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Gulf sees a chemical future

By Robin Wigglesworth in Abu Dhabi
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In the US film The Graduate, a family friend offers the protagonist, played by Dustin Hoffman, some simple career advice: "I want to say one word to you. Just one word. Plastics."

It is counsel the Gulf states have heeded. Seeking to capitalise on their comparative advantage - abundant and cheap access to hydrocarbons, the building blocks for many petrochemicals - governments have invested heavily in domestic industries.

The credit crunch, however, has thumped the chemical industry in recent months. A collapse in global manufacturing has sent the price of plastics, synthetic rubber and other petrochemical products tumbling - and with them, the profits of the industry.

The two largest chemicals producers in the Gulf, Saudi Basic Industries Corporation (Sabic) and Industries Qatar, saw their fourth-quarter profits plummet 95 per cent and 93 per cent respectively. With stocks of petrochemical products building up in warehouses across the world, analysts forecast prices will remain stagnant for some time.

Khadem Al Qubaisi, managing director of International Petroleum Investment Company, Abu Dhabi's state-owned hydrocarbon and chemical investment arm, admits "2009 will be a tough year; a year for restructuring".

The picture may appear gloomy, but analysts and industry experts say that, aside from near-term pressures on margins, the crisis may be the making of the Gulf's chemicals industry.

"The situation doesn't look great right now, but the future still looks good for the Middle East petrochemical companies," says Ankit Gupta, a senior analyst at Securities and Investment Company, a Bahraini investment bank.

Chiefly this is because of easy and cut-price access to gas and oil. The average price of 1m British thermal units of energy is $7-$8 in the US but just 75 cents in Saudi Arabia, according to a KPMG report published in December.

Seeking to capitalise on this advantage, governments have thrown cash at their petrochemical industries in recent years, expanding total output to €46bn ($59.6bn) and an annual growth rate of more than 9 per cent since 1997, the consultancy says.

Seemingly undeterred by the credit crunch, several Gulf countries are pressing ahead with expansion plans, with only limited delays where financing is still to be organised, says Mr Gupta.

In the Middle East, $79bn of investments in petrochemicals is planned in the 2007-11 period, according to KPMG. Abu Dhabi is building a $20bn chemicals city called Chemaweyaat, and Saudi Arabia plans a $26bn refinery and petrochemicals complex at Ras Tanura. Both states, along with Qatar, have identified the industry as an integral component in diversifying their economies and creating jobs.

Ipic, which is involved in the Chemaweyaat development, is "not stopping any projects, as they are the backbone of our economy", says Mr Qubaisi. "Chemicals represents the future for us. It will create a lot of jobs for Abu Dhabi and put us on the petrochemical map."

A further 53 new plants are due to come online in the Middle East by 2012, and the regional industry will grow nearly 10 per cent a year until 2020, more than twice the global average, according to KPMG.

The Gulf focuses mostly on basic petrochemicals such as ethylene, poly-olefins, polyethylene and polypropylene, but will soon be able to produce a wider array of chemical products. It is already a leading manufacturer of fertilisers.

But analysts say acquisitions may be a swifter and now cheaper way of moving up the supply chain. The credit crunch has made even the world's largest chemicals producers available to the larger Gulf companies.

Sabic bought GE Plastics for $11.6bn in 2007, giving it a downstream plastics producing capability, but has since had to cut 10 per cent of its acquisition's workforce because of the credit crunch. However, the Saudi company is undeterred and remains on the hunt.

"The company is working to increase its market share in international markets and looking for opportunities to buy assets within these markets and to set up joint ventures," Sabic said in its annual report. "It will take advantage of the big decline in international production among high-cost producers."

Mr Gupta says Sabic has more than $13bn of cash available and is likely to look primarily for Asian chemicals companies situated close to the important markets of India and China.

Ipic, which controls Borealis, a plastics company, recently bought Canada's Nova Chemicals for $2bn and said it was looking for more acquisitions.

Middle East groups may also enter into joint ventures with leading international chemical companies.

A planned $15bn joint project between Dow Chemicals and Kuwait's Petrochemical Industries Company collapsed last year due to political wrangling in Kuwait, but Dow has said it is looking elsewhere in the region for partners.

"We will see more joint ventures; the failure of the PIC-Dow Chemicals project will be an exception rather than the rule," says Mr Gupta. "US and European petrochemical firms will have to consolidate production in the face of the advantages of the Middle East and Chinese producers."