

# News Release



June 13, 2007

Press Conference in Trostberg, Germany

June 13, 2007

P 294/07e

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## **BASF Construction Chemicals Competence in Chemistry and Construction**

Speech by Dr. Andreas Kreimeyer,  
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**The spoken word applies!**

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Good morning ladies and gentlemen!

I would like to welcome you all very warmly to today's press conference at BASF Construction Chemicals in Trostberg. Chemistry for construction is one of our core competencies, and the construction industry is one of our largest and most important customers. BASF offers a wide range of products that save energy and conserve resources during construction. The most recent building block in our product range consists of the construction chemicals that we acquired from Degussa almost exactly one year ago.

Through this acquisition, we gained the most competent and strongest chemistry partner to the construction industry. In doing so, we have added an innovative and profitable business to BASF's Performance Products segment. A business that operates in a large market that is growing faster than the chemical industry as a whole. The excellent team of former Degussa employees has considerably strengthened our competence in chemistry for the construction sector. In short, the acquisition has made us Number 1 in construction chemicals.

Today, we would like to explain what construction chemicals are and how this business fits into our Performance Products segment here in Trostberg, the location of BASF's Polymers for Inorganics competence center.

### **Importance of the Performance Products segment to BASF's value chains**

[Chart 2] Performance products are those products and business in BASF's value chains that are close to end customers. In 2006, the Performance Products segment accounted for approximately 20 percent of BASF's sales and 12 percent of earnings before special items. On average, we are investing some €300 million to €350 million per year in tangible assets in this segment and are spending around €300 million

on research and development, which corresponded to about one-quarter of BASF's entire R&D budget in 2006.

[Chart 3] Performance products are characterized by:

- businesses that are close to end customers;
- a high need for raw materials from BASF's Verbund;
- customer-specific formulation and technology know-how;
- a focus, on large market segments that grow faster than the chemical industry as a whole;
- a broad customer portfolio that includes large multinationals as well as thousands of small to medium-sized companies and even craftsmen.

Another characteristic of our performance products is that we develop and market tailor-made products, system solutions, applications and services in close cooperation with our customers. In order to be successful we therefore need a thorough understanding of our customers' products and process. The basic requirement for this is technological competence to solve our partners' problems quickly and according to their requirements. In a nutshell: Our success is based on the customer-specific application of our competence in chemistry.

To achieve this, we have developed innovative business models tailored to the needs of our customers and their markets. We supply our customers via a global network of production plants, sales support offices and technical service centers.

With our products, we are often not just suppliers, but are directly integrated into our customers' processes. That means that we frequently sell entire service packages consisting of products, applications and technical service. You may have heard about this in our Coatings division, where we don't just sell the paint but are jointly responsible for the fully coated car body.

The integration into BASF's Verbund helps us in all these customer-oriented business models: We can produce efficiently, achieve competitive advantages and simultaneously offer a broad portfolio of know-how and products.

[Chart 4] Performance products contribute to the functionality and performance of numerous everyday products.

I'll just mention a few examples that you might be familiar with from our advertising campaigns:

- Chemicals for the production and finishing of paper and cardboard [Chart 4]
- High-value textile coatings that guarantee important properties such as water resistance und breathability [Chart 5]
- Asphalt additives to make our roads more weatherproof and durable and thus particularly long-lasting [Chart 6]
- Innovative polymers for water treatment that enable seawater desalination plants to operate using less energy [Chart 7]
- Fuel additives that make engines run cleaner and help reduce fuel consumption and emissions [Chart 8]
- Additives to improve construction materials. As a result, concrete is easier to process and considerably stronger, enabling the construction of durable bridges [Chart 9].

[Chart 10] Our product portfolio is young and dynamic. In this segment, we generate approximately 20 percent of sales with products that are less than five years old. In the past 10 years, we have changed about 50 percent of our product portfolio.

Active portfolio management is a core task in this regard. We do this through capital expenditures and acquisitions, research and development, partnerships – for example with customers and development partners –, and also through consolidation in the form of plant closures and divestments.

We focus on highly innovative businesses that grow faster than the market, that reduce the cyclicity of our portfolio and in which we have a competitive advantage. With this in mind, in the last six years we have closed 24 plants that were no longer competitive and sold businesses that either no longer fitted with our core businesses or into BASF's Verbund, or that suffered from a permanent competitive disadvantage.

On the other hand, we have invested in 27 new plants. We spend around €300 million per year on research and development. And we have used partnerships and acquisitions to expand our chemical competence and further strengthen our innovativeness and have added business with strong market and competitive positions. This is particularly true with regard to construction chemicals.

[Chart 11] Following the acquisition of the construction chemicals business, BASF's Performance Products segment is now organized in four operating divisions. The "old" divisions:

- Functional Polymers: These include chemicals for the production of adhesives, paper and sanitary products such as superabsorbents for diapers.
- Performance Chemicals, for example chemicals for the coatings, detergent, automotive, leather, textile and oil industries
- Coatings: automotive (OEM) coatings, refinish coatings, industrial coatings and decorative paints.
- And the new division Construction Chemicals with its two strategic business units.

The product portfolio in the Performance Chemicals and Functional Polymers divisions stretches from intermediates to an extensive range of polymers. Coatings and also the new family member, Construction Chemicals, on the other hand is almost exclusively active at the formulation level of the value chains. In these divisions, various raw materials and especially products from BASF's Verbund are turned into higher value consumer-focused products.

## **BASF Construction Chemicals expands our chemical competence for the construction industry**

[Chart 12] The acquisition of Degussa's construction chemicals business has added innovative profitable and fast growing products for the construction industry to BASF's range of business activities.

The true value of this acquisition and of BASF's Verbund strategy can only be fully recognized by taking a closer look at this value chain philosophy.

The construction chemical value chain stretches from suppliers of chemicals such as BASF with its functional polymers and performance chemicals via formulators and packagers right as far as wholesalers and retailers. The formulators such as BASF Construction Chemicals play a key role in this chain: Their know-how turns chemical raw materials and construction materials into tailor-made customer solutions such as ready-to-use tile adhesives, mortars, concrete additives or sealants.

Even before the acquisition, BASF supplied numerous key raw materials for construction chemicals. Following the acquisition, however, BASF is now forward integrated to the level of the formulators. Because we have everything available in-house from raw materials through to formulators, we can considerably shorten time to market for our innovations. Importantly, margins are also significantly higher at this level of the value chain.

[Chart 13] The acquisition of the construction chemicals business increased the importance of the construction industry as one of BASF's key customers and it now accounts for between 10 and 15 percent of our sales. We offer a broad range of customer-specific products – everything from foams for thermal insulation, plastics for solar heating systems, dispersions for paints, cable insulation material, latent heat

stores, glues for particleboard, all types of mortar and concrete plasticizers. The new Construction Chemicals division is responsible for an important and profitable selection of these products.

[Chart 14] Construction chemicals are basically additives that improve the functionality and performance of construction materials such as concrete or render.

Our Construction Chemicals division is active in two areas:

- Admixture Systems, for example, concrete plasticizers, retarders, accelerators, products for mining and underground construction
- Construction Systems, for example, mortars, tile adhesives, industrial and sports flooring, coatings, façades, wood protection.

BASF's competent construction chemicals team consists of approximately 7,500 employees in 57 countries. On a regional basis, Europe accounts for approximately 50 percent of sales, North America for 25 percent; Asia Pacific for 15 percent; and South America, Africa, Middle East for 10 percent.

[Chart 15] The strengths of the construction chemicals business and of the BASF Group complement each other ideally. The Construction Chemicals division is the global market leader in large, attractive markets. Success in construction chemicals is based on longstanding and extensive knowledge of the business and customer needs. The business has highly innovative products and established customer relations. Strong brands such as PCI therefore have a high level of recognition. Further strengths are to be found in the supply chain and logistics.

For BASF, the acquisition of the construction chemicals business offers a successful means of forward integration and builds on our strong position in raw materials for construction chemicals. We also have an excellent regional setup and are particularly strong in Asia. Together

with the advantages of our Verbund and our financial strength, we can open up additional growth potential for the acquired business. Furthermore, the acquisition strengthens the innovation platforms of our Research Verbund.

Because of the excellent fit, the acquisition was strategically important and valuable to BASF.

### **Operational integration of acquired construction chemicals business completed**

[Chart 16] Let me take a quick look back at the course of the acquisition. In December 2005, we announced our interest in the business. For journalists like yourselves, the acquisition was perhaps not as exiting as that of Engelhard, but that was not the case internally. In two months, a team of almost 100 people carried out in-depth due diligence and negotiated an extensive contract. But the real work started after the negotiations and the signing of the purchase contract. I would say that negotiating an acquisition is perhaps 10 percent of the work. The remaining 90 percent consists of integrating the new colleagues and business into the company and forming a united team. The fact that most acquisitions fail to live up to expectations is due to mistakes during the integration.

The preparations for the integration started once the purchase contract was signed at the end of February 2006 and took up several months. In this phase, we worked out the details of the integration and communication concept and identified the members of the integration team. Above all, it was important to actively involve the new colleagues and build on their know-how.

The year-long integration process then started once the transaction closed on July 1. This involved integrating the new colleagues into the BASF team, integrating business processes and systems, and

developing a new strategy. The integration team comprises about 250 employees worldwide.

[Chart 17] The integration is taking place in number of phases. The top priority was and remains to ensure the continued success of construction chemicals and to ensure that business continued as usual. This is why marketing, sales, the supply chain and production are substantially unchanged. Business-process critical functions and services such as IT and logistics are being integrated into BASF structures step by step.

The most important element of the integration was and is to reach and win the hearts of the new employees. The key success factor for this business is the team – the colleagues who have built up this business and made it as strong and successful as we see it today.

[Chart 18] The combination of two corporate cultures, which are by no means identical, requires a great deal of sensitivity: The former Degussa business had a structure like that of a medium-sized company with more than 100 individual and independent companies. So far, I believe we have succeeded very well in this. The experience, know-how and merits of the two corporate cultures complement one another superbly. The organizational part of the integration is now largely completed, but we will be working on many details until 2009.

[Chart 19] We have identified synergies for the BASF Group amounting to €100 million per year by 2010. These synergies are due mainly to backward integration into BASF's Verbund, greater efficiency in purchasing and administration, and BASF's strength in Asia and innovation.

As with every integration, we want to ensure that 1 + 1 makes at least 3. This integration, however, is not associated with the drastic job reductions that often follow such deals – after all no one knows this

business better than our construction chemicals team. The job reduction of 200 positions that we announced are therefore all in service and administration functions. This will be compensated for by job increases in accordance with our strategy in the individual business segments, since we want to expand on our position as Number 1 in the construction chemicals industry.

[Chart 20] Achieving this goal will be much helped by the integration into BASF's Verbund and by the competence, know-how and resources it provides. The businesses are a good fit with BASF and the market for construction chemicals is highly attractive. It has a volume of €29 billion and is growing at 4 to 5 percent per year. The acquired business was very successful over the past years: It grew by an average of 7 percent per year between 2002 and 2005 and was highly profitable. This has also continued in the first year the business was part of BASF, and our expectations have been far exceeded. We now want to proceed on this growth path and continue to grow faster than the market. Our goal is to grow by 7 to 8 percent in the coming years and thus double our sales to approximately €4 billion by 2015.

[Chart 21] We will offer our full commitment to achieve these ambitious goals:

Firstly: We aim to expand existing regional businesses by employing technologies and know-how supraregionally. We plan to translate business models that are successful in one region to other regions. BASF's strong regional setup will help us in this.

Second: We aim to increase our innovative strength and speed. We will use BASF's competences to create better product solutions and achieve rapid market access.

Thirdly: We aim to generate more business in growth markets. We see a great deal of potential here, especially for Admixture Systems and in Asia.

Acquisitions in growth markets, like that of HiCon in China at the end of 2006, will also help us to achieve these goals.

As you can see, we have a lot of plans, and we will continue to report on our progress in the future.