Allegro
Commodity Management

How to Prepare for Volatility in the Chemicals Sector

With considerable uncertainty all around the globe, chemical manufacturers must be prepared for swings in their feedstock costs. A CTRM system could be the way forward.

TABLE OF CONTENTS

Political and economic uncertainty the world over has led to extraordinary change for a number of industries across the Americas, Europe, the Middle East and the Asia-Pacific. Often, the inability to forecast with anything beyond moderate confidence, at best, has created considerable volatility in the global markets.

One such industry that's faced a multitude of challenges and questions in recent years is chemical manufacturing, and, unfortunately, the worries don't appear to be on the verge of diminishing. In fact, chemical manufacturers likely will be forced to cope with a series of potentially destabilizing shifts. In particular, five areas require close watching, any or all of which could have noticeable effects on the supplies and costs of feedstocks and on the demand, prices and distribution of finished products.

But the mere observation of world events as they unfold won't be nearly enough to keep chemical businesses flourishing. What's truly important is that these companies have the plans and systems in place to minimize and avoid the negative impacts of these events.

> We needed a centralized ETRM system to manage our energy trading business, and we selected the Allegro platform because we found it innovative, sophisticated and adaptable to our trading and risk management needs. We strongly believe that Allegro's technology will help us achieve better portfolio, trade life cycle and risk management, which are ultimately our business goals.
>
> - Said Al Maawali, VP Petrochemicals and Business Development, Oman Trading International

Brexit

The U.K.'s impending exit from the European Union could weigh on the economic health of the entire EU. Britain's departure is likely to pressure the EU for some time to come as financial markets adjust to the new reality. For chemical manufacturers, the effect of the U.K.'s decision probably will be mixed, at best. It conceivably could push the entire block into recession, thereby dampening demand for manufactured chemicals, which will also lessen demand for feedstock. If other nations were to one day follow, the pressure would increase even more.

OPEC Production Cuts

Production curtailments from OPEC drove the price of crude oil back into the $50 Bbl price range for the first few months of 2017, which, in turn, increased the cost of feedstock for chemical plants. However, for countries such as Saudi Arabia, which source their chemical-plant feedstock locally, high crude prices give them a competitive advantage compared with companies that have to buy feedstock on the world market. If the price of oil continues to climb, and remains above $50 Bbl, chemical manufacturers will need to start watching their feedstock costs more closely and thinking more about hedging and other strategies to maintain competitive feedstock costs and volumes.

U.S. Elections

The November 2016 elections in the U.S. put Republicans in solid control of the White House, Senate and House of Representatives. Beyond that, state legislatures are overwhelmingly Republican, as well. As a result, the U.S. is expected to enter a period of deregulation and lower business taxes. President Donald Trump's position on projects such as the Keystone XL and Dakota Access pipelines have shown that there are likely to be concrete actions coming, which could make U.S. chemical manufacturers more competitive and lower the costs of U.S.-sourced feedstocks, as well as lift U.S. demand for chemicals.

However, trade-related actions, such as renegotiating NAFTA and exiting the TPP, may dampen demand abroad for U.S. chemicals and, if punitive tariffs are enacted, make U.S. products uncompetitive for several countries. As such, chemical companies need to understand and manage their feedstock supplies and product demands to ensure they're in balance.

Slowing Chinese Demand

China is the world's largest consumer of chemicals. As its economic growth rate has slowed in recent years, chemical selling prices have fallen even faster than feedstock costs, compressing the margins of chemical manufacturers around the world. President Trump's push to bring manufacturing back to the U.S., coupled with Brexit, means that demand for Chinese manufactured products probably won't grow significantly in the near term.

In turn, China's demand for chemicals won't expand greatly, either. And until China builds up much stronger internal consumer demand, the world's chemical manufacturers can't rely on the Chinese market to purchase their products in ever-higher quantities. Therefore, companies need to be prepared to manage their chemical manufacturing inputs and outputs in a lower-demand environment.

Cyber Attacks and Terrorism

This is the most troubling challenge on the list – intentional acts that are meant to disrupt normal life and business operations. Clearly, any events that are impossible to foresee, such as terrorist attacks or cybercrime, could be extremely damaging to chemical distributors. If anything happened to cause significant shortages of feedstocks or finished chemical products, prices could surge until operations return to normal.

With security expenses increasing the cost of doing business, it makes optimizing logistics costs even more critical. Additionally, having a system that can ensure you have adequate feedstocks on hand to cope with any act that stops supply can mean the difference between staying in production and shutting down the operation. Furthermore, if an outage, were to be more than a few days long, it would require a comprehensive and sophisticated system to secure alternative means of supply and distribution.

> Before Allegro, we operated primarily on spreadsheets. Using Allegro has really helped us to highlight and pinpoint certain areas where we can do better, for example, credit exposure. If I could describe Allegro, I would say it's scalable and innovative. It moves with our business.
>
> \- Corey Terrance, Manager
> IS Applications, at EOG Resources

Managing Volatility With Allegro

Without question, other events beyond the five described here are capable of disrupting the chemical industry. The primary point is that, in this climate of high volatility, prices for feedstocks and manufactured chemicals can swing dramatically, which may put profitability, and perhaps even the ability to remain in business, at risk for chemical makers and distributors. Without a plan for managing volatility, even a single event can impact not just one quarter, but perhaps many years of financial results.

To best deal with increasing volatility, one needs a dedicated and robust commodity trading and risk management system. It's no longer sufficient to rely on systems that are designed for plant operations and accounting, or, as often is the case, to base your business around spreadsheets. Today's chemical businesses have to track and manage feedstocks and products, including buying, selling and hedging, along with logistics and distribution. With an integrated platform, one can minimize feedstock expenses by matching feedstocks to demand, maximize the selling price of produced chemicals, and hedge both the feedstock and the production to lock in profitability.

Allegro is the system of choice for chemical manufacturers facing greater volatility. Allegro has a powerful trading platform that's capable of handling multiple commodities, traded in multiple currencies around the world. As a risk management platform, it helps maintain operations and shows the impacts of feedstock procurement and distribution on the business. Furthermore, it has built-in functionality to manage hedging, and it oversees logistics to ensure that feedstocks are delivered and that chemicals are distributed in the most efficient manner possible.

Allegro's logistics functionality is also multi-MOT (mode of transportation) and can handle any combination of truck, rail, barge, vessel and pipeline movements to get feedstock to chemical plants and chemical products to end customers. Plus, Allegro has the ability to interface with accounting packages like SAP, but it can manage settlement and a significant amount of accounting on its own.

Finally, Allegro is built using .NET technology on top of an SQL or Oracle database, with an inherently open architecture designed to be extended by customers, if necessary. This means Allegro can grow as your business grows and that new functionality can be added without waiting for the next software release. All of these features make Allegro the system most capable of handling the complex, ever-changing and increasingly volatile world that chemical manufacturers face today.

COMMODITY MANAGEMENT INNOVATION

Allegro is a leading provider of commodity trading and risk management software, serving companies who buy, sell, produce or consume commodities. With more than 30 years of deep industry expertise, Allegro provides intelligence and decision-making capabilities, from the source of the commodity, through transportation, to the commodity consumer.

The Allegro software platform enables customers to handle their physical and financial positions and to optimize their assets and portfolios using tools that quantify and manage commodity risk.

Allegro is headquartered in Dallas and has offices in London, Singapore, Houston, Jakarta, Calgary, Dubai and Zurich, along with a global network of partners.

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