KPMG Insights from the World Petrochemical Conference

Houston

Chemicals, materials and ag: Transition and transformation in a multi-speed world

This year's World Petrochemical Conference in Houston highlighted an industry that is still in flux. Although the mood among CEOs was more positive than last year, when commentators rightly predicted a rough year ahead, the outlook for the short-term is not positive. That said, there is room for optimism in the three themes that stood out: a multi-speed world, the influence of government policy, and continued transition. Additionally, North America looks to be in better shape on most fronts than other regions.

1. Hitting the multi-speed dial

The petrochemicals, chemicals, materials and agricultural inputs sectors are global in nature and in reality. Global suppliers have always needed to respond to different dynamics across the world – at the same time. But now different structural economic issues in different regions have resulted in a multi-speed world: while some areas advance, others stagnate.

In North America, despite some evidence of recovery, the industry remained in recession through the full 2023 calendar year "Chemicals snapshot: Recession, reaction – rebound", KPMG LLP, 2023. Overall economic growth, however, particularly in the U.S., remains strong, with productivity growing even with the new uncertainty around the Federal Reserve easing interest rates this year. And the sector is continuing to benefit from relatively cheap raw material feedstock and energy. We believe the U.S. is still the premier location to invest in the industry.

On the other side of the pond, the consensus from European CEO delegates was negative. Little or no economic growth and a challenging policy environment (see more below) has led to fears for the future of the sector. We've already seen multiple plant closures over the last 12 months from both European and non-European players in the region. In more than one forum, executives foresaw a future scenario characterized by a hollowed-out industrial base, including a shrunken chemicals, materials and ag inputs sector. Likely to be protected by more trade barriers, it is increasingly being isolated from the global industry. The challenge is to find areas that are still competitive, particularly in advanced and environmentally friendly materials. But the sector needs regulatory support.

In China, the chemicals, materials and ag inputs sector is currently over supplied across many value chains, largely coming from within the country. The economy continues to face structural issues manifested by a real estate crisis and the challenge of converting the wider economy from being investment and export-led to consumer-led. (Consumer spending represents only 53% of GDP, compared with 72% for the world.[1])

There are bright spots, though, for example the rapid rise of Chinese champions in downstream industries which drive demand for chemicals and materials. The leading electric vehicle and personal care brands in the country are Chinese-owned, not western. Also, due to its size as the world's largest chemicals, materials and ag inputs market, China will remain colossal. For non-Chinese suppliers, however, the strategy is likely to be two-pronged: 'in China for China' and diversification and re-shoring of supply chains for other markets, e.g., in other parts of the Far East.

2. Policy power play

The economic dislocation in our industry is being made worse by regional differences in policy, particularly between the U.S. and Europe. In America, while the ability to get permits is still a challenge for investment, the Inflation Reduction Act (IRA) has been welcomed by the industry as being positive and supportive. This will likely continue to encourage capital investment into the industry, though one concern voiced by delegates was that the legislation was being over-subscribed with potential delays in accessing funding.

The opposite is true of Europe with senior executives expressing frustration with the legislative environment and fear that the European Union has already lost global competitiveness. CEOs are particularly exasperated about the prescriptive and subsidy-based nature of policy with a narrow focus on the allowable solution set around decarbonization. Executives felt they should be allowed to do what they are best at: innovating to find solutions to climate-related problems. They also want market forces to dictate which solutions are best applied to industry.

Several delegates from around the world called for increased regulatory support with respect to the development of a global carbon market. The IRA has made efforts here through Section 45Q: providing tax credits for qualified carbon dioxide which is captured, securely stored underground or reused. But it was felt that more work was needed to develop a globally applied, equitable model.

[1] Source: The Economist, Hong Kong, "Can China's consumers save its economy?" (February 6, 2024)

3. Transitioning

Materials transitioning was another important conference theme, though there is nothing new in this. The chemicals, materials and ag inputs sector has been innovating to shift to new materials throughout their company lives, especially over the last 20 years with regards to sustainability.

CEOs also see transition in the coming years in two areas: recycling and artificial intelligence. Investment in both mechanical and chemical recycling continues apace. While plastic waste collection remains a challenge, chemicals and materials firms are increasingly interested in waste management acquisitions or partnerships to build the recycling ecosystems.

As general artificial intelligence (GenAI) is becoming pervasive, the chemicals, materials and ag inputs sector has been taking a considered approach with initial use cases around finance, supply chain, procurement, and IT. The recent economic climate has not been supportive as companies focus on costs and cash.

Our advice to companies in the sector is three-fold: (i) explore GenAI potential as the opportunities for efficiencies are vast; (ii) be clear on what you are trying to solve and define the uses accordingly; and (iii) focus on security: for every $1 spent on AI, you should spend $1 on cyber security.

Overall, we believe chemicals, materials and agricultural inputs companies will adapt to the unprecedented changes we are experiencing through performance improvement, innovation and investment in new technologies. North America will likely be at the fore front where economic conditions should improve later in the year and where the IRA and regulatory environment will provide additional stimulus.

How KPMG can help

KPMG serves clients across the global chemicals, materials and ag inputs industries, helping with strategy implementation, M&A planning and execution, performance improvement and application of GenAI.

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