



Indian Specialty
Chemicals Industry:
ready for a
quantum leap

June 2023

Foreword >>

Indian Chemical Industry: A Path Towards Global Leadership

The Indian specialty chemicals industry has emerged as a vital component of our nation's economic growth and development. It has exhibited resilience and adaptability, demonstrating consistent growth amidst a rapidly evolving global economic landscape.

They are the key enablers that enhance the performance, efficiency, and sustainability of various products and processes.

The specialty chemicals sector, expected to contribute significantly to overall industry growth, is anticipated to reach \$40 billion by 2025¹. Additionally, India has established itself as the 14th largest exporter of chemicals globally, positioning the country as a key player in the international market.

The initiatives taken by the government to support the industry have been commendable. Policies such as the Public Procurement (Preference to Make in India) policy, along with schemes like the establishment of plastic parks and centers of excellence, the Chemicals Promotion and Development Scheme, and the Proposed New Petroleum, Chemicals and Petrochemicals Investment Region (PCPIR) Policy 2020-35, have played a crucial role in shaping policy formulations and driving this sector forward.

Despite recent challenges faced by the global chemical industry, including the impact of the geopolitical tensions in Europe and demand fluctuations, there is significant belief on the resilience of the specialty chemicals sector in India. As we navigate through this phase, it is essential for companies to focus on their core competencies, strengthen backward and forward integration, and leverage strategic thinking to enhance in-house efficiencies, develop new products, and harness emerging technologies.

The Ministry of Chemicals and Fertilisers has labelled the industry as a sunrise sector and is working towards implementing the Production Linked Incentive (PLI) scheme to boost domestic production and exports. This recognition further validates its role as a crucial contributor to industrial and agricultural development, providing vital building blocks for downstream industries.

While pursuing growth and expansion, it is crucial to prioritize sustainability and environmental consciousness. The specialty chemicals industry should embrace green technology, minimize its environmental impact, and work towards achieving a net-zero carbon footprint in the future. The government's support for environmental investments and the establishment of industrial parks with efficient effluent treatment systems will contribute to the vibrancy and global competitiveness of our industry.

ASSOCHAM, as the apex chamber of commerce and industry in India, actively champions the interests of the Indian industry. Through its national councils on chemicals and petrochemicals, the chamber consistently engages with central and state governments, advocating for policies that foster industry growth and competitiveness.

ASSOCHAM thanks EY, India the knowledge partner, for their support in creating this insightful report that will be helpful for all stakeholders. We hope that the Chemical Conclave provides a platform to bring together all stakeholders to collaborate, innovate, and adapt to the evolving landscape of the chemicals industry, especially as it transitions towards going green.



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Preface »

The Indian specialty chemicals sector looks at a period of fast-paced growth driven by several market forces. India is emerging as a preferred manufacturing hub for specialty chemicals for domestic and export markets.

Approximately 20% of the total chemicals market in India², the specialty chemicals sector has been playing a pivotal role in driving the chemicals industry's growth.

The Indian chemicals industry is a major player in the global market, ranking 6th in production and 14th in exports³. The sector provides essential building blocks and raw materials for many industries, including agrochemicals, pharmaceuticals, textiles, paper, paints, and soaps. It is valued at US\$220b, and projected to grow by approx. 9% p.a. during 2020-25 to reach US\$300b by FY 2025. The sector is expected to hit the US\$1t mark by FY 2040.⁴

Indian specialty chemicals companies are at their lifetime high capex with healthy revenue and earnings growth over FY19-22. They benefit from strong demand from global clients as they look beyond China and increase domestic consumption. Stock prices are also at their lifetime peak and remain well above global valuations.

In the future, strong demand uptick from domestic and international markets will continue to aid revenue growth for Indian specialty chemical players. This growth will result in strong earnings in the medium term and sustain high valuations. Companies with robust chemistry and technical skills and a healthy balance sheet are expected to continue outperforming cyclical/ bulk commodity players, which may experience price volatility once China ramps up production in CY23.

The fast-paced growth of the Indian specialty chemicals industry is inevitable. However, companies will need agility to adapt quickly to the evolving macroeconomic and industry landscape to ensure sustainable and transformative growth over the longer term. They also have to focus on customer value creation through product differentiation, identification of customer needs through focused customer collaboration, and building resilient supply chains supported by higher investments in R&D and digital. They must reduce their carbon footprint by adopting alternative methods that create a green ecosystem. The industry will seek continued government support to create a business-friendly environment and world-class infrastructure, including additional PCPIRs and feedstock availability to fuel growth.

In conclusion, while the macroeconomic levers of growth, such as rising population and increasing disposable income coupled with exports, will provide the requisite tailwinds, the Indian specialty chemicals industry will need to consciously focus on innovation, decarbonization, digitalization, automation, and investing in skilling its workforce to make the quantum leap.



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Executive summary

The global specialty chemicals industry has grown steadily in the last few years. The APAC region's emerging economies have been the main driving force behind the growth in various sectors such as construction, cosmetics, adhesives, plastics, and water treatment. There are several factors that are expected to contribute to the rapid growth of India's industry. These include the abundance of available labor, favorable government policies, easy access to suppliers, and a well-developed infrastructure. The Indian specialty chemicals sector will be worth more than US\$60 billion by 2026 as urbanization and industrialization grow. Construction, flavor and fragrances, homecare ingredients, water treatment chemicals, and dyes and pigments would constitute the highest growth sectors, although other sub-sectors also hold good growth potential overall.

India has a significant cost advantage over other markets, enabling it to become one of the fastest-growing specialty chemicals sectors globally. Labor and power costs in India are a mere fraction of the global average, and the sector is growing at twice the worldwide average rate.

Besides that, the Indian government has put in place various stimulus packages to aid the industry during and after the COVID pandemic. As a result of these factors, the Indian specialty chemicals sector is witnessing healthy growth. Various other factors are contributing to the development of the industry in India. The European energy crisis has also led to an increase in demand for the sector in India. India's limited reliance on natural gas and lower production cost may shift a lot of global supply chains towards India.

Sustainability is a top priority for all industries globally, and the specialty chemicals sector contributes to it in various ways, including clean energy, water and waste management, and overall circular economy development. As China's dominance in the global supply chain destination continues to reduce, the Indian specialty chemicals sector is increasingly growing in relevance globally. This report discusses some of India's most high-growth specialty chemicals segments and the key strategies for success in the Indian market.

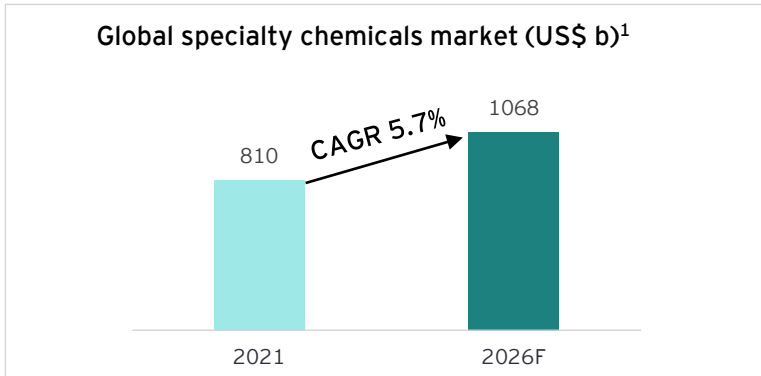
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Specialty chemicals industry at
a glance

Global specialty chemicals market overview

Specialty chemicals sector is expected to grow at a steady pace of 5.7% until 2026 and cross US\$1 trillion market size with major growth coming from the APAC region (46% revenue share)

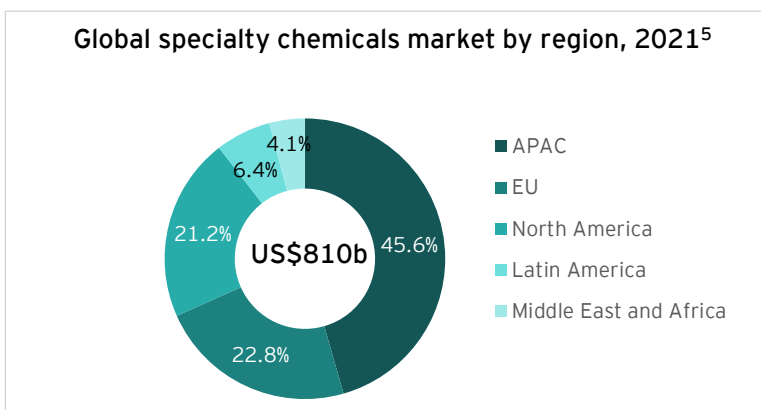
Global specialty chemicals industry	 5.7% CAGR from 2021-26	~46% Market share of APAC region in 2021	Agrochemicals and fertilizers have the highest market share (~28%) in the global specialty chemicals market
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Source: Axis Capital

The global specialty chemicals market is witnessing a **steady growth** over the last few years. The market is expected to grow further, driven by **robust demand** from end-use industries such as **construction, water treatment, personal care** along with **rising demand in emerging economies of the APAC region**.

Stringent regulations pertaining to **emission norms** along with integration of digital technologies in operations are expected to transform the specialty chemicals industry.

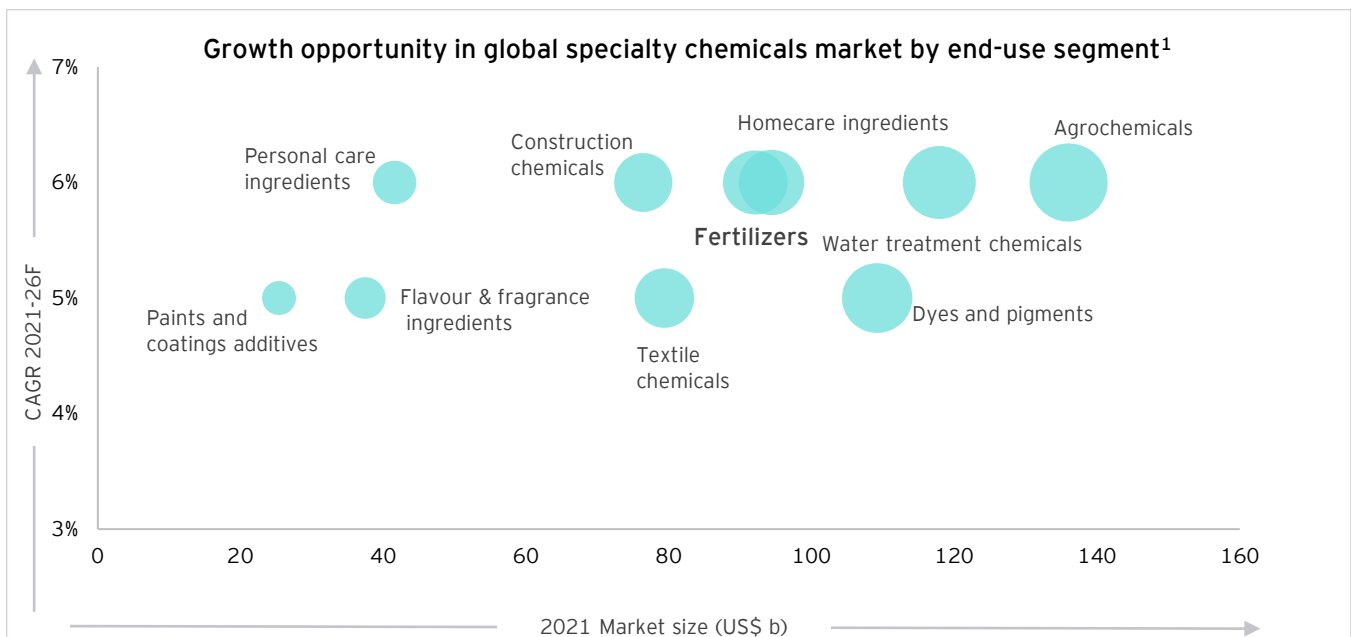


Source: Secondary research, EY analysis

APAC is the leading market for specialty chemicals and is expected to grow further. Demand for cosmetics, electronics, adhesives and plastics from the packaging industry, along with water treatment systems is expected to drive the market.

Factors include low cost and high availability of labour, attractive government policies, supplier availability and infrastructure support to facilitate growth.


China (~58% of APAC market share) and India (~8% of APAC)⁵ are the dominant players owing to rapid urbanization and industrialization.



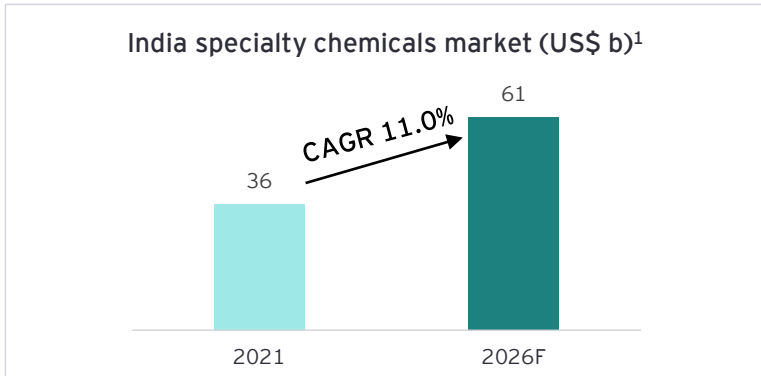
Source: Axis Capital

Indian specialty chemicals market overview

Indian specialty chemicals market is poised for a strong growth and is expected to be worth more than US\$60 billion by 2026, driven by rising demand in end-user industries due to rapid urbanization and industrialization

Indian specialty chemicals industry	 11.0% CAGR from 2021-26	Construction chemicals segment is expected to witness the highest growth	4th largest producer of agrochemicals globally (as of 2021)
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Source: Chemicalmarketforecast.com

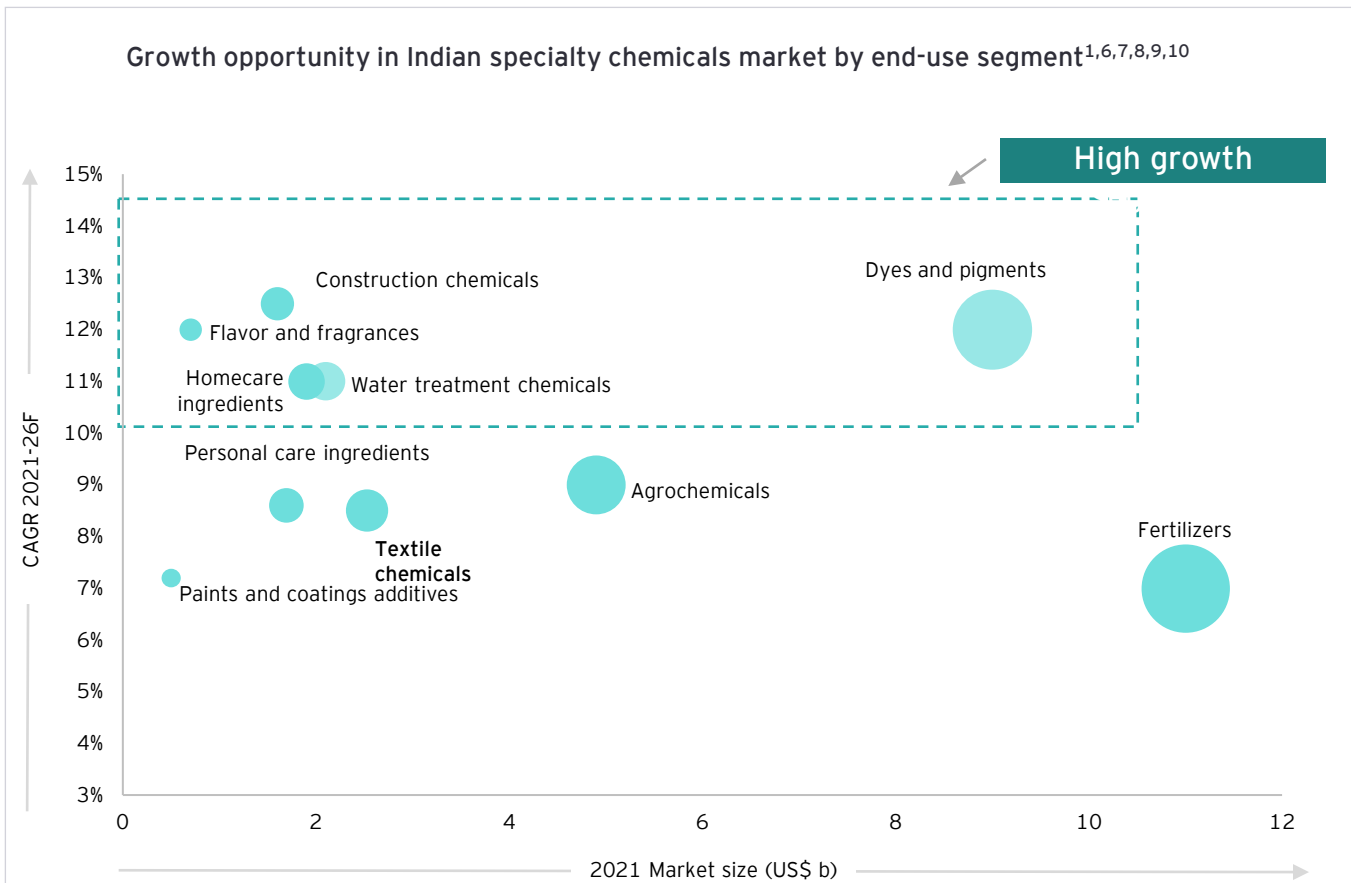


Source: Axis Capital, EY analysis

Indian specialty chemicals market is expected to grow strongly and register a double-digit CAGR till 2026. Growing population, rising disposable income and increasing exports are key factors contributing to the growth.

Low-cost manufacturing, process engineering expertise, and sufficient workforce supply have made India a favoured manufacturing destination for global businesses.

The specialized chemicals business in India is **highly fragmented**, with a few scaled-up firms in most segments.



Source: Axis Capital, secondary reports, EY analysis

Rise in demand in **end-user industries** (due to increasing population and urbanization), along with **increased investments** in infrastructure development is facilitating

the growth of key segments such as construction, fragrance and flavors chemicals, along with dyes and pigments.

Global vs. Indian specialty chemicals industry

Factors such as lower labour and power costs, along with rising demand are contributing to India's higher growth rate compared to global players

Global vs Indian industry		~6%	~2x	US\$1/hour
		India's share in global specialty chemicals market in the next five years	India's specialty chemicals growth rate compared to the global market	Manufacturing labour cost in India compared to global average of ~US\$25/hour

Source: Chemicalmarketforecast.com

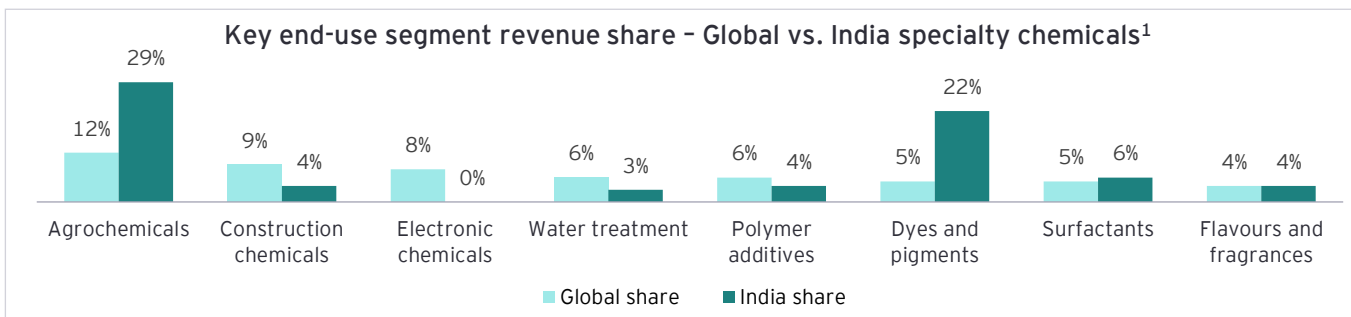
Global and Indian specialty chemicals industry market size and growth comparison¹

Market size	2021 (US\$ b)	2026F (US\$ b)	CAGR %
India	36	61	11.0%
Global	810	1068	5.7%

Source: Axis Capital, EY analysis

Several factors are proving to be beneficial for India when compared to developed economies, where the specialty chemicals market is already penetrated and manufacturing costs are high.

For example, rapid urbanization, increasing disposable income, rising living standards, and growing industrialization, along with low labor cost are resulting in higher growth of the specialty chemicals' market in India.



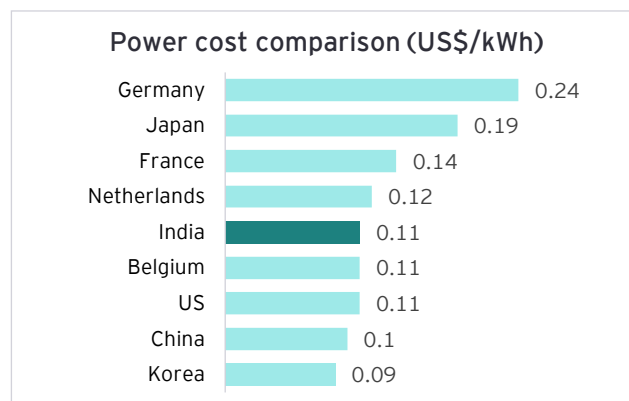
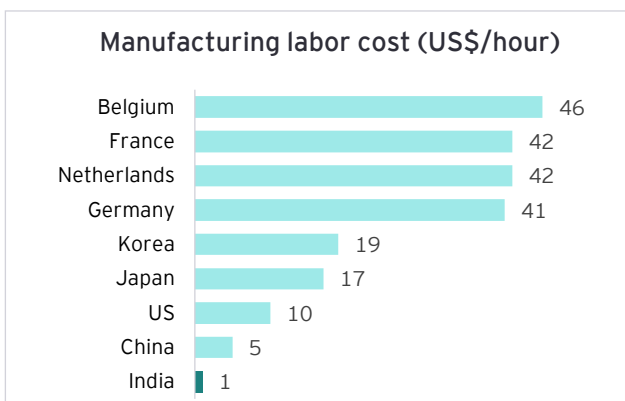
Source: Axis Capital, Jan'22

India has a large revenue share from agrochemicals due to relatively higher operational scale, high captive demand, rising exports and global acceptance.

Sectors such as construction, water treatment chemicals

along with flavors and fragrances and dyes and pigments are expected to witness high growth due to high rate of urbanization and industrialization along with rising income levels in India.

Global vs. India manufacturing cost comparison¹



Source: ILOSAT, Axis Capital, Jan'22

The cost of labor and power in India is very competitive compared to other developing and developed countries.

Since labor cost accounts for a significant share in the

fixed-cost component of chemicals manufacturing, overall production cost is low, having a positive impact on profit margins.

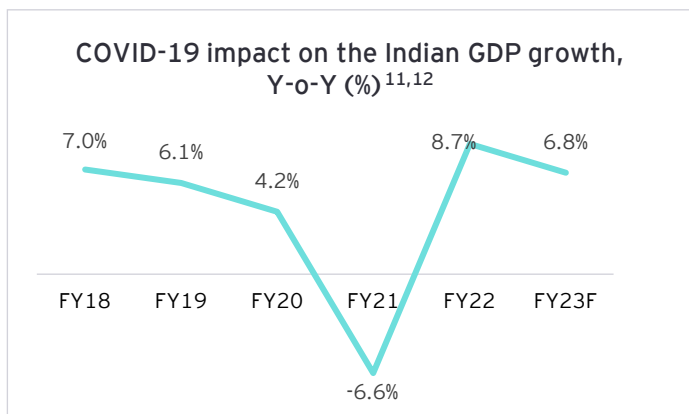


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Key trends and implications for
Indian specialty chemical players

Impact of COVID -19 on Indian specialty chemical industry

Though the COVID-19 outbreak led to unprecedented disruptions in the Indian specialty chemicals industry, it soon bounced back due to an increased demand for hygiene related and packaging products

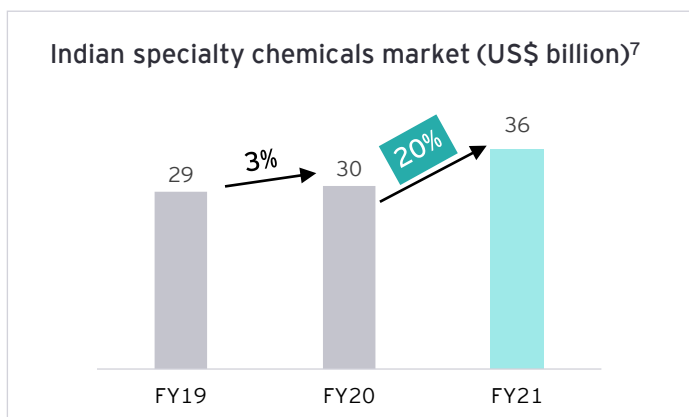


Source: India Briefing, RBI

India has exhibited an average 7% GDP growth rate in the last 20 years despite major recessions and economic slowdowns.

However, the country's GDP contracted by 6.6% in FY21 owing to the COVID-19 pandemic, followed by a **bounce back** of 8.7% in FY22, surpassing the major economies in the world.

India's economy witnessed a **V-shaped recovery**, supported by the **government's stimulus packages**, **strong market demand** and the **vaccination drive**.



Source: Secondary research, EY analysis

Indian specialty chemicals players witnessed a **low Y-o-Y** growth in FY20 due to the COVID-19 pandemic, along with factor such as market volatility and geopolitical challenges.

However, the market **rebounded** in FY21 as specialty players adjusted operations to tackle disruptions. Moreover, **increased health consciousness** increased demand for hygiene products, facilitating the rebound.

By May 2021, almost all specialty manufacturers had resumed operations (despite intermittent disruptions), with **capacity utilization levels at more than 80%**.⁷

Indian specialty chemicals industry growth during COVID-19

The industry was impacted by COVID-19 induced **supply chain disruptions**, but was one of the first to return to **normalcy**. Specialty chemicals **distribution networks** were in demand, even during the lockdown.

- COVID-19 induced disruptions faced by Indian specialty chemical players**

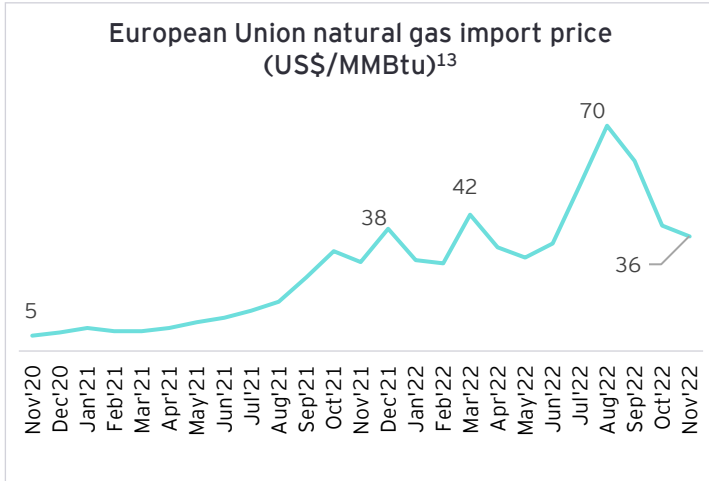
 - ▶ Limited transportation facilities, stock pile-ups at ports and unavailability of labour at plants impacted product processing and loading.
 - ▶ The supply chain however, realigned as the pandemic prompted multinational companies to seek suppliers beyond the Chinese market.
- Sub-segments that witnessed neutral to positive impact of COVID-19**

 - ▶ Increased demand for **flavors** (packaged foods), **fragrances** (sanitizers and soaps), **personal care ingredients** (hygiene products).
 - ▶ High demand for **polymer additives** (packaging) and water disinfectants, partially offset by a decline in automotive and industrial activity.
- Sub-segments that witnessed a negative impact of COVID-19**

 - ▶ Muted demand for **textile chemicals** due to headwinds in end-use market.
 - ▶ **Construction chemicals** demand negatively impacted due to decline in construction activity.

European energy crisis and implications for Indian specialty chemical players

While the overall impact of the European energy crisis may still be uncertain, the Indian specialty chemicals industry might witness increased export demand for inorganic chemicals in the mid to long-term



Source: Ycharts

350%
Y-o-Y increase in natural gas prices during the peak month of August 2022

The Europe energy crisis led to a rise in the already **high natural gas prices** in the EU starting in March 2022.

Energy inflation, production outages, and logistical challenges are resulting in higher costs of production for European specialty chemicals.

Gas shortage is over 70% in Europe, with winter demand expected to be 30% higher than for the rest of the year.¹⁴

Impact of the crisis on Indian specialty chemical players^{15,16}



Low dependence on natural gas

74% of electricity generation in India was via coal in CY21. Indian companies, hence, are **not much affected by rise in natural gas costs** as far as power costs are concerned.

Lower costs may help in shifting production lines to India

Over the medium-term, lower costs may translate into **more order wins, production lines shifting from Europe to Asia, and steady market share gains for Indian incumbents** (particularly those that have vertical integration or operate in higher-margin or niche value chains).



Exports for inorganic chemicals increased, while organic chemicals saw a decline in FY22

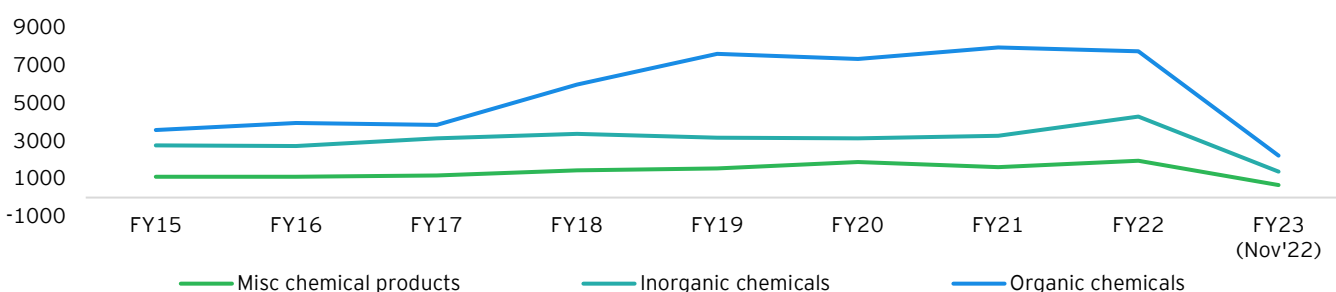
Chemical exports from India have witnessed an **8% CAGR** over FY12-22, with growth in the export of organic and inorganic chemicals at 9% and 5% resp. However, **organic chemical exports have fallen Y-o-Y in FY22** since most raw materials (methanol and acetic acid) are **imported into India and were impacted by the energy crisis**.

Lower costs may help in shifting production lines to India

Since **India is a net importer of crude oil**, a key raw material in specialty chemicals manufacturing, the **sharp increase in prices** due to geopolitical tensions proved to be challenging for the sector. Brent crude prices saw an increase of ~65% between December 2021 and the peak in June 2022 (before stabilizing slightly by November 2022).¹⁷



Chemical exports from India (tmt)¹⁵



Source: Motilal Oswal

Implications of China+1 on Indian specialty chemical players (1/2)

Geopolitical unrest, COVID-19 norms and environmental reforms in China are necessitating the need for alternative suppliers; India offers the advantage of low-cost labour and favourable investment policies

China's competitive advantage weakening

Lower labor costs, high subsidies (capital and export) and relaxed environmental norms were among the key factors that led China to dominance in the global specialty chemicals industry. However, many of these factors have proven to be unsustainable in the long run.

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China's **labor cost is on a sharp rise** since 2008 due to policy changes and is no longer the cheapest. As a result, **India** has emerged as a competitive region with one of the lowest labor costs globally.
- 

Stricter implementation of **pollution-control measures** and **withdrawal of subsidies** have weakened China's cost advantage.
- 

Relocation of toxic manufacturing plants to dedicated industrial parks, along with higher **operational and capital costs**, have adversely impacted the operations of Chinese specialty chemical companies, resulting in large **supply-chain disruptions**.

Global players shift to China+1 strategy, India stands to benefit

The US-China Trade war led specialty chemical players to look beyond China as a raw material supplier and manufacturing hub.

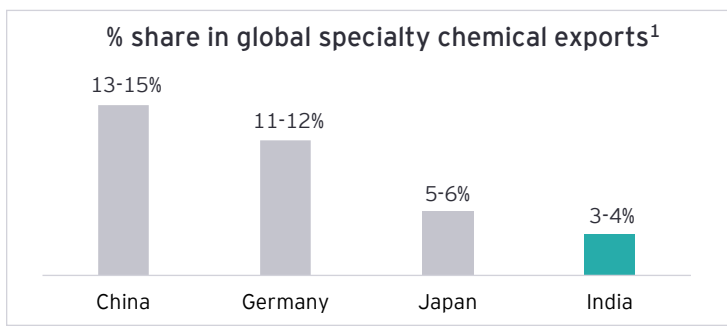
This shift was facilitated by the COVID-19 pandemic, which severely impacted global supply chains and highlighted the importance of diversified sourcing.

Global players are therefore focusing on a China+1 strategy to de-risk their supply chains.

India is in a unique position to benefit from the shift away from China owing to **competitive cost advantage** and **incentivized government policies** and reforms (such as allowing 100% FDI in chemicals). For instance a global specialty player in 2021, formed a JV with an Indian glycols player and plans to invest in ethylene oxide derivatives.

China's production capacity in **agrochemicals** is limited, proving beneficial for Indian players as they expand capacities (an Indian agrochemical company and an intermediates player are expanding production capacities).

~US\$8 billion
 Opportunity for Indian specialty chemical players if a 5% market share is shifted from China to India (currently China constitutes ~20-25% share in the global specialty chemicals market).⁷



China had benefitted from **shift in global chemicals manufacturing from Europe** over last two decades and has become the key player in global chemicals space with key focus in the bulk chemicals space (benefitting from economies of scale given large capacities). This has led to China occupying **~39% share in global chemical exports**. Of China's export dominance, **bulk chemicals account for >80% share**, while **specialty chemicals account for ~15%**.¹

Source: Axis Capital, Jan'22

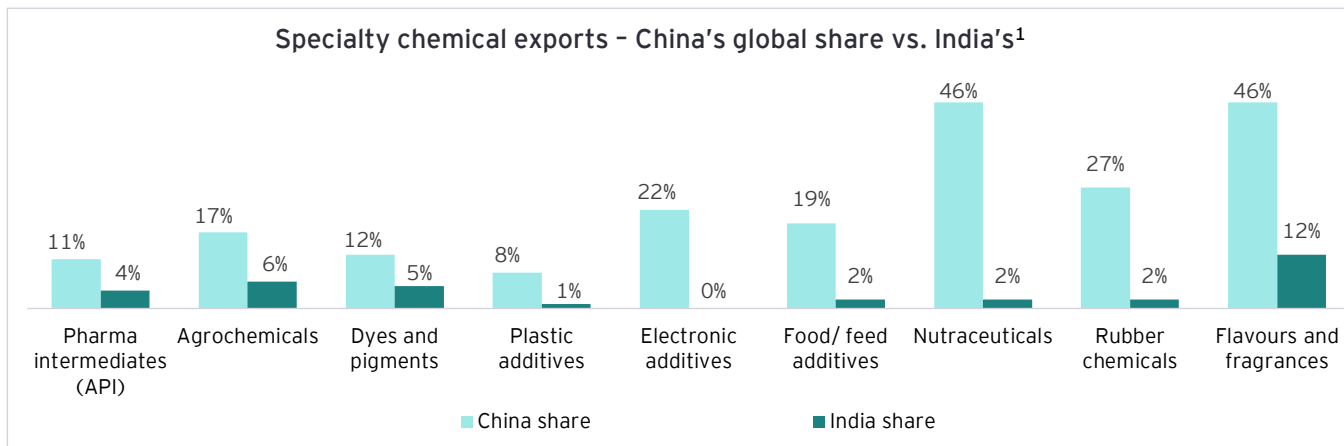
Source: Axis Capital

Implications of China+1 on Indian specialty chemical players(2/2)

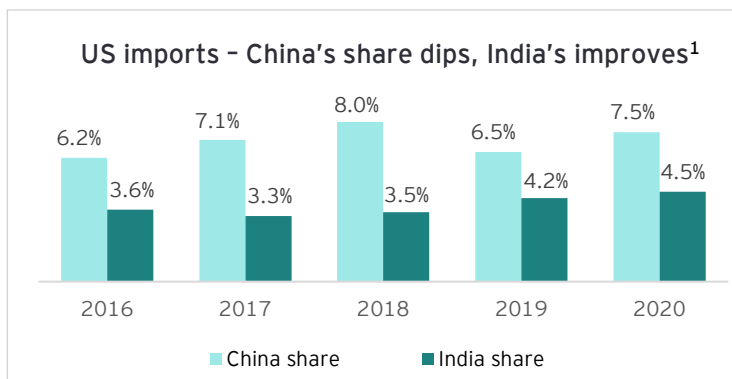
Indian specialty players stand to gain in specialty chemicals exports due to increasing interest from global clients; Companies have also been on a record capex spree to meet rising demand due to the shift away from China

While China has its advantage in bulk chemicals, there is a lot for India to gain in the specialty chemical space as Indian players have been garnering significant interest from global clients (Europe, Japan and now US also) and witnessing a steady wallet share gain.

Potentially, a 20% shift in specialty chemical supply chain from China to India can almost double the size of Indian industry.¹



Source: Axis Capital, Jan'22



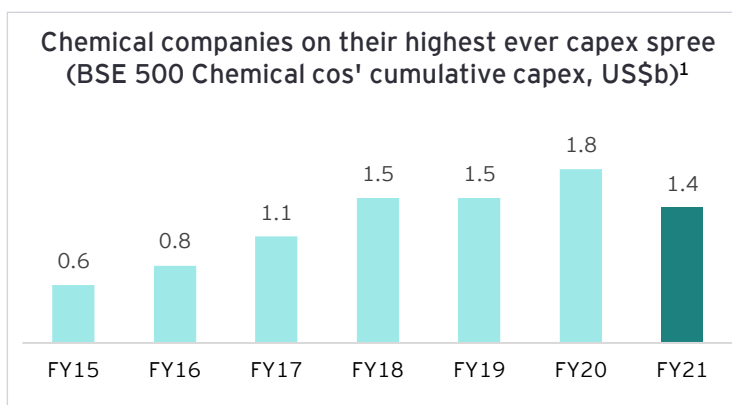
Source: Axis Capital, Jan'22

Europe and Japan have had a steady relationship with Indian specialty chemical suppliers over the years.

Currently, **US-based clients** have also increased their business enquiries due to its strict stance on China (duties imposed earlier on multiple products) and imposition of anti-dumping duties.

This can further help **drive up size and scale** for Indian specialty players.

Indian specialty chemical players building capacity to meet rising demand as a result of the shift away from China



Source: Axis Capital

Capex by Indian chemical companies are at record highs and are expected to remain elevated as Indian specialty **players build capacities to benefit from the expected demand from the shift away from China.**

Even historically, annual capex spends have seen a **steady rise** since FY17 (dip in FY21 possibly due to pandemic-led delays) wherein annual capex run rate has almost doubled from FY12-16 to FY18-21.



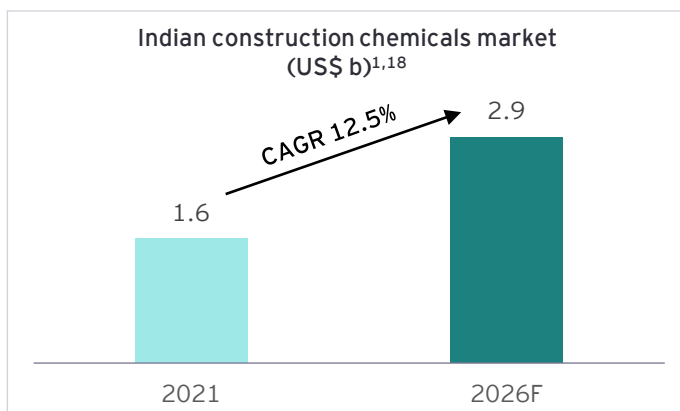


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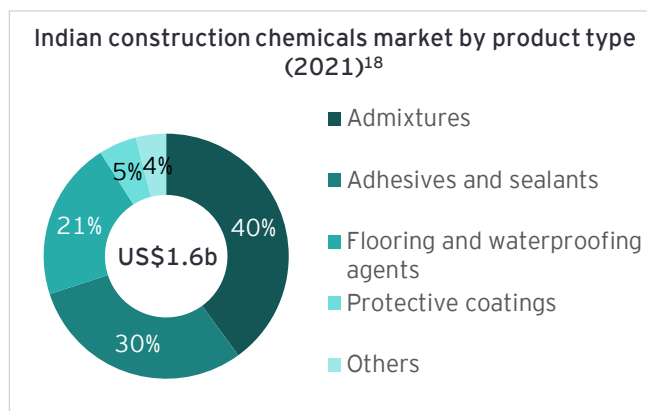
Key high-growth specialty
chemicals segments in India

Construction chemicals

Rising infrastructure demand, government initiatives, FDI and R&D investments are expected to drive growth in the Indian construction chemicals market



Source: Axis Capital, MaKreo report



Source: MaKreo report

Despite the slowdown caused by the COVID-19 pandemic, the Indian construction chemicals market rebounded quickly as the economy re-opened and demand recovered.

The market is dominated by organized players, with a balance of domestic and multinational companies, driven by the rising demand for high-quality construction chemical goods.

Construction chemicals improve quality of construction, increase productivity, and extend the life of structures. In 2021, admixtures accounted for the largest market share owing to the rising urbanization.

Market drivers



- ▶ **Government initiatives** such as 'Make in India', 'Smart City' plan and 'Housing for All' program are boosting the demand for construction chemicals.
- ▶ Population growth and economic development has increased the need for **transport infrastructure**, including roads, railways, and aviation, waterways.
- ▶ **Heavy investment in R&D**, has led to new techniques for construction that save time and cost, generating higher profits.

Emerging opportunities



- ▶ **Increasing Foreign Direct Investment**
100% FDI in construction development and real estate assures a boost in construction industry which is the second largest FDI recipient at US\$26b (Apr'00 to Mar'21). For instance, a French construction company plans to invest US\$53m for infrastructure projects in India by 2026.¹⁹
- ▶ **Rising demand for maintenance of existing substrates**
India is experiencing a rapid rise in urbanization and new structures, presenting a growth opportunity for flooring chemicals, sealants, admixtures, waterproofing, grouts for maintenance and repair.
- ▶ **India-Japan Trade Deal**
Japan has signed an agreement with India in 2021, providing a loan of US\$2.2b for infrastructure projects including Metro rail, waste management, clean construction and sustainable urban development.¹⁸

Strict environmental regulations

Stringent regulations discrediting the use of construction chemicals (formaldehyde, alkyl phenol and chlorinated polyethylene), have been put in place by various countries affecting their demand.

Restraints to growth

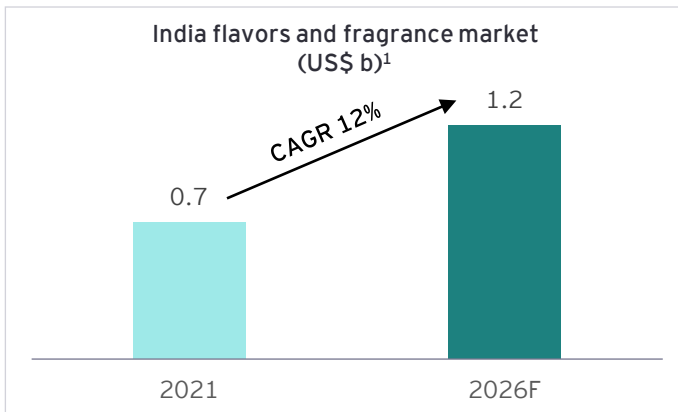


Low awareness among Indian consumers

Construction chemicals market in India is not as technologically advanced compared to major economies like US and China due to the lack of awareness among consumers in both rural and urban areas regarding new chemical techniques in construction.

Flavors and fragrances

Rapid urbanization, increased product differentiation and rising exports are facilitating the growth of India's flavors and fragrances market, making it one of the fastest growing markets in APAC



Source: Axis Capital

India is **one of the fastest growing** flavors and fragrance markets in the world.

The flavors and fragrance market has a high growth potential in India due to an increase in **disposal income**, along with the **rapidly evolving retail landscape** and **influx of multiple global brands**.

Market drivers



- ▶ **Urbanization rate** in India is set to increase to 45% in the next 40 years.⁷ Urban areas have a range of distribution outlets and cater to almost every individual in India.
- ▶ Most parts of the country in India experience **long summer and monsoon season** increasing demand for products such as deodorants, anti-perspirants, body talc and perfumes.
- ▶ India is a **significant exporter** of fine fragrance raw materials and is the world's largest supplier of mint, apart from jasmine and sandalwood. The country also provides ingredients for perfumery.

Emerging opportunities



- ▶ **Demand for organic flavors and fragrances**
Rising incomes and popularity of healthy food habits has created the demand for organic flavors and fragrances. In addition, stringent FSSAI regulations have forced companies to adhere to food safety standards facilitating the shift toward the use of natural food flavors in products.
- ▶ **Increasing product differentiation**
F&F companies are focusing on increasing demand from tier 2 and tier 3 cities and are launching a range of affordable deodorants, perfumes and colognes. They are also developing products inspired by aloe vera, pinebark and soy to cater to the growing demand for nature inspired flavors.
- ▶ **Packaged food proves to be a key industry**
India's packaged food industry was valued at US\$35b in 2021 and is expected to double in the next 5-10 years to US\$70b.²⁰ Packaged foods require high additive flavors to preserve the taste hence the rising demand.

Restraints to growth



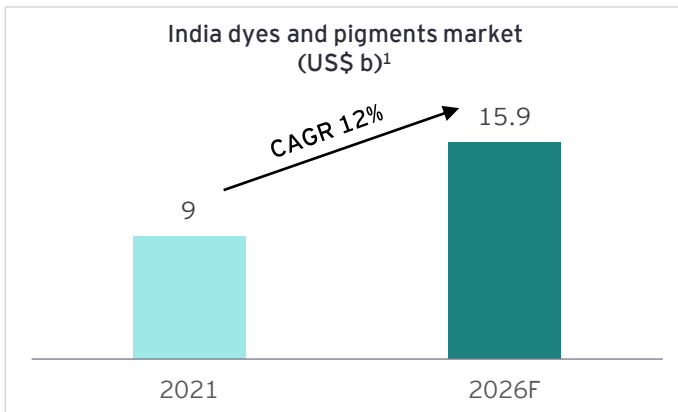
Lack of cold chain infrastructure in India

Since certain flavors and fragrances are perishable, they require cold chain logistics, which is still in a development phase in India.

In addition, **power outages or electricity fluctuations** can cause the breakdown of the powered cooling systems. Coolant failures and poor cooling circulations can also impact the cold chain management, leading to increased costs due to the maintenance needs.

Dyes and pigments

The growing beauty and paints and coatings industries, along with the emergence of eco-friendly dyes and rising R&D investments are expected to shape the dyes and pigments market in India



Source: Axis Capital

The dyes industry in India is expected to witness a **steady growth** in the coming years due to **environmental crackdowns** in China, resulting in a shutdown of several domestic dye companies. India is better placed due to the availability of the ecosystem, **feedstock, technology, and compliance** required for the industry.

Dyes find its applications in textiles, food, paper, and leather, among others.

Pigments find wide applications in paint and coatings, plastics, printing inks, and textiles sectors, among others.

Market drivers



- ▶ **Increasing demand for personal care products** such as **cosmetics**, which is a key end market, is driving demand for dyes and pigments. The Indian beauty industry is growing rapidly due to globalisation and the introduction of multiple new brands in India.
- ▶ Growth in the Indian **paints and coatings industry** (CAGR of 7% during 2021-27),²¹ is estimated to be one of the fastest-growing application sectors driving the market's growth. Architectural and decorative coatings account for a major consumption of pigments.

Emerging opportunities



- ▶ **Eco-friendly dyes**
Many textiles companies are adopting eco-friendly dyes for producing textiles and fabrics due to their positive environmental impact. Since most eco-friendly dyes are expensive, synthetic dyes and pigments manufacturers can focus on developing cost-effective organic alternatives.
- ▶ **Rising investment in R&D**
Synthetic dyes and pigments manufacturers are increasingly investing in R&D activities and technological innovation such as temperature resistance to develop products with enhanced physical and chemical properties.

Restraints to growth



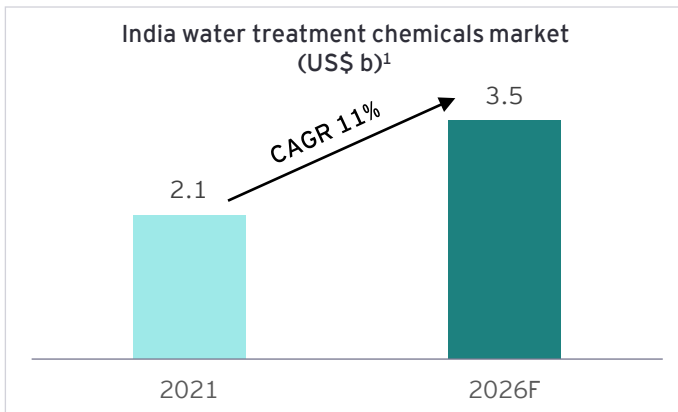
Toxicity of certain dyes and pigments

Since dyes and pigments are used in the cosmetics and apparel industries, they may have **side effects** on the human health.

Therefore, certain chemicals may face the scrutiny of regulations in the near term as the awareness about environmental and health impact increases.

Water treatment chemicals

India's water treatment chemicals segment is on a growth trajectory owing to rising demand in end-user industries, favorable government initiatives and stringent regulations for wastewater treatment



Source: Axis Capital

Water treatment chemicals (for e.g., biocides, disinfectants, coagulants, flocculants, corrosion inhibitors, defoamers, pH adjusters and softeners) process wastewater before it is reused or disposed off, to facilitate **longer equipment life** and follow **environmental regulations**.

Industries that utilize water treatment chemicals are power generation, oil and gas, chemical manufacturing, mining and mineral processing, municipal, food and beverage, along with pulp and paper.

Market drivers

- ▶ **Government initiatives** such as the **Swachh Bharat Mission (Urban) 2.0 (2021)**, allocated **INR159 billion** to states/UTs for wastewater or used water management. Furthermore, in the **Union Budget 2022**, the Govt of India (GoI) announced a package of **INR600 billion** to provide drinkable water to every household, thus boosting the demand for water treatment chemicals in the country.²²
- ▶ **Growing demand in end-user industries** such as chemicals, mining and mineral processing along with oil and gas in India has necessitated the need for water treatment chemicals.

Emerging opportunities

- ▶ **Power sector to dominate the market**
The Indian power sector, which is a key market for water treatment, is undergoing a significant change due to growing electricity demand in line with sustained economic growth. Thus, growing power generation from fossil sources and increasing installations of nuclear power provides a boost to the water treatment chemicals market.
- ▶ **Increasing demand for corrosion and scale inhibitors**
Due to a significant increase in the use of industrial equipment such as water boilers, heat exchangers and cooling systems, the demand for inhibitors is increasing to prevent metal loss.
- ▶ **Stringent regulations related to wastewater treatment**
As environmental awareness has increased, several jurisdictions in India have established reuse policies and Zero Liquid Discharge regulations to regulate water pollution, thus providing a growth opportunity for water treatment chemical players.

Restraints to growth

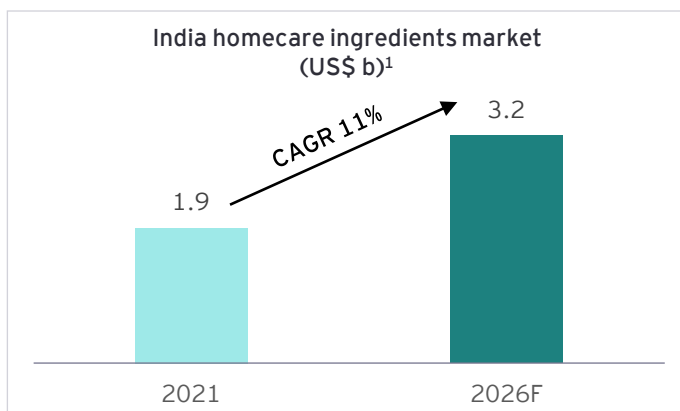
Toxicity of water treatment chemicals

Chemicals used to treat water may also have **side effects** on the human health, which can impact their demand in the future.

Bromate, chlorite, haloacetic acids and trihalomethanes are by-products of water disinfection. These chemicals are linked to an increased risk of cancer, anaemia, liver problems, kidney problems and effects on the nervous system.

Homecare ingredients

Increased awareness regarding hygiene, along with flexible government regulations and a boost in healthcare and housing sector is facilitating the rise of Indian homecare ingredients market



Source: Axis Capital

India continues to be an evolving market for homecare ingredients due to **favourable government regulations and increasing purchasing power** of the population. Additionally, **low-cost labour and lower cost of production** make the country a good manufacturing hub for home care ingredients.

Surfactants, enzymes, fragrances, pH adjusters, solvents, and dyes, among others, are used in manufacturing home care products such as **floor cleaners, toiletries, detergents, and surface cleaners**.

Market drivers



- ▶ **Increasing incidence of various infectious diseases and the COVID-19 pandemic** changed buying behaviour of Indian consumers and prompted them to buy home cleaning products in bulk. For instance, ~70% of people surveyed in urban areas agreed to buying home cleaning products in bulk in 2020.²³
- ▶ Home care ingredient manufacturers are expecting growth driven by **flexible government regulations** and the 'Make in India' and 'Vocal for Local' campaigns.
- ▶ Demand for cleaning chemicals is high among the household segment owing to the **large population base**, thus leading to the higher consumption of home care products.

Emerging opportunities



- ▶ **Setting up of new healthcare buildings and boost in the housing sector** is expected to propel the market for home care ingredients in India.
- ▶ **Expected rise in the tourism industry in India**
In the Union Budget 2022-23, INR24b (US\$289 m) has been allocated to the Ministry of Tourism which is 18.4% higher Y-o-Y.²⁴ International hotel chains are increasing their presence in India, thus boosting demand for home care products.
- ▶ **Emergence of inexpensive products**
Emerging economies such India, and China are witnessing an increase in the number of inexpensive products in the market, since customers are expected to remain price-centric.

Restraints to growth



Lack of awareness in India's rural areas can hamper growth

Poverty in India is a major challenge to the adoption of premium cleaning products. A huge population of the country lives in rural areas, villages, and slums. Lack of health and hygiene awareness in such areas can be a restraint to the market's growth.

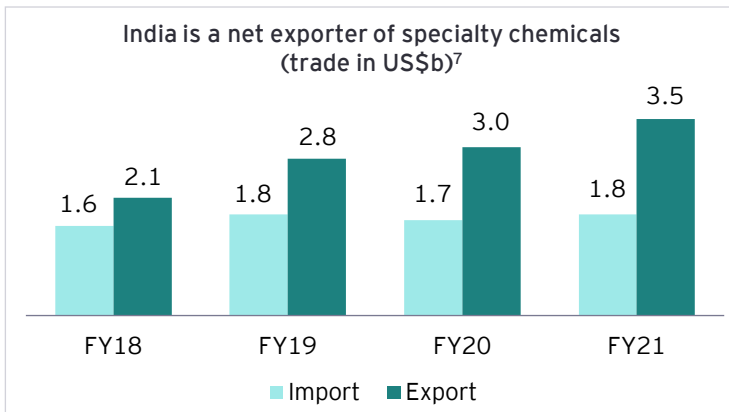


04

Key strategies for success in the
Indian market

Import substitution and cost competitive manufacturing

Indian specialty chemical players stand to take advantage of the expected rise in domestic demand and government initiatives to replace imports and manufacture/ source locally



Source: Axis Capital

India is already a net exporter of specialty chemicals owing to **low-cost manufacturing capabilities**, strong **standards of environmental compliance** and an increased number of products meeting the globally acceptable registration requirements, such as REACH.

However, the country still has import substitution potential due to the **net import** nature of sectors such as **dyes and pigments**, along with **certain polymers** (acrylic).

~US\$1 billion²⁵

Worth of chemicals were imported in India during FY22 offering a huge substitution potential.

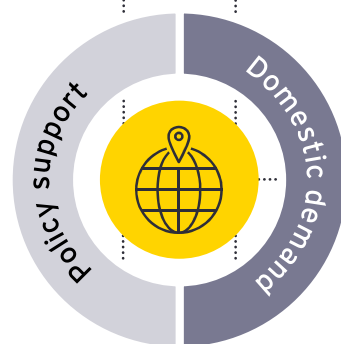
Due to high expected growth of these products, Indian players can bolster their earnings

India imports	FY22 opportunity
Benzene and toluene	~US\$470m
Epoxy resins, dapsone, resorcinol, p-cresols, pigments, dyes	~US\$330m
Fluorochemicals	~US\$330m

Specialty players in India can leverage policy support and a rising domestic demand to substitute imports and develop capabilities within the country

Some sub-sectors such as agrochemicals rely on imports for their raw materials. Schemes such as 'Make in India' are encouraging Indian companies to **backward integrate and manufacture intermediates** or replace imports by domestic sourcing.

The Government of India (GoI) announced setting-up of a **vision 2034 for chemicals** blueprint, exploring opportunities to improve domestic production, reduce imports and attract investments in the sector.



Per capita consumption level of chemicals in India is one-tenth of the global average, providing substantial domestic opportunity to specialty chemical players.

Rapid urbanization and a growing younger population with **disposable income** is expected to convert into rising discretionary demand for end user industries.

Due to the COVID-19 lockdown and ultimate realignment of the supply chain, a number of end user industries such as packaging, **substituted their international suppliers with domestic ones.**

Enhancing R&D spending to compete with global industry

Indian specialty chemical players need to increase focus on research and development in order to meet rising global demand for specialized products and be at par with global competition

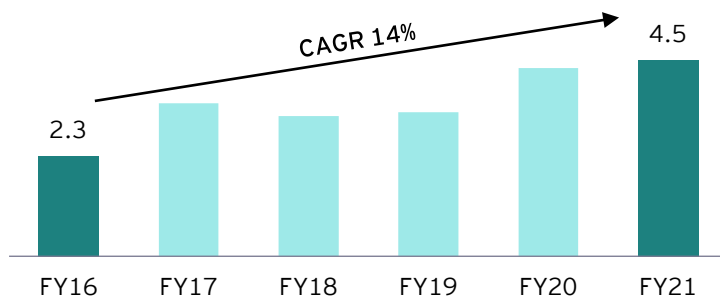
While average R&D spends (as % of revenue) of Indian specialty chemicals industry stands at ~1.5%, it varies from **0.5-3% of revenue** across key players (vis-à-vis 6-10% spent by global counterparts), highlighting the **potential for increasing R&D spending**²⁶

Strong **global demand** for **specialised chemicals** has led to a rise in the number of molecules under synthesis across key specialty players.

This has urged the need to **enhance R&D expenditure in terms of facilities and manpower** to meet this demand (else lost business opportunity).

However, **low availability of skilled technical manpower** can emerge as a challenge in the medium term.

Total R&D spend for top 10 Indian specialty chemicals companies (INR b)¹



Source: Axis Capital



The Indian specialty chemicals sector is expected to see an increase in R&D spending in the near-term.

The key areas of focus are expected to be **process improvisation, application engineering and new product development.**

Gol views R&D as key for self-reliance and plans to streamline it by launching **Production linked incentives and National Chemicals Policy**. Gol has also set up **CIPET*** with a focus on skill training and research.

The **COVID-19 pandemic** accelerated the push towards operational efficiency, cost and asset management. Specialty players are therefore investing in R&D and innovation to generate sustained growth.

Key drivers for R&D growth

Global clients are consolidating their vendor base for **efficient supply chain management**. Thus, Indian specialty companies are **expanding their core domain into adjacent chemistry** to capitalize on client relations, thus driving R&D.

Global clients are **outsourcing complex new molecule R&D to strategic partners**. India's low cost manufacturing, process expertise and IPR protection policies make it a preferred destination for **contract research manufacturing services**.

Indian specialty chemical players can focus on digitalization to bolster R&D and operations

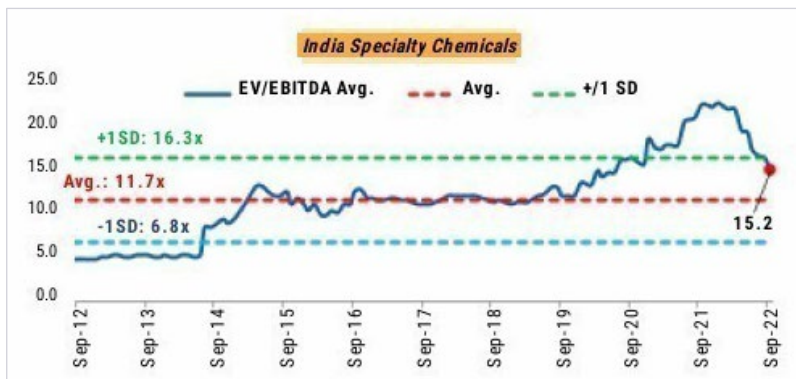
- ▶ **Building capabilities via digitalization:** Companies can adopt digital solutions (automation, digital simulation, AI and predictive analytics) to build manufacturing efficiencies for cost reduction, online product information and sales portals, and supply chain optimization.
- ▶ **New developments in manufacturing processes:** Prototyping and parallel experimentation supported by data analytics can help **improve response time**. In addition, digitalization can improve **traceability** and enable **quality assurance** of chemicals in **critical manufacturing processes**.
- ▶ **Digitalization in R&D and resource planning:** A leading global chemicals company is following an **integrated approach to digitalizing R&D** with focus on data science and connected knowledge systems. In India, a leading specialty chemicals player is building an **Enterprise Command Centre** on current ERP system to monitor data and information in real-time, ensuring operational efficiency.

*Central Institute of Plastic Engineering and Technology

Increasing M&A, IPO and investment in Indian specialty chemicals industry

India's cost-effective high growth potential in specialty chemicals is driving increased number of deals and facilitating IPOs at a premium price

Indian specialty chemical stock multiples have seen lesser corrections compared to global peers in the last 10 years²⁷



Indian specialty chemicals have **outperformed** regional and global peers both on a YTD basis as well as over the past two years due to the **broad-based correction** across global industry.

Keys to this have been **multi-year contract wins, greater investments into specialty products and improved pricing for key chemicals.**

In the near-term, **valuations are expected to remain elevated** despite macro headwinds.

Source: Company data, Morgan Stanley research estimates

Key M&A drivers for global players

Cost-effective manufacturing hub	Scale of assets	Access to high growth Indian market
<ul style="list-style-type: none"> ▶ Primarily driven by low-cost labour, production cost in India is lower than that in developed nations. ▶ Availability of skilled manpower and connectivity to South East Asia and Middle East, make India a preferable manufacturing hub in Asia. 	<ul style="list-style-type: none"> ▶ The specialty chemicals industry has a lot of scaled up assets, especially in larger sectors such as agrochemicals, flavors and fragrances, and dyes and pigments. ▶ This provides an attractive platform for global players to enter the market. 	<ul style="list-style-type: none"> ▶ The Indian specialty chemicals market is highly under-penetrated. ▶ It is expected to double its share in the next 5 years, making it an attractive market for players from developed nations where the growth rates are much lower.
Backward integration and supply chain realignment	Fragmented nature of the industry in India	Stretched timelines to set up greenfield ventures
<ul style="list-style-type: none"> ▶ India has companies manufacturing ingredients used by specialty chemical companies. ▶ Global players are looking to acquire these companies to control sourcing and fast track the development of new ingredients. 	<ul style="list-style-type: none"> ▶ The Indian specialty chemicals market is highly fragmented. ▶ Presence of small to mid-sized family-owned players with limited capital, management expertise and technology, make them attractive targets for M&A. 	<ul style="list-style-type: none"> ▶ Setting up a greenfield project in India can be time consuming as multiple permissions and clearances are required. ▶ Comparatively, acquiring another company is a faster route for an MNC as no uncertainty is involved.

Indian specialty chemicals IPOs are receiving favourable response due to high growth projection of the industry along with demand factors^{28,19,30,31,32}

Company	IPO date	Premium
Archean Chemicals	Nov'22	~11%
Tatva Chintan Pharma	Jul'21	~95%
Laxmi Organics	Mar'21	~20%
Rossari Biotech	Jul'20	~58%

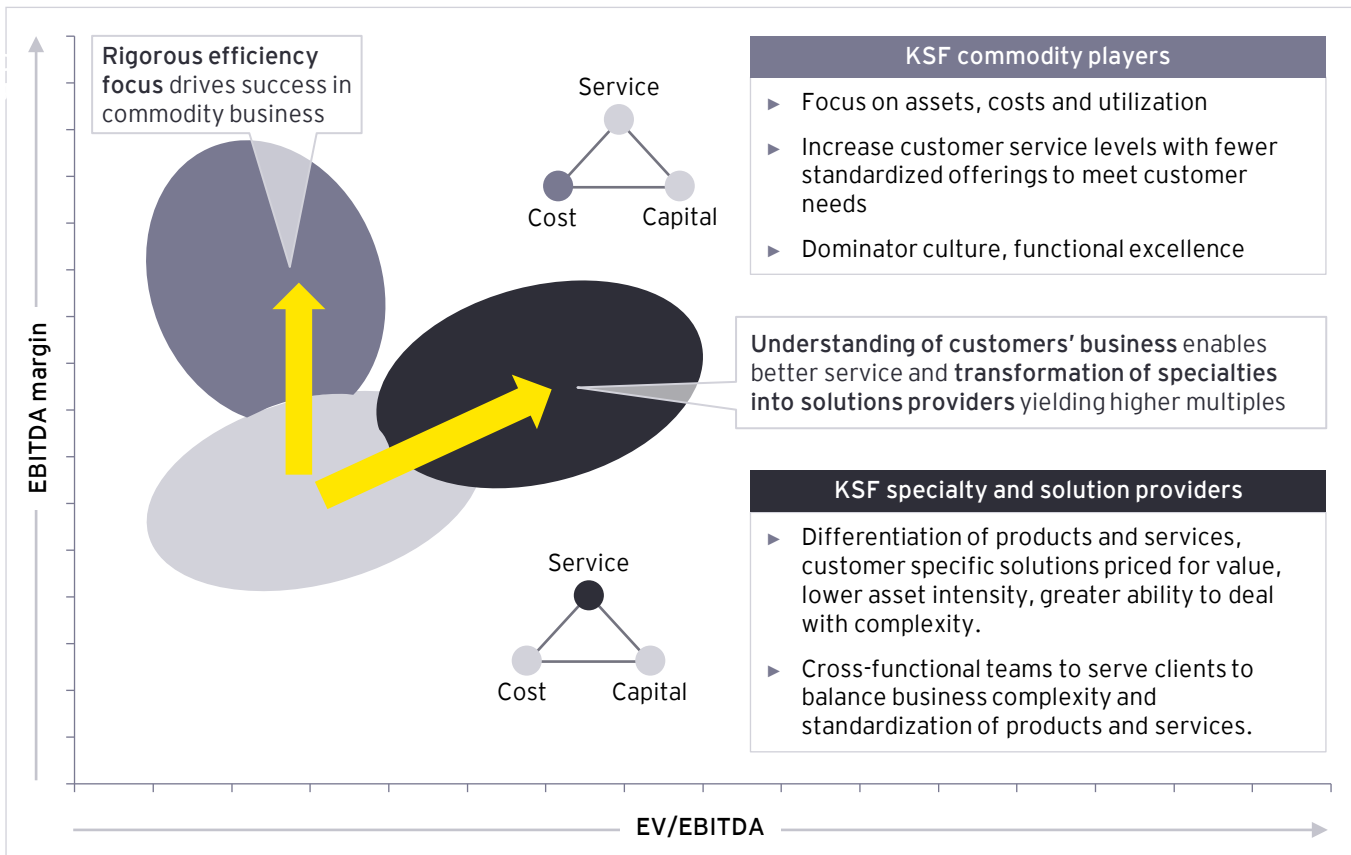
A number of specialty chemical companies are going the IPO route and receiving **premium prices** with high valuations.

Investors continue to remain optimistic about the strong growth outlook for the specialty chemicals industry in India.

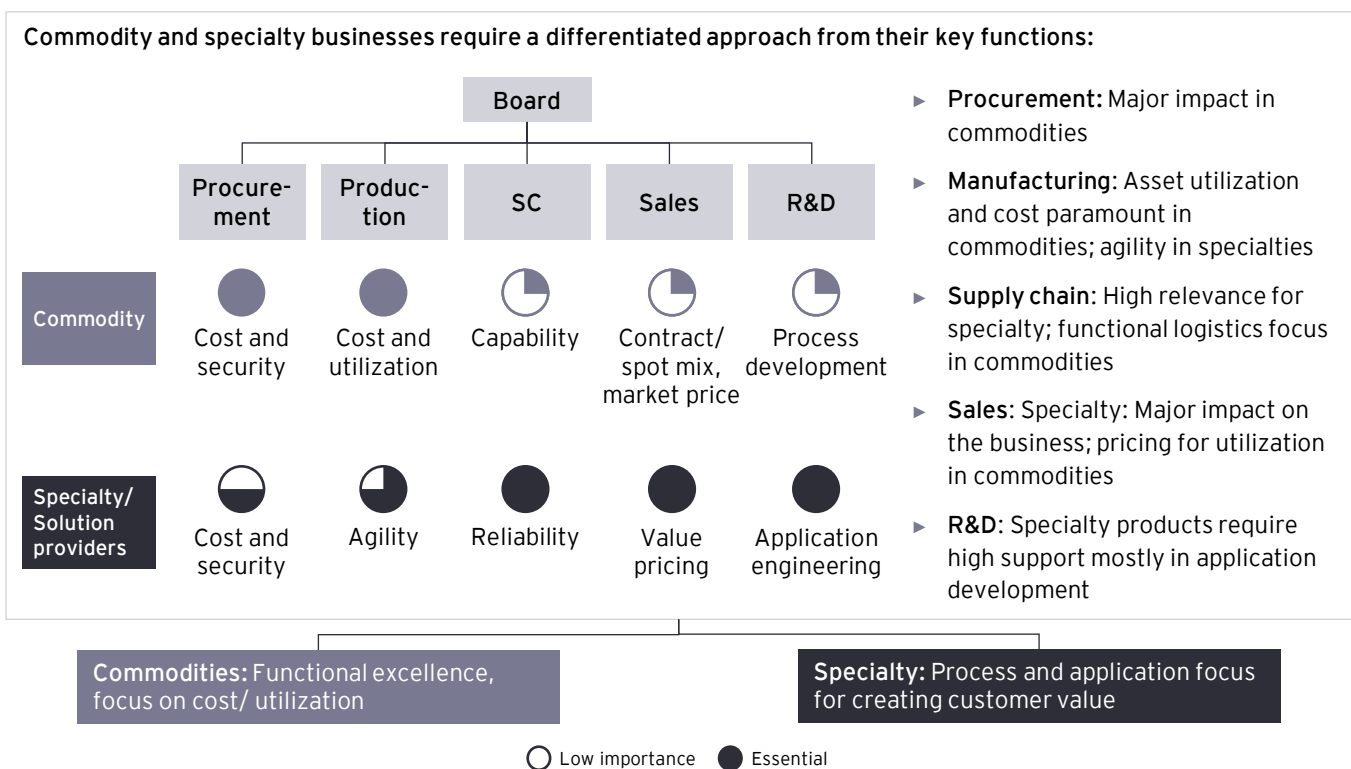
Key success factors in chemicals industry

While commodity players can focus on cost and utilization as Key Success Factors (KSF), for specialty chemical players, customer value creation by product differentiation, supply chain management, R&D and cross functional teams prove to facilitate success

Different key success factors for commodity players, specialty and solution providers



Commodity and specialty businesses display different key success factors also on the level of individual functions, which vary in relative importance







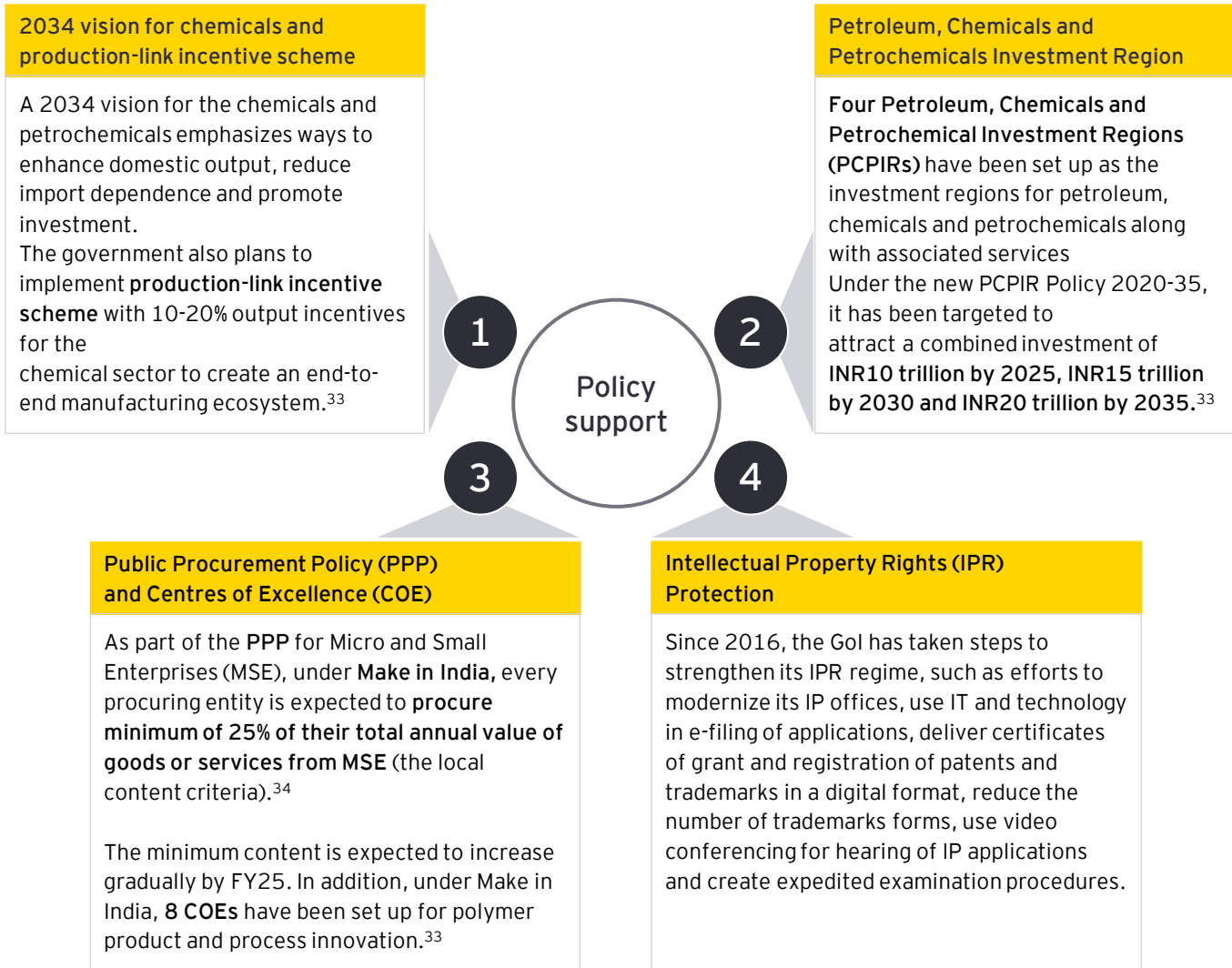
05

Government initiatives and policy recommendations

Government initiatives enabling growth of specialty chemicals industry in India

The GoI considers the chemicals sector as a key focus area and is establishing policies that enable strategic growth and domestic manufacturing and sourcing

GoI aims to provide the necessary support (including education, legislation and infrastructure) for growth of the industry



In addition, GoI is setting up **plastic parks** providing grant funding up to 50% of the project cost with a ceiling of **INR400 million** per project. The Centre has so far **approved eight parks** in various stages of development.³³

FDI policy

100%³⁵

FDI allowed in the chemical sector under automatic route, except in the case of hazardous chemicals.*

These government efforts have already yielded results. There has been a significant increase in FDI in the Indian chemical industry. The inflows decreased in FY21 due to disruptions caused by COVID-19, but are bouncing back.



US\$20.8 billion³⁵

The cumulative FDI equality inflow in the Chemicals industry (excluding fertilizers) during the period April 2000 to September 2022

Source: DPIIT

Policy recommendations

The Indian Government can undertake additional initiatives in order to improve infrastructure, technological and manufacturing capabilities, along with safeguarding the environment



Improving the 'Ease of Doing Business' in India for chemical companies (63 rank out of 190 countries in 2021)³⁶

- ▶ **Infrastructure development:** The GoI can improve policies regarding adequate power, water and energy, to enable uninterrupted production, safe transportation and storage. This can be supported by waste-water treatment and solid waste disposal facilities to ensure environmental impact is not compromised.
- ▶ **Optimizing time required for greenfield projects:** The government can adopt faster registration and clearance processes for domestic or foreign entities aiming to set up greenfield projects.



Incentivising R&D to improve competitiveness

- ▶ **Tax incentives for the private sector:** The GoI can consider reinstatement of the weighted tax deduction under the Income tax Act at previous levels to motivate the private sector to invest in R&D.
- ▶ **Technology upgradation fund (TUF):** A TUF can provide tax deductions, investment allowances and subsidies on acquisition of plant and machinery.
- ▶ **Dedicated skill development programs:** Sector specific skill-development programs to develop talent and expertise, particularly to enhance technical capabilities can benefit the specialty chemical industry in India.



Bolstering India's feedstock supply and facilitating self-sufficiency in chemical intermediates

- ▶ **Implementation of PCPIR:** Since industry players have only made investments in a few PCPIRs yet, the GoI can adopt a proactive role in their implementation.
- ▶ **Chemical parks for downstream players:** Integrated parks and development of a common infrastructure can help mitigate the challenges associated with transportation and disposal of chemicals.
- ▶ **Production linked incentive for critical intermediates:** GoI can introduce a PLI scheme targeted towards chemical intermediates (currently being imported in large quantities).



Fostering occupational safety along with adopting environment-friendly practices

- ▶ **Health and safety regulations:** Implementation of chemical (Management and Safety) rules can be expedited by the GoI to ensure protection of human health and the environment impacted by chemical use.
- ▶ **Incorporating environmental protection:** The government can create the incentives for promoting adoption of environment-friendly manufacturing practices.

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The Associated Chambers of Commerce & Industry of India (ASSOCHAM) is the country's oldest apex chamber. It brings in actionable insights to strengthen the Indian ecosystem, leveraging its network of more than 4,50,000 members, of which MSMEs represent a large segment. With a strong presence in states, and key cities globally, ASSOCHAM also has more than 400 associations, federations and regional chambers in its fold.

Aligned with the vision of creating a New India, ASSOCHAM works as a conduit between the industry and the Government. The Chamber is an agile and forward looking institution, leading various initiatives to enhance the global competitiveness of the Indian industry, while strengthening the domestic ecosystem.

With more than 100 national and regional sector councils, ASSOCHAM is an impactful representative of the Indian industry. These Councils are led by well-known industry leaders, academicians, economists and independent professionals. The Chamber focuses on aligning critical needs and interests of the industry with the growth aspirations of the nation.

ASSOCHAM is driving four strategic priorities - Sustainability, Empowerment, Entrepreneurship and Digitisation. The Chamber believes that affirmative action in these areas would help drive an inclusive and sustainable socio-economic growth for the country.

ASSOCHAM is working hand in hand with the government, regulators and national and international think tanks to contribute to the policy making process and share vital feedback on implementation of decisions of far-reaching consequences. In line with its focus on being future-ready, the Chamber is building a strong network of knowledge architects. Thus, ASSOCHAM is all set to redefine the dynamics of growth and development in the technology-driven 'Knowledge-Based Economy'. The Chamber aims to empower stakeholders in the Indian economy by inculcating knowledge that will be the catalyst of growth in the dynamic global environment.

The Chamber also supports civil society through citizenship programmes, to drive inclusive development. ASSOCHAM's member network leads initiatives in various segments such as empowerment, healthcare, education and skilling, hygiene, affirmative action, road safety, livelihood, life skills, sustainability, to name a few.



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