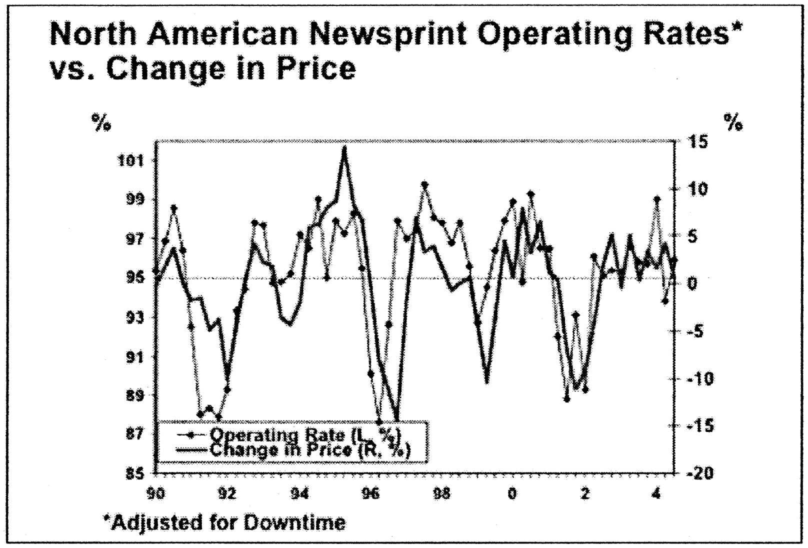
Historically speaking, when the North American operating rate climbs above 95% for two or more consecutive quarters, prices rise. This relationship exhibits a very tight correlation and makes good intuitive sense as well. Newsprint prices inflate when either demand jumps or supply falls such that the market is tighter than average. As noted above, the current operating rate is slightly higher than 95%, which means—in conjunction with rising ONP costs and a strong Canadian dollar—the current price increase ought to be moderately successful. Indeed, despite the fact that some suppliers have opted to delay implementation to October 1, other mills tell us that their order books are full through the balance of 2004.

Looking ahead, to 2005, it seems highly unlikely that operating rates will dip below 95%. The tiny projected gains in demand may fail to materialize, but falling capacity will lift the newsprint industry's utilization rate. Moreover, ongoing ONP inflation and persistent appreciation of the Canadian dollar will further induce producers to push for higher newsprint prices next year. The rise of the loonie, since the end of 2002, effectively wiped out all of the newsprint pricing gains for Canadian mills, and we expect the Canadian dollar to appreciate further over the next several months. Because of all of these factors, average pricing will consequently crest the $600/tonne threshold by next spring, and could get a second boost in the autumn. *The size of a second increase in 2005 and the ease of its acceptance, of course, will depend on: (1) Whether leading producers shutter more capacity, and (2) demand not evaporating as it did in 2001.* (Emphasis added)

[100] Source: *paperloop.com,* October 14, 2004.

[101] Tembec closed paper machine #1 at its Kapuskasing, ON mill. The machine had a newsprint capacity of 35,000 metric tonnes.

[102] The figure shows a dip in the ''real'' operating rate below 95% to 94% in the second quarter of 2004 before returning above 95% in the third quarter of 2004. Slide 15 discussed in Section F.4. above shows that Abitibi believed that the ''true'' operating rate was 87% in 2003 but that it would rise to 99% in 2004 due almost entirely to additional capacity removals by Abitibi.



I. Abitibi's Newsprint Capacity Closures 1999 to 2001

This section briefly reviews Abitibi's newsprint capacity closures between 1999 and 2001 and their likely impact on newsprint operating rates and prices.[103]

According to the Abitibi 1999 Annual Report (p. 6), Abitibi removed 450,000 metric tonnes of newsprint capacity from the market in 1999 almost 3% of NA capacity.

> ''We want to fully implement our capacity rationalization program in 1999, and together with the planned newsprint conversion next year, you'll see us close or convert 350,000 tonnes ''—John Weaver, 1998 Annual Report

> In fact, Abitibi-Consolidated permanently removed 450,000 tonnes of excess newsprint capacity in 1999, or nearly 3% of NorthAmerican capacity. We will continue to be a results-driven Company that benchmarks objectives and accomplishes them.

According to the Abitibi 2000 Annual Report, (p. 23), Abitibi announced in conjunction with its acquisition of Donohue in April 2000 that Abitibi would remove an additional 400,000 metric tonnes of newsprint capacity from the market during 2000 and 2001.

High-cost newsprint capacity rationalization program. In conjunction with the acquisition of Donohue, the Company announced its intention to permanently remove 400,000 tonnes of high-cost newsprint capacity. As part of this program, the Company shut down its 130,000 tornne West Tacoma newsprint mill, located in Steilacoom, Washington, in December 2000.

One paper machine with an annual capacity of 70,000 tonnes was shut down at the Lufkin, Texas mill, on November 1st, 2000 as part of the modernization program of the mill. At the end of December 2000, the Company shut down a value-added paper machine with an annual capacity of 45,000 tonnes at the Kénogami, Québec mill. The value-added groundwood paper grades produced on these machines will replace newsprint production at other mills.

Abitibi closed 200,000 metric tonnes of newsprint capacity in 2000 and 200,000 metric tonnes in 2001 for a total removal of 850,000 metric tonnes of newsprint capacity over the three year period or about 5% of NA newsprint capacity that existed at the beginning of 1999.

Abitibi's removal of 450,000 metric tonnes of newsprint capacity in 1999 raised the industry operating rate by almost 3%. In Section E.6., we noted that newsprint prices increased $145 or 30.2% between the third quarter of 1999 and the second quarter of 2001. As Chart E5 in Section E shows, the operating rate increased from 93.0% in the second quarter of 1999 to 97.7% in the fourth quarter of 1999, and, except for one quarter, remained above 97% through the end of 2000. Without the newsprint capacity removals of Abitibi during 1999, the industry operating rate would have been at 95% or somewhat below during the period 4Q 1999 to 2Q 2001. While prices may still have increased at these lower operating rates, the magnitude of the price increases would likely have been significantly lower than what actually occurred.

The ''Pulp & Paper North American 2000 Factbook,'' p. 194, summarizes the effect of Abitibi's capacity closures on the three $50 per metric tonne price increases that occurred between September 1999 and September 2000. The Factbook does not identify any other manufacturers that closed capacity from the market during this period.

Adding to market tightness and lending support to the price increases was Abitibi-Consolidated's vow to remove 400,000 mtons of newsprint from the North American market by 2001. In July 2000, Abitibi announced the closure of its 130,000 mtpy West Tacoma, Wash., newsprint mill at year-end. The company had already idled the No. 2 paper machine at the mill in 1999. Also in 1999, Abitibi idled the No. 7 paper machine at Iroquois Falls, Ont. (24,000 mtpy of newsprint). In addition, Abitibi idled and then subsequently sold its 125,000 mtpy Chandler, Que., mill with the condition that the new owners not produce newsprint.

The Factbook excerpt above notes that Abitibi's Chandler, QC newsprint mill was sold with the condition that the new owners not make newsprint. Abitibi closed the Chandler mill in 1999 and sold it in 2000. The condition that the Chandler mill not be used by the new owners to produce newsprint suggests that the mill's variable costs for producing newsprint were below prevailing newsprint prices at the time and that it would have been profitable for the new owners to use the mill to produce newsprint.

J. A Comparison of Newsprint Prices With the Prices of Uncoated Groundwood Specialty Grades 3Q 1999 to 4Q 2006

1. Introduction

In Section B above we described the similarities and differences between newsprint and uncoated groundwood specialty grades. The higher value uncoated groundwood grades generally are brighter than newsprint (i.e., the fibers in the pulp furnish have been subjected to more bleach) or glossier (i.e., clay is added to the pulp furnish). While newsprint is the lowest-quality and lowest value groundwood grade, the main inputs used to produce newsprint and uncoated groundwood specialty grades, in particular energy and fiber, are the same. Rises in common input costs should have a very similar impact on both NA newsprint mills and NA mills that produce uncoated groundwood specialty grades, other things being equal.

In Section J.2. below we explain why the impact of the increase in input prices over

[103] On behalf of the NAA and U.S. daily newspaper publishers, Economists Incorporated submitted to DOJ analyses of the likely competitive effects of the proposed acquisition of Donohue by Abitibi in 2000 and the proposed acquisition of Alliance by Bowater in 2001. Those analyses are still relevant to an understanding of the competitive conditions in the newsprint industry at that time as well as an understanding of the likely competitive effects of the currently proposed Abitibi-Bowater merger. There were two submissions to DOJ concerning the proposed acquisition of Donohue by Bowater. They are dated March 1, 2000 and March 31, 2000. The submission to DOJ concerning the proposed acquisition of Alliance by Bowater is dated May 7, 2001.

the past several years has been greater on Canadian mills than U.S. mills. In addition, the appreciation of the Canadian dollar to the U.S. dollar has also adversely affected Canadian mills compared to U.S. mills. We explain why these twin effects fall more heavily on NA manufacturers of uncoated groundwood paper in the aggregate than on NA manufacturers of newsprint in the aggregate.

In Section J.3. we compare the quarterly price of newsprint from the third quarter of 1999 to the second quarter of 2006 with the quarterly prices of four uncoated groundwood specialty grades. We find that the quarterly prices for newsprint as a percentage of its quarterly price in 3Q 1999 were significantly higher than the quarterly prices for three of the four uncoated groundwood specialty grades over the period 4Q 1999 to 2Q 2006. Based on these results, it is implausible that the increases in newsprint prices were caused by the increases in input prices. We find that the price trend of one uncoated groundwood specialty grade was similar to that of newsprint. It appears that Abitibi and Bowater are the dominant providers of that grade as well.

Section J.4. presents evidence that Abitibi's variable costs have been relatively constant since 2001. Since nearly all of the newsprint price increases over the period 2002 to 2006 were led by Abitibi, it seems unlikely that increases in Abitibi's input costs are a plausible justification for the price increases.

In Section J.5. we calculate quarterly newsprint revenues over the period 3Q 1999 to 2Q 2006 based on actual NA newsprint demand and actual newsprint prices. We then apply the quarter to quarter percentage price changes for each of the four uncoated groundwood specialty grades to the 3Q 1999 newsprint price and multiply the resulting adjusted newsprint prices by actual NA demand. For the three grades with percentage changes in prices significantly below the percentage changes in newsprint prices, total revenues over the period are reduced by $4.7 billion to $7.4 billion.

2. The Adverse Impact of the Increases in Input Prices and the Appreciation of the Canadian Dollar Has Fallen More Heavily on Producers of Uncoated Groundwood Specialty Grades Than on Producers of Newsprint

Both newsprint producers and producers of uncoated groundwood specialty grades have been subjected to increasing costs of inputs in recent years. The inputs that have increased in cost include fiber (both wood and recycled), energy and transportation. Advantages that Canadian mills once enjoyed in lower energy and fiber costs have been reversed.[104] Canadian mills are now at a cost disadvantage.

At the December 2006 Citigroup Conference, David Paterson of Bowater stated that Bowater's U.S. mills (which are all in the southeastern U.S. with the exception of the Ponderay mill in Washington) were more efficient than Bowater's Canadian mills (which are all in Eastern Canada). He said that due to energy and currency issues (discussed immediately below), the age of the equipment and other reasons, there is not much margin left at Bowater's Canadian newsprint mills. He also said that if Bowater had only U.S. mills, the Bowater's newsprint business would be pretty good at ''today's'' prices.[105]

In addition to increases in the cost of inputs, Canadian mills have been adversely affected by a significant increase in the value of the Canadian dollar relative to the U.S. dollar.[106] For a given price increase, U.S. mills will benefit more than Canadian mills if the value of the Canadian dollar is rising relative to the U.S. dollar. The combined effects of the input cost increases and the increasing value of the Canadian dollar have reduced the profitability of Canadian mills relative to U.S. mills.

A greater percentage of NA uncoated groundwood capacity is in Canada compared to the percentage of NA newsprint capacity in Canada.[107] In addition, Canadian uncoated groundwood specialty mills ship a greater percentage of their output to U.S. customers than the percentage of output that Canadian newsprint mills ship to U.S. customers.[108] As a result, the impact of increases in input costs and the appreciating Canadian dollar should fall more heavily on NA uncoated groundwood specialty manufacturers in the aggregate than on NA newsprint manufacturers in the aggregate.[109]

3. Comparing Quarterly Prices for Newsprint and Uncoated Groundwood Grades From 3Q 1999 Though 4Q 2006

There are two reasons to assume that price increases over the period should be greater for uncoated groundwood specialty grades than for newsprint over the period 3Q 1999 to 4Q 2006. First, the growth rate in consumption over this period has been positive for uncoated groundwood specialty grades in the aggregate, while the growth rate in consumption has been negative for newsprint. Between 1999 and 2006, total NA uncoated groundwood specialty grade consumption grew at a compound average growth rate of 3.1% per year. Over that same period, the compound average growth rate of NA newsprint consumption was a negative 4.0%.[110] Positive growth rates in consumption are usually associated with rising prices and negative growth rates in consumption are usually associated with falling prices.[111]

Second, as described in Section J.2. above, the rise in input costs and the appreciation in the Canadian dollar relative to the U.S. dollar have fallen more heavily on NA producers of uncoated groundwood specialty grades in the aggregate than on NA newsprint manufacturers in the aggregate.

Chart J1 below reflects the quarterly average price of newsprint and four uncoated specialty grades over the period 3Q 1999 to 2Q 2006.[112] The prices for each grade are expressed as a percentage of that grade's price for 3Q 1999. Three $50 per metric tonne price increases were implemented from September 1999 to September 2001.[113] 3Q 1999 was selected for the initial date of the analysis shown in Chart J1, because that was the quarter when the initial $50 price increase was announced. As was described in Section I above, Abitibi began closing capacity in 1999. The ''Pulp & Paper North American 2000 Factbook,'' p. 194. cited

[104] Source: ''Global Pulp & Paper Fact & Price Book 2006,'' pp. 149–152, which is published by RISI. (''RISI Fact & Price Book''). While the discussion of the increasing costs and declining fortunes faced by Canadian newsprint mills is in the newsprint section of the RISI publication, the discussion clearly would also apply to Canadian mills that produce uncoated groundwood specialty grades.

[105] Source: Audio recording of Paterson's comments at the December 2006 Citigroup Conference, starting at about 27:35. We have provided a copy of this audio recording to DOJ. The recording is no longer available on the Abitibi Web site.

[106] Newsprint is priced in U.S. dollars per metric tonne but the costs to the Canadian mill of producing a metric tonne of newsprint are denominated in Canadian dollars. If the value of the Canadian dollar increases relative to the U.S. dollar, the Canadian mill will receive fewer Canadian dollars from the sale of a metric tonne of newsprint to a U.S. customer when the U.S. dollars from the sale are converted to Canadian dollars.

[107] In 2005, 71.9% of uncoated groundwood specialty grade capacity was in Canada and 28.1% was in the U.S. By comparison, 61.4% of NA newsprint capacity was in Canada and 38.6% was in the U.S. Source: RISI Fact & Price Book, pp. 147, 148, and 164.

[108] In 2005, Canadian manufacturers of uncoated groundwood specialty grades shipped 76.6% of their output to U.S. customers. In contrast, Canadian newsprint mills shipped 61.2% of their output to U.S. customers. Source: RISI Fact & Price Book, pp. 142, 149, and 164.

[109] About 65.3% of Abitibi's NA newsprint capacity is in Canada and about 57.1% of Bowater's NA newsprint capacity is in Canada. For Abitibi and Bowater combined, 62.1% of their NA newsprint capacity is in Canada. See Table C1 in Attachment C. The increase in costs at their Canadian newsprint mills implied by the appreciation of the Canadian dollar is partially offset by the implied corresponding decrease in costs at the U.S. newsprint mills of Abitibi and Bowater. After Abitibi and Bowater, the next two largest newsprint manufacturers in NA in terms of capacity are White Birch and Kruger. See Table C2 in Attachment C. As can be determined from Table C1, 79.6% of White Birch's capacity is in Canada and 100.0% of Kruger's capacity is in Canada. The appreciation of the Canadian dollar has adversely affected White Birch's and Kruger's manufacturing costs more than it has Abitibi's or Bowater's manufacturing costs.

[110] Source: RISI Fact & Price Book, p. 142 and p. 169. The RISI Fact & Price Book does not provide annual consumption data by uncoated groundwood specialty grade.

[111] The 3Q 1999 price per metric tonne for each grade was as follows: newsprint = $480; Directory (22.1 lb.) = $733; Hi-Brite 65 (35 lb.) = $621; SCA (35 lb.) = $717; SCB (35 lb.) = $623. Source: RISI Fact and Price Book, p. 150 and p. 167.

[112] Source: RISI Fact and Price Book, p. 150 and p. 167 and Pulp & Paper Week. Except for newsprint, the prices are the average of the high and low prices for each quarter. The uncoated groundwood specialty grades were priced in short tons. These prices were converted to price per metric ton by multiplying by the ratio of the number of pounds in a metric tonne to the number of pounds in a short ton (2205/2000). The price for Directory paper is a spot price. About 80% to 90% of Directory paper is sold under one- to three-year contracts to RBOCs and independent directory publishers.

[113] Source: ''Pulp & Paper North American 2000 Factbook,'' p. 194.

Abitibi's past closures and announced future closures as ''[a]dding to market tightness and lending support to the price increases.''.

Chart J1. The Price of Newsprint and Four Uncoated Groundwood Specialty Grades by Quarter Expressed as a Percentage of the 3Q 1999 Price

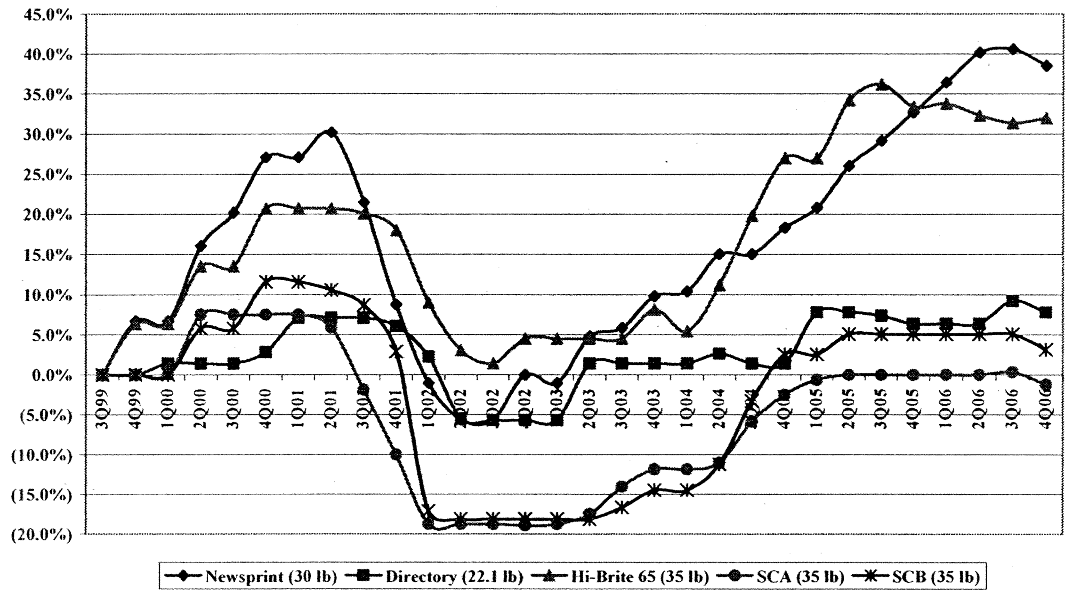


Chart J1 shows in a broad sense similar price movements for newsprint and the four uncoated specialty grades. For each of these grades, price rose from 3Q 1999 to 2001, followed by a rapid decline as the U.S. recession set in. Prices bottomed out in 2002 or so and began to climb until Q2 2006. However, the magnitudes and rates of the price movements are quite different for the five grades. The prices of both newsprint and Hi-Brites (brightness level = 65) rose significantly more than the other three grades between 3Q 1999 and 2001 and between bottoming out in 2002 and 4Q 2006. Chart J1 shows prices increasing within a quarter or two of bottoming out for these two grades. The price of both grades rose steadily from the bottom. The newsprint price rose to 39% above its 3Q 1999 price by 4Q 2006 and the Hi-Brite price rose to 36% above its 3Q 1999 price by 3Q 2005 before declining somewhat to 32% by 4Q 2006. In terms of dollars per metric tonne, the newsprint price in 4Q 2006 was $185 above its 3Q 1999 price and the Hi-Brite price was $196 above its 3Q 1999 price.

The Directory, SCA and SCB grades had much smaller price increases in the run-up to 2001 and, after the decline to 2002, the recovery in prices took much longer to occur than for newsprint and the Hi-Brite grade. The bottoms for the SCA and SCB prices were much deeper as a percentage of their 3Q 1999 prices than was the case for the bottoms for newsprint and Hi-Brite prices. The prices for the SCA and SCB grades also stayed at their bottoms for a much longer period of time than was the case for the prices for newsprint and the Hi-Brite grade. By 4Q 2006, the SCA price was 1.3% below its 3Q 1999 price and the SCB price was 3.1% above its 3Q 1999 price. In terms of dollars per metric tonne, the SCA price in 4Q 2006 was $11 below its 3Q 1999 price and the SCB price was $24 above its 3Q 1999 price. The price of Directory paper as a percentage of its 3Q 1999 price did not fall nearly as deeply as did the SCA and SCB prices and it recovered more quickly. By 4Q 2006, the Directory paper price was 7.8% or $61 above its 3Q 1999 price.

Why should 4Q 2006 prices for newsprint and Hi-Brites be so much higher than their 3Q 1999 prices both in percentage terms and as an absolute change in price compared to SCA, SCB, and Directory paper prices? One possible answer is that not only are Abitibi and Bowater dominant in newsprint, they are also dominant in Hi-Brites. During our interviews with newspaper newsprint buyers, we learned that there was also concern that the proposed Abitibi-Bowater merger could lead to higher Hi-Brite prices and Super Hi-Brite prices.[114] In addition to newsprint, these buyers also purchase these two uncoated groundwood specialty grades. We were told that Abitibi and Bowater are the only suppliers of Hi-Brite and Super Hi-Brite grades East of the Rockies. We were also told by the buyers that they were unaware of any European suppliers of Hi-Brites or Super Hi-Brites.

Our analysis of uncoated groundwood specialty grades in Attachment B confirms the statements of the newspaper newsprint buyers cited above regarding the availability of Hi-Brite and Super Hi-Brite suppliers. See Tables B5 and B6 in Attachment B. Besides Abitibi and Bowater, the only suppliers of Hi-Brites and Super Hi-Brites in NA that we were able to identify[115] were Catalyst, North Pacific, and Blue Heron, all of whose mills are located West of the Rockies.[116] In an NA relevant geographic market, Abitibi and Bowater would have a combined share of 76.5% of capacity based on our analysis. In an East of the Rockies relevant geographic market, Abitibi and Bowater would have a combined share of 100.0% of capacity.

The price comparisons shown in Chart J1 are not consistent with a hypothesis that newsprint price increases observed over the past four years are due to the rising costs of inputs. If the newsprint price increases were caused by input cost increases, we should at a minimum see similar price increases for newsprint and the four uncoated groundwood specialty grades. As argued above, the price increases should, in fact, be greater for uncoated groundwood specialty grades than for newsprint since the impact of the cost increases falls more heavily on uncoated groundwood specialty producers in the aggregate than it does on newsprint producers in the aggregate. In addition, the price increases should be greater for the uncoated groundwood specialty grades because of the steady demand growth for the specialty grades in contrast to the steady demand decline for newsprint.

The price comparisons shown in Chart J1 are consistent with the hypothesis that Abitibi and Bowater have jointly exercised

[114] The RISI Fact & Price Book does not provide a price series for Super-Brites.

[115] Because information on producers of specific uncoated groundwood specialty grades is often sketchy, our analysis should be regarded as a first approximation.

[116] Neither Abitibi nor Bowater produce Hi-Brite and Super Hi-Brite grades at mills located West of the Rockies.

significant market power in the NA newsprint market. The price comparisons shown in Chart J1, the observations of newspaper newsprint buyers cited above, and our own confirming analysis strongly suggest that Abitibi and Bowater have also jointly exercised significant market power in the sale of Hi-Brite paper to NA customers. The newspaper newsprint buyers we talked to also noted that the price increase of newsprint and the price increases of Hi-Brites and Super Hi-Brites tend to track each other. As Chart J1 shows, that is certainly the case with respect to price increases of Hi-Brites and newsprint and, as argued above, it is likely due to Abitibi's and Bowater's joint exercise of market power in the newsprint market and in the sale of Hi-Brites.

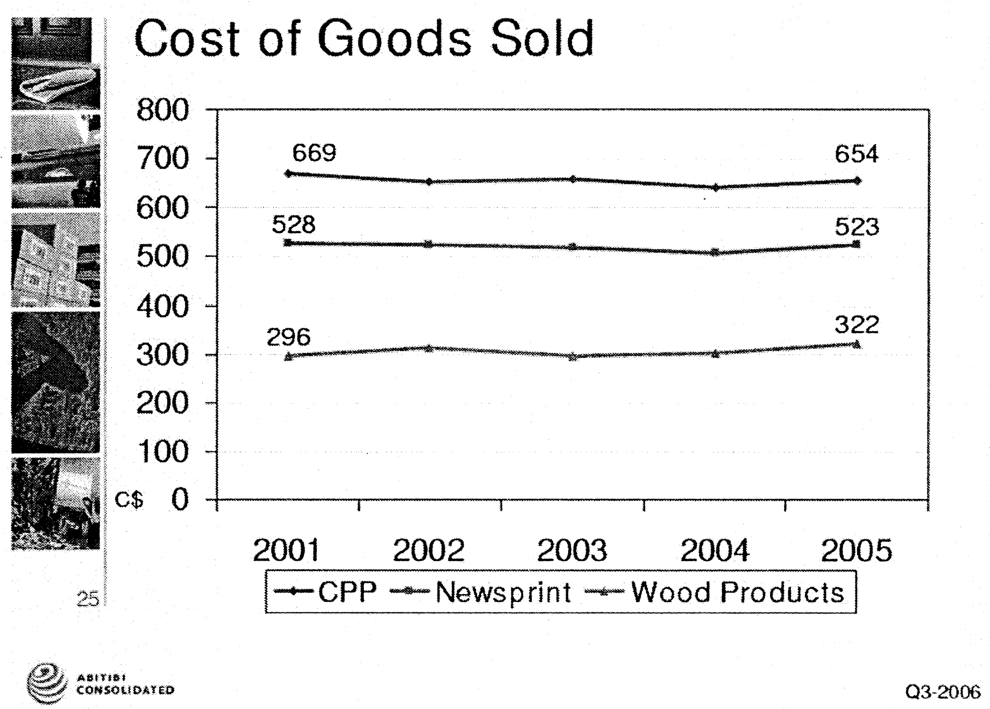
4. Abitibi's Variable Costs To Produce Newsprint and Uncoated Groundwood Specialty Grades Have Been Relatively Constant for the Period 2001–2005

While there have been cost increases in inputs used to make newsprint and uncoated groundwood specialty grades in recent years, Abitibi has been able to implement cost-saving measures to maintain relatively constant variable costs of producing these grades over the period 2001 to 2005.

See Slide 25 below from the December 2006 Citigroup Conference presentation of Abitibi's John Weaver. The slide shows the cost of goods sold (or variable costs) for uncoated groundwood specialty grades (called commercial printing papers or CPP by Abitibi), newsprint and wood products. The slide shows variable costs (in Canadian $) actually declining slightly for both newsprint and uncoated groundwood paper specialty grades from 2001 to 2005.[117]

In the audio recording of Weaver's comments on Slide 25, he said that despite the Canadian dollar and all the increase in input costs such as energy and fiber, ''You can see for the last 5 years Abitibi has basically managed to keep our costs relatively flat through all these escalating input costs. So I think this shows the focus of the company on cost reduction.'' [118]

Slide 25: Abitibi Citigroup 12/7/06



Since all or nearly all of the newsprint price increases over the period 2002 to 2006 were led by Abitibi, it seems unlikely that increases in Abitibi's input costs are a plausible justification for the price increases.

5. Applying the Percentage Price Changes for the Uncoated Groundwood Specialty Grades to the 3Q 1999 Price of Newsprint to Determine the Effect on Newsprint Revenues from Sales to NA Customers

We applied the percentage price changes calculated for the four uncoated groundwood specialty grades shown in Table J1 to the 3Q 1999 newsprint price ($480 per metric tonne) to generate four series of adjusted newsprint prices. Next we multiplied the actual newsprint price series and the four adjusted newsprint price series by quarterly NA demand (quantity purchased) shown in Chart E2. Finally, we summed over the 30 quarters to derive total revenues based on the five newsprint price series. The results are shown below.

[117] Slide 25 shows that Abitibi's variable cost to produce newsprint in 2005 was C$523. It was also C$523 in 2006. Source: presentation by Pierre Rogeau, Abitibi Senior VP for Corporate Development and CFO, at the Goldman Sachs Conference, 3/20/07, Slide 24.

[118] These comments begin at about 17:30 of the audio recording of Weaver's presentation, a copy of which we have provided to DOJ. The audio recording of Weaver's presentation and the 2006 Citigroup conference is no longer available on Abitibi's Web site. The slide show, however, is still available.

TABLE J1.—TOTAL NEWSPRINT REVENUES OVER THE PERIOD 3Q 1999 TO 2Q 2006 BASED ON QUARTERLY DEMAND AND FIVE QUARTERLY NEWSPRINT PRICE SERIES

[In billions of dollars]

	Actual newsprint price (30 lb)	Actual newsprint price adjusted by directory (22.1 lb) price % change	Actual newsprint price adjusted by hi-brite 65 (35 lb) price % change	Actual newsprint price adjusted by SCA (35 lb) price % change	Actual newsprint price adjusted by SCB (35 lb) price % change
Total Revenues Based on Actual and Adjusted Newsprint Prices	$44.1	$39.4	$44.4	$36.6	$37.5
Total Revenues Based on Actual Newsprint Prices Minus Total Revenues Based on Adjusted Newsprint Prices	0.0	4.7	(0.3)	7.5	6.6

Table J1 is broadly suggestive of the scope of overcharges to NA newsprint customers due to the behavior of Abitibi and Bowater over the period 3Q 1999 to 4Q 2006. In this context, it must be noted that we have done no analysis of the demand and supply conditions for the Directory, SCA, and SCB grades to ensure they are good ''but for'' world candidates. Nor have we done any analysis to determine the appropriate methodology to determine overcharges to NA newsprint customers. With this caveat and assuming that the price changes for Directory, SCA, and SCB paper over the period 3Q 1999 to 4Q 2006 represent a range of appropriate ''but for'' worlds and the methodology used to calculate the results in Table J1 is appropriate, overcharges to NA newsprint customers over the period 3Q 1999 to 4Q 2006 totaled in the range of $4.7 billion to $7.5 billion due to the anticompetitive behavior of Abitibi and Bowater.

K. Dominant Firm Model

The preceding sections, especially Sections F through J, have provided evidence that Abitibi and Bowater have acted to decrease newsprint output and increase the price of newsprint over the past four years. Their behavior can be interpreted as two firms acting together like a dominant firm. This section discusses a simple model of dominant firm behavior adapted to the newsprint industry. A more detailed description of this model can be found in Attachment 4.

The model allows us to address two questions:

- In theory, how could Abitibi and Bowater, acting together or as a merged entity, profitably raise price?
- Do the current conditions in the newsprint industry suggest that Abitibi and Bowater actually have the ability profitably to raise price further?

The model assumes that the industry is composed of a dominant firm (or firms) with a significant market share. The rest of the industry is made up of a large number of smaller firms, none of which is large enough to affect significantly the market price on its own. All firms produce the same undifferentiated product. Each firm is assumed to have a well-defined ''full capacity'' output level which cannot be exceeded at reasonable cost within the relevant time frame. It is further assumed that imports are unlikely to increase significantly from current low levels. These assumptions provide a reasonably accurate, if somewhat simplified, representation of the North American newsprint industry today.[119]

Dominant Firm Strategy

Under the conditions outlined above, the strategy available to the dominant firm is to remove fringe firms as competitive constraints by allowing them to fill up their plants. Once the fringe firms are operating at full capacity, they no longer can compete to draw sales away from the dominant firm. The dominant firm can then effectively behave as a monopolist with respect to the ''residual demand''—i.e., that portion of industry demand that is not satisfied by the fringe firms operating at full capacity. In this monopoly position, the dominant firm can raise price above the initial, competitive level.

Conceptually, one can think of the dominant firm's strategy as involving two steps. In Step 1, the dominant firm allows the fringe firms to reach full capacity. One way to do this is for the dominant firm to remove some of its productive capacity from the market, either temporarily or permanently. Customers that previously purchased from the dominant firm must then increase their purchases from fringe firms. Total industry output is unchanged, but a portion of industry output shifts from the dominant firm to the fringe firms. Once the fringe firms have reached full capacity, the dominant firm can take Step 2 and raise price without fear of being undercut by the fringe firms. The fringe firms will tend to raise their price along with the dominant firm, since they cannot produce any more product. Failure to raise price to the level of the dominant firm's price would unnecessarily sacrifice profit.

The same two conceptual steps can be achieved if the dominant firm simply announces a significant price increase. Initially, fringe firms behaving competitively do not follow the price increase. To the extent possible, customers divert their purchases from the higher-priced dominant firm to the lower-priced fringe firms. Once the fringe firms reach their capacity constraint, however, remaining purchases must be made from the dominant firm at its higher price. The dominant firm is the only available supplier capable of satisfying the ''residual demand.''

Applying the Model to the Newsprint Industry

In Attachment 4, the model is expressed formally using equations and various parameters. Whether the dominant firm will adopt this strategy depends on the associated gains and losses. The gains and losses depend on various factors, including initial capacity utilization of the fringe firms, the current market price, the dominant firm's variable contribution margin, the percentage price increase and the elasticity of demand. These factors are set forth in Table K1 below. Public sources provide at least a rough estimate of the values of these parameters for the North American newsprint industry, as shown in Table KI. Using these estimated values, the model predicts that it would be profitable under current conditions for a dominant firm with the combined shares of Abitibi and Bowater to exercise market power through the dominant firm strategy.

TABLE K1.—ESTIMATED PARAMETER VALUES FOR DOMINANT FIRM MODEL

Factor	Name	Symbol	Current value
1	Initial capacity utilization of fringe	Uc	[120] 95%

[119] The model makes the simplifying assumptions that a firm cannot expand its capacity and that imports do not increase. It may be more accurate to say that the supply response of capacity-constrained fringe firms and foreign producers is believed to be very small for small to moderate price increases. Relaxing the model's strict assumptions slightly does not change the general conclusions of the discussion. The effects of relaxing assumptions are discussed in Attachment 4.

TABLE K1.—ESTIMATED PARAMETER VALUES FOR DOMINANT FIRM MODEL—Continued

Factor	Name	Symbol	Current value
1a	Maximum cap. utilization of fringe	Um	[121] 98%
2	Initial industry unit price	P1	[122] $625
3	Dominant firm's unit variable cost	C	[123] $531
4	Hypothetical price increase	R	5%
5	Industry elasticity of demand	E	[124] 0.36
6	Initial share of dominant firm	S	[125] 41.5%

Using the parameter values in Table K1, the model predicts that the price increase yielding the greatest profit for a dominant firm under these conditions would be approximately 48 percent. If price were to increase by such a large percentage, it is quite possible that some of the assumptions of the model would have to be modified. In particular, if extremely high prices were sustained for a period of years, fringe firms may invest to expand their capacity, and imports may become a more significant factor than they are at current price levels. To avoid triggering these responses, the price increase a dominant firm would take might be lower than the estimated 48 percent above current levels.[126] Even allowing for such adjustments, the simple model presented here points to the profitability of a significant price increase. Changing various estimated parameters within a reasonable range does not alter this finding.

The model assumes Abitibi's average cost of production as the unit variable cost.

See Table K1 above. It is quite likely that the capacity that Abitibi and Bowater would idle when pursuing a dominant firm strategy would be their highest cost capacity. In his December 2006 presentation to the Citigroup Conference, Abitibi Bowater's David Paterson was asked how Bowater would be able to maintain sufficient cash flow to pay for dividends and interest payments if newsprint prices declined from current levels. As quoted in Section F.3 above from an audio recording of his remarks, Paterson responded,

So my belief[. . .]is that we have to move faster to stay ahead of that [demand] curve to maintain an operating rate that gives us some pricing leverage in the market and I can do that. We know which our high cost assets are and we will shut them down hopefully before rather than after price erosion with any significance.

Earlier in his presentation, Paterson had stated that Bowater's high-cost newsprint assets were located in Eastern Canada and that ''there is not a lot of margin left in the Canadian assets.''

Section L. Conclusions

Based on our economic analysis of the likely competitive effects of the proposed Abitibi-Bowater merger contained in Sections B through K above, we conclude that the merger, if it is permitted to proceed, will have very significant adverse competitive and economic effects on U.S. newspaper publishers and other NA consumers of newsprint.

Through their joint behavior over the past four years, Abitibi and Bowater have demonstrated that their combined share of NA newsprint capacity was large enough to enable them to consistently raise the price of newsprint in the face of steadily declining NA newsprint demand. Abitibi and Bowater matched declining consumption year after year with the amount of capacity removal needed to maintain high operating rates and increasing newsprint prices. This strategy has been remarkably successful as this White Paper documents. The title of one of the articles cited in Section H, ''New Paradigm: Newsprint Demand Falls, Prices Soar,'' captures this paradox of ''soaring'' prices in the face of declining consumption.

The fact that Abitibi and Bowater have been able to profitably reduce their own capacity to raise the price of newsprint is direct evidence that they have jointly possessed and exercised market power over a sustained period of time. A small firm would have no incentive unilaterally to close capacity to raise the price of newsprint because the loss of net margin from the closed capacity would outweigh the gain in margin from the price increase on the capacity that it would still operate.

As we have documented in this White Paper, the NA newsprint market was unconcentrated in 1995 but became highly concentrated by 2000 primarily due to mergers by Abitibi, Bowater, and the newsprint firms they acquired. Without these mergers, Abitibi and Bowater would have been unable to pursue their highly effective and highly anticompetitive joint strategy.

The newspaper newsprint buyers whom we talked to believe that it is certain that a combined Abitibi and Bowater will continue to pursue this anticompetitive strategy, but the merged firm will be able to do so more effectively. Coordination difficulties, costs, and uncertainties that Abitibi and Bowater faced as separate firms in their exercise of joint dominance would be removed by a merger. Future capacity closures to raise the price of newsprint will be more optimal and timely from the viewpoint of the merged firm and more harmful to NA consumers of newsprint. Without a merger, imperfect coordination between Abitibi and Bowater may break down in the coming months or years. With a merger, perfect coordination is certain.

Attachment A—Links to Newsprint-Related Web Sites

Two tables appearing in this comment are not able to be reprinted here. Copies of the comment with the tables are available at the Department of Justice Antitrust Division Web site, *http://www.usdoj.gov/atr,* at the Antitrust Documents Group of the Department of Justice Antitrust Division, 450 Fifth Street, N.W., Suite 1010, Washington, D.C. 20530, (202) 514–2481, and at the Office of the Clerk of the United States District Court for the District of Columbia, 333 Constitution Avenue, N.W., Washington, D.C. 20001.

Attachment B—Additional Analysis of Uncoated Groundwood Specialty Grades and Tables B1 to B7 for Section B

A. Comparing the Price of Newsprint With the Prices of Four Uncoated Groundwood Specialty Grades

Since the quality and value of newsprint is lower than the quality and value of all uncoated groundwood specialty grades, we would expect that newsprint would have a lower price. Table B1 below compares the February 2007 price (Eastern U.S.) of 30 lb. newsprint with the price of 35 lb. Hi-Brites (65 brightness level), the price of 35 lb. SCA,

[120] The PPPC February 2007 Flash Report shows the operating rate for North American newsprint mills for the first two months of 1997 at 95%.

[121] According to Andrew Battista, senior RISI economist, ''practical [maximum] capacity'' is ''98% of theoretical capacity.'' See. ''Is rising newsprint demand necessary to support higher prices in 2004?'' (*paperloop.com*, December 11, 2003).

[122] Pulp & Paper Week, February 19, 2007 and RISI news report, March 19, 2007.

[123] Abitibi reported its average cost of newsprint production in 2006 as C$523 (US$461). Abitibi Senior VP for Corporate Development and CFO Pierre Rougeau presentation to 2007 Goldman Sachs Paper & Forest Products Investor Day, 3/20/07, Slide 24. Abitibi's firm-wide cost of distribution is 15.2 percent of its firm-wide cost of production, averaged over 2002–2005. Abitibi 2005 Annual Report, p. 42. Using Abitibi's average delivered cost is conservative. In reality, Abitibi and Bowater pursuing a dominant firm strategy would tend to idle their highest cost plants first, chiefly those located in Eastern Canada.

[124] Jari Kuuluvainen, ''Structural Change in U.S. Newsprint Demand: GDP and Price Elasticities,'' University of Helsinki, Department of Forest Economics, Reports #34, 2004, p. 8.

[125] Sum of Abitibi and Bowater current shares adjusted for partial ownership of certain machines and mills by Abitibi and Bowater. See Tables Cl and C2 in Attachment 2. Since Abitibi has announced its intention to buy the minority owner's share of Augusta newsprint, 100% of that capacity is assigned to Abitibi for the purposes of this analysis.

[126] But note that the price of newsprint increased by 49% between the third quarter of 2002 and the third quarter of 2006 without triggering expansion by fringe firms or an increase in imports.

and the price of 35 lb. SCB. Table B1 also compares the price of 27.7 lb. newsprint with the price of 22.1 lb. directory paper.[1]

The SCB, Hi-Brite 65, and SCA 35 lb. February 2007 prices were 17.3% to 23.4% higher than the price of 30 lb. newsprint. If a newsprint buyer switched from 30 lb. newsprint to one of these higher basis weight grades, the buyer would incur a 14.3% reduction in printing surface. Taking the reduction in printing surface into account, a buyer of 30.0 lb. newsprint who switched to 35.0 lb. SCB, Hi-Brite 65, or SCA, would face an equivalent price increase per metric tonne of 30.0 lb. newsprint ranging from 34.0% to 47.0% based on February 2007 prices.

TABLE B1.—COMPARING FEBRUARY 2007 NEWSPRINT PRICES WITH THE PRICES OF FOUR UNCOATED GROUNDWOOD SPECIALTY GRADES

	February 2007 price per metric tonne	Price difference over the newsprint price	Percent price difference over the newsprint price	Percent ncrease (decrease) in square footage per metric tonne	Percent increase (decrease) in the effective price per metric tonne
Newsprint (30.0 lb.)	$630.00				
Hi-Brite 65 (35 lb.)	777.26	$147.26	23.4	(14.3)	41.0
SCA (35 lb.)	810.34	180.34	28.6	(14.3)	47.0
SCB (35 lb.)	738.68	108.68	17.3	(14.3)	34.0
Newsprint (27.7 lb.)	670.00				
Directory (22.1 lb.)	810.34	140.34	20.9	27.2	(12.0)

Source: RISI Pulp & Paper Week, February 19, 2007, p. 3.

Table B1 shows that the February 2007 price of 22.1 lb. directory paper was 20.9% higher than the price of 27.7 lb. newsprint. If a buyer of 27.7 lb. newsprint switched to the lower basis weight paper, the buyer would gain 27.2% in printing surface per metric tonne. Taking this increase in printing surface into account, a buyer of 27.7 lb. newsprint who switched to 22.1 lb. directory paper would receive an equivalent price reduction of 12.0% per metric tonne of 27.7 lb. newsprint based on February 2007 prices. However, as discussed in Section B.3.a.(4), the information provided to us by newsprint buyers leads us to conclude that the lower basis weight and thinner directory paper would not be suitable for use in a newspaper or for running on newspaper printing presses.

B. An Analysis of Estimated 2006 Abitibi and Bowater Shares of Uncoated Groundwood Specialty Grade Segments

1. Introduction

It is beyond the scope of this White Paper to delineate product markets composed of one or more uncoated groundwood specialty grades. Nonetheless, each of these grades is in some relevant product market. Both Abitibi and Bowater are significant producers of uncoated groundwood specialty grades.

We have estimated capacities and capacity shares for the following uncoated groundwood specialty grade segments: (1) All uncoated groundwood specialty grades; (2) directory paper; (3) SC/SNC glossy grades; (4) Hi-Brites/Super Hi-Brites; and (5) Bulky Book and Other. Attachment 1 contains tables showing capacity and capacity shares for NA mills for each of the first four segments shown above.[2] We also prepared a fifth table which shows East of the Rockies capacity for mills producing Hi-Brites and Super Hi-Brites. These five tables are discussed below.

Our primary source for the estimated capacity and capacity shares was the Uncoated Mechanical Papers chapter from the RISI 2006 Fact and Price Book (pp. 161–173). RISI provides capacity by manufacturer for total uncoated groundwood specialty grades, directory paper, and SC/SNC grades. Because most of the remaining capacity is for Hi-Brites and Super Hi-Brites, RISI implicitly provides capacity estimates for those two grades combined.

We supplemented the RISI uncoated groundwood specialty grade capacity data with the following sources: (1) Reported capacity for Abitibi and Bowater shown on p. 17 of their merger announcement presentation;[3] (2) Web sites of manufacturers; (3) annual reports and other public documents produced by manufacturers; and (4) online searches for additional information about manufacturers and their uncoated groundwood specialty capacity. While the results of our data search are preliminary and were subject to some exercise of judgment, we believe these results provide a good first approximation of manufacturer shares in each of the five segments described above. Additional data search would likely further refine the data.[4]

2. Abitibi-Bowater HHIs Based on Estimated 2006 Capacity and Capacity Shares by Manufacturer for Uncoated Groundwood Specialty Grade Segments

Tables B2 through B6 at the end of Attachment B show Abitibi-Bowater HHIs based on estimated 2006 capacity and capacity shares by manufacturer for the following uncoated groundwood specialty grade segments: (a) All uncoated groundwood specialty grade capacity in NA; (b) all directory paper in NA; (c) all SC/SNC glossy paper capacity in NA; (d) all Hi-Brite & Super Hi-Brite non-glossy paper capacity in NA; and (e) all HiBrite & Super Hi-Brite non-glossy paper capacity East of the Rockies. The results from Tables B2 through B6 plus Bulky Book and Other are summarized in Table B7 below.

[1] Source: RISI Pulp & Paper Week, February 19, 2007. Except for newsprint, the prices are the average of the high and low prices for February 2007. The price for directory paper is a spot price. About 80% to 90% of directory paper is sold under one to three year contracts to RBOCs and independent directory publishers. The prices in Pulp & Paper Week for the four uncoated groundwood specialty grades were per short ton. These prices were converted to price per metric tonne by multiplying the short ton prices by the ratio of the weight in pounds of a metric tonne (2,205 lbs.) to the weight in pounds of a short ton (2,000 lbs.). RISI notes that for the two newsprint grades and the four uncoated groundwood specialty grades that there had been some discounting below transaction prices.

[2] We could only identify Bulky Book capacity for Abitibi and Tembec. It appears that Bowater produces paper for the Bulky Book segment but Bowater does not specifically identify the amount of its capacity used to produce bulky book paper. Other firms may also produce Bulky Book paper, but we have not been able to identify them.

[3] This capacity is reported as uncoated mechanical by Abitibi or Bowater mill. The capacity is not further broken down by specific grades.

[4] The availability and accuracy of capacity data for manufacturers of uncoated groundwood specialty grades appears to be lower than for newsprint manufacturers.

TABLE B7.—ABITIBI-BOWATER HHIS BASED ON ESTIMATED 2006 NA CAPACITY AND CAPACITY SHARES BY MANUFACTURER FOR UNCOATED GROUNDWOOD SPECIALTY GRADE SEGMENTS

	Total NA uncoated groundwood specialty grades	NA directory lightweight paper	NA SC/SNC paper	NA hi-brites & super hi-brites non-glossy paper	East of the rockies hi-brites & super hi-brites paper	NA bulky book and other paper
Total Segment Capacity (1,000 Metric Tonnes)	6,997	1,291	3,360	2,122	1,624	224
Abitibi Capacity Share	30.2%	10.7%	26.0%	44.8%	58.5%	66.5%
Bowater Capacity Share	14.3%	0.0%	9.8%	31.8%	41.5%	0.0%
Combined Abitibi-Bowater Capacity Share	44.5%	10.7%	35.8%	76.5%	100.0%	66.5%
Pre-Merger HHI	1,516	2,319	1,454	3,286	5,144	0
Change in the HHI	749	0	511	1,392	4,856	0
Post-Merger HHI	2,265	2,319	1,965	4,679	10,000	0

Sources: RISI 2006 Global Pulp & Paper Fact & Price Book, pp. 163, 165, and 166, Abitibi-Bowater merger announcement presentation, p. 17, manufacturer Web sites, manufacturer annual reports, and other publicly available information.

Assuming the uncoated groundwood specialty segments shown in Table B7 above were relevant product and geographic markets, four of the segments (total NA uncoated groundwood specialty grades, NA SC/SNC glossy paper, NA Hi-Brite/Super Hi-Brite non-glossy paper, and East of the Rockies Hi-Brite/Super Hi-Brite non-glossy paper) show an increase in the HHI significantly greater than 100 resulting from an Abitibi-Bowater merger and these same four segments show a post-merger HHI greater than 1,800. In the case of NA Hi-Brite/Super Hi-Brite capacity, the post-merger HHI is 4,679. In the case of East of the Rockies Hi-Brite/Super Hi-Brite capacity, the post-merger HHI is 10,000. Two of the segments (Directory Paper and Bulky Book and Other) show no change in the HHI resulting from an Abitibi-Bowater merger. According to § 1.51(c) of the Merger Guidelines:

Where the post-merger HHI exceeds 1800, it will be presumed that mergers producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise.

Imports into NA vary by segment: (a) 2005 imports of SC paper into NA were 13.5% of 2006 NA SC/SCA capacity; (b) 2005 imports of Lightweight (Directory) paper into NA were 6.5% of 2006 NA Directory paper capacity; (b) all other 2005 imports were 1.9% of all other 2006 NA Uncoated Groundwood Specialty Grade capacity (i.e., Hi-Brite/Super Hi-Brite, Bulky Book, and Other).[5]

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[5] The source for the 2005 import data is the RISI 2006 Fact & Price Book, pp. 164 and 169. Canadian imports were not broken by SC, lightweight, and other. We assumed that the Canadian percentage breakdown was the same as the U.S. percentage breakdown for these three categories. The sources for the 2006 NA capacities by category are shown in Tables B2–B5.

Table B2. Abitibi-Bowater HHIs Based on Estimated Shares of 2006 NA Uncoated Groundwood Specialty Grades by Manufacturer

Rank	Manufacturer	2006 Capacity (1,000 Metric Tonnes)	2006 Capacity Share	2006 Cumulative Capacity Share	2006 Capacity Share Squared
1	Abitibi-Consolidated	2,111	30.2%	30.2%	910
2	Bowater	1,004	14.3%	44.5%	206
3	Catalyst	869	12.4%	56.9%	154
4	Fraser/Katahdin	635	9.1%	66.0%	82
5	Stora Enso	595	8.5%	74.5%	72
6	Irving	440	6.3%	80.8%	40
7	Kruger	280	4.0%	84.8%	16
8	St. Marys (Belgravia)	240	3.4%	88.2%	12
9	Madison Paper (Myllykoski)	220	3.1%	91.4%	10
10	Nippon Paper USA	165	2.4%	93.7%	6
11	Verso	100	1.4%	95.2%	2
12	White Birch (formerly Brant-Allen)	95	1.4%	96.5%	2
13	North Pacific	85	1.2%	97.7%	1
14	Blue Heron Paper	83	1.2%	98.9%	1
15	Tembec	75	1.1%	100.0%	1
	Total NA Capacity	**6,997**	**100.0%**		**1,516**

Pre-Merger HHI	**1,516**
Change in HHI	**749**
Post-Merger HHI	**2,265**

Sources: RISI 2006 Global Pulp & Paper Fact & Price Book, p. 163, Abitibi-Bowater merger announcement presentation, p. 17, manufacturer web sites, manufacturer annual reports, and other publicly available information.

Table B3. Abitibi-Bowater HHIs Based on Estimated Shares of 2006 NA Uncoated Groundwood Directory (aka Lightweight) Capacity by Manufacturer

Rank	Manufacturer	2006 Capacity (1,000 Metric Tonnes)	2006 Capacity Share	2006 Cumulative Capacity Share	2006 Capacity Share Squared
1	Fraser/Katahdin	455	35.2%	35.2%	1,242
2	Catalyst	338	26.2%	26.2%	685
3	Nippon Paper USA	165	12.8%	39.0%	163
4	Abitibi-Consolidated	138	10.7%	49.7%	114
5	Kruger	100	7.7%	57.4%	60
6	White Birch	95	7.4%	64.8%	54
	Total NA Capacity	**1,291**	**100.0%**		**2,319**

Pre-Merger HHI	**2,319**
Change in HHI	**0**
Post-Merger HHI	**2,319**

Sources: RISI 2006 Global Pulp & Paper Fact & Price Book, p. 166, Abitibi-Bowater merger announcement presentation, p. 17, manufacturer web sites, manufacturer annual reports, and other publicly available information.

Table B4. Abitibi-Bowater HHIs Based on Estimated Shares of 2006 NA Uncoated Groundwood SC and SNC Capacity by Manufacturer

Rank	Manufacturer	2006 Capacity (1,000 Metric Tonnes)	2006 Capacity Share	2006 Cumulative Capacity Share	2006 Capacity Share Squared
1	Abitibi-Consolidated	874	26.0%	26.0%	677
2	Stora Enso	595	17.7%	43.7%	314
3	Irving	440	13.1%	56.8%	171
4	Bowater	330	9.8%	66.6%	96
5	St. Marys (Belgravia)	240	7.1%	73.8%	51
6	Madison Paper (Myllykoski)	220	6.5%	80.3%	43
7	Catalyst	201	6.0%	86.3%	36
8	Kruger	180	5.4%	91.7%	29
9	Fraser/Katahdin	180	5.4%	97.0%	29
10	Verso	100	3.0%	100.0%	9
	Total NA Capacity	**3,360**	**100.0%**		**1,454**

Pre-Merger HHI	**1,454**
Change in HHI	**511**
Post-Merger HHI	**1,965**

Sources: RISI 2006 Global Pulp & Paper Fact & Price Book, p. 165, Abitibi-Bowater merger announcement presentation, p. 17, manufacturer web sites, manufacturer annual reports, and other publicly available information.

Table B5. Abitibi-Bowater HHIs Based on Estimated Shares of 2006 NA Uncoated Groundwood Hi-Brite/Super Hi-Brite Capacity by Manufacturer

	Manufacturer	2006 Capacity (1,000 Metric Tonnes)	2006 Capacity Share	2006 Cumulative Capacity Share	2006 Capacity Share Squared
1	Abitibi-Consolidated	950	44.8%	44.8%	2,004
2	Bowater	674	31.8%	76.5%	1,009
3	Catalyst	330	15.6%	92.1%	242
4	North Pacific	85	4.0%	96.1%	16
5	Blue Heron Paper	83	3.9%	100.0%	15
	Total NA Capacity	**2,122**	**100.0%**		**3,286**

Pre-Merger HHI	**3,286**
Change in HHI	**1,392**
Post-Merger HHI	**4,679**

Sources: RISI 2006 Global Pulp & Paper Fact & Price Book, pp. 163, 165, and 166, Abitibi-Bowater merger announcement presentation, p. 17, manufacturer web sites, manufacturer annual reports, and other publicly available information.

Table B6. Abitibi-Bowater HHIs Based on Estimated Shares of 2006 East of the Rockies Uncoated Groundwood Hi-Brite and Super Hi-Brite Capacity by Manufacturer

Rank	Manufacturer	2006 Capacity (1,000 Metric Tonnes)	2006 Capacity Share	2006 Cumulative Capacity Share	2006 Capacity Share Squared
1	Abitibi-Consolidated	950	58.5%	58.5%	3,422
2	Bowater	674	41.5%	100.0%	1,722
	Total NA Capacity	**1,624**	**100.0%**		**5,144**

Pre-Merger HHI	**5,144**
Change in HHI	**4,856**
Post-Merger HHI	**10,000**

Sources: RISI 2006 Global Pulp & Paper Fact & Price Book, pp. 163, 165, and 166, Abitibi-Bowater merger announcement presentation, p. 17, manufacturer web sites, manufacturer annual reports, and other publicly available information.

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Attachment C—Tables C1 to C3 for Section C

TABLE C1.—ESTIMATE OF 2006 U.S. AND CANADIAN NEWSPRINT CAPACITY BY MILL

U.S. Newsprint Mills

State/city	Company name and notes	Est. 2006 capacity metric tonnes
Alabama		
Claiborne	Alabama River Newsprint Company (Abitibi owns 100% of Alabama Newsprint.)	264,000
Coosa Pines	Bowater Incorporated	328,000
Arizona		
Snowflake	Abitibi-Consolidated Inc	375,000
California		
Pomona	Blue Heron Paper Company (The company is owned by employees. The mill was acquired from Smurfit in 2005. Blue Heron recently announced the Pomona mill would be indefinitely idled beginning May 6, 2007.)	150,000
Georgia		
Augusta	Augusta Newsprint Company (Abitibi owns 52.5% of Augusta Newsprint. Woodbridge Co. owns the other 47.5%. Abitibi has announced its intention to buy Woodbridge's 47.5% share in Augusta Newsprint.)	426,000
Dublin	SP Newsprint Company (The company is owned by 3 newspaper publishers.)	565,000
Louisiana		
DeRidder	Boise Cascade Corporation (Abitibi is the exclusive marketing and sales agent for the newsprint produced at the DeRidder mill.)	405,000
Mississippi		
Grenada	Bowater Incorporated	249,000
Oregon		
Newberg	SP Newsprint Company (The company is owned by 3 newspaper publishers. The mill was acquired from Smurfit in 1999.)	395,000
Oregon City	Blue Heron Paper Company (The company is owned by employees. The mill was acquired from Smurfit in 2000.)	140,000

TABLE C1.—ESTIMATE OF 2006 U.S. AND CANADIAN NEWSPRINT CAPACITY BY MILL—Continued

U.S. Newsprint Mills

State/city	Company name and notes	Est. 2006 capacity metric tonnes
Tennessee		
Calhoun	Bowater Incorporated (Southern Division)	382,000
	(Bowater owns 51% of one newsprint machine at the Calhoun mill with approx. 205,000 metric tonnes of capacity. The Herald Company, Inc. owns the other 49%. Bowater owns 100% of remaining Calhoun newsprint capacity.)	
Texas		
Lufkin	Abitibi-Consolidated Inc	150,000
	(The mill has been idled indefinitely since December 2003.)	
Virginia		
Ashland	Bear Island Paper Company	235,000
	(The mill is owned by White Birch, a privately-held company.)	
Washington		
Longview	North Pacific Paper Company (NORPAC)	675,000
	(JV between Weyerhauser and Nippon Paper (Japan)).	
Milwood	Inland Empire Paper Company	135,000
	(The mill is owned by 2 newspaper publishers.)	
Usk	Ponderay Newsprint Company	249,00
	(Bowater owns 40% of Ponderay and is managing partner. The remaining 60% of Ponderary is owned by 5 newspaper publishers.)	

Canadian Newsprint Mills

Province/city	Company name and notes	Est. 2006 capacity metric tonnes
Alberta		
Whitecourt	Alberta Newsprint Company Ltd	269,000
	(JV between the Stern Group and West Fraser Timber.)	
British Columbia		
Campbell River	Catalyst	321,000
	(Norske Canada was re-named Catalyst in 2005. Norske Skog sold its minority interest in Norske Canada in 2005. Catalyst is publicly traded.)	
Crofton	Catalyst	198,000
	(Norske Canada was re-named Catalyst in 2005. Norske Skog sold its minority interest in Norske Canada in 2005. Catalyst is publicly traded.)	
Mackenzie	Abitibi-Consolidated Inc	186,000
Port Mellon	Howe Sound Pulp & Paper Ltd	215,000
	(JV between Canfor (BC) and Oji Paper (Japan))	
Powell River	Catalyst	181,000
	(Norske Canada was re-named Catalyst in 2005. Norske Skog sold its minority interest in Norske Canada in 2005. Catalyst is publicly traded.)	
Manitoba		
Pine Falls	Pine Falls Paper Company Ltd	185,000
	(Mill is owned by Tembec, a publicly-traded company.)	
New Brunswick		
Dalhousie	Bowater Maritimes Inc	213,000
	Bowater now owns 100% of Bowater-Maritimes. It recently acquired minority interests from two Japanese paper companies.	
Newfoundland		
Corner Brook	Kruger Inc. (Corner Brook Pulp and Paper Ltd.)	440,000
	(Kruger is a privately-held company.)	
Grand Falls	Abitibi-Consolidated Inc	191,000
	(Includes capacity of PM 7 (capacity = 60,000 metric tonnes), which has been indefinitely idled since the end of 2005.)	
Nova Scotia		
Liverpool	Bowater Mersey Paper Company Ltd	253,000
	(Bowater owns 51% of Bowater Mersey. The Washington Post owns the other 49%.)	
Nova Scotia		
Port Hawkesbury	Stora Enso North American Corp.	190,000
	(Newsprint machine restarted at end of November 2006 after being idled for almost a year due to labor contract problems and high energy costs.)	
Ontario		
Iroquois Falls	Abitibi-Consolidated Inc	240,000
Kapuskasing	Spruce Falls Inc	330,000
	(Mill is owned by Tembec, a publicly-traded company.)	

Canadian Newsprint Mills

Province/city	Company name and notes	Est. 2006 capacity metric tonnes
Thorold	Abitibi-Consolidated Inc	414,000
Thunder Bay	Bowater Canadian Forest Products Inc	380,000
	(Includes capacity of PM 4 (capacity = 146,000 metric tonnes), which has been indefinitely idled since September 2005.)	
Whitby	Atlantic Newsprint Co.	150,000
	(Atlantic Newsprint is a business unit within the Atlantic Group, a privately-held company.)	
Quebec		
Amos	Abitibi-Consolidated Inc	207,000
Baie Comeau	Abitibi-Consolidated Inc	577,000
Bromptonville	Kruger Inc	310,000
	(Kruger is a privately-held company.)	
Clermont	Abitibi-Consolidated Inc	354,000
	(Abitibi owns 51% of one newsprint machine at the Clermont mill with approx. 219,000 metric tonnes of capacity. The New York Times Co. owns the other 49%. Abitibi owns 100% of the remaining Clermont newsprint capacity.)	
Gatineau	Bowater Canadian Forest Products, Inc	432,000
Masson	Papier Masson Ltd	240,000
	(Acquired by White Birch in 2006.)	
Quebec	Stadacona, Inc	410,000
	(Acquired by White Birch in 2004.)	
Riviere-du-Loup	F.F. Soucy Inc	265,000
	(Owned by White Birch, a privately-held company)	
Shawinigan (Belgo)	Abitibi-Consolidated Inc	116,000
Trois-Rivieres	Kruger Inc	370,000
	(Kruger is a privately-held company.)	

Sources and Notes

1. The capacity estimates for Abitibi, Bowater and Ponderay Newsprint mills are from the Abitibi-Bowater merger announcement presentation, ''Creating a Global Leader in Paper and Forest Products,'' January 29, 2007, p. 17. *http://www.abitibiconsolidated.com/aciwebsitev3.nsf/site/en/images/pdf/Final_Investor_Presentation.pdf/$file/Final_Investor_Presentation.pdf.*

2. The capacity estimates for the White Birch Paper newsprint mills are from the White Birch Paper Web site: *http://www.whitebirchpaper.com/en/p2.html.*

3. The capacity estimates for the Kruger newsprint mills are from the Kruger Web site: *http://www.kruger.com/english/D_Newsprint/Newsprint_INTRO_A.html.*

4. The capacity estimates for the Catalyst newsprint mills are from the Catalyst Web site: *http://www.catalystpaper.com/aboutus/aboutus_ourdivisions.xml*.

5. The capacity estimates for the Tembec newsprint mills are from the Tembec 2006 Annual Report, p. 29. *http://www.tembec.com/public/Investisseurs/Rapports-financiers.html.*

6. The capacity estimate for the Alberta Newsprint mill is from the Alberta Newsprint Web site: *http://www.albertanewsprint.com/profile/information.htm.*

7. The capacity estimate for the Stora Enso's Port Hawkesbury, NS newsprint mill is from the Stora Enso Web site: *http://www.storaenso.com/CDAvgn/main/0,,1_-3429-4370-,00.html*. The Port Hawkesbury mill, including its newsprint machine, was idled on December 2005 due to labor contract and energy cost problems. The newsprint machine was restarted at the end of November 2006 following the resolution of these problems. See *http://www.paperage.com/2006news/11_27_2006stora.html.*

8. Annual capacity estimates for the SP Newsprint, North Pacific, Boise Cascade, Blue Heron, Howe Sound, Atlantic Newsprint, and Inland Empire mills in Table C1 are from the July 2004 preliminary forecast shown in the Pulp and Paper Products Council (PPPC) July 9, 2004 update titled ''Update of North American Mechanical Printing Papers Capacity Forecast.'' This update can be found on the PPPC Web site under press releases: *http://www.pppc.org/en/1_0/index.html*. The Web sites for these seven manufacturers did not clearly and unambiguously identify their respective annual newsprint mill capacities.

9. Capacity at Abitibi's Kenora ON, La Baie (Port-Alfred) QC, and Stephenville NF newsprint mills are included in the PPPC July 2004 preliminary forecast. Those mills have been permanently closed. See the Abitibi 2005 Annual Report, p. 18 and the Abitibi 2004 Annual Report, p. 50. The PPPC July 2004 preliminary forecast also shows Abitibi's Alma, QC mill with newsprint capacity. The Alma mill's newsprint capacity has been converted to the production of higher value uncoated groundwood specialty grades. See the Abitibi 2004 Annual Report, p. 50.

10. The PPPC July 2004 update also notes on p. 1 that the capacities of three newsprint machines at Abitibi's Sheldon, TX mill and the #3 newsprint machine at Bowater's Thunder Bay ON mill that had been idled for over a year were no longer included in the forecast. The Abitibi Sheldon, TX mill has been permanently closed. See Abitibi 2004 Annual Report, p. 50. The Bowater Thunder Bay #3 newsprint machine will not be restarted according to Bowater. See Bowater February 6, 2007 news release ''Bowater Announces Fourth Quarter and Full Year 2006 Financial Results,'' Note 1. ''Based on the continued decline of North American newsprint consumption through the third quarter of 2006, Bowater now has no plans to restart the machine.''

11. The PPPC March 2006 forecast of 2006 NA newsprint capacity is 12,625,000 metric tonnes. Compared to the total in Table C2 above, this is a difference of 135,000 metric tonnes or 1.4%. In its forecast, the PPPC does not provide a breakdown by manufacturer or by mill so the reasons for the difference cannot be ascertained with certainty. The PPPC does not include the 150,000 metric tonne capacity of Abitibi's Lufkin, TX mill in its 2006 forecast because the mill has been indefinitely idled since December 2003. The capacity of the Lufkin, TX mill is included in Tables C1–C3, however, because Abitibi continues to count the Lufkin capacity in its public documents, including the Abitibi-Bowater merger announcement presentation. See the Abitibi-Bowater merger announcement presentation, ''Creating a Global Leader in Paper and Forest Products,'' January 29, 2007, p. 17. From an antitrust perspective, it is appropriate to include the Lufkin, TX capacity in Abitibi's total newsprint capacity if the mill could be re-started within a year. See the product market discussion in Section B regarding ''Firms That Participate Through Supply Response.'' If the Lufkin, TX mill's capacity is added to the PPPC 2006 forecast, the difference between the Table C2 total and the PPPC forecast for 2006 is reduced to 15,000 metric tonnes or 0.1%.

12. Two other mills included in the PPPC July 2004 preliminary forecast, Katahdin Paper and Irving Paper, no longer manufacture newsprint. Their newsprint capacity has been converted to the production of higher value uncoated groundwood specialty grades. In addition, the PPPC July 2004 preliminary forecast shows a small amount of newsprint capacity at Kruger's Manistique, MI mill. The mill no longer produces newsprint and Kruger no longer owns the mill.

13. According to an article in Editor & Publisher by Debra Garcia, dated March 28, 2007,''Blue Heron Paper Co. [recently] announced it would indefinitely idle its 140,000 tonnes/year 100% recycled newsprint mill in Pomona, Calif., due to high wastepaper and energy costs and declining newsprint consumption. The shutdown is slated to begin about May 6.''

14. The information on which the notes in Table C1 are based can generally be found on manufacturer web sites, including annual reports and 10K reports available as pdf files on the web sites of publicly-traded newsprint manufacturers. The source for Abitibi's plans to purchase the remaining 47.5% interest in Augusta Newsprint is the Abitibi presentation ''Our Story on Paper'' by President and CEO John Weaver at the Citigroup 11th Annual Global Paper and Forest Products Conference, December 7, 2006, p. 26, which is available on the Abitibi Web site.

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Table C2: Abitibi-Bowater HHIs Based on Estimated 2006 North American Newsprint Capacity and Capacity Shares by Manufacturer

)00 tonr	Manufacturer	2006 Capacity (1,000 Metric Tonnes)	2006 Capacity Share	2006 Cumulative Capacity Share	2006 Capacity Share Squared
1	Abitibi-Consolidated	3,500	27.4%	27.4%	752
2	Bowater	2,237	17.5%	45.0%	307
3	White Birch Paper (formerly Brant-Allen)	1,150	9.0%	54.0%	81
4	Kruger	1,120	8.8%	62.8%	77
5	SP Newsprint (formerly Southeast Paper)	960	7.5%	70.3%	57
6	Catalyst (formerly Norske Canada)	700	5.5%	75.8%	30
7	North Pacific Paper (NORPAC)	675	5.3%	81.1%	28
8	Tembec	515	4.0%	85.1%	16
9	Boise Cascade	405	3.2%	88.3%	10
10	Blue Heron Paper	290	2.3%	90.5%	5
11	Alberta Newsprint	269	2.1%	92.6%	4
12	Ponderay Newsprint (Bowater owns 40% of Ponderay)	249	2.0%	94.6%	4
13	Howe Sound Pulp & Paper	215	1.7%	96.3%	3
14	Stora Enso	190	1.5%	97.8%	2
15	Atlantic Newsprint	150	1.2%	98.9%	1
16	Inland Empire Paper	135	1.1%	100.0%	1
	Total NA Capacity	**12,760**	**100.0%**		**1,380**

Pre-Merger HHI	**1,380**
Change in HHI	**962**
Post-Merger HHI	**2,342**

Note 1: See Table C1 for estimated NA capacity by mill and Sources and Notes for the mill specific capacity estimates. The capacity estimates for each NA manufacturer in Table C2 were compiled from the mill specific capacity estimates.

Note 2: The PPPC March 2006 forecast of 2006 NA newsprint capacity is 12,625,000 metric tonnes. Compared to the total in Table C2 above, this is a difference of 135,000 metric tonnes or 1.4%. In its forecast, the PPPC does not provide a breakdown by manufacturer or by mill so the reasons for the difference cannot ascertained with certainty. The PPPC does not include the 150,000 metric tonne capacity of Abitibi's Lufkin, TX mill in its 2006 forecast because the mill has been indefinitely idled since December 2003. The capacity of the Lufkin TX mill is included in Tables C1-C3, however, because Abitibi continues to count the Lufkin capacity in its public documents, including the Abitibi-Bowater merger announcement presentation. Furthermore, from an antitrust perspective, it is likely appropriate to include the Lufkin mill capacity in the NA total capacity estimate. If the Lufkin TX mill's capacity is added to the PPPC 2006 forecast, the difference between the Table C2 total and the PPPC forecast for 2006 is reduced to 15,000 metric tonnes or 0.1%. See Sources and Note 11 on p. 6 of Table C1 for more details and analysis.

Table C3: Abitibi-Bowater HHIs Based on Estimated 2006 East of the Rockies Newsprint Capacity and Capacity Shares by Manufacturer

)00 tonr	Manufacturer	2006 Capacity (1,000 Metric Tonnes)	2006 Capacity Share	2006 Cumulative Capacity Share	2006 Capacity Share Squared
1	Abitibi-Consolidated	2,939	30.8%	30.8%	949
2	Bowater	2,237	23.4%	54.3%	550
3	White Birch Paper (formerly Brant-Allen)	1,150	12.1%	66.3%	145
4	Kruger	1,120	11.7%	78.1%	138
5	SP Newsprint (formerly Southeast Paper)	565	5.9%	84.0%	35
6	Tembec	515	5.4%	89.4%	29
7	Boise Cascade	405	4.2%	93.6%	18
8	Alberta Newsprint	269	2.8%	96.4%	8
9	Stora Enso	190	2.0%	98.4%	4
10	Atlantic Newsprint	150	1.6%	100.0%	2
	Total East of Rockies Capacity	**9,540**	**100.0%**		**1,876**

Pre-Merger HHI	1,876
Change in HHI	1,445
Post-Merger HHI	3,321

Note 1: See Tables C1 and C2 for Sources and Notes.

Note 2: The following North America.newsprint manufactuers have all of their newsprint capacity in mills located West of the Rockies: Catalyst, North Pacific, Blue Heron, Ponderay, Howe Sound, and Inland Empire. In addition, the following North American newsprint manufacturers have some but not all of their newsprint capacity in mills located West of the Rockies: Abitibi (561,000 metric tonnes at mills in Mackenzie, BC and Snowflake, AZ) and SP Newsprint (395,000 metric tonnes at a mill in Newberg, OR).

Attachment D—Tables D1 to D4 for Section D

Table D1: Abitibi-Bowater Merger: HHIs Based on 1995 NA Newsprint Capacity and Capacity Shares (1,000 tonnes)

1995 Rank	Manufacturer	1995 Capacity (1,000 Metric Tonnes)	1995 Capacity Share	1995 Cumulative Capacity Share	1995 Capacity Share Squared
1	Abitibi-Price	1,808	11.2%	11.2%	126
2	Stone-Consolidated	1,450	9.0%	20.2%	81
3	Bowater	1,310	8.1%	35.3%	66
4	Avenor	1,115	6.9%	27.2%	48
5	Kruger	919	5.7%	41.0%	33
6	QUNO	842	5.2%	46.3%	27
7	Fletcher Challenge	705	4.4%	50.6%	19
8	Champion International	684	4.3%	54.9%	18
9	North Pacific	677	4.2%	59.1%	18
10	Smurfit	676	4.2%	63.3%	18
11	MacMillan Bloedel	509	3.2%	66.5%	10
12	Donohue	485	3.0%	69.5%	9
13	Southeast Paper	445	2.8%	72.2%	8
14	Daishowa	398	2.5%	74.7%	6
15	Boise-Cascade	384	2.4%	77.1%	6
16	Spruce Falls	360	2.2%	79.3%	5
17	Kimberly-Clark	285	1.8%	81.1%	3
18	Ponderary Newsprint	240	1.5%	82.6%	2
19	Alberta Newsprint	235	1.5%	84.1%	2
20	Newsprint South	223	1.4%	85.4%	2
21	Garden State	214	1.3%	86.8%	2
22	James Maclaren	214	1.3%	88.1%	2
23	Irving Paper	207	1.3%	89.4%	2
24	Alliance	203	1.3%	90.6%	2
25	Bear Island Paper	200	1.2%	91.9%	2
26	Howe Sound	199	1.2%	93.1%	2
27	Finley Forest	195	1.2%	94.3%	1
28	F.F. Soucy	190	1.2%	95.5%	1
29	Stora	185	1.1%	96.7%	1
30	Pine Falls	170	1.1%	97.7%	1
31	Atlantic Newsprint	148	0.9%	98.6%	1
32	FSC Paper	130	0.8%	99.5%	1
33	Inland Empire	70	0.4%	99.9%	0
34	James River	18	0.1%	100.0%	0
		16,093	**100.0%**		**524**

Hypothetical Abitibi-Bowater Merger in 1995

Pre-Merger HHI	**524**
Change in HHI	**183**
Post-Merger HHI	**707**

Source: "Newsprint: A Pulp & Paper Market Focus Book (1999)," p. 113, 1999.

Note: In 1995, Avenor owned a 40% minority interest in Ponderay Newsprint. For the purposes of this analysis, Ponderay Newsprint is identified as a separate firm.

Table D2: Acquisitions, Exits and Other Changes by NA Newsprint Manufacturers Since 1995

1995 Rank	Manufacturer	1995 Capacity Share	Acquisitions, Exits, and Other Changes Since 1995
1	Abitibi-Price	11.2%	Announced merger with Bowater (2007).
2	Stone-Consolidated	9.0%	Acquired by Abitibi-Price to become Abitibi-Consolidated (1997).
3	Bowater	8.1%	Announced merger with Abitibi-Consolidated (2007). Sold East Millinocket, ME mill (1999 newsprint capacity = 168,000 metric tonnes) to Great Northern Paper (1999). Mill acquired by Katahdin (2003). Mill exited from newsprint production in 2005-2006 by converting newsprint capacity to other paper grades .
4	Avenor	6.9%	Acquired by Bowater (1998).
5	Kruger	5.7%	Sold Manistique, MI mill (1999 newsprint capacity = 100,000 metric tonnes) to privately-owned company. Mill has exited from newsprint production by converting newsprint capacity to other paper grades . .
6	QUNO	5.2%	Acquired by Donohue (1996), which was acquired by Abitibi (2000).
7	Fletcher Challenge	4.4%	Acquired by Norske Skog (2000). Renamed Norske Canada and then Catalyst. Norske Skog sold interest in Catalyst in 2006.
8	Champion International	4.3%	Two newsprint mills acquired by Donohue (1998), which was acquired by Abitibi (2000).
9	North Pacific	4.2%	No significant change since 1995.
10	Smurfit	4.2%	In 1995, Smurfit operated three mills. Smurfit sold one mill to SP Newsprint (2000) and two mills to Blue Heron (2000 & 2005).
11	MacMillan Bloedel	3.2%	Acquired by Pacifica (1998). Acquired by Norske Skog (2001). Renamed Norske Canada and then Catalyst. Norske Skog sold interest in Catalyst in 2006.
12	Donohue	3.0%	Acquired by Abitibi-Consolidated (2000).
13	Southeast Paper (renamed SP Newsprint)	2.8%	Acquired Newberg, OR mill from Smurfit (2000).
14	Daishowa (Stadacona)	2.5%	Acquired by Enron (2001). Acquired by White Birch (2004).
15	Boise-Cascade	2.4%	No significant change since 1995.
16	Spruce Falls	2.2%	Acquired by Tembec (1997).
17	Kimberly-Clark	1.8%	Coosa Pines, AL mill acquired by Alliance (1998), which was acquired by Bowater (2001)
18	Ponderay Newsprint	1.5%	No significant change since 1995.
19	Alberta Newsprint	1.5%	No significant change since 1995.
20	Newsprint South	1.4%	Acquired by Bowater (2000).
21	Garden State	1.3%	Acquired by Enron (2000). Exited from newsprint production when mill permanently closed (2001)
22	James Maclaren	1.3%	Acquired by Papier Masson (1998). Acquired by White Birch (2006).
23	Irving Paper	1.3%	Exited from newsprint production by converting newsprint capacity to other paper grades . (2005).
24	Alliance	1.3%	Acquired by Bowater (2001).
25	Bear Island Paper	1.2%	Owned by Brant-Allen in 1995 (renamed White Birch). No significant change since 1995.
26	Howe Sound	1.2%	No significant change since 1995.
27	Finley Forest	1.2%	Acquired by Donohue (1999) which was acquired by Abitibi (2000).
28	F.F. Soucy	1.2%	Owned by Brant-Allen in 1995 (renamed White Birch). No significant change since 1995.
29	Stora Enso	1.1%	No significant change since 1995.
30	Pine Falls	1.1%	Acquired by Tembec (1998).
31	Atlantic Newsprint	0.9%	No significant change since 1995.
32	FSC Paper	0.8%	Acquired by Madison (2000). Exited from newsprint production by converting newsprint capacity to other paper grades. (2001)
33	Inland Empire	0.4%	Installed new newsprint machine and shut down old newsprint machine (2001).
34	James River	0.1%	Exited from newsprint production.
	Total	**100.0%**	

Sources: "Newsprint: A *Pulp & Paper* Market Focus Book (1999)," pp. 18, 23, 24, and 113-115; Pulp & Paper 2000 North American Factbook, pp. 46-48, 100 and 187-189; and Pulp & Paper Week, April 9, 2000, company web sites, annual reports and other industry sources.

Table D3: 1995 NA Newsprint Capacity Adjusted to Account for Acquisitions Since 1995 (1,000 Metric Tonnes)

Rank 1995 Adjusted Capacity	Manufacturer	Original 1995 Capacity	Original 1995 Capacity Share	Acquisition of Capacity Since 1995	Share of Acquisition of Capacity Since 1995	Adjusted 1995 Capacity	Adjusted 1995 Capacity Share	Change in Capacity Share Original 1995 to Adjusted 1995
1	Abitibi-Consolidated	1,808	11.2%	3,656	46.8%	5,464	34.0%	22.7%
2	Bowater	1,310	8.1%	1,658	21.2%	2,968	18.4%	10.3%
3	White Birch (formerly Brant-Allen)	390	2.4%	612	7.8%	1,002	6.2%	3.8%
4	Kruger	919	5.7%	0	0.0%	919	5.7%	0.0%
5	SP Newsprint (formerly Southeast Paper)	445	2.8%	386	4.9%	831	5.2%	2.4%
6	Catalyst (formerly Norske Skog)	705	4.4%	509	6.5%	1,214	7.5%	3.2%
7	North Pacific	677	4.2%	0	0.0%	677	4.2%	0.0%
8	Tembec	0	0.0%	530	6.8%	530	3.3%	3.3%
9	Boise-Cascade	384	2.4%	0	0.0%	384	2.4%	0.0%
10	Blue Heron	0	0.0%	290	3.7%	290	1.8%	1.8%
11	Ponderay Newsprint	240	1.5%	0	0.0%	240	1.5%	0.0%
12	Alberta Newsprint	235	1.5%	0	0.0%	235	1.5%	0.0%
13	Howe Sound	199	1.2%	0	0.0%	199	1.2%	0.0%
14	Stora Enso	185	1.1%	0	0.0%	185	1.1%	0.0%
15	Atlantic Newsprint	148	0.9%	0	0.0%	148	0.9%	0.0%
16	Inland Empire	70	0.4%	0	0.0%	70	0.4%	0.0%
17	Garden State	214	1.3%	0	0.0%	214	1.3%	0.0%
18	Irving Paper	207	1.3%	0	0.0%	207	1.3%	0.0%
19	Katahdin	0	0.0%	168	2.2%	168	1.0%	1.0%
20	FSC Paper	130	0.8%	0	0.0%	130	0.8%	0.0%
21	James River	18	0.1%	0	0.0%	18	0.1%	0.0%
	Total	**8,284**	**51.5%**	**7,809**	**100.0%**	**16,093**	**100.0%**	**48.5%**

Source: Tables D1 and D2.

[shaded box] Identifies firms that exited from the NA newsprint market between 1995 and 2006

Table D4: Net Reductions in NA Newsprint Capacity 1995-2006 (1,000 Metric Tonnes)

2006 Rank	Manufacturer	Adjusted 1995 Capacity	Adjusted 1995 Capacity Share	Estimated 2006 Capacity	Estimated 2006 Capacity Share	Change in Capacity Share from Adjusted 1995 to 2006	Net Capacity Change 1995-2006	Share of Net Capacity Change 1995-2006
1	Abitibi-Consolidated	5,464	34.0%	3,500	27.4%	(6.5%)	(1,964)	58.9%
2	Bowater	2,968	18.4%	2,237	17.5%	(0.9%)	(731)	21.9%
3	White Birch (formerly Brant-Allen)	1,002	6.2%	1,150	9.0%	2.8%	148	(4.4%)
4	Kruger	919	5.7%	1,120	8.8%	3.1%	201	(6.0%)
5	SP Newsprint (formerly Southeast Paper)	831	5.2%	960	7.5%	2.4%	129	(3.9%)
6	Catalyst (formerly Norske Skog)	1,214	7.5%	700	5.5%	(2.1%)	(514)	15.4%
7	North Pacific	677	4.2%	675	5.3%	1.1%	(2)	0.1%
8	Tembec	530	3.3%	515	4.0%	0.7%	(15)	0.5%
9	Boise-Cascade	384	2.4%	405	3.2%	0.8%	21	(0.6%)
10	Blue Heron	290	1.8%	290	2.3%	0.5%	0	0.0%
11	Alberta Newsprint	235	1.5%	269	2.1%	0.6%	34	(1.0%)
12	Ponderay Newsprint	240	1.5%	249	2.0%	0.5%	9	(0.3%)
13	Howe Sound	199	1.2%	215	1.7%	0.4%	16	(0.5%)
14	Stora Enso	185	1.1%	190	1.5%	0.3%	5	(0.2%)
15	Atlantic Newsprint	148	0.9%	150	1.2%	0.3%	2	(0.1%)
16	Inland Empire	70	0.4%	135	1.1%	0.6%	65	(2.0%)
17	Garden State	214	1.3%	0	0.0%	(1.3%)	(214)	6.4%
18	Irving Paper	207	1.3%	0	0.0%	(1.3%)	(207)	6.2%
19	Katahdin	168	1.0%	0	0.0%	(1.0%)	(168)	5.0%
20	FSC Paper	130	0.8%	0	0.0%	(0.8%)	(130)	3.9%
21	James River	18	0.1%	0	0.0%	(0.1%)	(18)	0.5%
	Total	**16,093**	**100.0%**	**12,760**	**100.0%**	**0.0%**	**(3,333)**	**100.0%**

Source: Tables C2 and D3.

[shaded box] Identifies firms that exited from the NA newsprint market between 1995 and 2006

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Attachment K—Technical Appendix to Section K Dominant Firm Model

Dominant Firm Model

This section provides a formal model of a dominant firm in an industry with fixed capacity constraints producing a homogeneous product. Fringe firms are assumed to be price-takers. Imports are assumed to be fixed. Under these conditions, a dominant firm may find it profitable to remove fringe firms as competitive constraints by allowing them to fill up their plants (Step 1). Once the fringe firms are operating at full capacity, they no longer can compete to draw sales away from the dominant firm. The dominant firm can then effectively behave as a monopolist with respect to the ''residual demand''—i.e., that portion of industry demand that is not satisfied by the fringe firms operating at full capacity. In this monopoly position, the dominant firm can raise price above the initial, competitive level (Step 2).

Whether the dominant firm will adopt this strategy of reducing output to bring the fringe to capacity and then raising its price depends on the associated gains and losses from doing so. The gains and losses, in turn, depend on various factors discussed below. The losses can be thought of in two parts, L1 and L2, corresponding to Step 1 and Step 2.

L1: In Step 1, the dominant firm gives up some of its sales to the fringe firms. The cost of doing this is the variable profit that the dominant firm would have earned on those sales. This variable profit can be calculated as the forgone quantity times the unit variable margin on those sales. The forgone quantity is the quantity needed to move the fringe firms from their initial capacity utilization to full capacity utilization. The unit variable margin is the difference between the initial industry price and the dominant firm's unit variable cost for the capacity that it idles.

The greater is L1, the less likely it is that the benefits of the dominant firm strategy will outweigh the costs. Three factors are particularly important in determining the magnitude of L1. The first factor is the capacity utilization of the fringe firms, and the second and third factors pertain to the variable profit margins on the lost sales.

- Factor 1. Initial capacity utilization of the fringe firms. if the fringe firms are operating at a high level of capacity utilization, the quantity that the dominant firm must give up to move them to full capacity is relatively small, and L1 is proportionately small. On the other hand, if initial capacity utilization is low, the dominant firm will have to give up a larger quantity to bring the fringe firms to full capacity, and L1 will tend to be large.
- Factor 2. Initial price level. Suppose the initial industry price level is low relative to the variable cost of the capacity to be idled. This means that the dominant firm's variable margin is low for the idled capacity, and the

profits it loses by giving up quantity to the fringe firms, L1, is correspondingly low. By contrast, if the initial price level is high relative to the variable cost of the capacity to be idled, the profits lost on each unit of quantity given up to the fringe firms are relatively high, making L1 large.

• Factor 3. Dominant firm's variable cost of production. The variable cost of production operates as the flip side of the initial price level. The higher the variable cost (relative to price), the smaller is L1, and the lower is variable cost (relative to price), the greater is L1. (Note that the relevant variable margin is the margin in those plants that the dominant firm would remove from production. Rationally, the dominant firm would first remove its capacity with the highest costs. For this reason, using the firm-wide average variable cost margin overstates the loss of margin in L1. The same point applies to L2 below.)

L2: In Step 2, when the dominant firm raises price above the initial level, industry customers will tend to respond by reducing their total purchases. This relationship between price and quantity demanded follows the basic ''law of demand.'' In order to keep the competitive fringe at full capacity, the dominant firm absorbs this entire decrease in quantity. As with L1, the reduction in profits in L2 is the reduction in quantity times the variable margin on those sales. We have already noted how the initial price and variable cost of production, Factor 2 and Factor 3, are important in determining the variable margin. Two additional factors also affect L2.

• Factor 4. Percentage price increase. Obviously, the greater the percentage price increase, the larger will be the associated loss of quantity along the demand curve.

• Factor 5. Elasticity of demand. Elasticity of demand is defined as the percentage change in quantity demanded that occurs in response to a one-percent change in price. The greater the elasticity of demand, the larger is the loss of quantity resulting from the price increase, and the larger is L2. Since the dominant firm is absorbing the quantity reduction for the entire industry, the appropriate demand elasticity to use is the industry demand elasticity.

The dominant firm strategy will be adopted only if the benefit or gain (G) exceeds the sum of L1 and L2. The gain the dominant firm receives from the strategy is that it receives a higher price on all of its remaining output. The relevance of the initial price level (Factor 2) and the percentage increase in price (Factor 4) is quite apparent. The other factor determining the dominant firm's profit gain is its initial sales and market share.

• Factor 6. Initial sales and share of the dominant firm. To determine the quantity of sales on which the dominant firm will enjoy the price increase, one takes the dominant firm's initial quantity and subtracts the quantity reductions associated with L1 and L2.

To see the role of initial share, take the rather extreme case in which the dominant firm has low initial sales due to a low share, and that its sales are approximately equal to the quantity losses associated with L1 and L2. In that position, the dominant firm could absorb the quantity needed to move the fringe to full capacity and absorb the decrease in quantity resulting from the increased price. However, the dominant firm would have little or no remaining sales to make at the higher price, and hence little or no benefit or gain from the strategy. In this situation, the dominant firm will not adopt the price increase strategy. By contrast, if the dominant firm has large initial sales due to a large initial share, it is more likely to still have a large quantity to sell after absorbing the losses (L1 and L2). In this situation, the dominant firm would realize a large gain from the price increase, and the price increase strategy is more likely to be adopted by the dominant firm than if it had a low initial share.

Note that the share of the dominant firm also affects L1. A large initial share for the dominant firm indicates that there is a smaller competitive fringe. This would reduce the amount of quantity that must be absorbed in Step 1 to bring the fringe to full capacity (i.e., reduces L1) for any given level of fringe capacity utilization.

Though mentioned last, the share of the dominant firm may have the greatest relevance because it is the only factor directly affected by merger enforcement policy. The initial share affects the likelihood of a significant price increase and the potential magnitude of a price increase, both of which are central antitrust concerns.

Mathematical model

Table K1 shows the six factors discussed above, the symbol used in this attachment to represent each factor, and an estimate of the current value of each factor. Factor 1a, the maximum potential capacity utilization rate for the fringe firms, is added to assist in calibrating the model to current industry conditions.

TABLE K1.—ESTIMATED PARAMETER VALUES FOR DOMINANT FIRM MODEL

Factor	Name	Symbol	Current value
1	Initial capacity utilization of fringe	Uc	[1] 95%
1a	Maximum cap. utilization of fringe	Um	[2] 98%
2	Initial industry unit price	P1	[3] $625
3	Dominant firm's unit variable cost	C	[4] $531
4	Hypothetical price increase	R	5%
5	Industry elasticity of demand	E	[5] 0.36
6	Initial share of dominant firm	S	[6] 41.5%

Under the strategy modeled here, the dominant firm first reduces its output through removal of capacity from the market to the point that the fringe firms reach their maximum capacity. The reduction in dominant firm profits in this first step is L1. The dominant firm then raises price. This price increase further reduces the dominant firm's profits through a further reduction in quantity. This profit reduction is L2. The firm increases its profits through an increase in the price at which it sells its remaining units. This profit increase is G. The dominant firm strategy is likely to be adopted if $G - L1 - L2>O$.

LI is the product of the dominant firm's per-unit variable margin and the quantity reduction needed to bring the fringe firms to their maximum capacity. Per-unit variable margin is represented as $P1 - C$. For convenience, and in the absence of more exact information about the actual shape of the cost curve, it is assumed that the

[1] The PPPC February 2007 Flash Report shows the operating rate for North American newsprint mills for the first two months of 1997 at 95%.

[2] According to Andrew Battista, senior RISI economist, ''practical [maximum] capacity'' is ''98% of theoretical capacity.'' See. ''Is rising newsprint demand necessary to support higher prices in 2004?'' (paperloop.com, December 11, 2003)

[3] Pulp & Paper Week, February 19, 2007 and RISI news report, March 19, 2007.

[4] Abitibi reported its average cost of newsprint production in 2006 as C$523 (U.S.$461). Abitibi Senior VP for Corporate Development and CFO Pierre Rougeau presentation to 2007 Goldman Sachs Paper & Forest Products Investor Day, 3/20/07, Slide 24. Abitibi's firm-wide cost of distribution is 15.2 percent of its firm-wide cost of production, averaged over 2002–2005. Abitibi 2005 Annual Report, p. 42. Using Abitibi's average delivered cost is conservative. In reality, Abitibi and Bowater pursuing a dominant firm strategy would tend to idle their highest cost plants first, chiefly those located in Eastern Canada.

[5] Jan Kuuluvainen, ''Structural Change in U.S. Newsprint Demand: GDP and Price Elasticities,'' University of Helsinki, Department of Forest Economics, Reports #34, 2004, p. 8.

[6] Sum of Abitibi and Bowater current shares adjusted for partial ownership of certain machines and mills by Abitibi and Bowater. See Tables C1 and C2 in Attachment 2. Since Abitibi has announced its intention to buy the minority owners share of Augusta newsprint, 100% of that capacity is assigned to Abitibi for the purposes of this analysis.

dominant firm's unit variable costs are constant in the relevant range.[7]

As a further convenience, quantity units will be chosen such that the industry's total nominal capacity is one unit. Under this assumption, the total capacity of the dominant firm is S and the total capacity of the fringe firms is 1 − S. Maximum practical capacity, Um, is permitted to he below maximum nominal capacity. To change fringe firms' capacity utilization from the initial level, Uc, to Um requires that the fringe's quantity be increased, and the dominant firm's quantity be decreased, by (1 − S) (Um − Uc). Thus

[1] LI = (P1 − C) (1 − S) (Um − Uc)

Once fringe firms are operating at maximum capacity, the dominant firm raises price by some percentage R. The dominant firm absorbs the entire reduction in industry quantity demanded resulting from the price increase. The quantity reduction is given by the product of R (the percentage price increase), E (the industry elasticity of demand), and Uc (initial industry quantity demanded). As before, unit variable margin for the dominant firm is given by P1 − C. The profit reduction due to the loss of quantity resulting from the price increase is given by

[2] L2 = (P1 − C) (R E Uc)

The profit increase the dominant firm gains from raising price is the price increase multiplied by the quantity the dominant firm will sell after the price increase. The change in price is R multiplied by P1. The quantity sold is the dominant firm's initial quantity, S Uc, less the quantity reductions associated with L1 and L2, which are (1 − S) (Um − Uc) and (R E Uc), respectively. The profit increase can be written

[3] G = (RPI) [(SUc) − (1 − S) (Um − Uc) − (R E Uc)]

The entire profit consequences of the dominant firm strategy can be expressed as

[4] G − L1 − L2 = (R P 1) [(S Uc) − (1 − S) (Um − Uc) − (R E Uc)]
− [(P1 − C) (1 − S) (Um − Uc)] − [(P1 − C) (R E Uc)]

From Equation [4] one can find the profit-maximizing price increase, R*, by taking the first derivative with respect to R, setting the derivative equal to zero, and solving for R*. The resulting expression is

$$[5]\ R^* = \frac{S}{2E} - \frac{(1-S)*(Um-Uc)}{2\ E\ Uc} - \frac{(P1-C)}{2P1}$$

Results and Sensitivities

Equation [5] can be solved using the parameter values in [Table 3.1]. The model predicts that the profit-maximizing price increase for a dominant firm under these circumstances would be approximately 48 percent above current levels.

This result should not be viewed as a prediction that price will necessarily increase by 48 percent above current levels. If price were to increase by such a large percentage, it is quite possible that some fringe firms would make investments that would increase capacity. It is also possible that imported newsprint would become a significant factor. It also is possible that newsprint purchasers would consider additional alternatives if price were to increase by such a large percentage. Conceptually, reactions could be accommodated in the model by reflecting additional loss of quantity experienced by the dominant firm.[8]

Several of the parameters in Table K1 are estimated; hence, their true value could be higher or lower than shown. Significant further price increases are predicted by the model even if some of the parameters are altered. As explained above, production cost in the plants that Abitibi and Bowater would idle when pursuing a dominant firm strategy would likely be higher than the average cost used in the model.

However, suppose that the level of variable cost were 20 percent lower than shown in Table K1. Suppose further that the elasticity of demand were 20 percent larger than shown in Table K1. With these changed parameters, the profit-maximizing price increase would still be 30 percent.

Attachment C—Supplement 1 to the White Paper by Economists Incorporated, Submitted on Behalf of the NAA to DOJ on July 9, 2007

Economists Incorporated

An Economic Analysis of the Competitive Effects of the Proposed Abitibi-Bowater Merger

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Response to Issues Raised at Our Meeting With the DOJ Staff on April 20, 2007

Submitted to DOJ on Behalf of NAA

John H. Preston, Kent W. Mikkelsen, Ph.D., Economists Incorporated, Washington, DC, July 9, 2007.

A. Introduction

On April 11, 2007, Economists Incorporated presented an economic analysis of the likely competitive effects of the proposed Abitibi-Bowater merger in the North American (''NA'') newsprint market (''White Paper'') to the U.S. Department of Justice (''DOJ'') to assist the Department in its investigation of the proposed merger. This economic analysis was prepared on behalf of the Newspaper Association of America (''NAA''), an association of U.S. daily newspapers.

The evidence we presented to DOJ in the White Paper demonstrates that Abitibi and Bowater jointly exercised market power to raise newsprint prices significantly above competitive levels during the period 2002 to 2006. We do not believe that any alternative explanation of the aggregate 49% increase in newsprint prices from the third quarter of 2002 through the third quarter of 2006 is remotely plausible.[1] We label our hypothesis that Abitibi and Bowater jointly exercised market power over the period 2002 to 2006 the ''Dominant Firm Hypothesis.''[2] We label the principal competing hypothesis the ''Competitive Response Hypothesis.''

On April 20, 2007, we met with the DOJ staff investigating the proposed merger to discuss our White Paper. In our discussion with DOJ, several questions were raised concerning our analysis and evidence regarding the joint exercise of market power by Abitibi and Bowater. One staff member suggested that the rise in the price of newsprint might be explained as a competitive response by newsprint producers to the appreciation of the Canadian dollar relative to the U.S. dollar. Another staff member asked whether the maximum practical operating rate for the production of uncoated groundwood specialty grades might be lower than the maximum practical operating rate for the production of newsprint.[3] The staff also asked us if the

[7] The dominant firm may be able to reduce its losses in L1 and L2 if, instead of idling capacity, it can ''dump'' some of its production in overseas markets from which they will not be re-imported.

[8] For instance, suppose that a 5 percent increase in price would result in a 1 percent loss of sales to imports or expanded fringe firms. The profit-maximizing price increase for a dominant firm with a 41.5 percent share would then be 27 percent rather than 48 percent.

[1] See especially Section J of the White Paper, which shows that it is implausible that the newsprint price increases were primarily due to input cost increases or the appreciation of the Canadian dollar relative to the U.S. dollar. The analysis in Section J is based on a comparison of price increases for newsprint and price increases for several closely related uncoated groundwood specialty grades over the period 3Q 1999 though 4Q 2006. [Note: When the Canadian dollar appreciates relative to the U.S. dollar, the cost of producing newsprint in Canadian mills increases in terms of U.S. dollars relative to the cost of producing newsprint in U.S. mills and vice versa. Newsprint is priced in U.S. dollars.J The implications of the divergence of NA operating rates between the production of newsprint and the production of uncoated groundwood specialty grades from 2002 to 2006 are discussed in Section C.3. below. This divergence in operating rates provides additional support for the conclusions in Section J of the White Paper.

[2] Our analysis and evidence for the Dominant Firm Hypothesis were presented in Sections F through K of the White Paper.

[3] During our meeting with DOJ, we had pointed out that the significantly lower price increases for uncoated groundwood specialty grades compared to the price increases for newsprint over the period 2002 to 2006 could be largely explained by the significantly lower operating rates for uncoated groundwood specialty grades. See Section J of the White Paper and Section C.3. below.

acceleration in the rate of decline of NA newsprint consumption [4] might eliminate the ability of a merged Abitibi-Bowater to engage in the type of anticompetitive behavior that we had alleged.

We divide our response to issues raised by the DOJ staff into the following five sections:

Section A. Introduction

Section B. Events Since the Merger Was Announced in January 2007 Confirm the Dominant Firm Hypothesis

1. In 2007, NA Newsprint Demand and Prices Have Declined Significantly While the Value of the Canadian Dollar Relative to the U.S. Dollar Has Increased Significantly
2. Abitibi and Bowater Have Not Taken Significant Actions To Remove Newsprint Capacity From the Market Since They Announced Their Merger in January 2007
3. Newsprint Industry Analysts and Competitors of Abitibi and Bowater Do Not Expect Abitibi and Bowater To Take Any Significant Action To Remove Newsprint Capacity From the Market Until After They Have Merged

Section C. Additional Evidence That Abitibi and Bowater Exercised Market Power Over the Period 2002 to 2006

1. Based on Publicly Available Information, the Cash Costs of NA Newsprint Mills Were Below the Price of Newsprint in 2003 and 2005.
2. Based on Publicly Available Information, the Cash Costs of NA Newsprint Mills Were Below the Price of Newsprint in 4Q 2006
3. A Comparison of Operating Rates for Newsprint and Uncoated Groundwood Specialty Grades 1999 to 2006

Section D. Additional Analysis Based on the Dominant Firm Model (DFM) Including a Revision of the DFM Designed To Consider Multi-Period Dynamics

1. Introduction
2. The Relevance of a Paper by Matthew Gentzhow to Our Conclusions Regarding the DFM
3. Would the Dominant Firm Strategy Be Profitable for Abitibi or Bowater Acting Independently?
4. What Are the Effects on Dominant Firm Behavior of a Decline in Demand?
5. A Description of a Revision of the DFM Designed to Consider Multi-period Dynamics

Section E. Conclusion

B. Events Since the Merger Was Announced in January 2007 Confirm the Dominant Firm Hypothesis

1. In 2007, NA Newsprint Demand and Prices Have Declined Significantly While the Value of the Canadian Dollar Relative to the U.S. Dollar Has Increased Significantly

a. NA Newsprint Demand Declined Significantly During the First Five Months of 2007

Table 1 below shows the percentage change in selected newsprint statistics for the first five months of 2007 compared to the first five months of 2006.[5] Table 1 also shows the percentage change in selected newsprint statistics for the twelve months of 2006 compared to the twelve months of 2005.

TABLE 1.—PERCENTAGE CHANGE FROM PRIOR YEAR FOR SELECTED PPPC NEWSPRINT STATISTICS—MAY 2007 YTD VS. MAY 2006 YTD AND DECEMBER 2006 YTD VS. DECEMBER 2005 YTD

PPPC newsprint flash report category	Percent change May 2007 year-to-date vs. May 2006 year-to-date	Percent change December 2006 year-to-date vs. December 2005 year-to-date
Total NA Demand	−10.8	−6.0
Consumption by U.S. Dailies	−9.1	−7.1
Imports from Overseas Mills	−51.3	−25.2
Shipments from NA Mills to NA Customers	−10.1	−5.6
Shipments by NA Mills to Overseas Customers	5.6	−9.8
Total Shipments by NA Mills	−7.3	−6.4

During the period January 2007 to May 2007 NA demand declined by 10.8% compared to the first five months of 2006 and consumption by U.S. daily newspapers declined by 9.1%. Imports of newsprint from overseas mills to NA customers declined by 51 .3% to an annual rate of 79,000 metric tonnes. At this rate, imports will account for 0.8% of NA demand in 2007.[6]

Table 1 also shows that shipments by NA newsprint mills to NA customers declined by 10.1% over the first five months of 2007. Partially offsetting the decline in shipments to NA customers, exports from NA mills to overseas customers increased by 5.6%. Total shipments by NA mills to both NA customers and overseas customers were down 7.3% for the five-month period.

Since March 2007, there has been a gradual improvement in NA demand and total shipments from NA mills to NA customers and overseas customers.[7] See Table 2 below.

TABLE 2.—PERCENTAGE CHANGE FROM PRIOR YEAR FOR SELECTED PPPC NEWSPRINT STATISTICS—JANUARY 2007, FEBRUARY 2007, MARCH 2007, APRIL 2007 AND MAY 2007

PPPC newsprint flash report category	Percent change January 2007 vs. January 2006	Percent change February 2007 vs. February 2006	Percent change March 2007 vs. March 2006	Percent change April 2007 vs. April 2006	Percent change May 2007 vs. May 2006
Total NA Demand	-10.5	−12.7	−13.4	−9.7	−8.7
Consumption by U.S. Dailies	−9.1	−9.4	−8.7	−9.8	−9.2
Imports from Overseas Mills	−58.1	−47.3	−62.6	−38.4	−68.7
Shipments from NA Mills to NA Customers	−9.6	−12.3	−12.6	−9.4	−7.2
Shipments by NA Mills to Overseas Customers	−17.2	10.1	7.0	−0.5	29.0

[4] See the NA newsprint consumption and production statistics for the first five months of 2007 presented in Section B.1.a below.

[5] See the Pulp and Paper Products Council (''PPPC'') Newsprint Flash Reports for May 2007, issued June 21, 2007, and December 2007, issued January 25, 2007. As apparently calculated by the PPPC, NA demand equals shipments from NA mills to NA customers plus imports from overseas mills to NA customers.

[6] In the White Paper, we concluded that significant imports by NA customers from new Chinese newsprint capacity were unlikely. See Section BA. of the White Paper for our analysis. The import statistics for the first five months of 2007 support that conclusion.

[7] See PPPC Flash Reports for March and April 2007. This is a ''gradual improvement'' in the sense that the decline in NA demand and total shipments from NA mills was lower in April and May 2007 compared to the first three months of 2007.

TABLE 2.—PERCENTAGE CHANGE FROM PRIOR YEAR FOR SELECTED PPPC NEWSPRINT STATISTICS—JANUARY 2007, FEBRUARY 2007, MARCH 2007, APRIL 2007 AND MAY 2007—Continued

PPPC newsprint flash report category	Percent change January 2007 vs. January 2006	Percent change February 2007 vs. February 2006	Percent change March 2007 vs. March 2006	Percent change April 2007 vs. April 2006	Percent change May 2007 vs. May 2006
Total Shipments by NA Mills	−10.8	−9.9	−8.6	−7.7	−0.7

Between January 2007 and March 2007, the rate of decline in total NA newsprint demand was higher than previously. In March 2007, NA demand was down 13.4% compared to March 2006. However, in April and May 2007, the rate of decline slowed. By May 2007, the decline in NA demand dropped to 8.7%.[8] The decline in shipments from NA mills to NA customers was almost cut in half: a decline of 12.6% in March vs. a decline of 7.2% in May.[9] In May 2007, total shipments from NA mills were down only 0.7% compared to May 2006 due to both the improvement in shipments to NA customers and strong export growth. After falling to 93% in March and April 2007, the operating rate for NA mills increased to 94% in May 2007. In 2006, the operating rate was 95% for all three months.

A comparison of the two columns in Table I reflects the gradual improvement in newsprint operating results over the period March 2007 to May 2007. The decline in consumption by U.S. daily newspapers increased from 7.1% for the twelve months of 2006 to 9.1% for the first five months of 2007, an increase of 2.0%. The decline in total shipments from NA newsprint mills increased from 6.4% for the twelve months of 2006 to 7.3% for the twelve months of 2006, and increase of 0.9%. Operating rates at NA newsprint mills for both the first five months of 2007 and the twelve months of 2006 were 94%.

We conclude that while there has been a modest increase in the rate of decline in newsprint consumption by U.S. daily newspapers for the first five months of 2007 compared to the twelve months of 2006, the overall operating results for NA newsprint mills over the two periods are not significantly different. As Table 2 shows, the operating results between 2006 and 2007 have been narrowing over the period March to May, not widening.

b. NA Newsprint Prices Declined Significantly During the First Five Months of 2007 While the Value of the Canadian Dollar Increased Significantly

The price of newsprint (30 lb, Eastern U.S.) reached a peak of $675 per metric tonne in May 2006 and stayed at $675 through September 2006 before declining gradually to $660 in December 2006. From December 2006 to June 2007, the NA newsprint price fell $75 to $575, a decline of 11.4%.[10]

While the price of newsprint was declining by 11.4% between December 2006 and June 2007, the value of the Canadian dollar was increasing 8.2% from $0.868 per U.S. dollar in December 2006 to $0.939 per U.S. dollar in June 2007.'' [11]

The RISI Pulp & Paper Week edition of May 21, 2007 shows a chart on page 11 comparing the price of newsprint on one vertical axis with the value of the Canadian dollar per U.S. dollar on the other vertical axis from May 2005 to April 2007. The chart shows both values tracking each other fairly closely in the 20 months from May 2005 through December 2006. From January 2007 through April 2007 the two values continuously diverge with the value of the Canadian dollar steadily increasing and the price of newsprint steadily decreasing.

Chart I below is an adaptation of the Pulp & Paper Week chart. It shows the percentage change from the respective May 2005 values for both the price of newsprint [12] and the exchange rate for the Canadian dollar in terms of U.S. dollars.[13] Between May 2005 and December 2006, the maximum difference between the two series in any month was 3.3%. In December 2006 the percentage changes from their respective May 2005 values were almost identical (a 9.1% increase for the price of newsprint and a 9.0% increase for the value of the Canadian dollar). In January 2007, the two series began to diverge. As Chart 1 shows, the divergence reached 21.2% in June 2007 as the value of the Canadian dollar increased to 17.9% above its May 2005 value and the price of newsprint declined to 3.3% below the May 2005 price.

[8] The decline in consumption by U.S. daily newspapers did not change significantly over the three months: −8.7% in March, −9.8% in April, and −9.2% in May.

[9] The decline in imports was reduced from −62.6% in March to −38.4% in April before increasing to −68.7% in May.

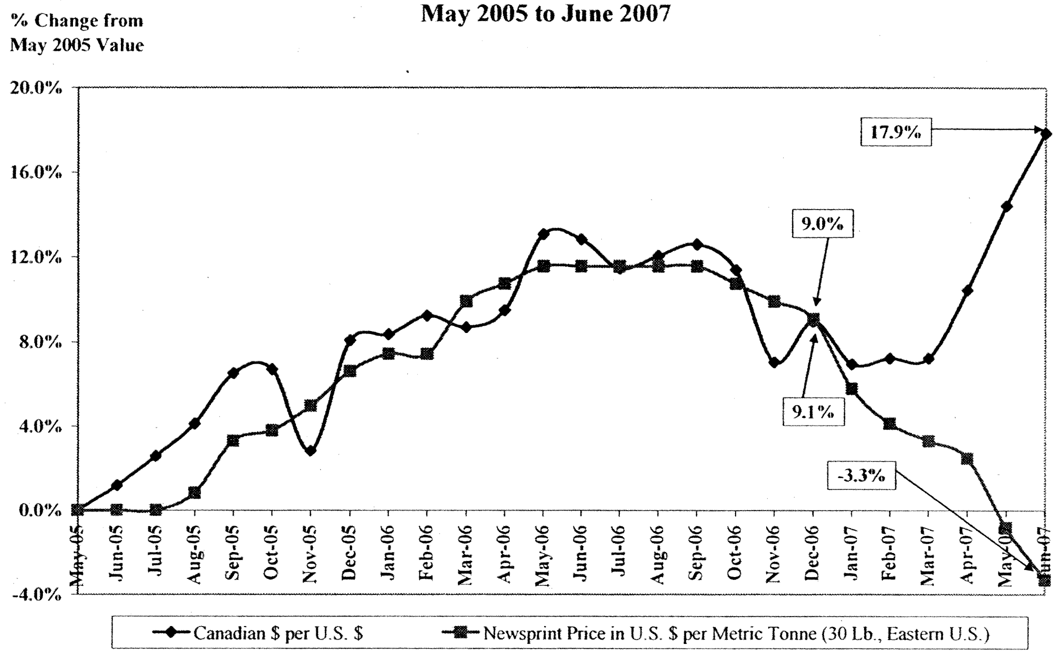
[10] The source for the monthly newsprint prices is the RISI publication Pulp & Paper Week.

[11] The source for the average monthly exchange rates is FXHistory: Historical currency exchange rates, *Oanda.com*.

[12] Source: RISI publication Pulp & Paper Week.

[13] Source: FXHistory: Historical currency exchange rates, *Oanda.com*.

Chart 1: Percentage Change in the Canadian $ per U.S. $ and the Price of Newsprint in U.S. $ per Metric Tonne (30 Lb., Eastern U.S.) May 2005 to June 2007



c. Implications of the Recent Decline in NA Newsprint Demand and Price and the Appreciation of the Canadian Dollar

Between the third quarter of 2002 and the third quarter of 2006, the price of NA newsprint rose an aggregate of 49% despite a steady decline in NA newsprint consumption.[14] As we argued in the White Paper, the strategic closure of newsprint capacity by Abitibi and Bowater was a joint exercise of market power responsible for the price increases. We believe these actions and their effects are well documented in the White Paper. As an alternative to the Dominant Firm Hypothesis, the Competitive Response Hypothesis asserts that the price increases are due to competitive responses to the appreciation of the Canadian dollar and increases in the prices of inputs.

As discussed below, since the merger announcement in early January and likely several months earlier, Abitibi and Bowater have stopped strategically closing capacity to raise the price of newsprint. In our view and the view of newsprint industry analysts and newsprint competitors of Abitibi and Bowater,[15] the reason that Abitibi and Bowater have stopped strategically closing capacity is the concern that it could very well lead to the rejection of the merger by U.S. and/or Canadian antitrust authorities. It is also our view and the view of newsprint industry analysts and newsprint competitors of Abitibi and Bowater[16] that if the merger is approved in the U.S. and Canada, a merged AbitibiBowater will take the actions necessary to restore the ''balance'' between newsprint demand and supply to again raise the price of newsprint above competitive levels.

The current decline in newsprint prices is the true competitive response to the decline in NA newsprint demand. In our view, the decline in newsprint prices is occurring because Abitibi and Bowater perceive it would be imprudent to close significant capacity during the merger review period. The current decline in newsprint prices is indicative of the declines that would have occurred over the period 2002 to 2006 had Abitibi and Bowater not intervened with their strategic removal of capacity.

The widening divergence between the percentage change in the appreciation of the Canadian dollar and the percentage change in NA newsprint prices from December 2006 to June 2007 as shown in Chart I is further evidence that the correlation between the appreciation of the Canadian dollar and the rise in the price of newsprint in prior years was due to the strategic behavior of Abitibi and Bowater and was not a competitive response to the appreciation.

Of course, higher newsprint costs must be reflected in newsprint prices and, as newsprint demand declines, the highest cost capacity will be forced to exit from the market. In 2007, we observe newsprint prices approaching or dropping below the cash costs of the highest cost mills. One mill (the Blue Heron Pomona, CA mill) has been indefinitely idled because it apparently can no longer cover its cash costs. In our view, the operation of the NA newsprint market in the face of declining demand in 2007 is reflective of a competitive market due to the temporary absence of the exercise of market power by Abitibi and Bowater.[17]

2. Abitibi and Bowater Have Not Taken Significant Actions To Remove Newsprint Capacity from the Market Since the Merger Was Announced in January 2007

Abitibi and Bowater began their merger discussions in June 2006 and concluded them with their merger announcement on January 29, 2007. As antitrust economists, we would expect that during the merger review by regulatory authorities neither Abitibi nor Bowater would take any actions that could be construed by antitrust regulators as anticompetitive, including the significant removal of capacity from the market to raise the price of newsprint.[18] It is likely that even before January 29, 2007, Abitibi and Bowater felt constrained from taking actions to

[14] See Chart E6 on p. 71 of the White Paper which shows steadily rising newsprint prices in the face of steadily declining newsprint demand.

[15] See Section B.3.a. below.

[16] See Section B.3a. below.

[17] According to a RISI news note dated June 29, 2007, Kruger announced a $25 per metric tonne price increase for 30 lb. newsprint effective September 1, 2007, According to RISI, ''Kruger is North America's fourth-largest newsprint producer in terms of capacity with 1.15 million tonnes/yr of production, all of it located in tEasterni Canada. Contacts said it was the first time they could remember that the company had sought to initiate a price increase round.'' We view Kruger's announced price increase as a competitive response primarily to the appreciation of the Canadian dollar, an action taken in the absence of the exercise of market power by Abitibi and Bowater since their merger announcement in January 2007. It is plausible that NA newsprint prices have fallen close to the cash costs of one or more Kruger newsprint mills, necessitating the price increase announcement. See Section C.2. below for a discussion of 4Q 2006 cash costs of NA newsprint mills. Whether the price increase announced by Kruger will be successfully implemented or not will depend mainly on the amount of excess capacity at NA newsprint mills in September and succeeding months.

[18] See ''Background of the Combination,'' in AbitibiBowater Amendment 3 to the Form S–4 Registration Statement (''Form S–4'') filed with the SEC. June 4, 2007 pp. 70–78.

aggressively remove capacity from the market.

We are not aware of any actions by Abitibi since June 2006 to indefinitely idle or permanently shut down newsprint capacity. No such actions are identified in the Abitibi 2006 Annual Report or in Abitibi's report on its 2007 first quarter results,[19] nor are we aware of any such actions identified in the trade press. In March 2007, Bowater indefinitely idled the No. 3 newsprint machine at its Gatineau, QC mill due to weak demand and increasing costs of recycled fiber and took downtime at other unidentified newsprint mills.[20]

These actions by Bowater, however, fall far short of the capacity removals needed to restore the ''balance'' between NA newsprint supply and demand. According to RISI economist Kevin Conley, ''At this point, the announced reduction in North American supply [*i.e.*, the closure of Blue Heron's Pomona, CA mill and Bowater's curtailment of production at its Gatineau, QC mill] could not possibly keep pace with the continued decline in North American demand.'' [21]

3. Newsprint Industry Analysts and Competitors of Abitibi and Bowater Do Not Expect Abitibi and Bowater to Take Any Significant Action to Remove Newsprint Capacity from the Market Until After They have Merged

a. Comments in the Trade Press

(1) ''We would expect that Abitibi and Bowater will be focused primarily on closing the merger, and therefore, unlikely in our opinion to rationalize any newsprint capacity in IH 2007,'' Goldman Sachs analyst Richard Skidmore told investors.[22]

(2) ''No one will close any capacity because they figure AbitibiBowater will do it for them. And Abitibi and Bowater will figure they can't be too aggressive on pricing or close capacity until their deal closes,'' said one contact.[23]

(3) North American newsprint capacity now exceeds orders, resulting in a declining market. Salman Partners indicated that the majority of newsprint producers are waiting to see what will happen after the merger of Abitibi-Consotidated Inc. with Bowater Inc. later this year before making any decisions on shutdowns.[24]

(4) At this point, the announced reduction in North American supply could not possibly keep pace with the continued decline in North American demand. It appears producers are waiting for the Abitibi/Bowater merger to be finalized in the hope that the new company will close necessary capacity to balance the market and bring an end to falling newsprint prices. However, this merger of North America's two largest newsprint producers will not be completed until the third quarter of 2007, at the earliest.[25]

(5) Other suppliers are hoping the union of the two companies will go through smoothly in anticipation that AbitibiBowater will quickly make the industry's capacity cuts. They see it as a silver bullet for the whole industry, allowing them to reap the benefits of a tighter North American paper market without the necessity of cutting production themselves.[26]

(6) Dillon expected a further newsprint price hike attempt later this year, despite the sluggish market. To be successful, the two biggest producers, Abitibi and Bowater, would have to support it, and that is not likely to occur until after the merger is completed ''due to concerns that such a move might he misread by regulators,'' said Dillon.[27]

b. Implications of Comments in the Trade Press

From the trade press commentary above, it is apparent that newsprint industry analysts and newsprint competitors of Abitibi and Bowater are waiting for the merger to be completed in anticipation that a merged Abitibi-Bowater will increase NA newsprint prices by shutting down enough newsprint capacity to create a tight market. It is also apparent that these same analysts and competitors believe that Abitibi and Bowater will not take any significant actions to remove capacity from the market until after their merger review is completed ''due to concerns that such a move might be misread by regulators.'' [28]

C. Additional Evidence That Abitibi and Bowater Exercised Market Power Over the Period 2002 to 2006

1. Based on Publicly Available Information, the Cash Costs of NA Newsprint Mills Were Below the Price of Newsprint in 2003 and 2005

a. Description of RISI Newsprint Cash Cost Benchmarking Studies 2003 and 2005

RISI conducts periodic cost benchmarking studies analyzing the cash cost of producing newsprint for each NA newsprint mill.[29] The supply curve for NA newsprint can be shown by arraying the cash costs by NA mill in ascending order.

Chart 2 below compares the cash costs for NA mills in 2003 and 2005. Chart 2 has been adapted from a report by a Canadian securities analyst for CIBC World Markets (''CIBC report'') [30] The vertical axis shows the

[19] See Abitibi 2006 Annual Report, pp-23–34 and Abitibi First Quarter 2007 Report to Shareholders, pp. 6–7. In June 2007, Abitibi shut down its Grand Falls, NL mill for three weeks to repair the damage from a fire at the mill. See RISI news note, June 21, 2007.

[20] See the Bowater 10–Q Report for 1Q 2007, p. 19. According to RISI economist Kevin Conley, ''Bowater is also responding to the sharp decline in demand and rapid rise in fiber prices, curtailing newsprint production at their Gatineau mill in Quebec. The company also stated they have selected other machines for downtime that are heavily dependent on recycled fiber.'' See ''Surviving the downturn in North American newsprint'', by Kevin Conley, RISI Economist, RISI News Service, April 19, 2007. The newsprint capacity of the No. 3 machine at the Gatineau mill is approximately 115,000 metric tonnes per year. Bowater also indefinitely idled its No. 4 newsprint machine at its Thunder Bay, ON mill in September 2006. See the Bowater 10–Q Report for 1Q 2007, p. 19 and p. 23. Bowater subsequently stated that it would restart this paper machine in May 2007 producing specialty grades rather than newsprint. The newsprint capacity of the Thunder Bay machine was 146,000 metric tonnes.

[21] ''Surviving the downturn in North American newsprint'', by Kevin Conley, RISI Economist, RISI News Service, April 19, 2007. In our view, the current idling of newsprint capacity at Bowater's Gatineau, QC mill, is a competitive response and not a strategic capacity closure in pursuit of a joint dominant firm strategy.

[22] ''Market abuzz over merger: concerns center on pricing and customer relationships,'' Pulp & Paper Week, February 5, 2007, p. 11.

[23] ''Market abuzz over merger: concerns center on pricing and customer relationships,'' Pulp & Paper Week, February 5, 2007, p. 11.

[24] ''Steeper Decline in Newsprint Data Reported in February,'' Debra Garcia, Editor & Publisher, March 28, 2007.

[25] ''Surviving the downturn in North American newsprint'', by Kevin Conley, RISI Economist, RISI News Service, April 19, 2007.

[26] ''The making of a merger: secret talks that could have derailed AbitibiBowater deal set tantalizing questions for analysts,'' Pulp & Paper Week, May 7, 2007, p.8. The title of the Pulp & Paper Week article refers to other strategic options Bowater was considering as alternatives to a merger with Abitibi. According to the AbitibiBowater Form S–4 filing: ''Throughout the period from July 2006 through December 2006, Bowater continued to consider a wide range of strategic alternatives with third parties, including acquisitions of assets or businesses and sales or distributions of certain of its businesses, and members of senior management had informal discussions with their counterparts at other paper companies. Bowater's Board of Directors was regularly updated on the status of these discussions. These discussions did not advance beyond intermediate stages in respect of transactions that would have precluded a combination with Abitibi. In August 2006, Bowater commenced discussions with a paper producer regarding a possible transaction in which Bowater would acquire the paper producer and possibly either sell or spin-off its newsprint assets. However, due to significant tax and structuring issues that would have made execution difficult and potentially adversely impact shareholder value, as well as significantly differing views as to the parties' respective valuations, the parties determined not to proceed with discussions regarding a possible transaction. During this period, Bowater also explored the potential sale of certain of its newsprint assets to another newsprint manufacturer. These discussions were terminated in January 2007.'' See AbitibiBowater Amendment 3 to the Form S–4 Registration Statement (''Form S–4'') filed with the SEC. June 4, 2007, p. 71.

[27] ''Newsprint Prices Continue to Sink,'' Debra Garcia, Editor & Publisher, July 5, 2007. Chip Dillon is a newsprint industry analyst with Citigroup Global Markets.

[28] ''Newsprint Prices Continue to Sink,'' Debra Garcia, Editor & Publisher, July 5, 2007.

[29] See the RISI Web site for more mformation on these benchmarking studies. RISI publishes these studies every two years. RISI also provides quarterly updates by CD. In addition, RISI provides cash cost benchmarking studies by newsprint machine. While NAA has not acquired any of the newsprint cost benchmarking studies ($12,500 for the 2006 NA newsprint mill study), we expect that the studies are available to DOJ from Abitibi, Bowater and other newsprint manufacturers through the discovery process.

[30] See ''World Newsprint Market: Winners and Losers,'' by Don Roberts, Managing Director, CIBC World Markets, April 24, 2006, Slide 35. CIBC World Markets was retained by Abitibi in June 2006 as its financial advisor with respect to the proposed merger with Bowater. See Form S–4, p. 70. The CIBC report states that the source for the cost curve comparison is ''Paperloop Benchmarking Service,'' a predecessor to RISI. We have added the four text boxes to the left of the chart and the two text boxes to the right. In addition, we have added the two horizontal green lines and the two horizontal red lines at the top of the chart.

cash costs per metric tonne of newsprint in U.S. dollars for each NA mill in 2003 and 2005. The horizontal axis of Chart 2 shows the capacity per NA newsprint mill in 2003 and 2005 arrayed from lowest cost mill to highest cost mill. Each vertical bar represents one mill. The paler vertical bars in the foreground of the chart represent the capacities and cash costs of NA newsprint mills in 2003. The vertical darker bars in the background of the chart represent the capacities and cash costs of NA newsprint mills in 2005. As the chart shows, the mill locations in 2003 and 2005 are identified by region: Canada West, Canada East, U.S. Northeast, U.S. South, and U.S. West. The mills were not further identified in Slide 35 of the CIBC Report, but the mill owners and specific mill locations (as opposed to regional locations) are identified in the underlying paperloop.com cost benchmarking study available from RISI.

A chart appearing in this comment is not able to be reprinted here. Copies of the comment with the chart are available at the Department of Justice Antitrust Division web site, *http://www.usdoj.gov/atr*, at the Antitrust Documents Group of the Department of Justice Antitrust Division, 450 Fifth Street, NW., Suite 1010, Washington, DC 20530, (202) 514–2481, and at the Office of the Clerk of the United States District Court for the District of Columbia, 333 Constitution Avenue, NW., Washington, DC 20001.

Chart 2 shows a reduction in NA newsprint capacity of about 1.4 million metric tonnes between 2003 and 2005. The aggregate NA capacity shown for 2003 is about 13.5 million metric tonnes and the aggregate NA capacity shown for 2005 is about 12.1 million metric tonnes. In Chart 2, the number of NA newsprint mills declined from 48 in 2003 to 44 in 2005.

In 2003 and 2005, Chart 2 shows that most of the highest cost mills in NA were located in Eastern Canada. In 2005, the top half of the cost curve is dominated by Eastern Canadian mills with the exception of one U.S. Northeast mill, three U.S. West mills, and one Western Canadian mill. The bottom half of the cost curve in 2005 is dominated by mills located in the U.S. South and in Western Canada. Between 2003 and 2005, the cost disadvantage of mills in Eastern Canada increased relative to other NA mills, particularly those mills located in the U.S. South. CIBC attributes this increased cost disadvantage ''largely to the strong C$,'' stating that the ''15% appreciation of the C$ made the cost curve steeper—up another 5% since then.'' [31]

CIBC Slide 35 does not identify the quarter in which the NA mill cash costs were estimated for either the 2003 or 2005 newsprint cost benchmarking studies. In Chart 2, the two horizontal green lines that we have drawn show the NA newsprint price (30 lb., Eastern U.S.) for 1Q 2003 ($475 per metric tonne) and 4Q 2003 ($527 per metric tonne).[32] As indicated by the lower text box on the right hand side of the chart, the highest mill cash cost in 2003 was about $430 per metric tonne, which was $45 per metric tonne lower than the 1Q 2003 newsprint price and $97 per metric tonne lower than the 4Q 2003 newsprint price.

In Chart 2, the two horizontal red lines that we have drawn show the NA newsprint price (30 lb., Eastern U.S.) for 1Q 2005 ($580 per metric tonne) and 4Q 2005 ($637 per metric tonne).[33] As indicated by the upper text box on the right hand side of the chart, the highest mill cash cost in 2005 was about $510 per metric tonne which was $70 per metric tonne lower than the 1Q 2005 newsprint price and $127 per metric tonne lower than the 4Q 2005 newsprint price.

b. Implications of the RISI 2003 and 2005 Cash Cost Studies

The newsprint capacity removals by Abitibi and Bowater during the period 2002 to 2006 are analyzed in Sections F through H of the White Paper. During that time Abitibi and Bowater combined capacity removals accounted for 80.8% of total NA capacity removals. Catalyst accounted for 7.3% of the capacity removals and two firms that exited from the newsprint market to produce uncoated groundwood specialty grades accounted for 9.7%. The other thirteen newsprint manufacturers that remain in the NA newsprint market today accounted for just 2.2% of the capacity removals.[34]

If the variable cost of the newsprint capacity that Abitibi and Bowater removed from the market during the period 2002 to 2006 was less than the price of newsprint, that capacity removal would be consistent with the hypothesis that Abitibi and Bowater were jointly exercising market power. Firms in competitive markets do not generally remove capacity from the market if that capacity is generating positive profit margin (i.e., when price exceeds variable cost).

Chart 2 above shows that the price of newsprint exceeded the 2003 cash cost of all NA newsprint mills in 1Q 2003 and 4Q 2003.[35] Similarly, Chart 2 shows that the price of newsprint exceeded the 2005 cash cost of all NA newsprint mills in 1Q 2005 and 4Q 2005.[36] Due to the limitations of Chart 2 discussed above, these results strongly suggest but do not prove that the cash cost of the newsprint capacity Abitibi and Bowater removed from the market during this period was less than the price of newsprint at the time of the capacity removal. However, as we pointed out at our meeting with the DOJ staff, DOJ should be able to determine if the cash cost of the capacity removed by Abitibi and Bowater was less than the price of newsprint at the time of the capacity removal with information available to DOJ through the discovery process, including the RISI NA newsprint mill cash cost benchmarking studies. Such a determination would provide additional evidence that the capacity removals were an exercise in market power in pursuit of their dominant firm strategy.

2. Based on Publicly Available Information, the Cash Costs of NA Newsprint Mills Were Below the Price of Newsprint in 4Q 2006

a. Description of RISI Newsprint Cash Cost Benchmarking Study 4Q 2006

Chart 3 below shows cash costs of NA mills in 4Q 2006. The chart is adapted from a chart that appeared in a RISI article in April 2007.[37]

[31] See CIBC Report, Slide 35.

[32] The source of the quarterly newsprint prices is the RISI 2006 Fact & Price Book, p. 150. The price of newsprint increased in each quarter of 2003. See Chart E6 on p. 71 of the White Paper.

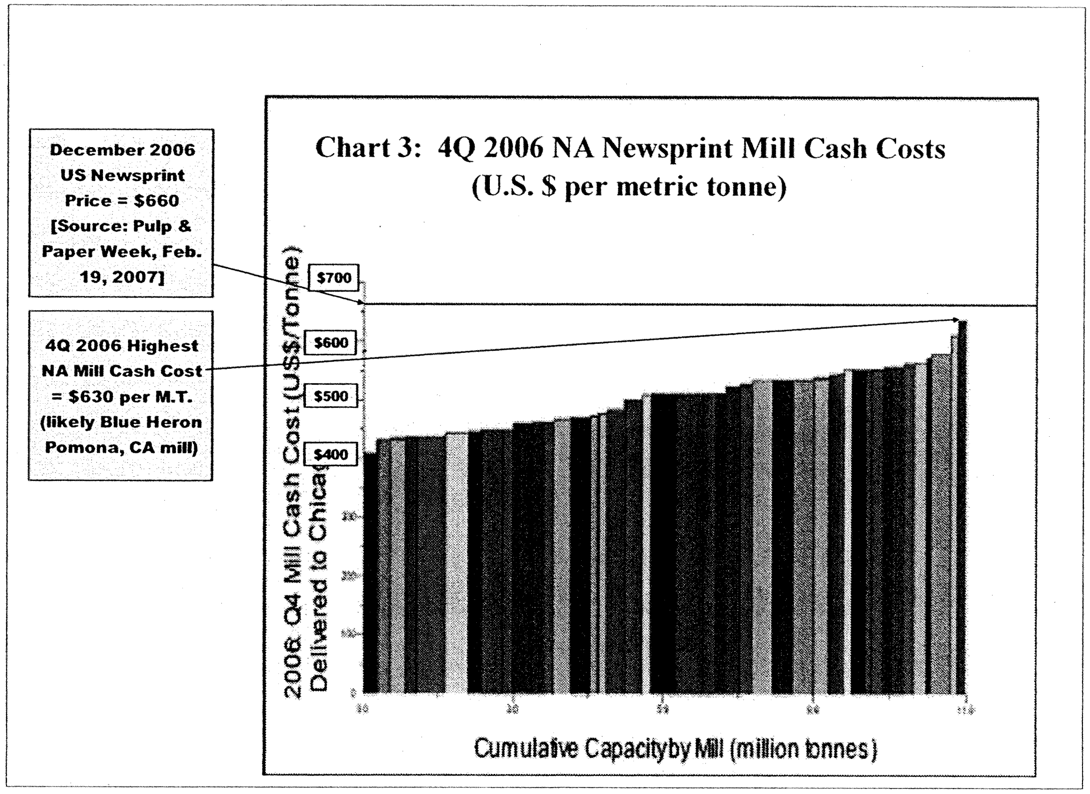
[33] The source of the quarterly newsprint prices is the RISI 2006 Fact & Price Book, p. 150. The price of newsprint increased in each quarter of 2005. See Chart E6 on p. 71 of the White Paper.

[34] See Chart G3 on p.91 of the White Paper.

[35] Since the price of newsprint increased in each quarter of 2003, the price exceeded the 2005 cash cost of each mill in the second and third quarters of 2003 as well.

[36] Since the price of newsprint increased in each quarter of 2005, price exceeded the 2005 cash cost in the second and third quarters of 2005 as well.

[37] See ''Surviving the downturn in North American newsprint'' by Kevin Conley, senior economist, RISI, April 19, 2007.



The interpretation of Chart 3 is similar to the interpretation of Chart 2 except that Chart 3 doesn't provide a color code to identify mills by region. As in Chart 2, the mill owners and specific mill locations are not identified. In Chart 3, 43 newsprint mills are shown and the aggregate NA total capacity is 11.9 million metric tonnes. The highest cost mill has a cash cost of about $630 per metric tonne which is $30 lower than the December 2006 newsprint price of $660 (30 lb., Eastern U.S.) as reported by RISI Pulp & Paper Week. The December 2006 newsprint price is indicated by the horizontal red line at the top of Chart 3.

b. Implications of the RISI 4Q 2006 Cash Cost Study

Since 4Q 2006, the price of newsprint has dropped from $660 per metric tonne to $585 in June 2007. In March 2007, Blue Heron announced that it would be indefinitely idling its Pomona, CA mill due primarily to significant increases in the cost of recycled fiber over the past year.[38] It seems likely that the high cost mill in Chart 3 at about $630 per metric tonne is the Blue Heron Pomona mill. If so, when the price of newsprint dropped below $630 to $625 in March 2007, the variable cost of production at the Pomona plant exceeded the price of newsprint.

3. A Comparison of Operating Rates for Newsprint and Uncoated Groundwood Specialty Grades 1999 to 2006

Section J of the White Paper compared newsprint prices with the prices of uncoated groundwood specialty grades 3Q 1999 to 4Q 2006. We showed that price increases for newsprint between 2002 and 2006 greatly exceeded price increases for three of four uncoated groundwood specialty grades for which data were available.[39] Since these three uncoated groundwood specialty grades were more adversely affected by the increase in input prices and the appreciation of the Canadian dollar than newsprint was over the period 2002 to 2006,[40] we would expect to see greater price increases for these uncoated groundwood specialty grades than for newsprint if the price increases for newsprint were competitively determined. The fact that the price increases for these uncoated groundwood specialty grades were considerably lower than the price increases for newsprint over this period contradicts the hypothesis that the newsprint price increases were a competitive response to input price increases and the appreciation of the Canadian dollar and confirms the Dominant Firm Hypothesis that the newsprint price increases were due to the joint exercise of market power by Abitibi and Bowater.

During our meeting with DOJ, we pointed out that the significantly lower price increases for uncoated groundwood specialty grades compared to the price increases for newsprint over the period 2002 to 2006 could be largely explained by the significantly lower operating rates for uncoated groundwood specialty grades. We were asked by the DOJ staff if the maximum practical operating rate for the production of uncoated groundwood specialty grades might be lower than the maximum practical operating rate for the production of newsprint.

Chart 4 below shows that the operating rates for both newsprint and uncoated groundwood specialty grades were nearly identical from 1999 to 2001 before diverging in 2002.[41] In 1999 and 2000, the operating

[38] The Blue Heron Pomona plant is a 100% recycled fiber plant. In March 2007, Bowater announced that it was indefinitely idling a newsprint machine at its Gatineau, QC mill due to high recycled fiber costs. See "Surviving the downturn in North American newsprint" by Kevin Conley, senior economist, RISI, April 19, 2007. SP newsprint, which also relies heavily on recycled fiber at its two mills, recently announced that it was evaluating its strategic options, including a possible sale of the two mills. One mill is located in Oregon and the other is located in Georgia. See RISI news note, May 17, 2007.

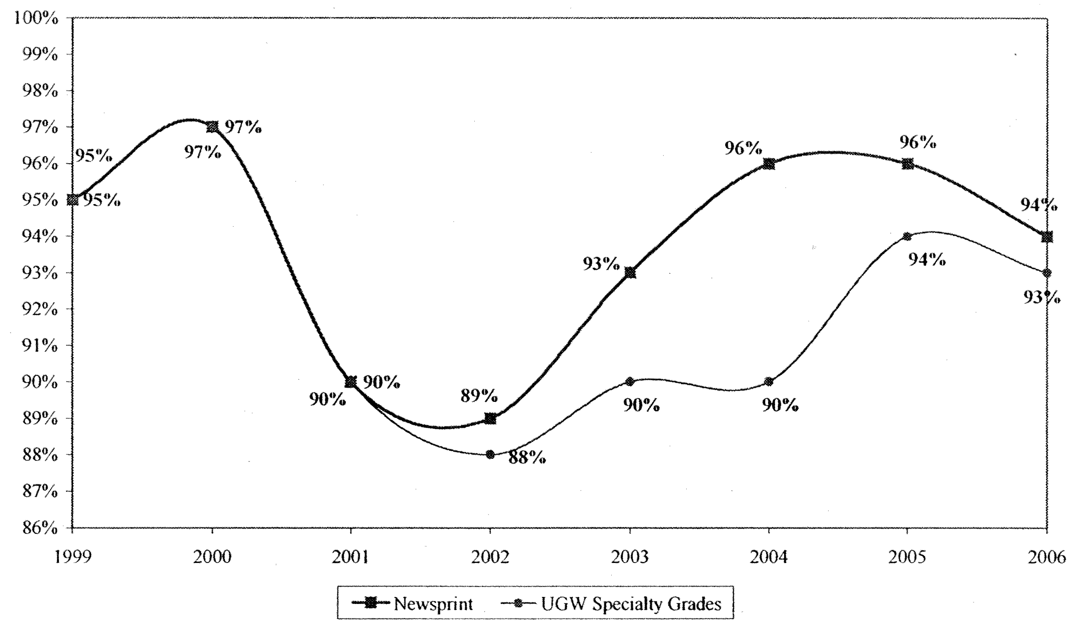
[39] The price changes were measured as a percentage of their respective 3Q 1999 prices. There was one exception to the significant divergence between newsprint prices and the prices of uncoated groundwood specialty grades over the period 2002 to 2006. The price of Hi-Brite 65 showed a similar increase to that of newsprint. The explanation for this similarity appears to be that Abitibi and Bowater are also dominant in the production of Hi-Brite grades. See p. 115 of the White Paper and Table B7 in Attachment B of the White Paper.

[40] See the discussion on pages 110–112 of the White Paper. In addition, demand for uncoated groundwood specialty grades was growing over the period 2002–2006 whereas the demand for newsprint was declining. Other things equal, these divergent growth rates should have led to higher price increases for uncoated groundwood specialty grades than for newsprint.

[41] Sources for Chart 4: (a) Newsprint operating rates 1999 to 2003 from PPPC North American Newsprint Statistics Monthly Bulletin, December 2001 to December 2004, and PPPC Newsprint Flash Reports, December 2005 and December 2006; (b) Uncoated groundwood specialty grade statistics from RISI Fact and Price Book, p. 164. The relevant statistics for the U.S. and Canada have been combined to calculate an NA operating rate for uncoated groundwood specialty grades for the period 1999 to 2006. The source for the uncoated

rates for both newsprint and uncoated groundwood specialty grades were 95% and 97% before falling to 90% in 2001. In 2002, the operating rate for newsprint exceeded the operating rate for uncoated groundwood specialty grades by 1%. This gap widened to 3% in 2003 and 6% in 2004 before narrowing to 2% in 2005 and 1% in 2006. These results show that high maximum practical operating rates are similarly attainable for uncoated groundwood specialty grades and provide further support for the hypothesis that the significantly greater increase in newsprint prices over the period 2002 to 2006 was due to the joint exercise of market power by Abitibi and Bowater.

Chart 4: A Comparison of the Operating Rates for Newsprint and Uncoated Groundwood Specialty Grades 1999 to 2006



D. Additional Analysis Based on the Dominant Firm Model (DFM) Including a Revision of the DFM Designed to Consider Multi-period Dynamics

1. Introduction

In Section K and Attachment K of the White Paper, we presented a model of dominant firm behavior adapted to the newsprint industry. The model allowed us to address two questions:

• In theory, how could Abitibi and Bowater, acting together or as a merged entity, profitably raise price?

• Do the current conditions in the newsprint industry suggest that Abitibi and Bowater actually have the ability profitably to raise price further? [42]

Using estimated values for the model's parameters, we showed that the model predicted that it would be profitable under current conditions [43] for a dominant firm with the combined shares of Abitibi and Bowater to exercise market power through the dominant firm strategy. We concluded that even allowing for adjustments to the parameter values, the model pointed to the profitability of a significant price increase. Changing various estimated parameters within a reasonable range did not alter this finding.

In this section, we address the following issues:

1. Introduction
2. The Relevance of a Paper by Matthew Gentzhow to Our Conclusions Regarding the DFM.
3. Would the Dominant Firm Strategy be Profitable for Abitibi or Bowater Acting Independently?
4. What Are the Effects on Dominant Firm Behavior of a Decline in Demand?
5. A Description of a Revision of the DFM Designed to Consider Multiperiod Dynamics.

2. The Relevance of a Paper by Matthew Gentzhow to Our Conclusions Regarding the DFM

In our April 20 meeting, the DOJ staff mentioned a paper by Matthew Gentzhow which analyzed how a newspaper's online activities affect the demand for its print edition.[44] Using information concerning the Washington Post, the author concluded that the Post's online edition reduced readership of the paid newspaper by a significant but very small amount: eliminating the online edition entirely would increase readership by only about 1.5% (p. 5).

The DOJ staff expressed interest in determining the rate at which the demand for newsprint will decline in the future. Extrapolating from Gentzhow's paper to newspapers other than the Post, demand for printed newspapers has been reduced very slightly by the introduction of newspaper websites. There is nothing in the article to suggest that newspaper websites (which are now quite widespread) will cause significant further reduction in the demand for printed newspapers (and hence newsprint) in the near future.

Data recently published by the NAA on newspaper print copy and newspaper online advertising revenues are consistent with this conclusion. On-line advertising revenues at U.S. daily newspapers increased from 5.5% of total newspaper advertising revenues in the first quarter of 2006 to 7.1% of total newspaper advertising revenues in the first

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groundwood specialty grades has been previously provided by NAA to DOJ.

[42] As discussed in Section B.1.a. above, operating results at NA newsprint mills have gradually improved over the period March 2007 to May 2007 after declining over the first three months of 2007. In May 2007, total shipments from NA mills were down only 0.7% compared to May 2006. See Table 2. One of the questions asked by DOJ concerned the applicability of the DFM in the context of a significant accelerating decline in operating results for NA newsprint mills. Given that the gap in operating results between the first five months of 2007 and the twelve months of 2006 has been narrowing over the past three months, this question may be obviated.

[43] To estimate the parameter values, we used the most current data publicly available at the time we prepared the White Paper.

[44] We believe the article staff referred to is Matthew Gentzhow, "Valuing New Goods in a Model with Complementarity: Online Newspapers" National Bureau of Economic Research (NBER) Working Paper 12562, January 24, 2006.

quarter of 2007.[45] While this is a non-trivial increase in on-line advertising revenues as a percentage of total newspaper advertising revenues, both the percentage increase and overall percentage of on-line revenues are still quite small relative to total newspaper advertising revenues.

3. Would the Dominant Firm Strategy be Profitable for Abitibi or Bowater Acting Independently?

In the White Paper model, as well as in a revised model designed to consider multi-period dynamics,[46] a dominant firm with initial share of about 25.7% (like Abitibi) or about 15.8% (like Bowater) can increase its profits by acting as a dominant firm. However, the optimal percentage price increase that either firm would find is lower than the price increase that would be preferred by a firm with their combined share (modeled as 41.5%).[47]

WHITE PAPER MODEL

Dominant Firm Share	No DF	41.5%	25.7%	15.8%
Price	$625	$922	$781	$692

REVISED MODEL

Dominant Firm Share	No DF	41.5%	25.7%	15.8%
Price	$590	$1,166	$782	$647

Under the White Paper model, the lowest initial dominant firm share from which it is profitable to engage in the dominant firm strategy, given the other assumed parameters, is about 16%. Using the revised model, the corresponding share is about 14.5%.

Both models indicate that it would be profitable for Abitibi or Bowater acting on its own to reduce capacity and elevate price. In both models, the dominant firm assumes that all other firms in the industry will act as fringe, increasing their output in response to a capacity reduction by the dominant firm. (In other words, there is no assumption of a coordinated anticompetitive response by the fringe.) As pointed out in the White Paper, however, both firms have been actively reducing capacity since at least 2002. We believe it unlikely that either of these firms assumes that the other firm will behave as part of the fringe.

4. What Are the Effects on Dominant Firm Behavior of a Decline in Demand?

a. A Decline in Demand Resulting in a Lower Newsprint Industry Capacity Utilization Rate

A decline in demand can be interpreted as affecting the initial conditions. Reducing demand starts the industry off with lower industry capacity utilization. Decreasing industry capacity utilization (i.e., increasing excess capacity in the initial conditions) reduces the optimal price increase for a dominant firm of a given size.

This question can be addressed with a simple adjustment to the White Paper model. We assumed that capacity utilization was 95% and that a dominant firm could begin to raise newsprint prices by removing capacity to bring utilization to 98%. A fall in demand could be thought of as changing the starting position from 95% capacity utilization to something lower: e.g., 90%. Leaving all the other parameters in the model the same (see Table K1 of the White Paper), the profit-maximizing dominant firm price increase at various levels of initial capacity utilization is as follows:

WHITE PAPER MODEL

Initial Capacity Utilization	95%	90%	80%	70%	63%
DF's profit-maximizing price increase	48%	43%	32%	18%	5%

Even if demand for newsprint fell to such an extent that capacity utilization was 63%, it would still be profitable for the dominant firm with a 41.5% initial share to withdraw capacity and raise price 5%.

Using a revised model, a fall in demand can be modeled as reducing the initial demand level such that, given the existing industry capacity and cost structure, the industry equilibrium output is at a lower level of capacity utilization. If demand were such that initial capacity utilization were as low as 73%, it would still be profitable for a dominant firm with a 41.5% initial share to engage in the dominant firm strategy.

REVISED MODEL

Initial Capacity Utilization	95%	90%	80%	75%	73%
DF's profit-maximizing price increase	98%	79%	47%	32%	26%

b. The Effect of an Increase in the Rate of Decline of Demand

Alternatively, a decline in demand can be interpreted as affecting the rate of decline of demand in future periods. A revised dominant firm model was created to consider multiple-period dynamics. To explore the effect of the rate of decline of demand, we contrasted the profits from two alternative strategies:

DF: The dominant firm acts as a dominant firm in the first period by withdrawing capacity and raising price, then it accepts the equilibrium price (given the reduced capacity) in subsequent periods.

No DF: The dominant firm accepts the equilibrium price and quantity in all periods.

The dominant firm prefers the strategy that yields the greatest discounted profit flow. With an initial share of 41.5%, the DF strategy is preferred even if demand is declining by as much as 20% per year.[48] It appears that no reasonable rate of future decline in demand would cause a dominant firm with this initial share to abandon dominant firm behavior entirely. Future decline in demand does not deter the dominant firm from withdrawing capacity and elevating price in the first period.

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[45] See ''Newspaper Online Ad Growth Slows—As Print Revenue Keeps Skidding,'' by Jennifer Saba, Editor & Publisher, May 29, 2007.

[46] See the description of this revised model in Section D.5. below.

[47] For the purposes our analysis of the DFM, the individual Abitibi and Bowater shares as well as their combined share have been adjusted to account for Abitibi aM Bowater partial ownership of certain newsprint mills and machines. See Table C.l. in Attachment C of the White Paper for information on their partial ownership of certain newsprint capacity.

[48] This rate is almost double the rate of decline in recent months. Higher rates of decline were not explored. During the period January 2007 to April 2007, total NA demand for newsprint declined 11.2% compared to the first four months of 2006. See Section 2.b. above.

If the dominant firm's initial share is sufficiently low (e.g., 15%), the No DF strategy is preferred when there is significant decline in future demand (e.g., 5% or 10% per year). Thus, it is possible that a dominant firm with a low initial share would act as a dominant firm when demand is declining slowly but choose not to act as a dominant firm when demand is declining rapidly. The intuition is as follows: with a small initial share, the dominant firm must close a major portion of its capacity to elevate the price in the first period. Accepting the competitive solution in subsequent periods, the dominant firm finds that the profits with a much-reduced output and slightly higher prices (as would result from the DF strategy) yields lower profits than taking its initial share of industry output at somewhat lower prices (as would result from the No DF strategy). When the two alternative strategies are considered for the initial period and multiple subsequent periods, the No DF strategy yields higher discounted profits.

Note that if there is an incentive not to act as a dominant firm, it comes from the assumption that capacity withdrawn by the dominant firm is permanently withdrawn and cannot be restarted. If the dominant firm were simply to ''idle'' capacity but retain the option of restarting the capacity in the future, then it suffers no penalty in future periods when the dominant firm behavior is no longer profitable. If capacity can be withdrawn on a temporary basis, future decreases in demand would not deter a dominant firm from behaving as a dominant firm when it is otherwise profitable to do so.

Using a model based on current industry conditions and plausible projected declines in North American demand for newsprint, we see no reason to believe that dominant firm behavior in the newsprint market will cease due to a more rapid decline in industry demand. The decline in newsprint demand is not new. With the exception of a few up-ticks in demand, the NA demand for newsprint has been steadily declining since the fourth quarter of 1999.[49] As separate firms, Abitibi and Bowater have been engaging in dominant firm behavior since at least the third quarter of 2002 in response to the decline in NA newsprint demand. Even if future rates of decline are higher than in previous years, the merger of two firms separately engaged in dominant firm activity in the past increases the likelihood that such behavior will be profitable in the future.

5. A Description of a Revision of the DFM Designed to Consider Multiperiod Dynamics

The model presented in the White Paper started with a stylized representation of current conditions and considered whether it would be profitable for a dominant firm to withdraw capacity. The revised model includes an expanded structure that permits calculation of an equilibrium price under various dominant firm behaviors and under different levels of industry demand. In particular, the revised model takes into account multi-period dynamics.

1. Information is available showing the variable cost per delivered tonne of all the mills in the industry as of 4Q 2006. See Chart 3 in Section C.2.a. above. Mills are arranged in order of increasing cost. Based on a slightly stylized version of this cost profile, it is assumed that the cost per tonne of the most efficient mill is $400, the cost per tonne of the least efficient mill is $600, and the cost per tonne of the rest of the capacity in the industry can be approximated by a straight line between these two end points. The industry cost of $600 per tonne occurs at full capacity of approximately 12,000,000 tonnes. This cost profile becomes the industry cost curve and is the supply curve under competitive conditions. Thus, if output were 12,000,000 tonnes, the cost of the least efficient mills would be $600 and, in a competitive equilibrium, $600 would be the price. $C = 400 + Q/60{,}000$.

2. For simplicity, it is further assumed that the dominant firm and the fringe have the same cost profile at corresponding degrees of capacity utilization, or in other words, that they have (approximately) the same mix of mills with various degrees of efficiency. The cost curve for the dominant firm runs from $400 at zero or low levels of output to $600 at full capacity utilization; likewise for the fringe. Added together, the two cost curves make up the industry supply curve.

3. There is an explicit industry demand equation: $Q = A P^{\alpha}$. This demand function is calibrated using the market elasticity of demand cited in the literature and assumed in the White Paper ($\alpha = -0.36$). The parameter A is chosen so that price is equal to cost in the initial scenario of interest. Decreases in demand are modeled as reductions in A. Reducing A by 10%, for instance, means that the quantity demanded at any given price would be 90% of what it previously was.

4. We start by looking at a situation in which the industry is at competitive equilibrium with capacity utilization of 95%. (For simplicity, we assume that the maximum achievable capacity utilization is 100%, rather than a lower level such as 98% in the White Paper model.) Given the industry capacity assumed, 95% capacity utilization is achieved at an output level of 12,000,000 * 95% = 11,400,000. Given the industry cost curve assumed, cost at this output level is $590 per tonne. The demand curve is parameterized with A = 113,347,403 so demand equals supply at this price and output. The assumption that the industry is currently at a competitive equilibrium follows the observation that price has been falling and capacity has not been withdrawn by either Abitibi or Bowater in the past few months.

5. At this stage, the dominant firm decides whether it is more profitable to stay at the competitive equilibrium or behave as a dominant firm, removing capacity from the market to increase price. When the industry is at a competitive equilibrium, the profit of the dominant firm is calculated as the area of a right triangle. The base of the triangle is the segment from $400 to the current industry cost level. The height of the triangle is the output of the dominant firm. In the initial scenario, output of the dominant firm is 95% times the capacity of the dominant firm.

6. If the dominant firm decides to increase price, its profit has two components. The first is a triangle as described previously (but with a reduced quantity for the dominant firm). The second is a rectangle. The height of the rectangle is the dominant firm's output and the base of the rectangle is the difference between price and the dominant firm's cost at the relevant output level. (As the dominant firm reduces capacity, the capacity with highest cost is eliminated first. For this reason, the marginal cost of the dominant firm's output declines as it reduces capacity.)

7. With these initial conditions, it is profitable for a firm with 41.5% share of capacity to remove capacity and increase price—the profit-maximizing price is almost double the initial price of $590. (One reason that such a large price increase is predicted is the assumption that demand elasticity does not increase as price increases.) At lower initial capacity levels, the profit-maximizing price is reduced. At an initial capacity level of about 14.5%, the profit-maximizing price under a dominant firm strategy yields no more profit than the competitive equilibrium. Separately and combined, Abitibi and Bowater currently have shares above 14.5%.

8. Suppose that a firm is at 15% initial capacity share. It is slightly more profitable for the first period to behave as a dominant firm. However, if demand declines 10% in each subsequent period, it is not profitable in these subsequent periods to behave as a dominant firm. The ''dominant firm'' accepts the market equilibrium in the second period and thereafter. Because the firm gave up share in the first period, however, its profits in all subsequent periods are reduced. For a firm with an initial share of 15%, the multi-period discounted profit flow is greater if the firm does not engage in the dominant firm strategy even in the first period.

9. Intuitively, whether it will be profitable to behave as a dominant firm for some number of periods will depend on the firm's initial share of capacity, the degree of capacity utilization initially, the rate of decline in demand, and the relevant discount rate. As noted above, acting as a dominant firm brings no penalty in later periods if the dominant firm idles, rather than permanently removes, capacity. In this case, considerations about reduced capacity in future periods would no longer deter a firm from pursuing a dominant firm strategy.

E. Conclusion

We met with the DOJ staff on April 20, 2007 to discuss our White Paper analyzing the likely competitive effects of the proposed Abitibi-Bowater merger.[50] This memorandum responds to several questions raised by the DOJ staff at our meeting. In our White Paper we provided considerable evidence that Abitibi and Bowater had used a dominant firm strategy to successfully exercise market power through strategic capacity closures over the period 2002 to 2006. We concluded that Abitibi and Bowater, if allowed to merge, would have an increased incentive and ability to pursue a dominant firm strategy

[49] See Chart E2 on p. 61 of the White Paper.

[50] The White Paper was submitted to DOJ on behalf of the Newspaper Association of America on April 11, 2007.

post-merger. The analysis contained in this response memorandum confirms our White Paper analysis and strengthens our conclusions.

In this response memorandum, we reach six main conclusions:

(1) Events in the NA newsprint market since the Abitibi-Bowater merger announcement in January 2007 demonstrate how the NA newsprint market would have functioned absent the exercise of market power by Abitibi and Bowater. As NA newsprint demand continued to decline in 2007, NA newsprint prices have declined to the cash costs of the highest cost NA newsprint mills. One mill (Blue Heron in Pomona, CA) has been indefinitely idled due to its high cash costs of newsprint production. In the absence of the exercise of a dominant firm strategy by Abitibi and Bowater while their proposed merger is under regulatory review, the NA newsprint market is performing competitively. See Sections B.1., B.2., B.3., and C.2. above.

(2) We conclude that if the merger is approved, Abitibi-Bowater will have an enhanced incentive and ability to engage in dominant firm behavior post-merger. As shown by trade press comments cited in Section B.3.a. above, it is widely anticipated by competitors of Abitibi and Bowater and by newsprint industry analysts that, once the merger is approved, Abitibi-Bowater will remove enough newsprint capacity from the market post-merger to create a tight market, thereby increasing newsprint prices above competitive levels.

(3) Prior to the merger announcement, changes in the price of newsprint were closely correlated with changes in the value of the Canadian dollar per U.S. dollar. Since the merger announcement in January, the value of the Canadian dollar has increased significantly while the price of newsprint has declined significantly. The divergence between the value of the Canadian dollar and the price of newsprint since the merger announcement provides strong support for the Dominant Firm hypothesis and contradicts the Competitive Response hypothesis. See Section B.1.b. and Chart 1 above.

(4) RISI benchmarking cash cost studies for NA newsprint mills strongly suggest that Abitibi and Bowater closed newsprint capacity over the period 2002–2006 even though the cash cost of that capacity was below the price of newsprint at the time of the capacity closures. Such behavior is consistent with the Dominant Firm hypothesis and contradicts the Competitive Response hypothesis. See Section C.1. and Chart 2 above.

(5) Between 1999 and 2001, the aggregate operating rates for NA newsprint mills and NA mills producing uncoated groundwood specialty grades were nearly identical. Beginning in 2002, the gap between newsprint mill operating rates and the operating rates of mills producing uncoated groundwood specialty grades began to widen. In 2004, the aggregate operating rate for newsprint mills was 6% greater than the aggregate operating rate for mills producing uncoated groundwood specialty grades. This divergence in operating rates is consistent with the Dominant Firm hypothesis and contradicts the Competitive Response Hypothesis. See Section C.3. and Chart 4 above.

(6) In Section D above, we revise the Dominant Firm Model to account for multi-period dynamics and the effect of an increase in the decline of newsprint demand on dominant firm strategy.[51] We also analyze whether Abitibi and bowater, acting independently could profitably pursue a dominant firm strategy. Our analysis shows that while it would be profitable for both Abitibi and Bowater to independently pursue a dominant firm strategy, a merged Abitibi-Bowater would have the incentive and ability to achieve higher prices and profits though a dominant firm strategy compared to the firms acting independently. We also show that a dominant firm strategy would be profitable even in the face of declines in newsprint demand considerably greater than currently experienced and over multiple periods.

[51] As shown in Section B.1.a. and Tables 1 and 2 above, the increase in the decline in NA newsprint mill operating results in the first three months of 2007 began to slow in April and May 2007. In May 2007, total shipments by NA newsprint mills were only 0.7% below the level for May 2006.

Attachment D—Supplement 2 to the White Paper by Economists Incorporated, Submitted on Behalf of the NAA to DOJ on July 20, 2007

Economists Incorporated

An Economic Analysis of the Competitive Effects of the Proposed Abitibi-Bowater Merger

Response to Issues Raised at Our Meeting With the DOJ Staff on April 20, 2007

Revision to the July 9, 2007 Response

Submitted to DOJ on Behalf of NAA

John H. Preston, Kent W. Mikkelsen, Ph.D., Economists Incorporated, Washington, DC, July 20, 2007.

A. Introduction

On July 9, 2007, Economists Incorporated submitted a response (''DOJ Response'') to issues raised by the Department of Justice (''DOJ'') staff concerning the likely competitive effects of the proposed Abitibi-Bowater merger in the North American (''NA'') newsprint market.[1] In this paper, we submit two revisions to our DOJ Response based on publicly-available information that we have received since we submitted the DOJ Response. The first revision concerns the strategy of Abitibi-Bowater competitors in the NA newsprint market who have recently announced a newsprint price increase effective in September 2007. The second revision concerns the plausibility of cost savings that Abitibi and Bowater have claimed will result from the merger.

[1] Our meeting with the DOJ staff was held on April 20, 2007. The purpose of the meeting was to discuss our economic analysis (''White Paper'') regarding the likely competitive effects of the proposed merger. We had submitted the White Paper on April 11, 2007 on behalf of the Newspaper Association of America (''NAA''), an association of U.S. daily newspapers.

B. The Strategy of NA Newsprint Competitors of Abitibi and Bowater Who Have Recently Announced a Newsprint Price Increase Effective September 1, 2007

In footnote 17 of our DOJ Response, we stated the following:

According to a RISI news note dated June 29, 2007, Kruger announced a $25 per metric tonne price increase for 30 lb. newsprint effective September 1, 2007. According to RISI, ''Kruger is North America's fourth-largest newsprint producer in terms of capacity with 1.15 million tonnes/yr of production, all of it located in [Eastern] Canada. Contacts said it was the first time they could remember that the company had sought to initiate a price increase round.'' We view Kruger's announced price increase as a competitive response primarily to the appreciation of the Canadian dollar, an action taken in the absence of the exercise of market power by Abitibi and Bowater since their merger announcement in January 2007. It is plausible that NA newsprint prices have fallen close to the cash costs of one or more Kruger newsprint mills, necessitating the price increase announcement. See Section C.2. below for a discussion of 4Q 2006 cash costs of NA newsprint mills. Whether the price increase will be successfully implemented or not will depend mainly on the amount of excess capacity at NA newsprint mills in September and succeeding months.

Subsequent trade press reports have made it clear that we were mistaken in our conclusion that Kruger's announced price increase should be viewed as a ''competitive response'' to the appreciation of the Canadian dollar. Instead, these subsequent trade press reports make it clear that the announced price increase is an anticompetitive continuation of the Abitibi-Bowater Dominant Firm strategy supported by coordination between Abitibi-Bowater and some of its leading NA newsprint competitors. According to an article in the July 16, 2007 edition of Pulp & Paper Week (p.7):[2]

Several newsprint producers including the largest North American supplier, Abitibi-Consolidated, began telling customers last week they planned to increase the price of 30-lb newsprint by $25/tonne effective Sept 1.

The move to raise prices $25 was kicked off at the end of June by Canadian supplier Kruger, the fourth largest newsprint maker in North America based on capacity. Contacts said Catalyst and Blue Heron were among suppliers also planning the increase, and No. 3 ranked White Birch was considering it.

''If this gets followed by capacity reduction announcements it would put some teeth into it,'' said one contact last week.

North American suppliers depend on Abitibi-Consolidated and Bowater, which

[2] See ''Newsprint: Price hike gains support; merger vote is dogged by asset sale uncertainties.'' See also RISI news notes ''$25/tonne US newsprint price hike gains momentum,'' July 12, 2007 and ''More North American newsprint supplies support $25/tonne price hike,'' July 16, 2007.

hope to merge in the third quarter, to close sufficient capacity to move North American newsprint supply in line with demand. Contacts estimate North American newsprint supply outpaces demand by about 500,000 tonnes this year.

No one expects the two companies to remove any capacity until after the U.S. Dept of Justice (DOJ) and Canada's Competition Bureau (CCB) disclose whether the terms of the deal require any asset divestments.

In our view, the most economically reasonable interpretation of the comments in the Pulp & Paper Week article above is as follows:

(1) Kruger, Catalyst, and Blue Heron announced a $25/tonne price increase at the end of June and in early July effective September 1, 2007 timed for the anticipated completion of the Abitibi-Bowater merger.

(2) The price increase will not succeed unless substantial capacity is closed.

(3) Abitibi-Bowater's NA newsprint competitors ''depend on Abitibi-Consolidated and Bowater * * * to close sufficient capacity to move North American newsprint supply in line with demand.'' [3]

(4) By also announcing a $25 price increase effective September 1, 2007, Abitibi has signaled to its NA newsprint competitors that it will close the capacity necessary to support the price increase.

(5) Abitibi-Bowater will not close the capacity necessary to support the price increase before their merger is approved by DOJ and the CCB, almost certainly out of concern that such an action would jeopardize regulatory approval of the merger.[4]

(6) Abitibi-Bowater will close the capacity necessary to support the price increase after the merger review period assuming the merger is approved by DOJ and CCB.

(7) In initiating the $25 price increase to become effective at the time of the anticipated completion of the Abitibi-Bowater merger, Kruger and the other Abitibi-Bowater competitors who have announced the price increase have engaged in coordinated interaction in support of the Abitibi-Bowater Dominant Finn strategy.

C. According to Abitibi's Largest Shareholder, the Probability is Low That the Merger Will Achieve the Efficiencies Claimed by Abitibi and Bowater

In previous submissions to DOJ, we have not addressed the synergies and other cost savings that Abitibi and Bowater have claimed will result from the merger. There are two reasons. First, as we do not have access to the non-public analyses supporting those claims, we are not in a good position to analyze those claims. Second, even assuming for the sake of argument that the magnitude of the claimed efficiencies were likely to be achieved, it is our opinion that the cost savings would not come close to offsetting the likely anticompetitive harm from the merger that we have analyzed in the White Paper and in the DOJ Response.[5]

The U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines set out stringent standards for determining if claimed efficiencies would be sufficient to prevent a merger from being anticompetitive.[6] In our view, the proposed merger falls far short of satisfying those stringent standards, even assuming for the sake of argument that all claimed efficiencies are cognizable as defined in the Merger Guidelines.

Third Avenue Management LLC (TAM) is Abitibi's largest shareholder with an ownership share of 12.44%.[7] TAM is a professional asset management company. In its press releases, TAM describes itself as follows:

Third Avenue Management LLC is a New York-based investment advisory firm that offers its services to private and institutional clients. Third Avenue adheres to a disciplined bottom-up value investment strategy to identify investment opportunities in undervalued securities of companies with high quality assets, understandable businesses and strong management teams that have the potential to create value over the long term. Third Avenue Management has $30 billion in assets under management and offers value-oriented strategies through mutual funds, separate accounts and alternative investment vehicles.

On July 16, 2007, TAM announced its opposition to the Abitibi-Bowater merger. Among the reasons cited for its opposition was that TAM has ''low confidence'' that the economic benefits and synergies claimed for the merger will be achieved.

Mr. Wadhwaney noted that, ''We have low confidence that the alleged economic benefits and synergies claimed by management will actually be realized, and urge shareholders to read carefully the risk factors and disclaimers that the companies have identified in their combined proxy circular.''[8]

D. Conclusion

If DOJ and the CCB approve the proposed Abitibi-Bowater merger, anticompetitive price increases to NA newsprint customers, beginning with the $25 per metric tonne price increase announced for September, 1, 2007, are virtually certain. If the Third Avenue Management analysis is correct, the synergies and other cost reductions claimed by Abitibi and Bowater are unlikely to be realized.

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[3] See Section B.3. of the DOJ Response for our similar comments by newsprint industry analysts and competitors of Abitibi-Bowater.

[4] See Section B.2. of the DOJ Response for our analysis of this issue.

[5] Based on estimates on pages 5 and 8 of the Abitibi-Bowater presentation ''Creating a Global Leader in Paper and Forest Products,'' January 29, 2007, Abitibi and Bowater were claiming that the merger would achieve cost savings of 1.6% of combined Abitibi-Bowater sales over all product lines by the end of year 1 and 3.2% by the end of year 2 and in subsequent years. (For the purposes of this discussion, we assume these percentages approximately apply to the combined NA newsprint operations of the two companies.) These claimed cost savings are small in comparison to the anticompetitive price increases that we analyzed in the White Paper (an aggregate price increase of 49% from 3Q 2002 to 3Q 2006) and the anticompetitive price increases that are likely to occur in future years if the merger is approved by DOJ and the CCB. The announced price increase of $25 discussed in Section B above is a 4.3% increase over the June 2007 newsprint price of $585 per metric tonne (30 lb., East) as published in Pulp & Paper Week. Of course, if successfully implemented, the competitive harm from the price increase to NA newspaper publishers and other NA newsprint customers would result not just from an increase in the price of newsprint sales by a merged Abitibi-Bowater but also from an increase in the price of newsprint sales by all other NA newsprint suppliers.

[6] See § 4. Efficiencies (Revised April 7, 1997) of the U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines. According to the Merger Guidelines, DOJ will consider only efficiencies that are merger-specific and cognizable. Cognizable efficiencies are defined as ''merger-specific efficiencies that have been verified and do not arise from anticompetitive reductions in output or service.'' The Merger Guidelines further state that ''When the potential adverse competitive effect of a merger is likely to be particularly large, extraordinarily great cognizable efficiencies would be necessary to prevent the merger from being anticompetitiVe.''

[7] See RISI news note ''Aitibi-Consolidated's biggest shareholder opposes merger with Bowater,'' July 16, 2007.

[8] Amit Wadhwaney is Portfolio Manager for TAM. See TAM press release, ''Third Avenue Management Opposes the Proposed Abitibi-Consolidated Merger with Bowater Incorporated,'' July 16, 2006. TAM also submitted a 13D filing to the SEC stating its opposition to the merger.