



GLOBAL PLASTICS LETTER

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“A World of Plastics Information”

MARCH 2007

Dear Colleague:

Underlying uncertainty upsetting upside... all predictions and indications seem to be for a stronger first half of 2007. Yet offsetting these early signals are the pervasive inflationary factors entering their fifth year driving down demand. Conversations with economists, and more importantly industry leaders, seem to be forecasting a weaker second half as we approach the season causing higher energy prices, which seem to have a deleterious effect on our industry.

Oil's dramatic price swings should end soon and we are hearing an average price of \$60 a barrel, through this year, with much less volatility. We experienced swings from \$50 to an all time high last July of \$78 a barrel – of course all tempered by the presumption of a relatively stable Middle East. At this point, oil supplies look to be slightly tighter in 2008...causing a rise to \$62 per barrel, which translates to gasoline at \$2.50/gallon.

Steel industry mergers appear set to pick up, with Russian companies hunting for new targets in North America. Others on the prowl are German companies such as ThyssenKrupp, which will likely prevail in acquiring Dofasco of Canada. More consolidation spells firmer prices as competition lessens and couple with low inventories likely increasing the price of hot-rolled steel to an average of \$650 a ton mid-year before settling down to \$600 by year end. Once again auguring opportunities for continued metals replacement by our industry if market development soothsayers structure their tactics correctly and don't succumb to shadow inflation in polymers.

China's economy will thrive more than most in the next 25 years and by 2050 may top the U.S. as the largest global economy. India is poised to pass Germany and Japan, as the third largest economy on the globe, by 2030 when its population is on track to exceed China's. Do your trade (import/export) plans include India and China? This would be crucial to both distributors and manufacturers, especially with private label plans as described in the NAW Executive Summit report, which follows. Having a presence in either or both of these countries is crucial to growth in the second decade of the 21st century.

TRENDS: We attended the National Association of Wholesalers annual Executive Summit, held in Washington, D.C. in late January and early February. Some highlights:

- Economic Forecasts, historically accurate, from Ecotrends, based on rates of change for several U.S. Industrial indicators, are predicting 2.7% growth in 2007 and 2.4% growth in 2008...and an 18 month *recession* in 2009-2010. Also expecting interest rates to move up late in 2007 and into 2008-2010 period. Oil prices going up in late 2007 and inflation growing into 2008.
- Manufacturing is growing but with fewer people...productivity is increasing.

- Wholesale trade of chemicals and allied products (including ours) will exhibit a slower rate of growth for the balance of this decade.
- India, Brazil and Mexico will have higher rates of GDP growth than U.S. in short term future.
- International Sourcing, especially to market private label products, (which is an idea whose time has come for many large wholesalers) requires a tactical approach enhanced by maintaining a local presence in the country of manufacture.
- Attend the Guangzhou Trade Fair in China to properly scout sources of supply.
- Read “The China Dream.”
- Read “Facing the Forces of Change: Lead the Way in the Supply Chain” new in 2007. It lays out clear trends such as: Private Label Products; Demand-driven channels; New profit models; Connected customers with online orders reaching 37% of distributor MRO supplies volume by 2012 (up from 17% in 2006); participate in forums such as: www.contractortalk.com to enhance customer contact beyond your website.
- Fee-for-service growing for distributors...almost 36% of profits for some.
- Private label products being marketed by 43% of the larger industrial distributors.

New techniques being practiced by some manufacturers of note in this business cycle, which is reminiscent of the 90's, are Lean Six Sigma, a process by which each sector can streamline methods for processing orders and delivering goods and services. Another initiative called Net Promoter Score by G.E. is a deceptively simple process by which G.E. businesses ask customers if they would recommend G.E. to others. On the basis of their answers, customers are tagged as promoters, neutral, or detractors. Subtract detractors from promoters, and that's the score. Have you tried this technique?

Wholesale-distributor revenues rose 9.8% in 2006 – to \$3.903 Trillion...with the Chemical (closest correlation with our plastics industry) sector up 7%. The MDM (courtesy of *Modern Distribution Management*) Inflation index was 3.47% higher during that same period.

OUTLOOK EUROPE: by John Douglas, our special imbedded correspondent in the U.K.

On the run up to K2007 (ending October 2007 in Dusseldorf), sad news from the UK, where the administrators have been called in at Storey Industrial Products (SIP). SIP is owned by the private venture group Alchemy Partners who took hold of the entire group in 1999. SIP has produced flexible and rigid sheet for many years under the Darvic and Vybak trade names. The market for these products has been reducing for many years and the arrival of Far Eastern produced product must have put pressure on the company. This is sad for the UK plastics industry that is seeing a reduction in UK produced stock shapes. The loss of 135 jobs is also a blow to the families of the employees. This leaves about 25 left in employment.

Roechling of Germany have made 2 purchases in the USA and Canada and these will be reported in our Mergers and Acquisitions section below.

The Palram group, the winner of the 2006 Best Sales and Marketing Initiative award, is pushing forward with the sales of its Palight PVC foamed sheet. The products are well known throughout Europe and Palram is also a respected producer of among other materials of PC sheet. Not much happening on the day to day front as everyone is trying to get a slice of that pie that we all talk about. I think it is coated with dream dust so that we all strive to achieve more.

I have heard (unofficially) that Quinn Plastics is interested in a European sheet and a North American distributor. They have cash and I think a bidding war could be put together with the Amari owners who are cash rich. They would bid for North American distributor. Quinn is No. 3 PC producer and close to Dow. They also have a relationship with Eastman on PETG. Eastman does not have the cash but Quinn does. Quinn does not have a track record in polymers but Eastman does. We shall wait and see.

PRICING: Dow Chemical announces price increase for PC of \$0.12/lb effective March 15, 2007 in North America and 200 Euros/metric tonne in Europe and the Middle East...benzene price rises blamed. ABS prices had risen in February. (See separate story on possible takeover of Dow below in the M&A section). Prices for PE, PP and PS start to rise again after a months long slide – only PVC is down or stable this month. We expect continual swings in prices for commodities throughout this year, with Engineering resins trending higher.

DISTRIBUTOR/MANUFACTURER BRIEFS: Acrix, Inc. introduces its Acriglas Neon Lights series of acrylic sheet offered in bright day-glow colors, targeted for the display industry.

Acetal and nylon resins for rotational molding use released by Aardvaark Polymers.

France's Rhodia is reported to have declared Force Majeure on nylon and its feedstock hexamethylenediamine (HDMA) because of a labor dispute – could cause nylon resin prices to rise sooner than expected. In a separate action, Rhodia has sold its 417 million annual Euro sales Silicone business to China BlueStar Corp.

Quadrant and its High Performance Plastics Division, reports 2006 annual sales of more than 800 million Swiss francs, a 36% increase due primarily to the first time consolidation with PolyHi Solidur which it acquired last year and has integrated into its Quadrant EPP unit.

PP fiber, with a high modulus is beginning to replace fiberglass as a lightweight reinforcement for thermoset composites – supplied by start-up Innegrity LLC in South Carolina.

ThyssenKrupp reports record quarterly sales and earnings with double digit growth in both categories – its industrial materials segment was contributory including Plastics in Europe.

Home Depot is evaluating its strategic position with its \$12 billion sales Home Depot Supply unit in an attempt to determine if it will grow going forward or that a sale or public offering will ensue – this is a sea change from what was believed to be an endless appetite for acquisitions just a few months ago.

Saudi Kayan, 35% owned by SABIC, is building a PC resin plant as well as a BPA feedstock facility in Saudi Arabia – both plants will have capacities over 200,000 tpa – fueling speculation that there is interest in Saudi Arabia for GE Plastics.

Arkema's 2006 sales rise 3%, with its Industrial Chemicals unit (includes PMMA), up 3.7%.

Graybar Electric records record profit in 2006, led by its \$100 million Enterprise Resource Planning (ERP) computer system, provided by IBM and SAP – more info available from NAW.

Degussa's Cyro Industries unit supplies fabricated Acrylite sheet in a “wave wall” effect used in Children's Hospital, Richmond, VA. Colors of FF, 1/4 inch thick sheet were routed and cut.

MERGERS, ACQUISITIONS, DIVESTITURES, ALLIANCES AND EXPANSIONS:

Speculation regarding the possible divestiture of \$ 6 billion sales GE Plastics (GEP) by parent GE was finally publicly addressed by the announcement that they are seeking bids from as many as six parties, including private equity firms, such as Bain, Blackstone, KKR, Apollo and others, as well as operating plastic and chemical companies. Statements from CEO Jeffrey Immelt left it unclear whether GE would divest the entire unit, sell the pieces separately, or even keep parts such as its flagship Lexan PC business and some higher performance specialty materials such as Ultem and its newest product Extrem. At this early stage some of the potential industry bidders (Goldman Sachs has been retained to seek out buyers) appear to be in two categories:

1. Competitors such as Dow, Bayer, BASF, DuPont and others
2. Benzene (a key component of many GEP resins) producers such as SABIC of Saudi Arabia
3. Chemical commodity producers such as Reliance of India and others with petrochemical interests.

In any case we should know the outcome by mid- 2007...stay tuned.

Dow Chemical itself has been in the news in late February with market speculation that it is a possible target of a private equity buy-out – seems that some key players in our industry are in flux and by 2008 the scenario cut look very different.

Speculation aside, we can report on some actual changes in ownership led by Rochling AG and its Rochling Engineering Plastics Group (REPG), which in addition to its January acquisition of thermoset sheet manufacturer Glastic, announced it has bought UHMW producer Symplastics of Canada and the U.S. REPG now has sales of over \$440 million with Symplastics contributing over \$18 million with 138 employees in Canada.

Jain, India and Gossen of the U.S. form global jv for marketing Jain's foam PVC sheet and Gossen's profiles throughout the world markets for these products.

Mitsubishi Rayon Co., Ltd and SCG Chemicals increase production of acrylic sheet and MMA monomer at their Thai MMA Co., Ltd plant in Thailand- 20,000 tons per year of sheet planned.

Ticona, unit of Celanese Corp. is planning new production in China of its POM and LCP resins, as well as building a new plant there to produce its GUR brand UHMW-PE resin.

BASE doubles capacity for PES resin at its Ludwischafen Germany facility, along with a new plant producing DHDPS feedstock, which it had purchased from outside sources.

Norplex-Micarta opens second office in China and is considering developing manufacturing facilities there in two to three years – thermoset sheet for the growing power generation industry in China are target markets for them.

INDUSTRY INTERVIEWS: ...Concluding our interview with **Dean Davis**, Vice President and General Manager, Alro Plastics, part of Alro Steel Corp., Jackson, Michigan.

Q. I note that you are ISO 9001 certified...what does that do for you?

A. *ISO certification has made us better...it is a tool for continuous improvement...not a marketing tool. We believe that as it benefits us and ultimately our customers, we will be a more valuable supplier to industry.*

Q. How big is Alro Steel Corp. and how does that affect your plastics business? How do you decide where to open new branches?

A. *Alro Steel is a privately held corporation and chooses not to share sales information, but suffice to say that we are a major metals distributor and will hit a record sales figure this year...Alro Plastics has grown every year...through internal growth, not acquisitions. We have opened up branches where the steel business's customer base is located.*

Q. How does the availability of metals delivery trucks affect your success?

A. *Originally we delivered product on our company's fleet of trucks, but now that delivery system is not the answer...how we deliver is based on the economics of the order and the circumstances of our customer.*

Q. What is your product mix as cut to size and machining versus straight material off the shelf?

A. *Machining represents about 25% of the product mix (including acrylic fabrication now), and pure distribution the other 75%. About 85-90% of what we ship is cut-to-size. As I stated, we specialize primarily in engineering plastics.*

Q. I note the use of much of your own literature, especially concentrating on engineering plastics for food processing, as well as machining guidelines...is this important to your marketing efforts?

A. *As I stated, that is our area of concentration and contributes to our success as we cross sell with our metals group – it has worked for us!*

Thank you.

Information contained in this newsletter has been taken from trade and statistical sources that we consider reliable but we cannot assure its accuracy or completeness. Any opinions expressed reflect our judgement as of this date and are subject to change.

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