



GLOBAL PLASTICS LETTER

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“A World of Plastics Information”

DECEMBER 2005

Dear Colleague:

Tentative times - trouble throughout ... we are witnessing the entry into a muddled business cycle as 2006 approaches. On the one hand economic growth is continuing in most sectors but inflationary pressures persist, which hold out a threat to slowing growth as businesses resist paying continued double digit increases for their materials costs.

Attempting to look ahead to a new year, a prediction from us is not an endorsement of the outcome, since we don't have a crystal (or plastic) ball. We are reporters, not soothsayers and by talking to the most knowledgeable sources we can find we hope to share some of these outlooks with you.

We foresee overall economic growth at 3% in 2006 as compared with 3.6% this year; inflation in the U.S. moderates slightly to 3.5% vs 4% this year (of course our industry's inflation goes to lower double digits as opposed to upper double digits this year). Interest rates (prime) will continue to climb, with the prime rate reaching 8% in '06 – a doubling which will affect bank loans and thus capital equipment investment will slow... never a good sign for our industry.

The U.S. dollar should continue its rise against the Euro and the Yen, affecting global trade.

Why the tepid response to higher gasoline prices this fall? First, many consumers usually view price hikes as temporary, as we have seen the last month. Secondly, car manufacturers usually cut prices of large cars during a period of rising gas prices. Income growth during this period on the part of businesses and individuals means the cost of driving is still a small expense as a percent of income. All of this points to the much smaller effect of this gas price cycle on industrial buying, despite inflation, than in the past...an optimistic look certainly.

As you examine your dollar sales growth for the past year and are elated, are distributors also tracking unit sales, so that the effect of inflation on selling prices is adjusted to reflect true growth? Surveys we have taken in the last month indicate not all are accounting for inflation in measuring 2005 results...needs to be done to plan for 2006. A practical approach is to track sheet and film sales by pounds or square footage – don't be too concerned with rod or tube which contribute a minor part of the unit metrics compared to sheet and film.

TRENDS: Can manufacturers and distributors really be “partners”? In a speech delivered by the president of the Specialty Tools and Fasteners Distributor Association (STAFDA) and reported in *Industrial Distribution*, - he contends the answer is NO.

Some significant excerpts: “... since 1977 this has been talked about endlessly” – “... many manufacturers are ‘brand brokers’” – “...prior to the ‘90s, manufacturers wrote the distributor agreements, set the policies, told them what to stock...and for the most part, distributors went along” In the old process “... getting started with a new supplier meant a long courtship with plenty of hoops to jump through, followed by a large stocking order.” – “... in the last decade the swing in power has been to the distributor, caused by excess capacity” “... to wrest back control, the manufacturer offered new programs but little else.” “...the bottom line is that I don’t believe either the distributor or manufacturer want to be partners with each other – but continue the relationship as supplier and customer.” “...rather manufacturers should create ‘strategic customers’ from their distributor base, rather than authorized distributors – with substantial price reductions in exchange for heavy lifting for new products and deep stocking”. “...it is the entrepreneurial spirit which will transcend the relationship troubles.” Some things won’t change!

(Editor’s note: For a complete transcript go to: www.industrialdistribution.com and access the 11/30/05 speech delivered by STAFDA president Marshall Jones.)

Some key strategic moves for 2006, based on current trends are:

- Recognize where you are in the generally accepted seven year growth cycle
- Expect lower growth rates in 2006 as we approach the expected 2009 recession
- Pass on price increases quickly
- Participate in consolidation trends...either as buyer or seller
- Manage risks... have a plan for disasters
- Recruit younger workers ...recognize that senior management is changing

Macro trends to watch for in the next decade (2010 and onward): Satellite communications and travel; Nanotechnology; Synthetic biology and materials creation; and Information ubiquity.

Inventories at the wholesale level rose in the U.S. by 0.6 percent, while sales rose 2.4 % and inventory-to-sales ratio (which measures how quickly stocks would be depleted at the current sales level) fell to its lowest level since May 2004.

There is a report just issued by Industrial Market Information Inc. that forecasts trends in our plastic shapes market, including historical data as well as forecasting trends by geographic regions and by SIC code... believed to be the only available market data for our industry. For more information, email us at: imimarketanalysis@globalplasticsletter.com

PRICING: Hurricane effects prevail as Rita and Wilma join Katrina to whip up prices even more than had been experienced the first half of the year. PE, PP and PVC supplies remain particularly tight with some allocation being experienced. Engineering resins, particularly nylon and acetal all went up in October as did MMA – even thermosets and PU joined the fray.

Of more particular concern for the medium term outlook is the drain on the global capacity base by incessant demand from China and India. Unless an acceleration in new capacity is accomplished in early 2006, it does not auger well for an abatement of price hikes, fueled by supply shortfalls as demand rises in the face of global economic expansion thru the balance of this decade. Somewhat balancing the all-time high resin prices we are seeing, is the fact that both copper and aluminum prices are also setting records, with stainless steel right behind. Of course this usually affords more opportunities for metal replacement applications to abound for our industry. It is to be hoped that these market development activities do not abate during this period so future growth is continuing and assured. The statistical lag between incremental plastic shapes price increases, when plotted against commensurate metal rod, tube and plate price inflation should still afford many new opportunities for our industry on a global basis.

OUTLOOK EUROPE:

Note: We introduce a new feature from one of our reporters – this month's filing is by John Douglas, our Special European Correspondent, embedded in the UK.

The UK, due to its lack of stock shape producers, is one of the few markets in Europe of any size, that shadow the North American example. The market is prime for the invasion of every producer in Europe and as well non EEC countries. The fact that the EEC does not recognize exclusive distribution agreements and anyone can sell or purchase product throughout the EEC, thus the door is wide open. This means if a distributor has a product and you want to sell his customer that product and you can get it from another EEC source then no one can stop you. The UK has only really Lucite Int. (Perspex PMMA sheet); Nylacast for cast Nylon and Westly Eng. again for cast nylon components as a mfg. base for product. The rest of the materials flow in from elsewhere.

The distribution market was dominated for many years by G. H. Bloore Ltd and Plastic Constructions PLC but both were sold ending up with Vink and Amari, then owned by Glynwed. The market was turned on its head by Amari when it started in the mid 70s and they created market growth in real terms by creative selling and service. The market today is changing and due to the lack of or the unwillingness of distributors to show loyalty to their brand, many producers have opted for their own operations. This requires them to walk a tight rope and service the independent distributors and at the same time attack the end user market. This is the case for Simona of Germany who in 1990 established a full service operation in the UK to regain market share after the disposal of Plastic Constructions PLC who represented them for 20 years plus. The Irpen cast MMA people from Spain did the same allowing them to support bulk users, including distributors, as well as go after the end user. Ensinger did the same including having their own machining centre in the UK. The creation of Perspex Dist. Ltd. was done so they could re-gain market share in their indigenous market as the distributors were not giving the loyalty they needed. The distribution market today is made up of a 2 major players- Cox Plastics and Amari Plastics.

There are a few regional distributors who are totally committed to plastics; most of these are also doing fabrication work. These include Bay Plastics (excellent web site) and DEL Ltd. There are those with a metals and plastics profile such as Rightons Ltd and those engaged in Safety products like SBA Ltd. (sounds like the old Cadco). The market is growing slowly at present and PETG market seems the one with the most potential. The market is about 2000 metric tons for the product in sheet and could go to 5000 if they keep prices below PC. The extruded market mainly for the pos and display market has been pegged at about 16,000 tons and Plastics Plus Ltd have been very good at servicing this market nationwide from two locations.(extruded PMMA only at 16,000).

The days when you needed a branch in every town are gone by the way side. The service element can be done from 2-3 strategically sited units and the country covered with your own transport. Does the UK need more distributors? The answer is yes IF they are interested in new markets and willing to invest in new application sales. The share shift market is still taking place with both distributors and manufacturers chasing the same market. The decline in the UK manufacturing base means pressure on eng. materials. However the POS and display market is still strong and that is good for the PMMA, foam PVC and Vinyl suppliers. This is evident in the revamping of Tufnol Ltd. who are still going strong But with machined components as a major priority. (no one likes phenolic machining). The tonnage numbers are Metric tons. The future is good and the opportunities are there for those willing to get into the European market place.

MERGERS, ACQUISITIONS, ALLIANCES, EXPANSIONS AND DIVESTITURES:

Lehigh Valley Plastics, Allentown, PA, is sold to an investment group – Rick Larsen is new CEO, Fred Ressler to remain as consultant. More on this next month. Lucite International appoints Foster Wheeler Energy Ltd. As contractor for its new MMA plant in Singapore. Also in Singapore, Eastman Chemical opened its China Lab – dedicated to R & D as well as application development.

Quinn Group, Northern Ireland, invests 150 million Euros in construction of new MMA plant near Leipzig Germany – to be a 100,000 ton facility.

Degussa of Germany acquires technology and patents for PEEK, formerly owned by Ticona. Ticona then invests 10 million Euros in POM compounding. Degussa in turn forms jv with JIDA High Performance Polymers in China to produce PEEK.

TriStar Plastics acquires Surface Sciences – to offer surface modification of EPM's.

A.Alexandrovitz of Israel merges with IML, largest Israeli distributor for engineering supplies

DISTRIBUTOR/MANUFACTURER BRIEFS: Westlake Plastics is said to close HTP International, its semiconductor materials plant in PA, just purchased in 2001.

Total Plastics, a unit of A.M. Castle Metals, records sales and profit increases for the first 6 months of 2005 versus 2004 – US\$55 million sales compared to US\$43 million...profit at 6%.

Spartech said sales for its fiscal 4Q increased 20% year over year...US\$367 million recorded.

Victrex introduces PEEK adhesive tape as an alternative to PTFE and polyimide – 220C (428F) continuous temperature resistance is claimed.

Perspex Distribution Ltd opens its third stocking center – at Tamworth, UK in Midlands region.

INDUSTRY INTERVIEWS: ... concluding our interview with Jim McCormick, VP Sales and Marketing, Cope Plastics.

Q. What does our industry need most to maintain its relevance in the next 10 years?

A. Taking costs out of the channel is key to both survival and maintaining position for both manufacturers and distributors. Some of this was done in the late 90's but there is still much to do. Our mutual customers are demanding this as they have with other supplier channels.

In addition, competition from Asia is coming on strong...it will rock our world! We must stay competitive and we can succeed if we address the needs of the channel once again.

Q. How do you see the effects of the Quadrant acquisition of PolyHi Solidur affecting you?

A. If they keep the needs of the customer and the marketplace in mind when they are engaged in decision making to affect the transition, they will be OK. They have to use a macro view in both curing redundancies as well as offering the market place the advantage of the combining of the two companies and their products and markets and applications.

Q. On a personal note, what was your first job?

A. Working on the ground crew at Busch Stadium (still standing but being torn down soon).

Q. What do you consider your greatest achievement?

A. My five children – ages 11 through 21!

Thank you.

Our best wishes to all our readers for a safe and happy holiday season. May next year bring good health and greater prosperity... and peace to the globe!

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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