

Opportunities, Challenges: The Healthy State of the Plastics Industry

By Mark Bennett

The plastics industry faces a number of challenges and advantages in 2018 that spell opportunity for investors and others offering equipment financing.

Uncertainty over tariffs and the future of the the status of the United States-Mexico-Canada Agreement (USMCA), as well as swings in resin pricing and a shortage of skilled labor, present challenges for the industry. At the same time, the industry is enjoying strong efficiency and capacity numbers, increasing demand, advancements in the packaging segment and the many benefits of automation.

Amid these trends, replacement costs for new equipment have declined and unit productivity has increased. Coupled with favorable depreciation treatment in recent changes to the US tax law, plastics manufacturers are in an advantageous position to consider upgrading machinery. A clearer understanding of the industry's current and future needs reveals opportunities for financiers to help the industry thrive.



STATE OF THE INDUSTRY

The overall state of the plastics industry is positive, if not increasingly competitive. [The Plastics Industry Association reports](#) the industry's capacity utilization was 80.1 percent in July 2017, significantly higher than the 76.7 percent total capacity utilization for US industrial production. Efficiencies in newer equipment and automation have sustained equivalent production levels, allowing current machinery to produce the same volume at 75 percent utilization as that requiring 80 percent use just a few years ago.

Machinery sales have recovered from the 2008 financial crisis. In 2016, injection molding machinery shipments reached 4,100 units, [according to analysis from the investment firm Gordon Brothers](#). This was driven by automotive industry demand for used late model machinery, as well as demand for smaller tonnage equipment in the bottling and medical industries.

Meanwhile, the plastics industry is enjoying increased activity from businesses relying on plastic materials and components. The plastic packaging market more broadly is forecast to grow at a CAGR of 5 percent through the same timeframe exceeding \$400 billion, [according to analysis firm Market Research Future](#). And while [St. Louis Federal Reserve data shows](#) domestic

auto production enduring a downward trend, healthy economic and employment conditions should mitigate the impact. Indeed, the [Center for Automotive Research expects](#) relatively steady light vehicle sales through 2022.

Overall, the plastics industry is operating in a largely healthy, favorable environment; however, challenges remain.

INDUSTRY CHALLENGES

Uncertainty stemming from international discussions on trade agreements and tariffs weighs on the plastics industry. Details of USMCA, the new trade agreement, remain to be seen, and leaders of Canada, Mexico and the United States continue to wrestle with internal politics and regional economics. Meanwhile, Mexico and Canada remain the largest and second largest export markets for US plastics, respectively. According to [a report from the Plastics Industry Association](#), in 2016, the industry enjoyed a \$719 million trade surplus with Canada and a \$10.7 billion surplus with Mexico, its largest. The surplus in Mexico is due largely to technology-intensive components and machinery that are harder for Mexican producers to source.

It's unclear what impact the USMCA would have on plastic production costs, and any loss of Mexican production would force domestic manufacturers to automate quickly

to compensate for labor cost increases. As negotiations on a new trade agreement continue, the plastics industry is challenged to plan for an unknown future.

The same uncertainty reigns in the area of placing and enforcing tariffs. US trade policy is in flux, with the ominous signs of trade wars emerging between long-time trading partners. Increased tariffs may impact equipment costs for the plastics industry. Chinese-produced machinery, for example, has improved in quality dramatically over the last five years, delivering a substantially lower cost with equivalent quality to machinery produced domestically. Changes in tariffs could diminish these cost savings. One potentially positive impact from tariffs is that the increased cost of imports may create pricing parity for domestically sourced machinery and bolster prices for used equipment.

The industry also faces the persistent challenge of managing material and labor costs. In addition, there is a growing public demand for more sustainable production processes. The consequences could include shortages of recyclable materials, as well as legal issues for legislative and regulatory noncompliance. What is more, persistent shortages in skilled labor continue to impact wages, production, and cost—and are pushing the plastics industry to turn to automated equipment.

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WHAT COMPANIES WANT

Borrowers in the industry seek to finance equipment in a way that aligns with the current economic trends, challenges and opportunities. Companies in the plastics industry want to:

- Obtain interim financing when anticipating a long delivery time between the build out of the line and the point at which equipment can generate revenue. Some companies may even request an additional two to three months of interest only while “proving-out” the line.
- Match expenses with revenue, generally preferring a fixed rate. Borrowers do not want variances in payment, especially as interest rates begin to rise.
- Finance equipment costs, since companies often must cover the cost of molds. Companies most often seek 100 percent financing.
- Borrow to own the equipment, which drives a preference for loans or a capital lease structure. Companies typically request five to seven year terms. Conversely, few companies are putting forward tax lease requests, unless they are prioritizing the lowest possible payment.

Ultimately, while the plastics industry faces headwinds, the overall outlook is decidedly positive. As companies navigate the uncertain future of international trade and material and labor costs, financing will continue to be a critical element in equipment acquisition and the industry’s long-term growth and profitability.

ABOUT THE AUTHOR

Mark Bennett is a Territory Manager with J.P. Morgan Equipment Finance. Mark has been with the company for 15 years in various roles, and currently covers nine markets in the South Region. He has experience in a variety of lease structures for both commercial and municipal leases, tax and non-tax related transactions, pricing issues and documentation.

MAJOR PLASTIC FORMING PROCESSES

Type	Advantages and Applications	Industries Served
Injection Molding 	The most common form of processing plastic components, it is known for cost-effectiveness, efficiency, reliability and versatility; components are also often stronger than other plastic products.	Automotive, Appliance, Technology, Recreation and Toys
Extrusion 	Providing fast, high-volume production, it is best suited for products formed through a continuous process and with a uniform shape (e.g., tubes/channels/piping used in construction).	Architectural and Plumbing, Packaging, Plastic Films
Blow Molding 	With great potential for automated manufacturing, this is ideal for high-volume production of small hollow objects (e.g., bottles). End users of blown products often have a related forming operation within their facilities.	Packaging, Bottle and Container Manufacturing
Rotational Molding 	While a slower process relative to others, this yields less waste, making it economical and environmentally friendly. The process is suited for discrete hollow products (e.g., large tanks).	Automotive, Recreation and Toys, Furniture, Architectural
Thermoforming 	Also called compression molding, this process can use many raw materials (e.g., fiberglass) and can create products as diverse as shower stalls, blister packaging and body armor.	Automotive, Packaging, Architectural
3-D Printing 	Known also as additive manufacturing, this is a cost-effective way to produce custom products, using digital inputs to “print” solid outputs with specialized resins and curing processes.	Aerospace, Automotive, Medicine; also: building protocols in Research and Design industries.