

Synthetic rubber market: cycle interrupted, but plans remain

The automotive industry has been hit hard by the COVID-19 pandemic. The Russian Ministry of Industry and Trade predicts a 30% decrease in domestic car production in 2020, which will affect related industries. The leading experts told the CREON Group about the prospects and realities of the synthetic rubber market.

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More tires

Due to quarantine restrictions in April and May, production stops and difficulties with the supply of imported components, as well as a general decrease in consumer demand amid the pandemic, the Russian production of vehicles (including trailers and semi-trailers) decreased by 42% compared to May 2019. The downturn in the automotive industry led to a production decrease in the tire industry, which is inextricably linked with the automotive.

According to the Rosstat statistics agency, in the first eight months of 2020, 33.4 million units of tires and rubber tubes were produced in Russia (-14.2% YoY). However, lower output wasn't a shocking news for Russian tire manufacturers: decline in production started last year with the outbreak of the trade war between the United States and China, as the latter was forced to target new markets for its products. In 2018, 67.5 million units were produced in Russia; in 2019 the output decreased by 10% to 60.5 million units.

Meanwhile, according to the Federal Customs Service, the share of imports increased in the same period by 7.5% to 34.4 million units or \$2 billion in monetary terms (excluding tires imported to Russia with new cars, trailers, bicycles and other vehicles, incl. spare tires).

In 2020, declining demand coincided with a pandemic, and Russian tire manufacturers actually missed the spring as the liveliest sales season, when winter tires are being replaced with summer ones. "Now it is difficult to make any predictions, but, according to our preliminary estimates, the tire market may fall by at least 24% by the end of the year," said Nadezhda Churmeeva, executive director of the Russian Tire Manufacturers Association.

Anatoly Antipov, General Director of Continental Kaluga, is also cautious in his forecasts: "Few in the automotive industry expect significant growth in the industry before 2025. According to analysts, sales of passenger cars in the country this year will decrease by 15-20%, against the background of such forecasts, growth in consumption of passenger tires cannot be expected in the near future."

Nevertheless, Antipov remains optimistic. "We managed to increase the export of tires to non-CIS countries in 9 months of 2020 more than two times compared to the same period last year," he said. Tire exports accounted for more than half of Continental's revenue.

Less feedstock

Following the fall in demand for the products of tire plants, related industries began to experience difficulties. For example, manufacturers of synthetic rubber, for which tire companies are the main consumers, were forced to reduce operation rates and perform annual turnarounds earlier in order to minimize the supply to the market during a period of low demand.

Nizhnekamskneftekhim (NKNKh), the leading supplier of synthetic rubber on the Russian market, describes the situation in the real sector of the world economy as "extremely uncertain": from March to May, such giants as Continental, Goodyear, Bridgestone, Pirelli, Cooper Tire, Hankook, Nokian Tires and more than 110 tire factories around the world were forced to stand idle, the disruption to supply chains has led to overstocking of warehouses. "The demand for synthetic rubber has been hit hard. According to our

estimates, taking into account the announced production stops alone, the world supply of tire products will decrease by 45-50 million units this year. This will lead to a reduction in global demand for synthetic rubber in 2020 - by at least 2% (or about 300-400 thousand tons)", the NKNKh report says.

According to Rosstat, the production of synthetic rubber in Russia in August decreased compared to July by 9.1% and amounted to 118 thousand tons, and compared to August 2019 the decline was 4.9%. In eight months of this year, 901.9 thousand tons of rubber were produced (-1.2% YoY).

"If we talk about rubber for tire use, then the car segment is sinking, and in parallel consumers are buying less tires. The market will gradually recover, but it will take at least two to three years to return to the 2019 level. This situation concerns not only Russia, but the whole world," comments the representative of the largest petrochemical company in the Russian Federation. "With regard to other applications of rubber products like industrial manufacturing and construction, the situation is better in these segments, since the consumption decline is assumable short-term. During 2021, the situation in these industries should return to pre-crisis levels."

Nevertheless, the producers of synthetic rubber are not discouraged: "The rubber business is cyclical: cycles from four to seven years, boom and bust. Now the cycle has broken a little, but in general, the forecast data for 2020 is quite good," said one manufacturer.

At the same time, Russian companies are not abandoning their plans to launch new production facilities. For example, NKNKh continues to implement the previously announced project of styrene-divinyl synthetic rubber (DSSK). Commissioning should take place before the end of this year. In the long term (until 2030), the company is going to organize the production of ethylene-propylene synthetic rubber. VoronezhSintezKauchuk launched a new brand of high-viscosity polybutadiene rubber (SKD-ND VV) at the beginning of the year. UfaOrgSintez also launched production of six new EPDM brands.

State support

In early June, Russian deputy prime minister Yuri Borisov suggested that synthetic rubber be purchased by Rosrezerv (the Federal Agency for State Reserves) as a measure of state support for rubber producers. According to him, the agency could serve as a damping mechanism, buying synthetic rubber intended for tires from the manufacturers, as the demand for tires has significantly fallen. Two years later, companies would buy back their products with a 5-6% surplus.

"Our petrochemical producers supply about 80% of synthetic rubber for the benefit of Western tire manufacturers. But the demand has dropped, while the feedstock has strategic importance, and we have it on the list of Rosrezerv purchases," as Yuri Borisov reported to the Russian president Vladimir Putin about the problems of producers in the absence of demand. The Russian Ministry of Energy supported the idea and promised to work out the mechanism.

EU carbon tax

An additional factor that should be considered by tire and rubber producers is the carbon tax that the EU plans to introduce on all products imported into the EU in 2021-2022. "The inclusion in the European system of CO2 emissions trading will undoubtedly affect producers, especially exporters. On the one hand, this will be an additional financial burden, on the other, an incentive for the development of lean production," believes Antipov from Continental. According to him, the Kaluga plant is already taking into account the potential costs of carbon tax in the future.

"The measures planned by the European Union are a very serious factor that Russian tire and rubber manufacturers must take into account throughout the entire production chain, since this tax will apply not only to the final product, but also to all intermediate stages of its creation," warns Florian Willershausen, Director BD & CDO of Creon Capital. "Otherwise, Russian exporters may lose market share in the EU, and their niche will be taken by more environmentally friendly and sustainable competitors."