The Thais that bind

Global Business Reports prepared this special report on the chemicals sector in **Thailand**

Located between China and India, and at the heart of the ASEAN free trade zone, Thailand is well placed to benefit from the economic transformation of Asia. For the foreign chemicals company looking for new clients, partners or a new production or distribution location, Thailand has much to offer. It has open doors to foreign capital and has demonstrated strong commitment to the foreign investor.

With a GDP per capita of $8,100/year, Thailand offers substantially cheaper labour rates than the West, albeit not the cheapest in the region. However, chemicals bosses, Thai and foreign alike, claim that employers and customers can rely on high quality standards in Thailand. According to Ramesh C. Saboo, managing director of Thailand's largest APIs producer, Linaria Chemicals, productivity per worker is higher than in India and the 'Made in Thailand' tag adds value to the product.

Thailand should not be considered as a manufacturing base alone. Part of its attraction lies in its substantial domestic market, with a population of 65 million that is rapidly urbanising and gaining in purchasing power. Another is its access to 580 million people in ASEAN. Many chemicals products enjoy tariff-free status within the ASEAN, a community including fast-developing markets such as Vietnam and Indonesia.

S&J International, which contract manufactures for the international personal care and cosmetics market and deals with production, logistics and distribution for third parties in Thailand, saw revenue grow by 15% in 2009. Managing director Thirasak Vikitset argues that, whilst the economic crisis has had a negative effect on the cosmetics market as a whole and the lower price sector in particular, there are wider social and demographic trends driving consumption in Thailand.

A young and increasingly wealthy and sophisticated middle class is emerging with a healthy appetite for his products. The same factors will also have a positive effect on a wide range of consumer goods serviced by the chemicals industry, in his opinion

Sector overview

The evolution of the Thai chemicals sector is entwined with the discovery and development of large natural gas fields in the Gulf of Thailand during the 1980s, according to Chaveng Chao, chairman of the Federation of Thai Industry's Chemicals Club.

Adds Sanpong Bumpensanti, president of the Chemical Business Association: "The government of the day chose to use Thailand's gas as part of their wider import substitution policy by making chemicals rather than electricity with the gas".

The state oil and gas giant PTT was tasked with developing downstream chemicals plants. The country succeeded in attracting major players such as Dow and Aditya Birla in the earlier years, offering the carrot of investment promotion incentives and the stick of heavy import tariffs on many categories of product.

The Thai chemicals sector at the turn of the new decade is a sophisticated and diverse industry driven as much by direct exports as by the burgeoning domestic OEM and consumer markets. Petrochemicals still dominate the landscape but Thailand has also developed substantial pharmaceuticals, personal care and coatings sub-sectors.

In 2008 Thailand was estimated to have produced in excess of $34 billion of chemicals products, though the true figure is likely to have been higher. The industry is heavily focused on exports, be it directly or serving Thailand's numerous export-oriented finished goods producers. Some 40% of its production in 2008 was exported.

Current sentiment

Nearly four years on from the coup that deposed Prime Minister Thaksin Shinawatra, the ramifications are still very much in evidence on the streets of Bangkok, with rival demonstrations by pro- and anti-Thaksin 'red shirts' and 'yellow shirts' competing to testify their allegiance to the universally venerated king. During our two months of on-the-ground research in Thailand, political instability was the concern most often raised by the 40+ CEOs we interviewed.

Aman Bhattacharjee, managing director of Merck Thailand says: "The biggest challenge is the stability of government. But there is a mood of optimism here. Thailand has a history of bouncing back."

The military-installed government sent shivers through the international business community in 2006 when it imposed capital restrictions and openly talked of changing the laws regulating foreign investment. However, these restrictions were rapidly eased and subsequent governments have worked hard to demonstrate Thailand's commitment to investor rights.

Vinod K. Gupta is keenly aware of the investor's attitude to Thailand in general and the Thai chemicals sector in particular. This Indian national, a 22-year veteran of the sector is head of Indorama Chemicals.

"We are getting a good response from international investors, they are not nervous about the political situation," says Gupta. "The government and the prime minister are very pro-investment. The basic principles of investor rights and respect for property rights remain stable."

Map Ta Phut & CSR

As it happens, the 2006 coup has had massive, if unforeseen, ramifications for the chemicals industry. The military government introduced a new constitution in which Clause 64 reformed the environmental permitting process but this proved to be a crude fit with existing codes.

Subsequently, in 2009, a local NGO sought an injunction to suspend 64 industrial projects under development at Map Ta Phut, the centre of Thailand's chemicals business which had failed to gain the environmental permits required under the new constitution.

"There was no mechanism for administering the new permitting process," claims Chao. "These projects had already been approved under the existing regulations."

The case has gone as far as the Supreme Count and the prime minister has appointed a special panel to resolve the issue. Some believe that an early resolution to the issue could add 0.5% GDP in 2010.

Amongst the projects planned are $1 billion worth of Siam Cement Group projects including a new polyethylene catalyst and eighteen PTT schemes, including a sixth gas separation plant. The courts have already given the green light to some, but until the legal situation is clarified, they are unlikely to leave the draughtsman's board.

Those within the industry say that they are happy to comply with the law and are keen to meet their environmental obligations. The issue is one of process rather than any concerted effort on the part of law makers to stifle industrial development, according to Gupta.

"The situation at Map Ta Phut is not a political issue. The constitution written after the coup was muddled and the relevant clauses were in conflict with existing laws," he says. For future schemes, though, the government needs to establish a clear process for environmental permits and bring the two conflicting laws into harmony.

Thais go global

There are many clichéd views regarding Asian business practices. Perhaps, it takes a Thai with an international perspective to confirm what makes the Thai business environment special.

Weerasak Suthapong, country director of the giant American water treatment and environmental services company Nalco, says that relationships have traditionally been very important in the Thai business world.

In this Buddhist country, it is considered important not to come into conflict or to push others into making decisions. This is a way of thinking that can put Thais at a disadvantage when trying to do business abroad.

Suthapong adds that, whilst relationships are still hugely important and a non-confrontational approach is still valued, Thais are learning how to prosper in the global business environment. Today, Thai companies, large and small, operate in the global marketplace and have learnt to compete on merit alone.

"Some 70% of our GDP is generated from exports," says Veerasak Kositpaisal, president and CEO of Thailand's largest chemicals company PTT Chem, "The Thai market is too small for us. Today 50% of our products are exported."

PTT Chem is primarily an olefins company, producing some 1.28 million tonnes of ethylene and 440,000 of propylene in 2008, and this remains the focus. However, the first action of its international subsidiary PTT Chem International was to acquire the oleochemicals business of Cognis in partnership with Sime Derby of Malaysia and rename it Emery Oleochemicals.

"We are reviewing the company and turning it around. The strategy is to focus on industries that we know well and opportunities that offer synergies with our existing businesses," Kositpaisal explains. "We are interested in any opportunity, whether it is a grass-roots project, M&A or a JV.

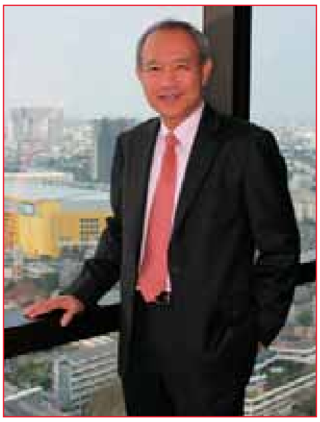
SMEs look for growth

Although the likes of PTT grab the headlines, Thailand's shift towards global integration will be driven by the multitude of medium-sized companies that have outgrown their small domestic markets. In a sector dominated by small and medium-sized family firms, fear of international markets and an overwhelming desire to retain family control of businesses often stifles opportunities for growth.

Ek Suwatthanaphim of Selic Chemical, a family-owned producer of adhesives for the shoe industry that has diversified into food and tannery chemicals, recognises that his company must both open its doors to external expertise and capital and chase his market. He and his father, who founded Selic some 30 years ago, have therefore taken the rare step of selling part of the company to a private equity firm with the intention of listing by 2015.

This move has as much to do with opening the doors to new talent as it does with raising capital. The Suwatthanaphim family realises that smaller companies struggle to retain top-level employees as career paths are limited, especially when senior positions are monopolised by family members.

By mapping out a clear growth strategy, fuelled by new capital and external expertise and with an end goal of becoming a public company, Selic hopes to attract and retain the best talent. However, Suwatthanaphim realises that it must seek new georgraphical



Kositpaisal - Focus on synergies

locations in order to stay in its core market of adhesives for shoes.

"We have been driven to focus on the international market by the fact that our key markets, the footwear and clothing sectors, are highly footloose," he says. "Clothing is a sunset industry in Thailand. It follows cheap labour and that is now found in places like Bangladesh. We will follow the market wherever it is."

Thai chemicals manufacturers are going to the most surprising of markets in their desire to grow revenue and profits, though the process has not always been smooth and the learning curve has often been steep. Selic for one took four years to build a foothold beyond its traditional Asian markets.

"In the past four years we have started focusing on new markets such as Ghana, Madagascar and Ethiopia. We have also expanded into Latin America and are working on the Middle Eastern market," Suwatthanaphim says.

He adds that this cannot be undertaken alone and that finding a strong local partner is vital. Selic, like PTT, intend to build an international operation, rather than rely solely on exports. "Thailand is just a base for us now. I hope that within five or six years Thailand will be one small unit of a larger international business. We will start building a plant in Bangladesh in the near future".

New plants

In 2007 investment in the Thai chemicals market hit a peak with billion dollar mega-projects from PTT, Siam Chemicals and Dow being announced. The global recession which is seen very much as a product of the West in general and the USA in particular, has inevitably dampened the flow of new projects being announced.

However, engineering, procurement and construction (EPC) firms are still very busy in Thailand and the major projects are mostly due to be completed in 2011. There are also many Korean firms pursuing contracts.

Hironobu Iriya, President and CEO of Thailand's largest indigenous EPC firm Toyo Thai, believes that Thailand is well placed to capitalise upon the flow of inward investment: Indeed, he adds, it is a reflection of the strength of the Thai chemicals EPC industry that Toyo Thai has undertaken work in the USA and is pursuing projects in Central Asia, the Middle East, Africa and Russia.

Conclusion

There is a mood of optimism amongst the leaders of Thailand's chemicals industry. Although this is not a country free of problems and the chemicals industry is facing its own special crisis at Map Ta Phut, Thailand's political situation should be viewed in context. Many other developing markets face far worse instability and some of those that do not, such as Vietnam or China, are outright dictatorships.

The situation at Map Ta Phut is damaging, but it reflects a respect for the rule of law and a desire to do things properly in terms of quality standards and the environment. As one of the founding fathers of the Thai chemicals industry Kian Chaisuparakul, founder and head of the DOP and DINP producer South City Group, notes, Thailand has never had a major chemicals disaster. Perhaps the stand-off on Map Ta Phut suggests why.

As the chemicals industry in Thailand has matured, so it has evolved from a simple base chemical production centre for the domestic market into a producer of specialist products for markets across the globe. Today Thailand offers the attraction of an increasingly affluent domestic market, privileged access to 580 million people in the ASEAN and proximity to the mega-markets of China and India. Thai companies, small, medium and large, are seizing the opportunity presented by their location and are can be found aggressively pursuing market share across the world.

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