

# YEAR-END ISSUES AND '03 INDUSTRY OUTLOOK

***Susan Anderson***

*Director, Global Business Development*

**The ChemQuest Group, Inc.**

Cincinnati, Ohio

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***Modern Paint and Coatings –  
“Paint Doctor”***

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**Q: What are the Continuing Economic Issues that are affecting the Recovery of the Coatings Industry?**

A: During the first quarter of this year The ChemQuest Group predicted that the Coatings Industry would grow very slightly in the first half of 2002. Why? Because the housing market, both new and existing homes, and the automotive market remained surprisingly strong, supporting coatings sales into those markets. However, the rest of the economy, especially the non-automotive and non-military industrial sectors remained weak, leaving the OEM and Special Purpose Coatings businesses struggling to recover.

However, restructuring and cost cutting initiatives put the Coatings Industry in the enviable position early in the year of margin improvement, despite flat to decreasing sales volume. In addition, lower energy costs kept raw material prices at bay. Companies in the Coatings Value Chain remained cautiously optimistic that the recovery was going to gain momentum in the last half of the year, particularly in the battered industrial markets. This was due to anticipated increases in capital investment and continued positive trends in the production index and other leading economic indicators.

As a result ChemQuest forecast that the Coatings Industry would grow at the predicted GDP rate of about 3% during the last half of 2002. As we know, despite improvements in some sectors, this target has remained elusive.

Although the automotive and housing industries are continuing to perk along, fueling spending in related industries, there is concern that the “housing bubble” may be ready to break and that the zero financing that has fueled automobile purchases will ultimately adversely affect the industry. Capital expenditures have not increased and production indicators have leveled off from a trend of continuous monthly improvement. Capacity utilization remains below investment levels. Major coatings consuming industries, such as travel, have not yet recovered. Rising unemployment, particularly in white collar and management ranks, rising health care costs, and the poor performance of



the stock market have reduced household spendable income. Though consumer spending remains reasonably high, it is expected to level off or decrease in the coming months. Exports continue to be challenged by the continued relative strength of the US dollar, despite recent weakening, and the stagnant global economy. Energy costs have risen (and will continue to rise if a war on Iraq materializes), as have raw material prices, diminishing the growth in margins seen earlier in the year.

***Q: What is the effect on the coatings industry?***

A:

- There is increased competitive pressure as companies vie for core business, putting further pressure on pricing.
- In Architectural Coatings the “Big Box” distribution channels are gaining share and forcing additional price concessions from coatings formulators who will pass it back to raw material suppliers.
- Consolidation will continue.
- As their customers expand globally, coatings companies will continue to follow and so must raw material suppliers.
- Non-automotive industrial coatings markets are still struggling and are not expected to show signs of sustainable recovery until at least the end of Quarter 1, 2003.
- Companies that are reporting growth are growing through the introduction of new products and technologies, replacing existing coatings business, or through acquisitions..
- Architectural coatings are expected to remain strong.
- Motivated by OEM goals to cut costs, substrate suppliers will continue to aggressively research ways to eliminate the need for coatings. Coatings companies will in-turn look at ways to eliminate steps in the coatings process to make it more efficient, while improving performance or appearance.



***Q: What about 2003?***

A: Despite all of the challenges, many companies are beginning to report slight business growth and renewed interest in new products and formulations. Although few appear bullish on the remainder of 2002, many are looking to the first quarter of 2003 to show stronger recovery signs, despite uncertainties over the effects of the impending war in Iraq and potential for future terrorism attacks on the US.

Moderate economic expansion is expected throughout 2003 for the US, though the trend to manufacturing offshore will continue. In order to take advantage of this trend coatings companies must also globalize through exporting, foreign investment or partnering.

***Q: How can a company best manage the challenges of today and be ready for growth tomorrow?***

A:

- Develop a strong competitive intelligence network.
- Concentrate on markets that take best advantage of your company's core competencies, building a strategic plan from solid and unbiased knowledge of the markets, their dynamics and requirements, and potential for growth.
- Invest wisely in new product development, matching the investment with company goals and realistic market potential.
- Consider acquisitions and even divestitures to strengthen your business position today and in the future.
- Look to global markets for growth.



## About The Author



**Susan M. Anderson**

**Director, Global Business Development  
The ChemQuest Group, Inc.,**  
an international strategic management  
consulting firm specializing in the  
Adhesives, Sealants and Coatings industries,  
headquartered in Cincinnati, Ohio.

Susan joined The ChemQuest Group in 1997 after thirteen years with Zeneca Resins where she held numerous positions including Business Manager, Architectural Coatings, Business Manager, Adhesives & Sealants, Business Manager Graphic Arts, and General Sales Manager. During her tenure at Zeneca, she gained considerable experience in managing strategic planning teams, organizational change, and sales and marketing teams. Prior to Zeneca she spent six years in sales for Morton International Inc. and five years in product development and tech service for the 3M Company. She earned a B.A. in Chemistry and in Mathematics from Augsburg College.

Contact Sue at (781) 837-0222 or [sanderson@chemquest.com](mailto:sanderson@chemquest.com)

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Questions or request for additional copies of this paper may be directed to the author at:

**The ChemQuest Group, Inc.  
8150 Corporate Park Drive  
Suite 250  
Cincinnati, OH 45242**

**(513) 469-7555  
(513) 469-7779 – FAX**

[www.chemquest.com](http://www.chemquest.com)

