

Inflation/Factory Orders

Plastics Execs: Inflationary Pressures Easing; Industrial Economy Gaining in June

- *A Sharp Divide Exposed Between Industrial and Consumer Economies*
- *Resins Suppliers Not Keeping Up With Demand, Limiting Downward Price Moves*
- *Housing a Huge Drag for Major Appliance Mfrs as They Abruptly Reduce Resin Orders*

By Gary Rosenberger

NEW YORK (EconoPlay) July 13 – Ballooning inflationary pressures on plastic resins last spring have eased somewhat in June amid a pickup in industrial demand – reversing two alarming trends and pointing to a possible manufacturing upturn ahead, industry officials say.

Much of the rebound in demand occurred in the last six to eight weeks – although automotive is still shaking off the tsunami, defense is in disarray due to budget cuts, and housing remains in deep, deep trouble.

In fact, resins orders from appliance manufacturers took a sudden dive around Memorial Day, once it became clear that housing was not coming back – exposing a sharp divide between industrial and consumer demand.

Resin prices are still rising, but at a much slower rate – thanks mainly to the drop in the cost of crude oil. If there are any lingering inflationary pressures, they appear to be supply-driven – stemming from feedstock shortages or transportation disruptions from the Mississippi floods.

In addition, as resin manufacturers continue to consolidate, it makes it easier for them to wave off the fall in oil prices. Some purchasers suspect prices would be even lower but for artificial restraints on production.

Any lingering impact from the Japan tsunami is difficult to assess, although problems with Toyota and Honda are now being offset by the competition in Korea and Detroit.

One supplier with a national client base is getting a sense of cognitive dissonance in the way manufacturing data shows a slowdown while his own experiences say otherwise.

“June was pretty interesting when looking at the numbers out there and what we are actually seeing,” said Cody Bates, president of TDL Plastics in Corpus Christi, Texas.

“The Commerce Department said there was a slowdown in manufacturing. But this month we have seen a pretty solid uptick in activity from our end users,” he noted. “This leads us to believe that we are going to see some increase in those numbers in the coming months.”

That business is coming from a broad array of manufacturers – big and small, but mainly small. “We supply a lot of small custom-injection molders. They’re like little mom-and-pop

shops. We're seeing a pretty good uptick in business from them – and as they go, so goes everyone else," Bates said.

There were several supply shocks – including a case of force majeure on June 7 from BASF on PBT materials used for electric housings and other applications. "But those seem to be filtering through the market and stabilizing," he said.

The Consumer/Industrial Divide

"Everything that I saw last spring with major appliances has gone backwards," said Lloyd Schoen, of Entec Polymers in Chicago, a supplier of plastic resins.

The big appliance OEMs are now pushing out orders for resins "into October," reflecting weak a market for appliances this summer. The backpedaling began in late May when it became clear that housing was not going to recover this year.

"Guys that were ordering a million parts a month have slashed those orders to one third of that," Schoen said. "It has a lot to do with housing and all the appliance customers that got taken out by the appliance clunkers program last year."

On the other hand, his industrial customers are moving at full throttle, exposing a divide with the slower-moving consumer economy.

Orders from automotive manufacturers are also on the rise again, despite the factory shutdowns that occur this time of year. But there are lingering tsunami issues.

One of his customers is a tier one supplier to Toyota and Honda. "They've been flat on their back. But they picked up thanks to the Koreans and what I call the new domestics," Schoen said. "Hyundai and Kia have been incredibly strong – and Nissan is strong too. They've been launching a lot of new products."

Nissan came back earlier than Toyota or Honda because its sourcing was more global – and thus less exposed to ongoing supply disruptions in Japan, he said.

Schoen continues to see price increases for most resins because of shortages and supply shocks, in part from those Mississippi floods. The one exception is polypropylene, where prices have dropped by 20 cents a pound in June (more on that later).

Kelly Schwenk, general manager of Pyramid Plastics in Rockford, Illinois, just completed a third quarter cost survey and found resin prices continue to rise albeit at a more subdued pace than earlier this year.

“It’s a little bit of a supply issue created by the manufacturers themselves. It does follow prices for petroleum and natural gas, so prices should come down a little in the fourth quarter,” he said.

One thing is clear: None of his customers want to hold on to resin inventory. They are all “hand to mouth” because of the “uncertainty over where speculators will take prices.” And if resin prices do come down, nobody wants to be caught holding the bag at current prices.

“We have new business. There are more projects,” said Schwenk, whose client base covers everything from HVAC (heating, ventilation, and air conditioning) for trucks and cars to food and beverage companies, and consumer hardware for the likes of Home Depot.

But while his business is up, it is below original projections. “If a manufacturer was telling us they would need 100,000 parts a year, they’re only using 75,000,” Schwenk said.

His business has slowed a little from where it was in spring, and it could be more than just summer doldrums. “It has a little to do with the tsunami, but no more than 5 percent,” he said.

Business Up, Not Clear Why

“Prices are definitely coming down,” said Matt Davidson, president of Xten Industries in Kenosha, Wisconsin, an outsource manufacturer of a wide gamut of injection-molded plastic products.

“The question is whether prices were artificially inflated in the first place,” he said. “A number of us saw no justification for the 20 percent jump in polypropylene in the last couple of months. They’ve since settled back to a relatively normal range.”

His business is doing well. “Some of my customers are doing extremely well. Some are off around 20 percent,” Davidson said. “Most of our increase is from getting new customers. I see nothing in the overall economy that demonstrates robust growth.”

As he sees it, his outperforming customers are either gaining market share or just doing well in their own markets. “But it has nothing to do with the economy in general,” he said.

Others see things differently.

“From the way the economy affects our customers and our business, I would say we have seen some improvement,” said Arch Van Meter, president of Mega Corporation, in Schaumburg, Illinois, a producer of injection-molded components for military and industrial applications.

“The upturn happened, I would say, in the last six to eight weeks,” he added.

The second thing he noticed in that time frame is that “the aggressive price increases” he was seeing in the last 8 or 10 months “seem to have moderated.”

Oil prices have come down, but that only seems to have slowed the pace of price increases, which is not the same as prices being in retreat.

His business is somewhat divided between those exposed to military and government (both soft) and general industry, where all of the improvement came. For the former, he blames budget battles, which forced delays because of the lack of certitude over funding.

As for everyone else, Van Meter sees “maybe a slight pickup in sentiment that the economy is improving, so they’re more confident in starting projects that were on the shelf for several years.”

That pent-up demand seems to run the gamut of industrial products (his firm has little exposure to consumer products).

The Japanese tsunami did not have a noticeable direct effect on his business. “We had little exposure. We have minimal involvement with automotive and consumer electronics products.” he said. “Our business does assembly of industrial electronic components, but that sector was not appreciably affected by the tsunami.”

Nor did he see any increase in business as the result of companies shifting sourcing away from Japan.

Supply Crunch

Doreen Michelini, president of China Mexico Solutions, a consultancy based near Chicago, recently bought three Gaylord containers of highly engineered plastic resins for a medical client in Singapore.

“Prices were up a little but not like before. Still it was a price increase. About 4 percent,” she said. “Companies are always telling you to buy now because of price increases later.”

What is especially interesting is that this was a product that was in force majeure when she quoted it in May for August delivery. Then she got word last week that the delivery would come a month early on July 15 instead of August 15.

For lead times to be reduced that quickly is unusual – but she leaves it to others to figure out the significance of that.

She also suffers from the opposite problem – a shortage of engineered plastics. “Resins that my customers need in Asia are not available there. So I have to have it made here,” she said,

noting that this could be a hint of a lot of more molding work to come to U.S. job shops for eventual export.

The Specifics

Bates of TDL Plastics compiles a monthly State of the Market report for his customers and for interested bystanders. His latest June report suggests commodity pricing is beginning to ease at wholesale for a wide range of products as business conditions improve:

Polystyrene (think hamburger containers) and ABS (automotive trims, small kitchen appliances, and Legos) had “a pretty big jump” in May as flooding on the Mississippi disrupted barge movements. Prices have since settled back – although producers appear to be pushing for another increase in July.

Polypropylene (carpets, thermal underwear, automotive components) prices fell 15 cents a pound on June 8. “We expect to see a bit more of a drop in July as well, possibly around 5 cents a pound. We don’t see any reason for the price to go up as crude continues to fall,” Bates said.

Prices for PET (think polyester!) will probably be at the mercy of industry consolidation: “DAK is buying the operations of Wellman’s PET division, including their production plant,” Bates said. “This is the second big acquisition that DAK has made in the U.S. and is part of the ongoing consolidation that we are seeing in the PET industry.”

So he is bracing for the few big players to drive up PET prices for all end users, although prices are holding low due to the decline in crude oil prices, which makes it hard to justify any increase right now.

Even though there have been price increase announcements for polyethylene (perhaps the most popular product, used in packaging and plastic bags), “the lack of traction we have seen in the last two increases is leading us to believe that the run up in PE prices is over, and that we are going to start to see some decreases in the next month or two,” he said.

Bates is seeing some increase in demand from China for the Christmas build, which has been underway for a while – and that, too, should keep prices from falling too hard.

He thinks part of what’s behind his increased business is more stable pricing. “What happened last winter is that prices ran higher and, whenever they spike, it can put a kibosh on demand. People will hold off buying when prices run up,” Cody said.

It helps that prices of oil and benzene “are down and staying down for the time being – this is going to help overall on the prices of plastic for all of us,” he added.

Whether all this ultimately means a break for consumers on pricing remains to be seen. So far, the answer appears to be no.

Despite prices easing on the raw ingredients that go into pipes, housing wraps, and other petroleum-based building products, no manufacturer has responded by lowering prices yet, said George Pattee, CEO of Parksite Group near Chicago, a building materials supplier.

“They raised prices last spring. But there’s been no talk about rescinding them,” he said.

One such example is Tyvek, a weatherproofing housing wrap made from polypropylene that is produced by DuPont. It saw a price increase last spring, despite little home construction to speak of.

Polypropylene prices “have definitely come down” and yet “there’s no sign” of Tyvek prices following suit. In fact, Pattee can’t think of a single oil-based building product where prices have come down. “Not one,” he said.

As he sees it, with inflationary pressures easing on such products, it puts manufacturers in a quandary over whether use the windfall to invest for the future or capitulate to market pressures and drop prices.

The Labor Department is scheduled to release the producer price index for June tomorrow. Commerce releases durable goods orders data for June on Wednesday, July 27 at 8:30 a.m. ET. The above also provides an early reading into factory orders, industrial production, and ISM.

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