

CHEMICALS TARIFF ALERT

CURRENT TRENDS

- Although some chemical products have seen increases in demand due to the pandemic, the American Chemistry Council expects total chemical production to decrease by 9.3% in 2020.
- Total U.S. chemicals trade is projected to decrease by 16.4% in 2020. A full recovery to pre-COVID-19 levels is not expected until late 2022 or early 2023.
- The domestic chemicals industry responded to the COVID-19 pandemic by pivoting its production capacity toward the products and materials needed to combat the outbreak, such as isopropyl alcohol for hand sanitizers, polypropylene used to make fibers for masks, and polyethylene used in packaging.

PROJECTED VALUES (12-MONTH OUTLOOK)



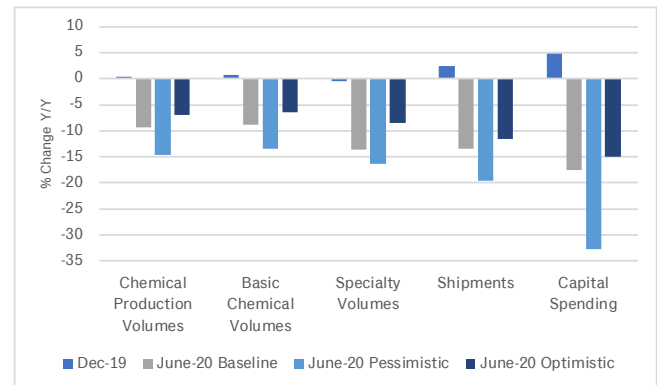
APPROXIMATE NET RECOVERY ON COST

45-60%
distributors

45-60%
oils/lubricants

35-50%
raw materials

U.S. CHEMICALS 2020 OUTLOOK AS COMPARED TO 2019



Source: American Chemistry Council

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IMPACT OF COVID-19 ON THE CHEMICALS INDUSTRY: The chemical industry is one of the United States' largest manufacturing industries, serving a significant domestic and global market. The COVID-19 pandemic has launched the U.S. and world economies into the worst recession in decades; however, the U.S. chemical industry was considered essential and allowed to operate as normal during the pandemic shutdown period, while following Centers for Disease Control and Prevention workforce and customer protection guidance. Precursor raw materials chemical transport by truck was also permitted. Nevertheless, with petrochemical feedstock pricing declining due to oil prices, many related chemical prices such as ethylene, naphtha, benzene, and propane dropped significantly in early 2020, although they have since recovered. Pricing for other products has also been impacted by the pandemic, some negatively due to reduced industrial activity and others positively, such as isopropanol and cleaning-related solvents.

DECLINE FORECASTED FOR 2020: Despite classification as an essential industry during the shutdown, the U.S. chemical industry is expected to see a decline in revenue in 2020 before recuperating in 2021. In its midyear report issued in June, the American Chemistry Council's (ACC) baseline projection was for a 9.3-percent decline in U.S. chemical production volume for 2020. Its downside forecast, in which COVID-19 cases spike again in the second half of the year, reflects a 14.7-percent production decline, and its optimistic scenario, where the economy benefits from a V-shaped recovery, is for a 7.0-percent decline. The ACC predicts the U.S. chemical industry will scale down by about 20,000 jobs in 2020, representing a decline of 3.6 percent from 2019 levels. The ACC also expects capital spending for 2020 to decline about 17.6 percent, to \$29 billion as companies pull back on general equipment and other spending. It is important to note however, that the projected downturn in spending is expected to be largely reversed by a 15.7-percent increase in capital spending in 2021 followed by decelerating annual growth through 2025.

Although there was an initial demand drop worldwide due to shutdowns in March and April, by August 2020, demand for most types of chemicals had improved due to the economic and industrial recovery, especially in the construction and automotive sectors. The Institute for Supply Management reported that business is good and that production cannot keep up with demand in its latest Purchasing Manager's Survey released on September 1, 2020; however, the survey noted that some upstream supply chains are starting to have issues with the availability of raw material

and transportation. Demand for certain chemicals remains tight due to high demand, such as isopropyl alcohol, or due to supply limitations in the aftermath of Atlantic hurricanes Laura in late August and Sally in early September as well as the disruption earlier in the year due to COVID-19 related issues.

U.S. CHEMICALS TRADE UNSTABLE: U.S. chemical exports are projected to fall sharply in 2020, as import demand in partner economies has deflated and will remain unstable. U.S. chemical exports are expected to fall 14.5 percent in 2020, with shipments down to all destinations, and then recover by 10.9 percent in 2021 according to information from the ACC Midyear Situation Outlook. Per the ACC Outlook, full recovery to pre-COVID-19 levels is not expected until 2022. Trade in chemicals used as inputs into manufacturing supply chains where activity had stalled, for example the auto manufacturing supply chain, will be down sharply. U.S. chemical imports will fall 19.1 percent in 2020 due to the weakness in U.S. industrial activity and reduced consumer and business spending. Imports will recover in 2021, growing 11.9 percent; however, full recovery to pre-pandemic levels is not expected until late 2022 or early 2023. Total U.S. chemicals trade will fall 16.4 percent in 2020 to \$199 billion. The U.S. chemical industry is expected to maintain its net exporter position, supporting total U.S. goods exports. Net exports of chemicals are projected to reach \$37 billion by 2025.

Steep tariffs on chemicals and downstream products remain in place even after phase I of the U.S.-China trade deal was signed in January 2020 and reaffirmed by country leadership in late August. Further deterioration in relations and increased trade policy uncertainty with regards to trade with China as well other trade partners could cause the recovery of the industry and/or the economy to regress.

VALUATION OUTLOOK: While it is clear that prices and demand for all types of chemicals are going to be volatile and subject to swings as the marketplace rebalances due to the combined impact of the COVID-19 pandemic as well as petroleum price volatility, Gordon Brothers believes that appraisal values for inventory on a market-to-market basis should be relatively stable once the immediate marketplace impacts are resolved.

The Expert: Alex Sutton



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