The Growing Opportunity for Chemical Distributors

Reducing Complexity for Producers Through Tailored Service Offerings

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Between 2008 and 2012, the worldwide chemical distribution market grew approximately 9 percent annually, in nominal terms, to roughly €165 billion—outpacing chemical consumption growth and creating opportunities for distributors (especially in emerging markets).

**Preferred Partnerships Help Reduce Complexity**
Producers turn to third-party distributors to help reduce complexity and expand into new markets. The trend now is for producers to establish preferred partnerships with fewer distributors, particularly those that offer a broad range of services.

**Sophisticated Value-Added Services Are in Demand**
Value-added services, such as outsourced inventory management or formulation, are increasingly important to producers and often drive their choice of distributor.

**Opportunities for Market Leaders and Local Champions**
International distributors are better equipped to meet increasing quality standards; they need to improve their reach and segment-specific expertise. Local champions with established networks will remain important players; they need to expand their local offerings and coverage. Smaller players need to grow into local champions.
IN 2010, THE BOSTON Consulting Group published a study on the evolving global distribution market for chemical producers.1 The study identified an increasing need for new approaches to distribution that strike the proper balance between providing differentiated offerings and containing the resulting costs of complexity. In the three years since, the trends we identified have continued to develop, and new market factors for success have become apparent. To map the current competitive landscape for chemical distributors, we updated our findings by evaluating the most recent market data, conducting a comprehensive survey, and interviewing more than 150 key players in the industry—producers, distributors, and customers.

Distribution in the Chemical Industry Is Growing

The chemical industry is large, fragmented, and complex. It includes more than 100,000 products across a range of technical categories, including petrochemicals, solvents, polymers, and customized specialty chemicals, such as those in the cosmetic or food industry. The size of the customer base for these products varies widely, and the marketing, sales, and logistical challenges of these products also increase complexity—some products can only be distributed by pipeline, while others are shipped by tank wagons, containers, barrels, sacks, or packages as small as a few kilograms. Another relevant aspect is the increasing demand for customer-specific solutions in the specialty chemicals segment. As a result, producers face significant complexity in getting their products to customers, and distributors are increasingly considered a vital element of their go-to-market strategy.

Between 2008 and 2012, the global chemical distribution market grew approximately 9 percent annually in nominal terms (or 7 percent excluding inflation) and was worth roughly €165 billion in 2012—corresponding to approximately 10 percent of the market value of all distributable chemicals. (The majority of chemicals are still distributed directly by the companies that produce them.) Such growth outpaced the expansion in chemical consumption worldwide, at a nominal 8 percent per year over the same time period, reaching €2,560 billion in 2012.2

We expect the real growth rate in the chemical distribution market to slow from 7 percent to a stable 6 percent per year within the next five years, mainly due to a weaker underlying economic situation that will reduce chemical consumption. Fundamentally, this means that the tailwinds that have spurred the growth of the chemical distribution market are slowing slightly, and a higher share of future growth is expected to come from increased value-added services. (See Exhibit 1.)
Chemical consumption is the main underlying driver for growth. Between 2008 and 2012, overall growth in the chemical distribution market was due largely to a rebound in chemical consumption. When our 2010 report was published, the industry was coming out of a downturn in 2009 stemming from the global financial crisis; the industry is now in a tentative recovery phase. Chemical consumption has shown slow but steady growth in developed markets—1 percent in Europe and 3 percent in North America. The consumption of chemicals is typically linked to the maturity of industrialization, particularly in rapidly developing economies, in which chemicals—like other basic materials such as steel or cement—form the key ingredients for industrial development. As a result, emerging markets often show above-average rates of chemical consumption, such as Latin America (7 percent) and Africa and the Middle East (8 percent), though these markets are starting from a smaller base. Overall, regional chemical consumption grew fastest in Asia, at 14 percent per year.3

Increased outsourcing to, and extended services offered by, distributors are driving additional growth. There is also growth in the chemical distribution market that is not attributable to expanded chemical consumption. Between 2008 and 2012, growth of roughly 1.2 percent per year resulted from a greater share of outsourced distribution among producers and a broader portfolio of value-added services offered by distributors.

In addition, varying regional developments require distributors to be able to meet very different market needs. For example, in areas like China and (especially) India—which both offer the possibility for strong growth in the chemical distribution market—producers must service a very fragmented customer base (including small purchasers in local markets) via a complex internal or third-party logistics network.
Distributors with the greatest reach (for example, access to difficult-to-reach customers) can stand out from the competition. In mature markets such as the United States, by comparison, the customer base is more consolidated and it is easier for all distributors to achieve a respectable market reach. As a result, more advanced capabilities—mainly industry expertise—are key differentiators for distributors in these markets. For example, being able to cater to the needs of the growing U.S. shale gas industry gives specific distributors a clear advantage in the competition to win an increasing share of this industry’s projected growth over the next five years. (Exhibit 2 shows overall market sizes and chemical consumption rates by country.)

Steady market growth and changing market conditions are the result of developments along the chemical industry value chain. In the discussion that follows, we present the results of our 2013 survey and highlight the key trends that will affect chemical producers, distributors, and customers.

Key Trends Among Chemical Producers
Our 2013 survey reveals that the primary reason chemical producers use third-party distributors has remained consistent since 2010—to reduce complexity in their own sales function by outsourcing distribution to small customers and subcritical markets. However, new considerations, such as value-added services, are increasingly driving the decision of which specific distributor to use. Moreover, these services can potentially protect the distribution margin. (See Exhibit 3.)

Despite the steady growth of distribution outsourcing, most chemicals—about 90 percent of total industry volume—are distributed directly by producers to their end customers. For certain product and customer segments (primarily bulk chemicals and commodities, and large customers that can receive shipments in full tank- or shiploads) direct distribution remains straightforward for producers. (In general, 80 percent of the revenues of a chemical sales portfolio come from 20 percent of its customers, and those customers that buy in bulk are generally the easiest to service. In these situations, third-party distributors can provide little value.)

Complexity drives the decision on whether to outsource distribution; market expertise and value-added services drive the decision on which distributor to use. While producers can distribute to the bulk of their customers fairly easily, reaching the B- and C-level customers that place smaller orders or are located in less-developed regions is more challenging for many of them. As a result, producers typically outsource distribution to these customers. Outsourced distribution is also favored when it comes to specialty chemicals, as compared with commodities. In these cases, greater complexity—in both the breadth of products and the order size and requirements of customers—is driving outsourced distribution. By contrast, specific market expertise and value-added services offered by distributors—such as packaging, mixing, and formulating—influence the decision on which vendor a producer will use. Offering such services helps distributors to expand into new segments of the producers’ value chain.

Access to emerging markets is a critical factor. Our latest survey also finds that the second main reason cited by chemical producers for outsourcing distribution
## Exhibit 2 | Market Size and Chemical Consumption Vary by Region

<table>
<thead>
<tr>
<th>Region/market</th>
<th>Nominal GDP (€billions)</th>
<th>Chemical-consumption (€billions)</th>
<th>Chemicals as a percentage of GDP (%)</th>
<th>Distribution-relevant chemical-consumption (€billions)</th>
<th>Distribution-relevant chemical consumption as a share of all chemical consumption (%)</th>
<th>Share of third-party distribution (%)</th>
<th>Size of third-party distribution market (€billions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Europe</td>
<td>16,170</td>
<td>567</td>
<td>3.5</td>
<td>401</td>
<td>71</td>
<td>11</td>
<td>42.9</td>
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<td>Germany</td>
<td>2,644</td>
<td>119</td>
<td>4.5</td>
<td>86</td>
<td>72</td>
<td>10</td>
<td>8.5</td>
</tr>
<tr>
<td>France</td>
<td>2,029</td>
<td>88</td>
<td>4.3</td>
<td>56</td>
<td>64</td>
<td>9</td>
<td>5.1</td>
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<td>United Kingdom</td>
<td>1,901</td>
<td>42</td>
<td>2.2</td>
<td>26</td>
<td>62</td>
<td>11</td>
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<tr>
<td>Italy</td>
<td>1,569</td>
<td>54</td>
<td>3.4</td>
<td>47</td>
<td>87</td>
<td>11</td>
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<tr>
<td>Spain</td>
<td>1,066</td>
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<td>3.4</td>
<td>24</td>
<td>65</td>
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<td>Other Western Europe¹</td>
<td>3,615</td>
<td>121</td>
<td>3.3</td>
<td>80</td>
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<td>Turkey</td>
<td>614</td>
<td>28</td>
<td>4.6</td>
<td>24</td>
<td>84</td>
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<td>Other Central and Eastern Europe²</td>
<td>1,160</td>
<td>51</td>
<td>4.4</td>
<td>43</td>
<td>86</td>
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<tr>
<td>North America</td>
<td>13,613</td>
<td>393</td>
<td>2.9</td>
<td>215</td>
<td>55</td>
<td>14</td>
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<td>United States</td>
<td>12,198</td>
<td>361</td>
<td>3.0</td>
<td>190</td>
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<td>Asia-Pacific</td>
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<td>1,285</td>
<td>7.3</td>
<td>894</td>
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<td>Japan</td>
<td>4,638</td>
<td>180</td>
<td>3.9</td>
<td>103</td>
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<td>China</td>
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<td>India</td>
<td>1,461</td>
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<td>3.8</td>
<td>46</td>
<td>81</td>
<td>9</td>
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<tr>
<td>Other Asia-Pacific³</td>
<td>5,149</td>
<td>303</td>
<td>5.9</td>
<td>206</td>
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<td>Latin America</td>
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<td>208</td>
<td>4.4</td>
<td>141</td>
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<td>12</td>
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<td>Brazil</td>
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<td>4.6</td>
<td>53</td>
<td>66</td>
<td>12</td>
<td>6.5</td>
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<td>Mexico</td>
<td>916</td>
<td>46</td>
<td>5.0</td>
<td>27</td>
<td>59</td>
<td>14</td>
<td>3.9</td>
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<td>Other Latin America⁴</td>
<td>2,042</td>
<td>83</td>
<td>4.1</td>
<td>61</td>
<td>73</td>
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<td>Middle East¹</td>
<td>3,403</td>
<td>107</td>
<td>3.1</td>
<td>81</td>
<td>76</td>
<td>15</td>
<td>12.2</td>
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<tr>
<td>World (totals and averages)</td>
<td>55,504</td>
<td>2,560</td>
<td>4.6</td>
<td>1,732</td>
<td>68</td>
<td>10</td>
<td>164.8</td>
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</tbody>
</table>

**Sources:** Chemdata International; VCI; BCG market model 2013; BCG interviews, March/April 2013; Oxford Economics; Economist Intelligence Unit.  
**Note:** We have updated data from our 2010 study in order to include the most recent available market data. All data are from 2012. Any discrepancies in totals are due to rounding. Chemical consumption excludes end-user products, such as pharmaceuticals and household chemicals.  
¹Austria, Belgium, Denmark, Finland, Greece, Ireland, Luxembourg, Netherlands, Norway, Portugal, and Sweden.  
²Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Romania, Slovakia, and Slovenia.  
³Australia, Hong Kong, Indonesia, Malaysia, New Zealand, Pakistan, Philippines, Singapore, South Korea, Taiwan, Thailand, Vietnam, and other Asian markets.  
⁴Argentina, Chile, Colombia, Peru, Venezuela, and other Latin-American countries.  
⁵Algeria, Egypt, Iran, Israel, Morocco, Saudi Arabia, and other Middle East countries, as well as South Africa.
remains the same as in our 2010 study—improving market access and geographic reach (for example, through “spearheading” efforts, in cases in which a company may not have an operational presence or sufficient reach in a specific market and uses a distributor to improve access). In particular, this consideration is driving outsourcing to third-party distributors in emerging markets. Such markets offer attractive opportunities for producers to grow their customer base in areas that show increasing chemical consumption—making these markets appealing to international producers. But these markets are also fragmented and thus difficult to cover without appropriate market knowledge, often requiring outsourcing to distributors with local expertise. On the other hand, the promising growth rates in these markets have led some established chemical producers to set up their own in-country sales force. This trend could reduce outsourcing, but it may also lead to a more stable local relationship between producers and customers, with producers serving established key customers directly and letting a third-party distribution partner handle new and smaller accounts.

Producers are also seeking to reduce costs and manage their working capital effectively. Economic factors are driving the shift to outsourced distribution as well. Greater market volatility and cost pressures are spurring producers to reduce costs and manage their working capital more effectively. This economic pressure creates an opportunity for distributors. When distributors provide value-added services such as handling outsourced inventory, producers are able to reduce their own working capital needs, while also mitigating inventory risks and enabling long payment terms to the end customers (who are also under economic pressure). “Our suppliers ask us to give much more accurate and up-to-date revenue forecasts than a few years ago,” noted one regional distributor in Europe. “Deviations are not allowed, as the suppliers want to optimize their inventory.”
As a result, a distributor’s financial stability is critical for producers, and a distributor’s instability is considered the principal reason for switching to another vendor. (Some 75 percent of respondents to our 2013 survey identified financial challenges as a reason to switch distributors, compared with just 26 percent of respondents in 2010.) Financially weak distributors, especially smaller companies in currently challenging markets, may not have sufficient capital to continue operating. They will either shut down or merge with a larger player. This trend has intensified since 2009, not only in economically troubled regions such as southern Europe but also in Latin America and China. We expect that competitive pressures will prolong producers’ focus on reducing costs and managing working capital even after the economy recovers.

**Cost pressures are driving consolidation in distributor relationships.** Just as producers seek to reduce complexity by outsourcing to distributors, they are also reducing complexity by limiting the number of distributors they deal with—across regions and/or industries. Among our survey findings, 50 percent of producers are either currently reducing or plan to reduce the number of their distributor relationships.

Similarly, the geographic emphasis of distribution partnerships has shifted, reflected in the way that producers oversee their relationships with multiple distributors. Three years ago, 60 percent of respondents coordinated their distributor relationships on a national level, and 40 percent on a regional or global level. Today, that balance has flipped, and the majority of producers have global or regional distributor relationships (95 percent), rather than purely national relationships (5 percent). We expect this trend to continue, toward coordinated distributor management across business units (for example, by setting contract standards, defining evaluation criteria for distributors, or preparing audits).

The next step for producers is to move to global preferred partnerships, which put large distributors at a distinct advantage over smaller competitors with limited geographic coverage. “We are looking for a global distribution partner who can be a single go-to point and who can complement our regional distributors,” said one international chemical supplier. Still, the expertise of a distributor in the respective business-unit-specific segment and the target geography remain key criteria. And preferred partnership arrangements also bring a new set of requirements—for example, aligned strategic goals and operating standards between producers and their distributors.

The preferred-partnership trend is at different stages that vary by region. It is already well under way in North America and Europe. For example, in 2011, BASF restructured its North American distribution network, signing agreements with nine distributors for its personal care division, replacing a more complex arrangement in which each product line had multiple distributors.4 And while this trend is just starting in emerging markets, it will likely accelerate.

Despite this consolidation trend, local experts with local industry expertise are still needed because large international distributors cannot cover all geographies and industrial niches. “When you’re looking to find a partner in a certain local market and industry segment, there isn’t much choice,” said a representative from one
international distributor that services Europe, the Middle East, and Asia. “Really only a few partners—and not always the largest ones—can offer you the best mix of industry and local market expertise.” Therefore, international distributors will still need to improve their reach and knowledge in certain regions and industries in order to win market share from local competitors.

In addition, expectations are rising among producers regarding the geographic reach of their preferred distribution partners. What was considered a satisfactory reach among survey respondents in 2010 is not anymore. Some distributors, such as Brenntag and Univar, have extensively increased their global reach and made significant acquisitions; but when distributors take steps to meet increased expectations, producers ratchet up their requirements even higher.

Key Trends Among Distributors

The distributor model is continuously evolving in order to meet changing market demands. But it still fulfills the same basic function as in 2010—chemical distributors play a critical role in matching supply and demand in a fragmented market. To that end, they execute several functions: sourcing from multiple producers to ensure a broad and complementary product offering; taking physical ownership of the products and storing them until needed; mixing, blending, and repackaging products according to customers’ needs; and finally selling and physically transporting products to customers. There are two other types of distribution models that are not relevant to this discussion: logistics-only companies (which typically do not take ownership of products) and trading companies (which typically do not repack and assemble product portfolios according to their customers’ needs).

There are few powerhouse distribution players, but the market is consolidating. Today, the distribution market remains fragmented, with top companies dominating specific markets but few global powerhouses. As of 2011—the most recent year for which full company data are available—the three largest global distributors held a combined global market share of 12.5 percent (Brenntag at 5.9 percent, Univar at 4.7 percent, and Nexeo Solutions at 1.9 percent).

However, there are significant regional differences. North America is the most consolidated market, where the same three distributors hold a market share of 39 percent. By comparison, Asia is not only the largest distribution market but also the most fragmented; the number one player in Asia, the distribution section of Sinochem International, controls only 3.8 percent of the total share. (See Exhibit 4.)

Over time, we expect increasingly challenging conditions for small distributors, with producers favoring medium-sized local champions and large international players. Some 77 percent of survey respondents confirm these shifts, which have been shaping the market for the past several years and are likely to intensify in the future.

Consolidation is driven by preferred partnerships, regulation, and M&A. There are three main factors driving consolidation. The first is the reduction in the number of distributor relationships maintained by producers in favor of preferred partnerships (as noted above).
The second driver of consolidation is increasing regulation. New rules such as REACH in Europe—registration, evaluation, authorization, and restriction of chemicals—are currently being implemented. Similar regulations are likely coming in the United States, along with rules calling for an upgrading of facilities (such as in Brazil) and stronger environmental regulations (such as in China). While some markets still remain largely unregulated—including Africa and the Middle East—those are clear exceptions, and the trend toward increased regulation is expected to continue. The regulations place new burdens on midsize and larger operators, yet the challenges are correspondingly larger for smaller distributors that do not currently comply in many cases and cannot justify the investments needed to do so. Small-scale distributors in emerging markets are therefore at a crossroads. Either they “institutionalize” their businesses (for example, by fully implementing the measures necessary to comply with applicable regulations) or they will face increasingly stiff challenges.

The third major force spurring consolidation among distributors is M&A. Over the past several years, large international distributors have sought to increase their global footprint through acquisitions, particularly in emerging markets. As a result, large international distributors are building up sufficient market expertise that they are becoming legitimate alternatives to local players in many emerging markets. They are not yet on a par everywhere in terms of market insights, but they are
close. And they have an advantage in that they have standardized operations and are thus more professional. As one global producer put it, “When we go into a new geographic market, the perceived fragmentation is actually much lower. Only the top 20 players in each market can comply with our standards.”

While local distributors have captured a significant share of emerging markets growth—such as Sinochem International in China (which posted a compound annual growth rate of 49 percent from 2008 through 2011), ICC Chemical in Asia (22 percent), and quantiQ and M.Cassab in Latin America (31 percent and 27 percent respectively)—international distributors, with a few exceptions, either were not in those markets or were just getting established. One example of a distributor that has rapidly increased its footprint in emerging markets is the chemical distribution market leader, Brenntag, which has grown its revenues in Asia from €15 million in 2008 to more than €400 million in 2011, making it the number five regional player. Despite this growth, the Asian market share is still smaller for distributors than for producers. The leading non-Asian diversified chemical companies (BASF, Dow, and DuPont) realize, on average, 18 percent of their sales in Asia, while the three leading distributors (Brenntag, Univar, and Nexeo Solutions), realize only 5 percent of their sales in Asia.

Moving forward, international distributors will most likely gain a higher share of the growth in emerging markets. They have built up local knowledge and networks and can more easily fulfill the increasing quality standards. And as emerging markets mature, the increased presence of international distributors in those markets will drive the professionalization of third-party distribution, making it more attractive to international producers. As one supplier said, “In 2008, you had to go with a local distribution partner in China. Now, internationals are there and know the market sufficiently well.” We believe that this trend will continue, and international distributors will capture more of the growth in emerging markets such as Asia. In addition, global producers—which tend to outsource distribution in emerging markets to established international players—are expected to increase their local presence.

That said, international distributors will never be able to completely replace small and medium-sized local champions, especially those with strong relationships in place and the means to continue building their local networks with industry-specific service offerings. “When we look for a specialized distributor,” said one European chemicals supplier, “we often use local or regional players who just have better expertise in a very specific niche.”

M&A activity has shown signs of slowing—due to a lack of targets with sufficient quality, size, and market knowledge—and is now shifting to more clearly reflect distributors’ priorities. In mature markets such as the United States and Europe, large and medium-sized players are acquiring smaller companies with specific industry expertise. For example, U.S. market leader Univar has built up oil and gas industry expertise. In emerging markets, by comparison, large distributors are seeking companies that can help them expand their geographic reach. In the future, once their footprint is established, renowned distributors may shift their M&A focus in emerging markets to acquiring specific industry expertise, however there are few indications of such deals thus far.
As noted above, value-added services and deeper integration across the value chain are key trends for the future. In 2010, 18 percent of the producers who participated in our survey chose a distributor for its value-added services. By 2013, that number had risen to 40 percent. Again, there are regional differences, and the degree of value-added services in a distributor’s service model will vary depending on the maturity of the market. In early emerging markets such as Africa, distributors are likely to offer a very basic model that is oriented around reliable logistics. In more advanced markets, such as Asia, there is a strong need for “logistics-plus” services, such as simple packaging, filling, mixing, and vendor-managed inventories. And in mature markets such as the United States and Europe, distributors are increasingly becoming full-service partners of chemical producers, offering advanced technical and formulation services.

This trend will continue to play out for the foreseeable future, and opportunities for value-added services will increase in all markets. (See Exhibit 5.) Specific services with high growth potential include the following:

- **Vendor-managed inventory.** Some 21 percent of distributors who participated in our 2013 survey said that they get requests from producers regarding this service, and 62 percent said that they expect it to gain importance over the next five years. (In addition, 40 percent of customers said that inventory management is already important to them today.)

- **Mixing, blending, and formulating.** Nearly half of the distributors who took part in our survey reported getting requests for this service, and 69 percent expect that it will grow in importance. While mixing and blending services for some markets are partially commoditized, they may become more essential in others. For

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**EXHIBIT 5 | Distributors Expect Growth in Vendor-Managed Inventory and Formulation**

<table>
<thead>
<tr>
<th>Service</th>
<th>2013</th>
<th>In five years</th>
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<tbody>
<tr>
<td>Filling, packaging, labeling</td>
<td>34</td>
<td>66</td>
</tr>
<tr>
<td>Mixing, blending, formulating</td>
<td>48</td>
<td>69</td>
</tr>
<tr>
<td>Customs handling</td>
<td>38</td>
<td>41</td>
</tr>
<tr>
<td>Bundling of sourced material</td>
<td>38</td>
<td>48</td>
</tr>
<tr>
<td>Vendor-managed inventory</td>
<td>21</td>
<td>62</td>
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<tr>
<td>Others</td>
<td>24</td>
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</tr>
</tbody>
</table>

Source: BCG March/April 2013 market interviews and survey.

*In responding to our 2010 survey, 38 percent of distributors noted that they expected the demand for technical services to grow.*
example, U.S. shale gas requires individual blends, due to the varying composition of each individual shale gas basin.

Worth noting is that while packaging services remain important, they are largely commoditized. As a result, the perceived relevance of this service offering by distributors is decreasing.

In addition, the increasing emphasis on value-added services may bring HR challenges to some distributors, who may experience difficulty finding employees with the required technical expertise. As the CEO of one international distributor based in Russia said, “We have difficulties getting staff with broad technical expertise and good knowledge. This will become more important in the future.”

**Key Trends Among Customers**

The range of companies that buy chemicals is extremely broad—not only across different manufacturing sectors but also in terms of varying sizes (from multinational conglomerates to small, local manufacturers with as few as ten employees). Small customers are a particular challenge for chemical companies that may lack the infrastructure and processes to handle the distribution of low-volume purchases and products that are not in great demand. These challenges notwithstanding, our research indicates a few broad trends among customers.

**Increased market volatility is putting a focus on pricing.** First, just as producers have had to deal with increased market volatility due to macroeconomic issues, so too have the companies that buy chemicals. Many of these companies are facing reduced demand for their own products in local markets—for example, in southern Europe and selected emerging markets—and reduced demand for export goods.

Because of this volatility, it is not surprising that price has become even more important for customers when they purchase chemicals. Price was the top criterion in 2010, cited by 61 percent of our survey respondents, and that number grew in 2013, when 86 percent of respondents to our survey cited price as their primary consideration.

Customers are not necessarily focused on the price of the individual chemical. Instead, customers are interested in lowering the cost of their overall purchase—that is, their total cost of ownership. In our interviews, customers noted that they have specific initiatives in place to do just that, such as outsourced inventories managed by vendors; help with purchasing processes and systems; flexible and responsive delivery terms to keep stock low; and customized packaging that has been specifically adapted to their supply chain. Under the comprehensive view of the total cost of ownership, customers will be willing to pay distributors for these services, as long as there is a clear business case for doing so.

**Customers are looking to streamline purchasing.** The second trend among customers also has a parallel among chemical producers—the need to reduce the number of distributors they work with. In our findings, 29 percent of customers are currently planning such a step. Many customers have developed tenders for key supply segments, indicating that they want to bundle and simplify their sourcing.
Just like producers, many are also looking for preferred supplier relationships. Because customer companies have specific requirements regarding geographic reach and expertise, they will not be able to consolidate their distribution to a single vendor. In general, customers increasingly prefer international players with global reach. This preference points to continued gains in share for international distributors, provided they can continue to improve their industry expertise and geographic footprint. Last, for large orders, especially of commodity products, customers will likely continue to buy directly from producers, due to better sourcing arrangements.

Success Factors for Producers and Distributors

While the long-term projections indicate a growing market for third-party distribution, there are some key steps that individual companies—both producers and distributors—can take to strengthen their competitive position.

**Best practices for producers.** Chemical producers should reorganize their distribution networks on a regional and cross-business-unit level, and they should establish a consistent model for managing their distributors. A center for distribution management can help achieve this objective, by aligning the overall portfolio of distributors along products, customers, and regions. In addition, such a center can institute standard processes and rules across business units and markets. Over the longer term, producers will need to streamline their distribution networks, reducing the number of relationships, while striking the right balance between a global/regional strategy (which generates efficiency) and local reach and expertise (which can help the producer win in individual markets).

Last, producers should seek to make their relationships with distributors more akin to partnerships, rather than perceiving distributors as mere vendors. With the right approach, producers can get the best service offering for the product bundle to be outsourced, and ensure that both sides are working together toward common goals with maximum transparency.

**Best practices for distributors.** Specific success factors for distributors vary by the size of the company. Small and medium-sized distributors will need to ensure their survival by complying with local regulations—particularly in emerging markets—and establishing financial stability. If they lack critical mass and sufficient volume, they will have to partner with competitors or seek an acquisition or merger. Once their viability is assured, they can differentiate themselves and build market share by specializing in a way that larger competitors cannot. This process entails developing a differentiated offering in a specific niche, with local expertise, value-added services, and real adaptation to supplier needs. The small distributor model will work best in two situations: specialty chemicals with a high need for technical knowledge, and regions in which outsiders do not yet have any local insights or where access and reach are difficult.

For large, international distributors, the competitive priorities are different. Primarily, these companies must continue to increase their reach and industry expertise via M&A in key categories, such as fast-growing sectors (oil and gas or...
water treatment, among others). In emerging markets, in which buyout candidates are becoming scarce, they must stay vigilant in order to identify the right targets—for example, medium-sized companies that are unable to comply with evolving regulations. When growth into local markets is not possible through M&A, these companies will need to take steps that extend their reach through organic measures.

In addition, large distributors should focus on establishing preferred partnerships at both the regional and global level. Accordingly, they must build strong regional positions, which will increase their attractiveness for preferred partnerships in the most promising markets (for example, Asia).

When it comes to service offerings, large distributors—which are often financially more stable than smaller ones—should take the following steps. First, they should focus on offerings that decrease the total cost of ownership for customers, such as inventory management. These offerings effectively free up working capital for customers, helping them remain agile in challenging market conditions. Second, in terms of specialty products, large distributors need to invest in formulation and technical labs in order to build up their expertise in key industries, especially in developed markets. This investment will allow them to offer more sophisticated services and take over larger elements of producers’ business, boosting their revenue ahead of the industry’s overall growth. In the mid- to long term, this attention to specialty products will become more relevant for emerging markets, where the demand for specialty chemicals is likely to grow, thus increasing the need for related services. Thus, global distributors will have to spread their segment-specific know-how in specialty chemicals from established markets into emerging markets.

We found through our 2013 survey—just as we had through our 2010 survey—that the third-party chemical distribution market had outgrown overall chemical consumption in the preceding several years. We expect that it will continue to do so for the foreseeable future. There is a clear opportunity for distributors to create value. But to fully capture the potential value in various customer segments, distributors will need to develop a differentiated offering—one that requires operating on a global scale and across industries in order to realize benefits of scale and scope and one that creates efficiencies for both chemical producers and end customers.

Notes
2. Growth rates are expressed in nominal terms, reflecting sales in Euros. Excluding currency effects, the nominal growth rate of the distribution market is roughly 6.5 percent per year.
3. Excluding currency effects, the nominal market growth in chemical consumption per year, from 2008 to 2012, was roughly 2 percent for Europe, –1 percent for North America, 6 percent for Latin America, 8 percent for Asia, and 7 percent for the Middle East and Africa.
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