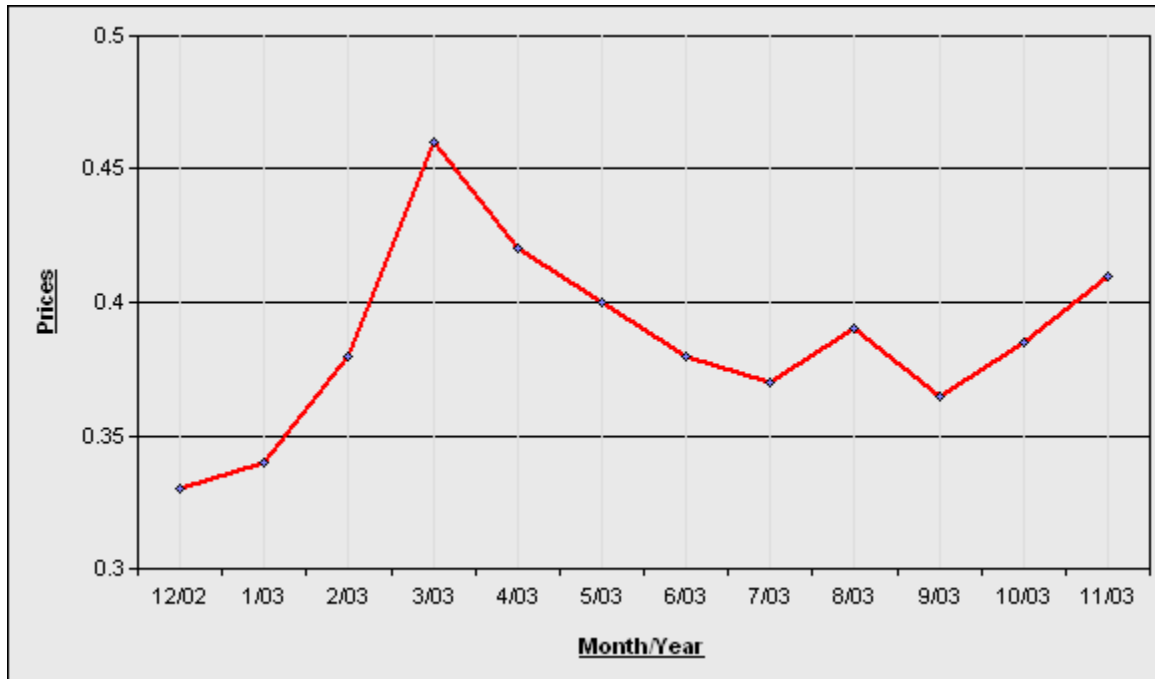


Pressure on Polyethylene Prices Increases

(source www.theplasticsexchange.com)



Polyethylene The \$.05/lb Polyethylene price increase that bounced around since June was finally implemented in October and some producers have backed this up with a newly announced \$.04/lb increase for December. Producers have been trying to regain losses from the beginning of the year that were mostly caused by higher energy and feedstock costs.

Even though natural gas prices eased during the summer, albeit only to prices still more than 2x prices of the 1990s, the price volatility has been a major influence to the plastics market. As natural gas prices rally, implementation of this ever-present price increases seems imminent, but each month during the critical period when the increase is tested, natural gas prices have fallen, leading to a failed resin price increase that is pushed back another month for yet another attempt.

So what happened in October? The battle for the price increase was on. Producers had successfully used the spot market to clear much of their surplus resin, so most were in a good position to restrict generic prime offers and only sell their branded prime the full 5-cents higher. Natural gas was down around \$4.60 mBtu, but over the next two weeks prices rallied sharply to \$5.80. People were fearfully discussing another winter price spike in gas and resin prices, it was at the right time and with that support, the price increase just made sense and so it stuck.

It then became known that the natural gas price run-up was really fueled by speculative short covering and buying to store for winter usage. Published reports indicated that enough natural gas was indeed stored to provide comfort that we might be okay after all, so an equally

extreme sell-off during the second half of the month sent natural gas prices tumbling back down to under \$4.50 mBtu.

Natural gas was strong enough long enough to support the polyethylene price increase and before the plastics market had time to realize that the cost-push pressures were relieved, producers nominated this 2nd price increase of \$.04/lb. This gave buyers something else to worry about rather than re-debating the 1st price increase. It was a great strategy: when the outcome is unknown stand up and declare victory-- and so the producers did, well played.

Producers now have their hard-fought price increase without specific cost-increases. This is very good and important for them considering the losses that most continue to record each quarter. Economic health at the producer level is ultimately good for the entire industry, as it encourages producer reinvestment in facilities, new product development and helps to avoid further consolidation.

In addition to reinforcing the first price increase, the announcement of the December \$.04/lb price increase gets the price protection clock ticking in case a significant natural gas price spike actually does occur. Better would be the time however, if we had a mild winter and found that the natural gas in storage was more than sufficient to satisfy winter demand. This would help cause energy and feedstock prices to fall and then producers would not need to implement this and potentially other price increases that could otherwise follow and we might find resin price equilibrium at a lower level. The industry could use a breather; it's been a tough year.

Our spot market has been very active with aggressive railcar offers of generic prime HDPE blow molding and injection grades finding satisfactory demand in the mid-high 30s; Low and Liner Low Density film grades have been scarcer. Butene prices could still start with a 3, Hexene is around .40-.42 as is Liner grade, and Clarity in the low-mid 40s. Throughout the month, large buyers have sought pre-price increase resin. To maintain or grab market share, some producers have sold it as spot or by rationalizing it as a competitive situation. The spot market quieted the last couple days of the month, prices might start out a little higher in Nov.

So what happens from here? Expect firm branded prime prices and some good generic spot opportunities. With volatile winter energy prices ahead, this newly implemented price increase for branded prime contracts should stick around for a while. However, production economics are positive, thus encouraging some producers to increase operating rates and sell commodity grade polyethylene into the market as generic prime. This might restrict advances in the contract market.

As we move towards the end of the year, how much inventory liquidation might we see? Maybe a lot...perhaps not. If producers believe that we could have an energy squeeze this winter, they might actually choose to build rather than reduce inventories. As always, producers will consider inventory liquidation for tax benefit, as well as increasing pounds sold for performance purposes. They will balance that against the sales discipline needed to maintain the price increase while they ultimately consider how good demand really is. I guess we will wait and see.