

Market trends

Increased infrastructure spending will further drive the construction chemicals growth in India say **ALASDAIR NISBET, BOARD-MEMBER** and **DEEPAK LADHA, EXECUTIVE DIRECTOR** of the **LADDERUP GROUP**.

The Indian construction industry, contributing more than 7 per cent to the nation's GDP, has witnessed a growth of over 16 per cent per annum, and is expected to touch the \$100 billion mark by 2017. With increasing penetration of multinational construction companies in India, the construction market in India is booming by the day, thereby leading to further growth in the Indian construction chemical industry. The construction chemical industry in India has been empirically recording a CAGR of 17 per cent for the period 2007-2012. The Indian construction chemical industry was valued at \$0.6 billion in 2012 and is anticipated to reach \$ 1.3 billion by 2017, essentially riding on the less explored market potential and the sturdy growth expected in the construction industry in the coming 5 to 7 years. The increased infrastructure spending proposed by the government accompanied by the growth in the real-estate industry could yield high growth in the construction chemicals market.

The overall market in India is fairly consolidated but there is substantial fragmentation of individual products and application areas. The construction chemical industry in India comprises a range of products - admixtures to flooring chemicals, sealants, grouts and waterproofing chemicals; with polymers being the key raw material for every formulation. Concrete admixtures cover the largest share in the Indian construction chemical market followed by flooring and waterproofing chemicals vis-à-vis the global construction chemical market where protective coatings form the most eminent group. The composition of tiling, sealants and waterproofing is currently low and that of flooring chemicals is relatively higher in the Indian market in comparison to the developed market. The escalating quality standards

worldwide have boosted innovation and the construction chemical industry today on average spends 3 per cent of its total sales on research and development of new applications and products.

Despite 300 companies functioning in this sector, the top five market players cover half of the segment. Fosroc, Sika, BASF and Pidilite are the leading players in the Indian construction chemicals market. The other 50 per cent can be attributed to the smaller players. The leaders typically have differential margins and are more profitable than the smaller players.

Employing these specialty chemicals in the construction process is not mandatory by law or any regulatory need. This has led to the creation of a huge market for sub-standard products in which most of these start-ups and unorganised companies operate; with scope to grow further subject to change in mindset of the end-users, regulatory enforcement, etc. New companies would want to align with the international product norms than the sub-standard products due to the rising quality and performance expectations.

The expansion of the construction chemical industry is conditional on the progress of the construction industry. With increased government attention and investment on infrastructural enhancement, a 100 per cent FDI allowance in the real estate sector, low labour cost, and advancing aspirations of middle income groups, the future prospects for the construction industry imply an enormous growth potential even for the construction chemical industry.



BOOMING DEMAND

Construction projects are becoming more sophisticated due to innovative and improved quality concrete, waterproofing, insulation (energy efficiency), bonding and safety. Concrete admixtures, for instance, which comprise majority of the construction chemical demand in India help reduce the cost of concrete construction and significant project quality enhancement. Continuous ideation such as increasing flowability at very low water to cement ratios, speeding-up setting time, improving water-reducing admixture quality and increasing durability helps the increase in demand for use of such construction chemical products. The demand for endurance in buildings and structures, improved safety, innovative roofing, low-energy housing, etc. is perpetually on the rise. This demand is enhanced by structures built years ago which need restoration and frequent repairs needed in constructions supported with sub-standard chemicals. The increasing adherence to global construction quality standards as well as government regulations for energy saving structures will further push up innovation and the market demand. Higher performance buildings and infrastructure require more construction chemicals.

In the present scenario in India, this segment of specialty chemicals is experiencing a 15 per cent growth which is twice the prevalent GDP growth rate of the nation. Construction chemicals in India today represent a mere 0.4 per cent of the total construction spend. However, going by its growth, it is soon expected to attain 1 per cent of the same, which is the standard for most developed nations. Hence, we comprehend that in terms of the growth rate, the construction chemical industry can even supersede the construction industry in the forthcoming years. Also, it plays a noteworthy role in

earning foreign exchange for the nation owing to its export contribution.

NEW CHALLENGES

In spite of these umpteen growth drivers, one of the major roadblocks for upcoming construction chemical producers is the incremental construction cost. These chemicals augment the value of the construction but not using them is no hindrance for the construction process. Thus, the cost-sensitive industry may render expenditure on these inputs unnecessary. A major issue in this regard is the low level of awareness about these chemicals in the end-user market. Barring the few paramount players, most construction companies do not understand the new-age chemicals and construction aids. Another obstacle in the way of construction chemical industry is hiring of unskilled labour by construction companies whereas the application of such chemicals demand a primary technical know-how. Although the start-ups in this industry are benefitted by a number of opportunities, they have to face tough competition as there are no stringent barriers to entry in this market segment and therefore, many small-scale companies have bloomed. Further, small players need continued investment in R&D in order to grow in the quality product space and encounter the threats from established companies.

M&A FOR GROWTH

Merger and acquisition remains a key focus area for larger western construction chemical companies. In the last ten years a lot of consolidation has taken place in the global construction chemical industry, creating larger and larger entities. Global companies like Sika, RPM and Henkel have consolidated their market positions by acquiring small regional businesses having unique products and technologies, domestic leadership positions and strong profitability. Sika has played leading role in market consolidation (five acquisitions worth \$333 million in 2013) with focus on increasing emerging market share and driving growth through continuous innovations (73 patents in 2013). Historically, there have been very few construction chemicals deals above \$1 billion. Some of the major deals in the sector include BASF acquisition of Degussa Construction chemicals in 2006 for \$3.3 billion, Wendel's acquisition of Materis for \$ 2.4 billion in 2006 and PPG's acquisition of SigmaKalon for \$3 billion in 2008. Large companies will continue to enhance growth through acquisitions and are considering expansion of



geographic presence and improving product portfolio by acquiring innovative products and technologies. Also synergies are one of the key drivers for consolidation. Synergies on acquisitions can be as high as 10 per cent of target sales. Sales synergies are achieved through cross-selling and pushing global products and cost synergies can be achieved through rationalisation of sales and distribution, manufacturing, administrative and purchasing functions. However there have been challenges for acquirers such as preserving the value of local brands, local constraints to rationalisation, environmental issues and legacy product liability (asbestos, lead, etc.). Fears of potential liabilities have reduced consolidation in the US and companies like W.R. Grace, RPM, PPG, Owen Corning and Sherwin are facing personal injury claims. In India, Pidilite continues to expand its portfolio primarily through outbound acquisitions. With Western companies looking to expand their emerging market presence and India being rapidly growing market, smaller regional companies are on radar of these global companies. The Indian construction chemicals sector is largely dominated by family-owned businesses and some first time entrepreneurs are exploring opportunities to exit their businesses due to succession issues. These family-owned businesses are likely to be acquired by large players, leading to consolidation.

The outlook of the construction industry is gradually changing. People are focusing not solely on the costs but also on the performance that extra costs deliver. Many multinational construction companies operating in India have even made the use of construction chemicals mandatory in their projects.

The construction chemical industry in India is also increasingly investing in developing more innovative products with the help of their R&D team as well as inputs from constant ideation and consultation with the construction companies and craftsmen.

Ladderup Group is a Mumbai-based investment bank with over two decades of insight and experience with strong mid-market focus.

CHALLENGES FOR START-UPS	POSSIBLE SOLUTIONS
Multiple product offering	<ul style="list-style-type: none"> Specialisation in niche segments and tend to become a market leader for such specific products
Increased demand for quality products	<ul style="list-style-type: none"> Emphasis on developing quality rather than sub-standard products Focus on innovative products, new product development
Pass-on increase in price / Demand high price on products	<ul style="list-style-type: none"> Emphasis on developing quality rather than sub-standard products Focus on innovative products, new product development
Geographic Presence - Owing to the small scale of operations, may penetrate a limited market region	<ul style="list-style-type: none"> Focus on developing a reputed brand Increase presence in contiguous/ homogeneous regions with time and growth in business
Rising Competition - New firms coming up and existing global players	<ul style="list-style-type: none"> Specialised product offering and developing Company's own market Develop brand loyalty with time Increase R&D efforts Focus on enhancing distribution reach to be attractive to global players
Inorganic growth - advantage to established players	