



Emerging markets Destination next for paint manufacturers

Paints and coatings companies world over, especially from the developed nations, are focussing on the emerging markets to expand their business, as studies reveal that these countries will be contributing the maximum towards the growth of the global economy.



■ Dr Mosongo Moukwa

The global economy is expanding at a fast pace. Although no one knows how long the present expansion will last, it is reasonable to expect several years of solid growth. In the past, growth phases have lasted seven to nine years. The present phase is different from the previous ones in the sense that, most of that growth will come from the fastest growing and largest emerging economies. Finding a CEO who is not evangelical about emerging markets these days is like finding a hen's teeth. Because countries in emerging markets will contribute substantially to the global growth, it is little wonder that businesses are trumpeting their plans to expand in such markets.

Emerging countries

At the moment, the developed world still accounts for 65 per cent of the global GDP. Of the rest, a new paper by Goldman Sachs identifies a number of large emerging

economies as the 'growth markets'. Countries such as China and Brazil are expected to provide the lion's share of global growth in the coming years. Going forward, by 2020, these markets will contribute a huge share to the growth boom.

The US is the only country from the developed world that will deliver a significant portion to global growth. Japan and Korea get on to the chart, but no European country seems to make it. Countries such as Turkey and Indonesia will add more to global wealth over the next decade than Germany, France or the UK. However, these countries will only be able to deliver that growth within a freely trading world economy.

The GDP growth in China is around 9 per cent, with the chemical industry growing at double-digits. India, with favourable demographics, is posting a growth rate of 7.8 per cent, but it still has to solve infrastructure and regulatory problems. Even if it does overcome these barriers, experts believe that growth will still not be as dynamic as in China because the country is more decentralised.

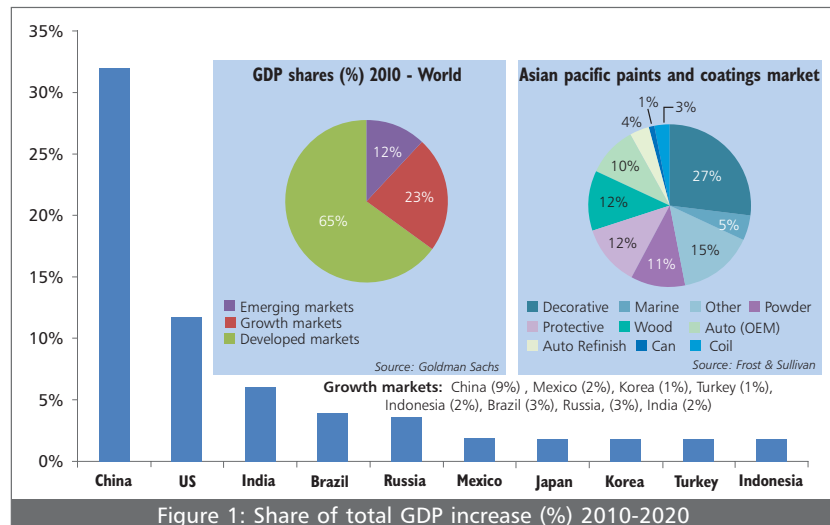
Paints industry

Industry players are optimistic of double-digit growth in Asia-Pacific region because of the demand from end-user industries such as steel, automotive, furniture and construction. The paints and coatings industry depends heavily on the end-user industries it serves. Positive growth is projected in those segments. Countries such as China, India, Vietnam and Indonesia are identified as high-growth countries where there are more opportunities for development of the paints and coatings market. However, the specific high-growth segments vary between countries.

In India, the paints and coatings market has increased by approximately 15 per cent since 2009, reaching a market size of \$ 3.8 billion in 2010. The market is expected to continue to exhibit double-digit growth between 2011 and 2013. Decorative and industrial coatings accounted for 63 per cent and 10 per cent of the total Indian paints and coatings market, respectively. Industrial coatings are expected to witness a higher growth rate compared to decorative coatings, owing to the increasing number of industrial facilities in India.

US and EU companies in emerging markets

The US companies have been expanding in emerging markets, particularly China, for many years and some are reaping the benefits of those investments. Dow Chemical, a global chemical manufacturer, has seen its volume up by 27 per cent year-on-year. In China, its volume was up 46 per cent against 11 per cent in both North America and Europe. In 2010, Dow Chemical vigorously expanded its market in the Asia-Pacific region. It had made new investments in Thailand, Korea, China and Vietnam. Annual sales in emerging markets reached a record \$ 16 billion. In addition, sales in the Asia-Pacific region, for the first time in history, touched \$ 9-billion



mark, an increase of 25 per cent. The company also has one of its largest research and development facilities in China, stressing the long-term strategic importance.

Apart from the US companies, European companies are also venturing into emerging markets. For example, AkzoNobel, a global leader in paints & coatings and a major producer of specialty chemicals, is aiming to get half their sales from such countries in the next few years. According to the company's annual report, the Dutch company was investing nearly all its money in emerging markets. Indeed, the company has put in place a series of investments. It just built a new multi-site in Ningbo, China. The facility is AkzoNobel's largest ever investment outside of an acquisition and underlines the increasing importance of the world's high growth markets as they look to establish themselves as the leading coatings and specialty chemicals company globally.

One advantage European companies might have is the fact that their domestic markets are smaller than their American counterparts. This means that they are more used to getting a big part of their sales and growth from abroad, and are geared towards exports. Due to this, they tend to have decentralised management

models, something that should bode well in the emerging markets, with some exceptions. This also leads to some disadvantages. Put it simply, decentralisation makes Europeans good at adjusting well to each country, but leaves them with higher costs because they are slow to implement change across the company. Language and culture would tend to favour Americans, with US companies and universities better able to attract bright young minds from emerging markets. Some of them get deployed back to their countries after a few years of working experience in the US.

European companies have increased their investments in emerging markets not just for production, but also for research. Some in Europe argue that such a move away from the continent can go on only so long before Europe's own industrial base is harmed deeply. Some in the US share the same sentiment.

Vibrant mergers and acquisitions

The paints and coatings industry itself has been witnessing a sea change. The industry is also facing major price increase in some key raw materials, and in some cases even shortage. One way out of this situation could be by controlling raw materials right

Table 1: Market capitalisation: Chemical stocks had another strong year in 2010

Rank 2010	Rank 2009	Company	Market capitalisation (\$ millions) 2010	Change from 2009	Position in emerging markets
1	1	BASF	73,430	42.0	Planned investments of Euro 2.3 billion (\$ 3.2 billion) between 2011 and 2015. In China, it is planning expansion of its existing joint-venture plant with Chinese oil and petrochemical giant Sinopec, by extending its acrylics value chain.
2	1	Dow Chemical	39,848	25.4	Growth in emerging regions surpassed \$ 16 billion in revenues for the first time. Sales in Asia-Pacific topped \$ 9 billion in the year, also representing an all-time record. Invested in Thailand, China and Korea.
6	6	PPG Industries	13,485	39.0	During 2010, it began construction of a new coatings resin facility in China and expanded the manufacturing.
10	9	Celanese	6,414	38.4	Announced a newly developed advanced technology to produce and expand the strategic acetate ventures in China. These actions will contribute to earnings growth in 2011 and beyond.

Note: Based on share prices as on December 31, 2009, and December 2010. These are companies that generate more than half of their revenues through chemical manufacturing. Figures from companies that report in native currencies were converted to dollars and average annual exchange rates from the Federal Reserve.

at the source and monitoring the full value chain. With some exceptions, companies have never pursued this option. Take for example BASF, which makes pigments and urethane systems, as well as formulated paint for automobile and coil coatings. This is also the case for DuPont, which produces TiO₂ and also formulate paints.

Mergers and acquisitions will remain vibrant in the near term. After staying conservative during the downturn, companies have a lot of cash on their balance sheets, now that business has turned around. Rather than clamouring for special dividends and stock buy-backs, institutional investors that own chemicals stocks are encouraging companies to invest in growth. Only time will tell whether any of those transactions are big enough to reshuffle the Top 10 companies. But the push towards growth is likely to have an impact on the chemical industry for several years. To what extent this may change the scenario in emerging countries, no one knows.

Understanding local customers

While Western companies are investing in emerging markets, higher domestic demand in emerging Asian

countries encourages the growth of domestic players. More local players are expected to enter the industrial coatings segment, especially given the technology transfer that occurred during collaboration with multinational companies. The rise of domestic competitors will happen

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faster than most MNCs expect. Some local companies in some high growth markets have already established themselves. For example, Asian Paints has established itself as the leader in architectural paints in India. Today, it is ranks fifth globally in architectural paints. Multinationals aiming to garner a strong marketshare, a few years down the line, need to establish themselves now.

Questions abound over how well European and the US companies understand consumers in emerging

markets. Customers in these markets have different needs than those in developed countries. Multinationals looking to capitalise on opportunities there should be ready to do business in hundreds of locations, not just in a handful of mega cities. This has tremendous implications on resources distribution and choice of business partners.

Multinationals would do well, if they step up their innovation activities to meet the 'really-demanding and price-sensitive' needs of consumers in the emerging countries. Perhaps then, the real threat to European and the US groups will be companies from emerging markets that might lack the technology but understand the customers. ■



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