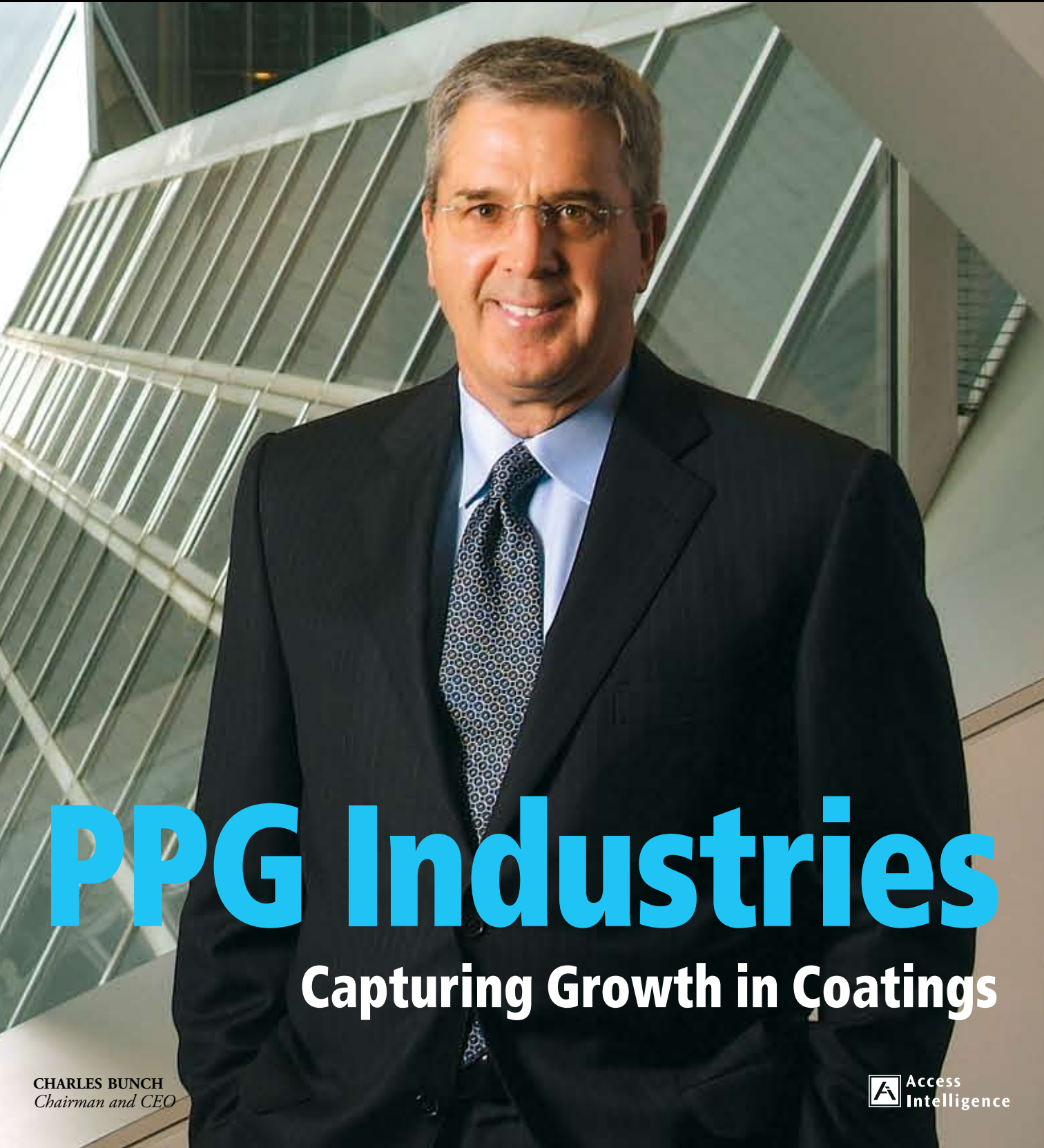


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PPG Industries

Capturing Growth in Coatings

CHARLES BUNCH
Chairman and CEO

 Access
Intelligence



PPG Industries

Capturing Growth in Coatings

PPG Industries has accelerated its shift beyond roots in glass and chemicals, transforming itself into a leading global coatings player. Coatings now account for nearly 75% of annual revenues, including pending acquisitions, up from 42% ten years ago.

“Many of the strategic steps we’ve taken over the past 18 months have been critical to our solid organic growth and continued solid financial success this year, despite what

has been a challenging economic backdrop,” PPG chairman and CEO Charles Bunch told investors late last month.

PPG’s biggest move this year has been its €2.2-billion (\$3.2-billion) agreement to acquire SigmaKalon Group (Uithoorn, the Netherlands), a leading European maker of architectural, marine, and industrial coatings, from private equity firm Bain Capital (Boston). PPG will have 10% of the global \$85-billion coatings market once the deal is completed, which is expected by early 2008.

That will place it second to Akzo Nobel, which will widen its lead in coatings with its planned £8.1-billion (\$16.1-billion) acquisition of ICI. The 2007 M&A activity clearly defines the two largest global coating companies, Bunch told investors. “We fully expect the pace of technological change and globalization to quicken,” Bunch says. “The acquisition of SigmaKalon allows PPG to compete effectively in a rapidly consolidating industry.”

PPG is also shedding lower-margin businesses as part of the portfolio shift.

Divestitures this year include the sale its \$1-billion/year auto OEM and replacement glass businesses to Platinum Equity (Los Angeles) for approximately \$500 million, and the sale of its fine chemicals business to ZaCh System (Milan) for \$65 million. PPG also closed a Venezuelan fiberglass joint venture and recently announced plans to sell its jv stake in Azdel, a maker of thermoplastic composites.

Coatings and optical and specialty products will account for 80% of revenues when the SigmaKalon deal is completed, up from 66% just last year, PPG says. U.S. and Canada will account for just under 50% of revenues, down

from 68% in 2006. SigmaKalon is one of five acquisitions for PPG this year, following 12 in 2006. All have been focused on coatings or PPG's optical products business. The 2006 deals will add \$750 million to revenue in 2007, and generate "high single-digit margins," the company says.

Revenues increased 13% through the first nine months of 2007, to \$8.3 billion. Acquisitions accounted for 7% of revenue growth. Income from continuing operations was \$622 million, up 24% from the same year-ago period. PPG officials contend that its strong performance so far in 2007 should dispel the impression that PPG is a slow growth company that suffers from cyclical exposure to U.S. automotive and housing markets. Markets are soft in the U.S., but that is being offset by the "broad geographic balance that we have been developing over the past 10 years," Bunch says. "We have very strong fundamentals on a global basis. We continue to have excellent growth in Asia. And European economies are stronger than they've been in four or five years."

The recognition of coatings as a distinct segment could also raise the profile of the company as investors target pure-play investments in attractive segments such as coatings. "Ten years ago, no one really talked about coatings as a separate industry segment," Bunch says. "You're starting to see that now with the emergence of a group of players such as PPG, Sherwin-Williams, and Valspar." Bunch cites industrial gases and fine chemicals as examples of industry sectors that are now recognized as distinct segments.

"We are a 125-year-old company, and there are some perceptions that go back a long way," Bunch says. "We have not received full

credit or recognition for the progress that we've made in building a leading coatings and specialty products company."

Analysts are starting to take note of the shift. "Management made a strong case [at its recent investor meeting] in dispelling misperceptions of PPG as a U.S. auto and housing play," says Robert Koort, analyst with Goldman Sachs (New York). "Respect for its rock-solid management team and leading coatings platform continues to be offset by anxiety around weakness in the auto and housing markets and the eventual cyclical downturn in chlor-alkali. However, as investors focus on the accretion of the pending SigmaKalon acquisition and the changing portfolio mix toward higher margins and higher growth, we expect the stock to regain its upward momentum."

PPG started to state its results in five business segments early this year, as opposed to its traditional three, to improve clarity around its core businesses. Coatings is now split into two segments, industrial and automotive OEM coatings; and performance and applied coatings, which includes refinish, architectural, and aerospace. Chemicals have been split into commodity chemicals, mainly chlor-alkali and derivatives, and optical and specialty products; and the fifth segment is glass, which includes PPG's remaining glass operations in performance glazing as well as fiberglass. The company is likely to add a sixth reporting segment next year, European decorative coatings, after the acquisition of SigmaKalon closes. "We want to be completely transparent" about how the acquired business performs, PPG CFO William Hernandez told investors last month.

PPG remains one of the few companies that does not host live analyst calls for earnings each quarter, instead delivering commentary on results and trends through pre-recorded statements by its CFO. The company will modify that starting January, and will conduct a live conference call once per year in January to provide more direct interaction with investors.

The company has generated roughly \$550 million in cash from operations through the first nine months of 2007, Hernandez says. PPG will retain its balanced and disciplined approach to use of cash, he says. The first priority remains funding businesses through capital spending as necessary to insure organic growth and keep the businesses healthy and competitive. The annual



Hernandez: Strong cash flow funds growth.

capital expenditure target is about 4% of sales, he adds. The next priorities, in rough order of importance, are dividends, acquisitions, and share repurchases, Hernandez says. The SigmaKalon deal will significantly boost PPG's cash generation capability, Bunch says. The company has generated an average of \$1 billion in cash flow from 2001-2006, and that should increase 25%-30% within two years after SigmaKalon closes, he says.

"We came away [from recent meetings] with further conviction that PPG is on a transformational path toward a predominantly specialty chemical portfolio versus a hybrid portfolio," says Kevin McCarthy, analyst with Bank of America Securities (New York). "The Sigma-Kalon deal will likely be accretive in 2008, and we anticipate the probable separation of the remaining glass portfolio, fiber glass and flat glass, in coming years."

Performance across all of PPG's segments has been solid in 2007. Performance and applied coatings sales increased 24%, to \$2.79 billion through the first nine months of 2007, with volume growth in aerospace and refinish businesses offsetting a volume decline in North American architectural coatings. Industrial coatings sales increased 14%, to \$2.71 billion. Optical and specialty materials sales increased 14%, to \$786 million, for the first nine months of 2007. Commodity chemicals, mainly chlor-alkali and derivatives, increased 1%, to \$1.2 billion for the first nine months of 2007. Chlor-alkali remains a strong generator of cash, officials say. "We are still supporting and investing in the business," says Kevin F. Sullivan, senior v.p./chemicals at PPG. The company completed a \$100-million modernization of its Lake Charles, LA chlor-alkali unit, converting from mercury to membrane technology. "Our goal is to generate cash and maximize profitability so the company can invest in areas where we have said we are interested in growing in coatings and optical."

PPG's quarterly volumes this year represent some of the best and most consistent growth that PPG has had in the past several years, and that, "although it is only one month into the quarter, our October results came in better than we had estimated," Bunch said late last month.

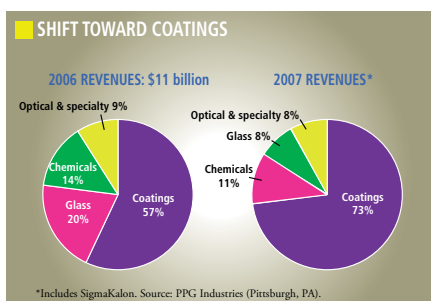
"The strength of PPG's global portfolio, exposure to higher-growth markets, and strategic positioning in more mature markets, is behind the better-than-expected [early fourth-quarter] trends," says Frank Mitsch,

analyst with BB&T Capital Markets. "We believe that these three very important traits will be enhanced following the completion of the automotive glass disposal and the addition of SigmaKalon. PPG's track record on coatings acquisitions is impressive, so we're of the opinion that they will make SigmaKalon work. We are in favor of PPG's transformation to a faster-growth, top-line, and bottom-line company."

Growth in emerging markets is accelerating, with revenues in Asia, Eastern Europe, and Latin America up 40% through the first nine months of 2007. China is a particular area of focus, but the company is not sacrificing margins to gain market share, officials say. "We're not getting bigger for the sake of size" in the region, Bunch says. "We've maintained our typical profit margin in China."

Investments in China include an aircraft cockpit window overhaul and repair facility in Suzhou. PPG is also building a paint facility at Wuhu, China to supply Chery Automotive, one of the largest and most

Chlor-alkali: PPG recently completed a \$100-million upgrade at its Lake Charles, LA plant.



aggressive Chinese domestic auto producers. Chery's facility at Wuhu is designed to produce as many as 1 million cars/year.

PPG employs an approach in Asia that is similar to developed markets, company officials say. "The products are very similar, in many cases exactly the same," Bunch says. "These are big global customers. Whether it's an automotive OEMs, computer manufacturer such as Dell, or an appliance maker such as Whirlpool, they're expecting the same product worldwide," Bunch says.

PPG is also gaining strong footholds with domestic Asian producers. "Ten years ago we typically entered China to supply our global customers," Bunch says. "What you've seen

over the past five years is the emergence of strong domestic producers [such as Chery]."

Acquisitions will continue to form a key part of strategy. "Deals will remain targeted," Bunch says. "We're not actively looking for another leg to the company. There are plenty of opportunities within the categories we operate in now."

Optical products is one area that will be built via acquisitions. PPG's activities in optical products include its Transitions-branded photochromic lenses, sunlenses, optical materials, and polarized film. Recent deals include International Polarizer, the world's largest manufacturer of sunglass polarizers, located in Marlborough, MA, and Intercast Europe, the world's leading manufacturer of nonprescription hard resin sunlenses. Continued development of its Transitions business, and greater penetration into lenses and materials for high-end sunglasses, are an area of focus, says Rick Elias, v.p./optical at PPG. Segments such as optical and aerospace play to PPG's strengths, Bunch says. "These are businesses that pay for technology when it's differentiated," he says. "We're well-positioned as the

market leader with the best technology in those segments."

PPG is targeting overall growth of twice the overall market in core businesses. "We are focused on share gain, and monitoring the market space, making sure we are keeping customers," says Richard A. Beuke, v.p./growth initiatives at PPG, a new position created last year to facilitate cross-business

growth and improve the company's sales capabilities. PPG is working to ensure that it has a rich pipeline of projects, while also maintaining discipline to make sure that initiatives that aren't meeting targets are identified quickly so corrective action can be taken or the project can be killed, Beuke says. Efforts will also include a small investment in a venture capital unit to

invest in companies or technologies in core or adjacent businesses.

"All in all, it has been a very active year at PPG," Bunch says. "And we know we have a full plate in 2008. The successful integration of SigmaKalon will be the primary focus, while at the same time we will continue our efforts to meet our aggressive targets in other areas."

—ROBERT WESTERVELT in Pittsburgh

Coatings revenues have increased from 40% to 75% of revenues since 1997.