BUOYANT DESPITE ECONOMIC DOWNTURN

While several countries have been striving to overcome the far and wide impact of recession, recovery from its aftermath had not been smooth, especially in Western countries. The only silver lining is the growth being witnessed in Asia, albeit slow. Amid all these, what is noteworthy is that the crisis has underscored the financial resilience of the chemical industry, which has made a strong comeback despite uncertainties.

■ Dr Mosongo Moukwa

In the Western countries, the economic recovery has been slow and fragile. In the US – which accounts for the world's largest debt at $ 14.7 trillion – 98 per cent of the gross domestic product (GDP) hangs over the economy, thus hindering growth. In Europe, the situation is far worse. Greece has been teetering on the edge of default for more than a year. Countries like Italy, Ireland, Portugal and Spain also have dangerously high sovereign debts. The crisis has hobbled the economy of the entire European Union (EU), with no end in sight. In Asia, the GDP growth of China and India is still impressive, although it has slightly slowed.

Despite this gloomy economic picture, the top 50 chemical companies have done well (Table 1). The data based on companies' performance results show that the chemical industry has made a strong recovery from 2009, performing better than it had in more than a decade. The crisis has interestingly underscored the financial resilience of this segment.

Earnings survive unstable recovery

Most companies have posted profits, and indeed 2010 was an outstanding year for chemical companies. Although 2008 was the high-water mark for industry sales, profits for the top 50 chemical companies were only $ 60 billion that year compared to $ 93.6 billion in 2010. The aggregate profit margin for the group was 11.4 per cent in 2010. One would have to go all the way back to 1995, when the industry posted a 13.7 per cent margin, to find a better profitability.

The leading performers have been the petrochemical companies. Observers had long expected that all the new capacity petrochemicals makers that were opening in 2010 would haunt the industry, but that did not happen. Developing countries, especially China, proved to have an insatiable need for chemicals to fuel their industrial expansion.

The petrochemicals producers in the top 10 – Sinopec, Exxon Mobil, Shell, Formosa Plastics, SABIC and Lyondell – each posted revenue gains of at least 30 per cent. All of them enjoyed strong profit gains. Petrochemical businesses across the world are flush with cash as a result of steep increases in their product prices during the recovery from the 2008 financial crisis, and from the reductions they have made in their operating costs to ensure survival during the recession. Investment in new capacity in the petrochemical sector is still cautious, but some regions are more buoyant than others, with the US and Middle East once again considering large projects, but for different reasons.

For the rest of the chemical industry, individual company results are even more amazing. For example, BASF and Dow have posted respectively, 300 per cent and 100 per cent gains in profits over 2009. Despite the volatile changes in sales, the pecking order has changed little from previous years. BASF, Dow and Sinopec have emerged yet again as the top three chemical companies this year.

Demand from customers supported price increases, often in double-digits, but most chemical firms did not report significant sales volume growth during the quarter. Higher prices came out ahead of volume increase. With the price increases, DuPont boosted sales by 19 per cent to $ 10.3 billion compared with last year's second quarter. Its $ 1.3 billion in earnings beat analysts' expectations. Higher pricing also came out ahead of volume increases at Dow. The company saw earnings jump 61 per cent just under $ 1 billion. Dow was able to raise prices because of strong demands in the energy, health, nutrition, and additives markets.

Coatings: A weak spot

Coatings were a weak spot. For example, Cytec Industries saw volumes sink by 9

Ranking of global chemical companies

2010	2009	Company	Chemical sales ($ millions) 2010	Change from 2009 (in %)	Chemical sales as % of total sales	Chemical operating profits ($ millions)	Change from 2009 (in %)	Profits as % of total operating profit	Operating profit margin (in %)	Return on chemical assets (in %)
1	1	BASF	70,391	34.90	83.10	7,197	291.00	69.95	10.20	10.80
2	2	Dow Chemical	53,674	19.60	100	3,625	108.2	100	6.8	5.2
3	3	Sinopec	47,444	50.2	12.1	2,221	8.9	14.3	4.7	12
4	5	Exxon Mobil	35,521	32.3	9.6	4,913	112.8	16.1	13.8	18.7
5	8	Royal Dutch/Shell	35,277	43.5	9.6	na	na	na	na	na
6	7	Formosa Plastics	34,663	30	64.9	3,810	118.1	76.2	11	17.1
7	9	SABIC	33,712	46	83.2	11,490	85.8	88.8	34.1	16.4
8	6	DuPont	31,312	20.6	99.4	4,578	85	94.2	14.6	23.6
9	11	Lyondell Basell Industries	27,682	38.5	67.3	2,666	325.2	97.1	9.6	na
10	14	Mitsubishi Chemical	26,021	45.6	72.1	1,646	nm	63.8	6.3	6.8

Note : Some figures converted at 2010 average exchange rates of $ 1=1.7601 Brazilian Reals, 6.7696 Chinese Renminbi, 0.7541 Euros, 45.65 Indian Rupees, 87.78 Japanese Yen, 1155.74 Korean Won, 6.0451 Norwegian Krone, 3.75 Saudi Riyals, 1.0432 Swiss Francs, 31.498 Taiwanese Dollars. *Source : www.cen-online.org*

per cent compared to the same quarter in the previous year. The company made up the difference with the higher prices, and favourable exchange rates brought on by the weak dollar. And its engineered materials and process operation business saw an increase in sales volumes. But overall, Cytec's quarter earnings of $ 46 million were down 15 per cent compared to the earlier year in the same quarter.

Eastman Chemical also beat the volume blahs by selling 15 per cent more in its largest segments, performance chemicals and intermediates, than in the second quarter of 2010. It also raised prices by 19 per cent. They have reported that its plasticiser and acetyl chemical product lines were in high demand. Higher prices were a response to higher raw materials and energy costs, strengthened demand in the US, and tight industrial supply. Overall, Eastman's sales soared 26 per cent compared with the year-ago quarter, while its earnings rose 40 per cent to $ 200 million.

Mergers and acquisitions

The wobbly economic recovery did not stop deal-making. According to KPMG, in 2010 the number of M&A deals in the global chemical industry totalled 1,261 as against 1,211 in 2007 (returning to levels last seen before the financial crisis in 2008), but the total value of the mergers and acquisitions, at $ 76 billion, was half that of three years ago. It is expected that the number and total value of deals will continue to increase at least through to the end of 2012.

The revival in M&As activity in the global chemical industry has not been strongly felt in petrochemicals. There is much more interest in downstream areas. Even in emerging markets bulk chemical companies are looking to move down the value chain – though not necessarily as far as going into specialties but shifting in that direction. The only dramatic acquisition related change to the ranking is Brazil-based Braskem's rise from 37 to 22, thanks to its purchase of Sunoco's propylene business and of its Brazilian rival Quattor.

Over the past two to three years, takeovers in the specialties segment have been increasing at a faster rate than those in bulk chemicals as companies seek the financial benefits of products with added value. Increasingly, the specialties market is becoming dominated by larger portfolio players with multi-chemical capability, bringing management sophistication, scale and global reach.

It remains to be seen whether the new chemical company combinations will be stronger in the face of slow growth or even a possible double-dip recession. Rising energy prices; the supply chain shock emanating from Japan; European debt crisis; US debt issues; uncertainty and other factors are working against the recovery.

Growth in Asia

While the advanced economies of the world have stagnated since 2008, countries like China, India, Brazil and parts of Southeast Asia have enjoyed growth rates in the 7-9 per cent range. Although several have slowed this year, they are still faring better than the economies of the US and Europe. Regardless of the end-market or state of the economy, chemical firms will be primarily looking overseas for growth in the near future.

Ultimately, creating value is all about driving sustainable growth, which can be attributed to a strong portfolio and innovation management. The portfolio side incorporates both the business and geographic aspects of portfolio management. Companies such as US-based coatings firm PPG Industries are managing the geographic aspects of their portfolios, and illustrate the value that can be garnered from optimising along this dimension in the context of what may be considered a low-growth portfolio. ■

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