

# 2007 STATE-OF-THE-INDUSTRY REPORT

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***Adhesives & Sealants Industry (ASI)***

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The North American Adhesives and Sealants industry is in pursuit of \$15 billion mark in sales revenue. The road here has been over a tumultuous terrain since the beginning of the new millennium. Manufacturers face multiple diverging challenges in their business that require thoughtful analysis and precise maneuvering.

As illustrated in Figures 1-2, the industry reached \$14.5Bn in revenue in 2006 and 8.9 million dry lbs. reflecting year over year growth of 3.7% in volume and 5.5% in revenue respectively. However 2007 has been more challenging. The economy is sluggish with consumer spending down, the housing sector is in retreat and the U.S. auto makers woes worsen dipping below 50% market share. As a result, we are forecasting modest revenue growth of 3% due to price actions passing through raw material increases. However, we are forecasting a 2% decline in volume, with a prospect for further decline if the construction market forecasts continue to worsen.

**Figure 1. Adhesives and Sealants Growth Trends 1996-2007F**

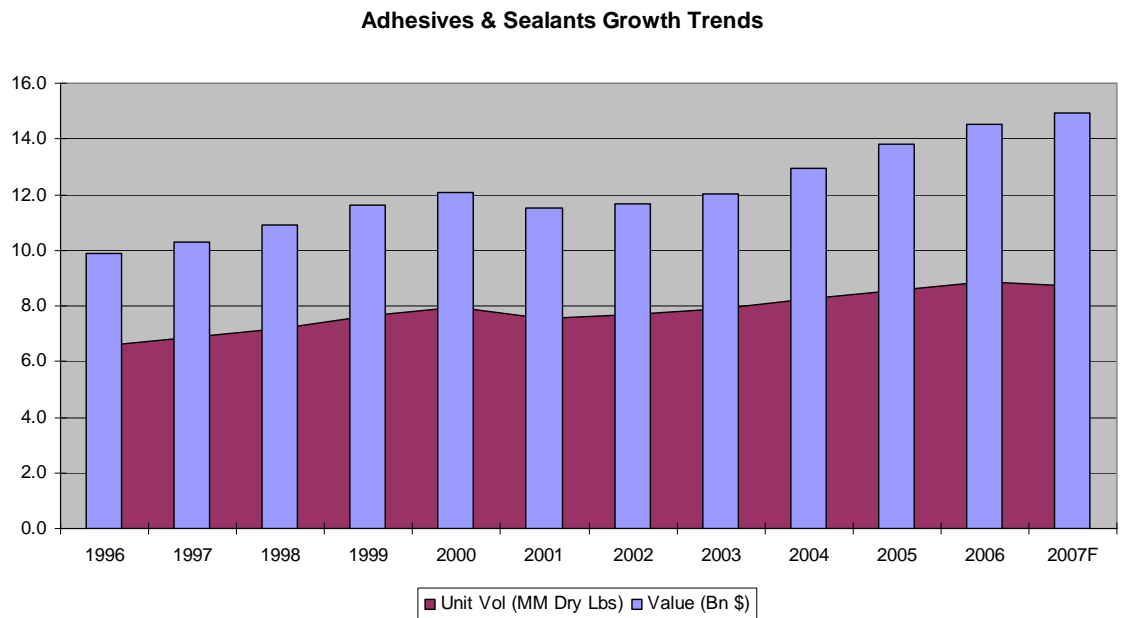
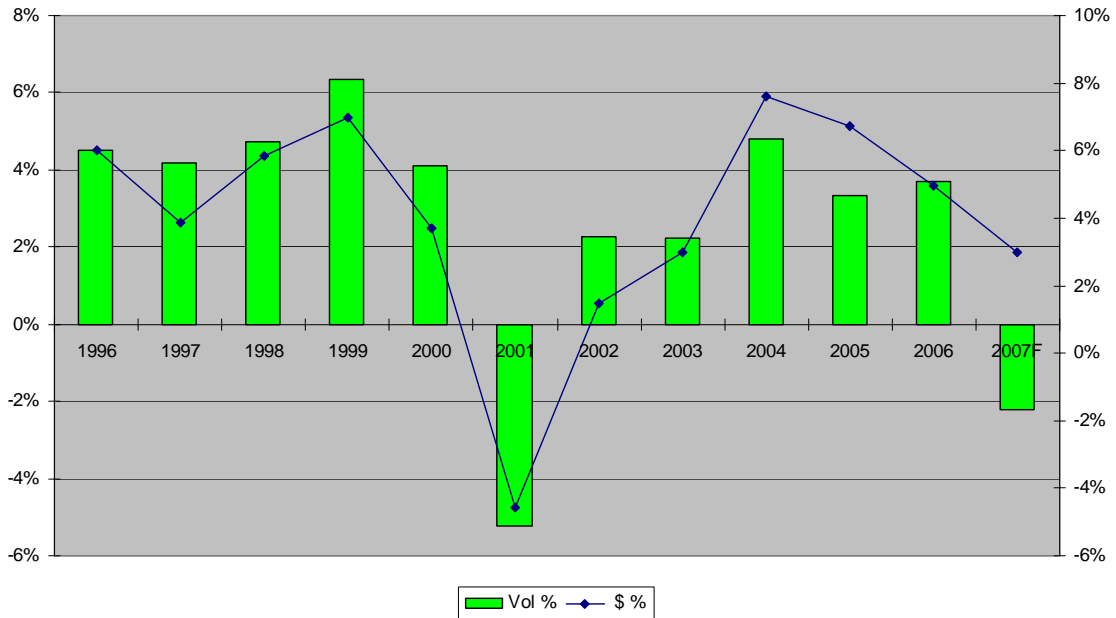


Figure 2. Year-Over-Year Growth Trends



Following are the top 10 challenges manufacturers said they will face in 2008 and through the remainder of the decade:

1. Rising raw material costs- how HIGH will OIL go and how soon will it get there?
2. The ability to continue to raise prices.
3. The condition of the U.S. economy.
4. Product innovation - finding higher margin markets and/or dealing with the changing face of regulatory requirements i.e. health, safety and environmental issues
5. The availability of key raw materials. The rate at which emerging economies, such as China, continue to gobble global demand. China is absorbing 25% of global commodities output.
6. Maneuvering changes in competitive landscape due to continued consolidation. At the time of this writing, ICI had announced an agreement to sell its business to Akzo Nobel, which subsequently will sell National Starch to Henkel.
7. Perceived commoditization in the eyes of the customers.
8. Dealing with offshoring markets – deciding whether to partner with foreign suppliers and manufacturers and/or follow the customer to emerging markets.
9. Changes needed to the sales approach.
10. Focusing on core business by reducing product lines and/or services.



While oil cost is a major concern for the industry, the news is not all bad. In fact, in this authors opinion, high oil pricing may actually drive adhesives and sealants growth at a faster rate. Additionally, adhesives and sealants have always been valued considerably lower than the importance they deliver to the final product. Typical value in use is 1-2%.

We are already beginning to see four positive results as a result of high oil pricing:

1. Engineers are designing for better fuel efficiency: more composites, down-gauging and down-sizing to improve fuel efficiency. This trend heavily favors greater use of adhesives and sealants at the expense of industrial fasteners and welding, as demonstrated by Boeing’s Dreamliner and Airbus’s A-380.
2. Emergence of new applications that previously did not use adhesives and sealants, such as wind turbine assembly.
3. Acceleration of adhesive and sealant penetration into energy-saving applications such as insulated glass and window films.
4. Margin discipline among manufacturers is driving toward a much-deserved higher value.

Aiding in this higher value perception, the industry experienced a rare phenomenon in 2006 where raw material pricing de-coupled from the price of oil. Key raw materials were in short supply due a balance of demand. Examples include Vinyl Acetate Monomer (VAM), Acrylic Esters, Methanol and Isoprene.

ChemQuest forecasts manufacturers’ margins in the range of 30-40% on a gross profit basis, as illustrated in Table 1.

**Table 1. Average U.S. Adhesive and Sealant Manufacturers Cost Structure**

<b>Income</b>	<b>100%</b>
<b>Cost of Goods Sold</b>	
Raw Materials*	50-58%
Packaging	2%
Labor	2-3%
Energy	1%
Ovehead, Taxes, Ins., Dep.	5-7%
<b>Total COGS</b>	<b>60-71%</b>
<b>Gross Profit</b>	<b>29-40%</b>
<b>SG&amp;A</b>	<b>17-23%</b>
<b>EBIT</b>	<b>6-23%</b>

\* Highly dependent on mix of technology



Manufacturers have done a good job of recouping lost margins, but on average still lag about 3-6 months and need to recoup an additional six points of margin. In a soft economy led by housing declines and lower automotive sales, this is very difficult and may in fact obstruct needed pricing actions.

Adhesive and sealant manufacturers will continue to meet these never ending challenges by improving internal efficiencies, finding product niches, developing new markets and competing in a changing paradigm, but in the end it comes down to maintaining their margins. Without a healthy bottom line to support these influencing factors, top line growth will be challenging.



## About the Author



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an international strategic management  
consulting firm specializing in the Adhesives,  
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Dan joined The ChemQuest Group, Inc. in 1996 from the Rohm & Haas Company where he was most recently European Director, Industrial Coatings. Prior to R&H, he spent thirteen years with Unocal Polymers where his career took him from technical service positions to Director of Marketing. He directed the sale of the Unocal Polymers Business to Rohm & Haas, working closely with Morgan Stanley, numerous attorneys, as well as the FTC. His entire career has been dedicated to the Coatings and Adhesives Industries. His particular strengths lie in strategic assessment and value creation on behalf of clients. He holds degrees from Wabash College (BS Chemistry) and William & Mary (MBA).

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