

PF Exclusive:

The 2008 Coating Survey

by Kate Hand
Managing Editor

IN UNCERTAIN ECONOMIC TIMES, COATERS TALK ABOUT CHALLENGES, GROWTH AND WHAT THEY'RE DOING TO WEATHER THE STORM

Every few years, *Products Finishing* invites its readers to comment on the state of their respective industries—to evaluate today and posit conjectures for the future. But rarely has this assessment come during a time of such social, political and economic upheaval. This year, the answers aren't so simple.

THE ECONOMY IN CRISIS

As this is written, newspapers trumpet the greatest drop in factory activity in 26 years. According to Reuters, The Institute for Supply Management says its index of national factory activity fell to 38.9 in October from 43.5 in September. Put in perspective, a level of 50 separates contraction from expansion, and a reading below 40 is considered "exceptionally weak." After four years of sustained expansion, this rapid decline is attributed, quite simply, to a lack of demand. Output has fallen every month since March.

New orders are also falling at a record pace. The index reveals that the global economic downturn has made it harder for manufacturers here to secure new orders from abroad. In response, businesses have cut their workforces, with around 30% of manufacturers reporting lower employment levels.

Words like "grim" are used to describe the economic situation, and the question of recession is no longer "if" but "how long?" It's near impossible to get through the day without hearing of catastrophe

on Wall Street, mourning taxpayer-funded bailouts or suppressing fatalistic thoughts about one's dwindling 401(k).

Yet, according to this year's Coating Survey, 86% of those performing painting, electrocoating and powder coating forecast that 2009 will be about the same, somewhat improved or substantially improved compared with 2008. Eighty-six percent!—nearly 14% of which fall into the “substantially improved” category. Additionally, only 1.3% predict that the coming year's business will be substantially lower.

That's not to say coaters aren't aware of the global economy. Sixty-one percent of respondents say one of the biggest challenges facing their business is the general condition of the market. Coming in second and third are global competition and lack of a quality workforce. To combat the mounting storm, 97% of coaters are employing in-house training, 68% are cutting costs and 48% are concentrating on new products.

With all the talk of depression, it seems coaters are hunkering down, focusing on fulfilling today's orders and securing tomorrow's customer. When taken out of the anonymity of percentages, the answer comes down to a sentiment heard time and time again, and expressed best by Kim Johnson, of Team Powder Coating, when he says, “Walk outside. Life is still going on.”

LIFE GOES ON

Johnson is currently in the process of buying the business he has presided over as general manager for the last three years. Over the next few months, Team Powder Coating will end years of leasing, buy its own building and purchase more than \$600,000 worth of brand new equipment. “We decided it's the right time to scrap our existing equipment, take the plunge

and test that economic water,” Johnson says.

Team Powder Coating, currently based in Isanti, MN, is strictly a powder shop, with a mix of about half OEM and half job shop work. The company has a diverse customer base, with minimal ties to the struggling automotive industry. “It's a scary time, no question, but the upper Midwest seems to be pretty strong,” says Johnson. “It helps that we're not as automotive-driven, but the Twin Cities have been strong in medical, and big in power sports, leisure and golfing. We get everything from industrial component hoppers to snowmobiles and jet skis.”

The company's largest customer is Par Aide Products, a worldwide purveyor of golf course equipment that turned to powder—and Team Powder Coating—nine years ago. In addition, the company recently purchased a powder line specifically designed for the fishing tackle component industry. The line, set to debut in the first quarter of 2009 with the ability to coat 4,000 lures per hour, is expected to provide a windfall.

CATERING TO EMERGING MARKETS

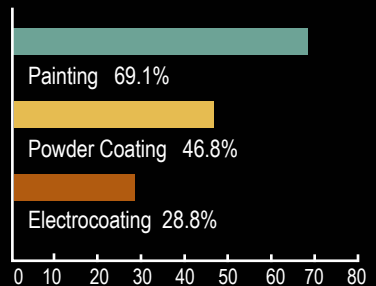
“The fishing tackle industry is just now discovering powder coating,” says Johnson. “They've been pretty much only liquid coating up until now, and the environmentally friendly technology of powder coating, plus the diversity of colors and textures, are really starting to take off. It's exciting.”

The tackle industry is an ideal example of one of Johnson's driving philosophies: “Grow with the little guy.” In tackle, he sees the potential to supply not only one of the world's largest component manufacturers, which happens to be located nearby, but also countless “ma and pa” shops. “There are successful projects that guys start

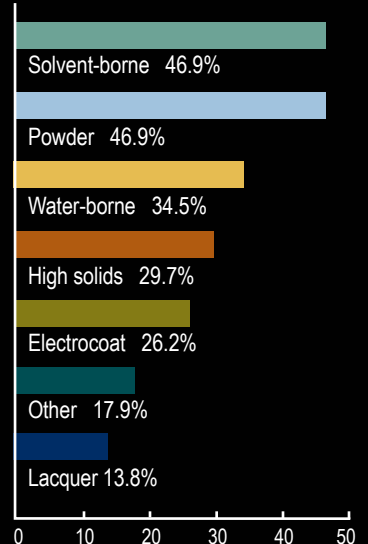
THE PARTICIPANTS

The 232 respondents to this year's Coating Survey conducted in September and October of 2008, represent a cross-section of OEM and job shop coaters nationwide.

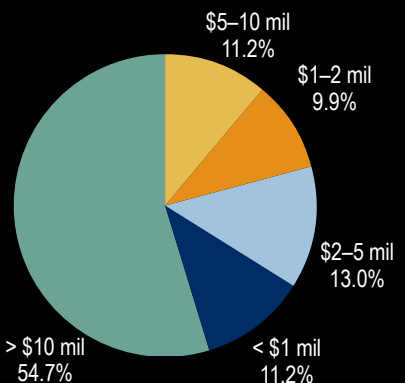
Types of Finishing Performed



Coatings Used



Annual Sales Volume



in the garage,” says Johnson. “We understand that entrepreneurial mindset and we make sure we help them grow. That’s been pretty successful.” Based on word of mouth alone, the company is receiving a call day regarding the new technology.

In addition to the tackle line,

“I wouldn’t be signing my personal guarantees to these deals if I didn’t believe that there is and will continue to be a market for powder coating,”

Johnson is installing a five-stage washer, doubling his line speed and quadrupling throughput capacity. He expects the company, which has been growing at 10–15% for the last three years, will be able to support further growth with the added capacity of the new facility.

And what about liquidity for this venture? No problem. While big national banks seem to be dropping like flies, Johnson says he sees that “local banks are hungry for good solid folks with good solid business plans.” He has been working with two local banks to get small business loan funding, a venture bolstered by state and

local economic development programs such as JOBZ, Minnesota’s Job Opportunity Building Zones operation. “Outside of the Twin Cities metro area, they’re trying to attract businesses with positive incentives,” says Johnson. An initiative supported by Gov. Tim Pawlenty, JOBZ provides local and

state tax exemptions to new and expanding businesses. According to Johnson, his company won’t pay property tax, sales tax or state income tax through the year 2016. And it’s conceivable that the credits could be extended, depending on the success stories that come out of the initiative.

Johnson is convinced his company will be one of them. “I wouldn’t be signing my personal guarantees to these deals if I didn’t believe that there is and will continue to be a market for powder coating,” he says.

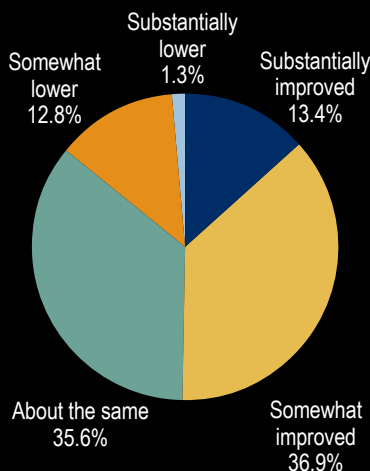
He also wouldn’t be moving his company 30 miles away from its customers. Team Powder Coating

is relocating to an existing building in Hinckley, MN, a town that’s biggest claim to fame is the caramel rolls at Tobie’s Restaurant, a rest stop that marks the halfway point between Minnesota and Duluth.

Hinckley has few manufacturing jobs, with most of the local economy built around the hospitality and gaming industries. The hope is that Team Powder Coating will eventually spur residual businesses. The company will create its own new jobs as well, if only on a small scale to start. As part of the subsidy agreement with the city, the business has guaranteed 100% growth of full-time employees within two years. This means going from five to 10 employees, initially.

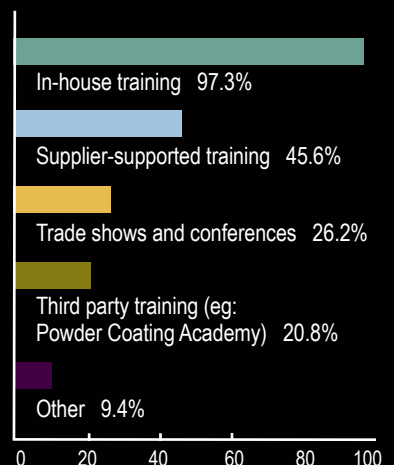
“We’re a small operation,” says Johnson. “I answer the phone and I dump my own trash. We take turns cleaning the bathroom, and we try to be as flexible as possible.” The shop is non-union, giving Johnson the flexibility of ever-evolving duties for his workers. Team members can step into any role at any given moment, a method Johnson admits may not have the efficiency of a larger operation, but one he views as critical for such a tight operation.

2009 Business Forecast



80% of respondents are employing lean manufacturing to reduce costs and improve productivity.

Types of Employee Training



WORRY AND OPPORTUNITY

Despite Johnson's determination to buck the nation's economic woes, there are aspects of being a small business owner that keep him up at night. He thinks about offshore competition once he gets into larger volumes, but his biggest concern is a more immediate danger. "As a small company, we worry about catastrophic things," he says. "We don't have duplicate and triplicate backup as far as people or equipment. That's why we're going with all new equipment and warranties—we can't afford downtime."

Being farther from its customer base means Team Powder Coating will spend more on fuel and transportation, one aspect of the move that has Johnson a bit concerned. "We pick up and redeliver product in our truck many times next-day—that's a niche we've carved out, and I may have to go to a second truck." He considers the investment well worth it. "That type of high-level service is infectious," he says. "I'll even throw stuff in the back of my own truck and deliver in a crunch, and my powder suppliers do the same for me."

It's the service that fuels John-

son's confidence in his company, and, indeed, all well-run small companies. "They say it is hard to raise a boat when the tide is going out," he says, "but I come from a manufacturing background understanding how my customers and my customers' customers need to keep inventory and lead times as short as possible. We've customized and filled that niche with a quick-response, nimble company that will do whatever needs to be done."

"There is value there that we can capture."

A BRIGHT FUTURE

Larry Dietz, general manager for Professional Plating, a plating and coating job shop in Brillion, WI, that's in the process of adding 65,000 ft² of workspace, recounts a similar story.

"Professional Plating is about to celebrate its 30th anniversary, and we're doing the opposite of what other people are doing right now—growing and adding on," Dietz says.

"We're blessed," he continues. "I'm reading a morning business newsletter from a local paper and I see that Kohler Co. is laying off another 80 workers. There's not

a day that goes by that we don't see everyone around us being affected."

Professional Plating's name doesn't tell its whole story. The company does about 30% plating business, with the rest made up by powder coating, liquid and E-coat lines. "Painting is really a bigger ticket because of the diversity it provides," says Dietz.

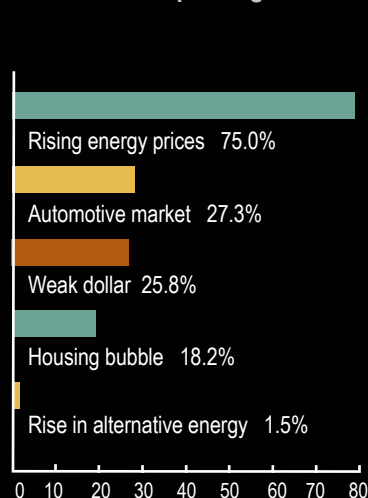
Brillion, located about a half hour's drive from Green Bay, enjoys some of the same industries that have kept Team Powder Coating strong. "There is a lot of diversity in our coating business," says Dietz. "About a third is in outdoor power equipment, and another third is in recreational and outdoor equipment." The diversity has proved beneficial. The downturn in automotive has hurt the company's electrocoat business—a 30% toll across the board.

"This little blip—and we do look at it as a blip—when it goes away, there will be a really bright future that will take us another step forward," Dietz says. Like Johnson, Dietz has focused his energies on carving out a service niche for his customers. "We understand the need to do commodity stuff, but

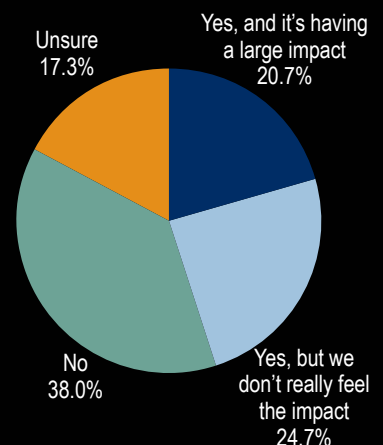
Challenges Facing Coaters



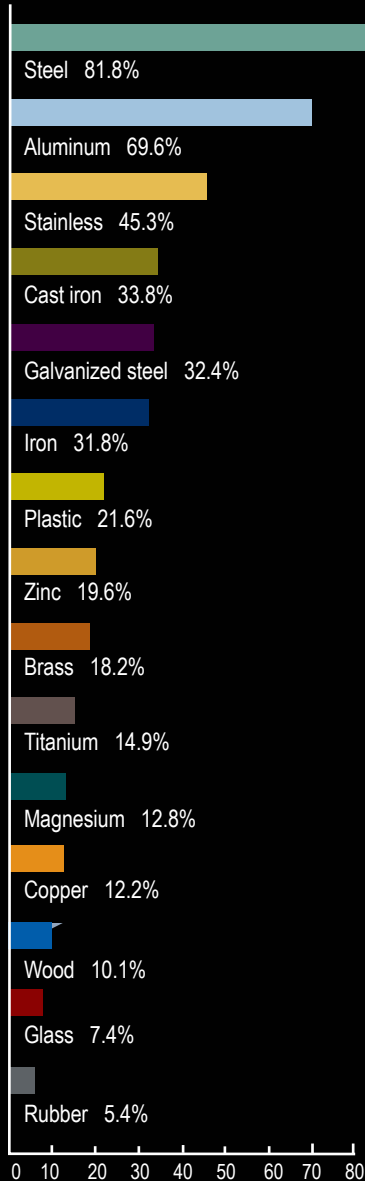
Conditions Impacting Business



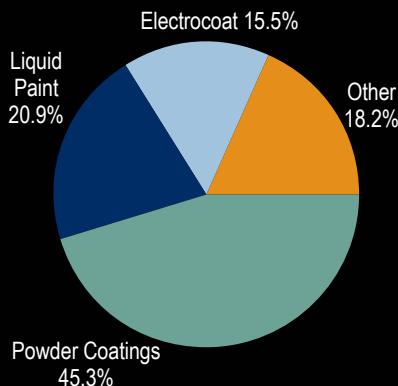
Are you losing business to foreign countries?



Substrates Coated



What do you think will be the predominant coating over the next 5–10 years?



we're a finisher that does more complicated jobs—racking, masking, labeling. Harder is better because you get paid more." Dietz says that while commodity jobs are easy, those are the customers that ask to "cut a penny three ways" and when faced with changing economic conditions, are more likely to ship the work overseas. He encourages his sales team to hunt for jobs where the company can provide value in precision and accuracy.

For instance, says Dietz, Professional Plating has a customer for which they paint and assemble Harley-Davidson motorcycle parts, sending the parts, weather-stripping and all, straight to the Harley assembly line. The company's quality controls make that type of value possible.

With the upcoming expansion, Professional is adding more than \$2 million worth of new equipment, in hopes of positioning itself as a one-stop shop for those seeking finishing capability. Referring to the current recession, Dietz says: "As a country, we're in the middle of a serious correction. And there will be more people that will drop out. We want to be a mall where a customer can do their shopping all at one place—one purchase order, one set of trucks, one customer service representative. If it comes down to a company having to whittle down its service to only one painter, we want to be the one."

Dietz's advice to solvent companies is spend money to make money. Co-investment by the community and the city will pay off in the end, he says. For instance, Professional has secured a grant for WAT, Workplace Advancement Training, from the government to be applied to local technical colleges. "We can sit around and complain that jobs have gone overseas or we can get stronger and

smarter," Dietz says, describing his company's belief that businesses of the future will employ workers with skills beyond their job descriptions. Skills such as demonstrating a positive attitude, working cooperatively in teams and following direction are considered core for the company's 130 employees. Yearly performance-based raises or bonuses are considered high ROI. "People have to make decisions in a mature and fast-paced environment," Dietz says, "We value that."

WORKING THROUGH UNCERTAINTY

Although Dietz and Johnson offer uplifting stories in the midst of a downturn, it's likely that far more companies can relate to C.R. Hudgins Plating. The 100,000-ft² powder coating job shop is located in Lychburg, VA, a small service town of about 70,000 people in the foothills of the Blue Ridge Mountains.

Byron Hudgins represents the fourth generation in his family's coating business, which does work for the banking, telecommunications and automotive industries in addition to a wealth of one-offs for other industries. Byron's father, James Hudgins, will be retiring soon, and as Byron and his sister, Renee Hudgins Owen, take the reins more fully, they look to an uncertain future. "The back half of the year has been pretty good," says Byron Hudgins. "The first half was really flat, and it has picked up some. Honestly, we don't know the cause. It could be a case of some industries pulling work back from overseas. But we just don't know."

James Hudgins is curious as to what the future will bring as well. He knows the company has a strong past and a bright future, but all national indications seem to point to a difficult road ahead.

“I would have to say from watching what we see on the news, to what we’re actually producing... well, the two don’t match up.” His observation mirrors that of many coaters, experiencing relative bounty right now, perhaps hinged on a weak dollar.

C.R. Hudgins is reacting to the news by taking a number of traditional steps to weather the downturn. The first is holding onto its cash supply. The company is seeing customer payments spread over longer time periods, so it is holding its own cash supply for longer when it can, spreading out payments to suppliers. Managers are also keeping vigilant watch on costs. “Technically, we could put on seven or eight more people,” Byron Hudgins says. “But if we honestly feel the quantity of work will break come the first of the year, we’d rather have people work overtime, not hire people we would then have to lay off in another three to four months. We’re trying to do more with less.”

Byron says that although the company’s indicators look good, he doesn’t have any real way to predict what the upcoming six months to a year will bring. “We can’t see anything on the horizon,” he says.

COATING WILL PREVAIL

Rodger Talbert sees uncertainly on a daily basis in his job as a Grand Rapids, MI-based coating consultant. “What I see is a lot of fear,” Talbert says. “A lot of companies are putting products on hold or cutting them out altogether. And they’re not doing it because their revenues are on hold—they’re doing it because they’re afraid.”

Talbert says he is fairly surprised that the economic crisis hasn’t caught up with manufacturing in a broader sense. “It’s very reassuring,” he says, “but that could be

a delayed reaction. As consumer spending falls, it’s inevitable that manufacturing will feel the pinch.”

Where manufacturing goes, coating will follow, he points out. One coating shop in Grand Rapids, heavily dependent on the automotive industry, recently closed its doors after years of steady decline. But Talbert can also point to as many shops that are thriving right now, specifically in the agricultural sector.

“Prices have been driven up on corn, so farmers wanting to take advantage of high crop prices can pay for equipment and get a much faster return on their investment,” says Talbert. “Coaters in the agricultural equipment sector are investing heavily to stay ahead of the competition.”

Outside of agriculture, he says, liquidity is tight. Companies that might have considered buying a new piece of equipment a year ago are hesitant now, and for good reason. “When there’s a hiccup in the stream of work, suddenly small-to-medium-sized businesses that were puttering along can now have 30 people standing around cleaning the shop.”

Like all of the companies interviewed for this article have found, diversity is key, Talbert says. Coaters who are not exclusive to automotive or tied too tight to any other sector that may see a drop are better equipped to weather the storm.

SURVIVAL TIPS

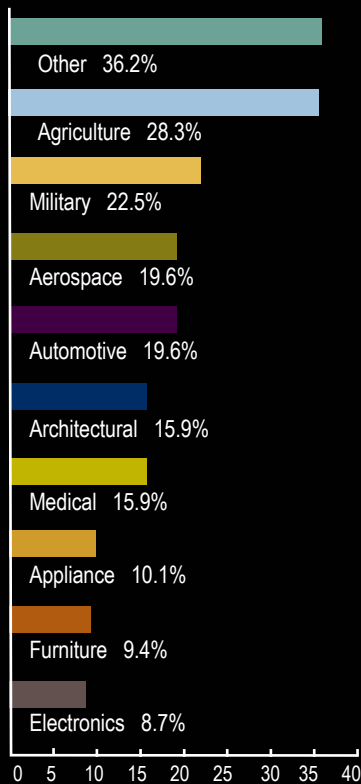
So what is a coater to do? Talbert’s advice to companies looking to make changes to compensate for waning business conditions is the same as it has always been—seek out and correct inefficiencies. “Where it might have been okay to have a leak in a compressed air line before, it’s inexcusable now,” he says. “It might have been

68%
of companies surveyed are cutting costs to make up for a changing business climate.

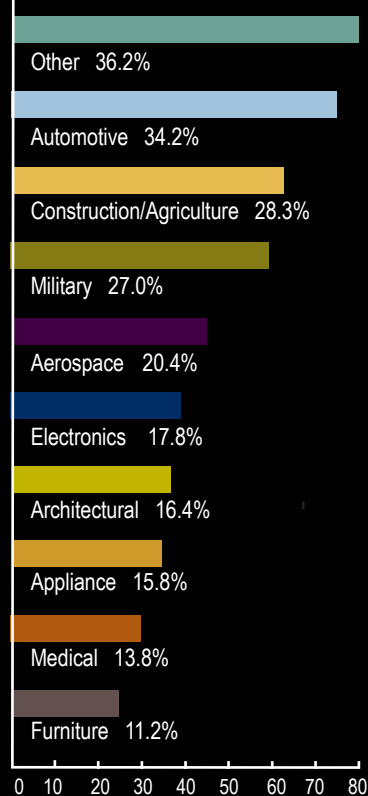
Strategies Employed to Compensate for Changing Business Conditions



Industries with the Largest Growth Potential



Industries Companies are Currently Involved In



OK to have an oven that was old and not running efficiently. But you need it to be running efficiently now.”

Go through a fuel efficiency checklist in your shop to look for places where you can save on energy costs. Avoiding waste will allow you to produce your product at a lower cost, with every extra cent going straight to the bottom line.

Talbert advises using a detailed recording method to chart your material usage and transfer efficiency. “It’s critical to look at material handling, paint usage, coating flow, labor, anything that will streamline so that you can get more profit out of the same work,” he says. “That’s my excuse for being in business. I save time and

a little bit of sheet metal that just saved you a lot of money.”

THE NEXT BIG THING

When asked to make a forecast, Talbert says he believes the coating industry will come out of the recession intact. “In the last three years or so, I helped put in more paint systems than probably any other time in my career,” he says. “The edges are just now starting to crumble, but companies have been doing well, so they have capital reserves that will shore them up in lean times.”

As Managing Director of Key Bank Capital Markets responsible for coverage of the chemical industry, Lee Harrs has been covering specialty chemical companies for about 15 years. He

Time invested in improving your business, ramping up customer service, cutting out inefficiencies, seeking out emerging markets, training your workforce and diversifying your offerings will be time well spent.

money by eliminating waste.”

Changes can be big, like investing in robots or other capital equipment, but many improvements don’t have to run into the tens of thousands of dollars. It could be as simple as changing out the contents of a tank to a lower-temperature cleaning chemical. It may be changing from a seven-stage washer to a five-stage, turning down the flow rate on your powder guns or rearranging the air flow to your environmental room to cut cooling costs.

“A simple example is if you have a lot of heat loss in your oven, nobody wants to see energy escape, so you put an extension on the entrance or exit that adds length.” Talbert says. “An extended vestibule is nothing but

agrees with Talbert that coatings will probably see a dip and then come back strong. “I’m bullish on the coatings sector,” he says. “Coatings touches on so many end markets that the long-term prospects are good.” Harrs calls coatings a “GDP-plus” product, a sector that he expects will grow at a better clip than the nation’s Gross Domestic Product.

“I would concur that things are bad generally,” says Harrs, “but different sectors of chemical companies are feeling different degrees of the downturn. My observation is that those that are subject to automotive and construction are feeling it the worst.”

When it comes to banking, he agrees with Johnson’s assessment. “Banks are issuing and extend-

ing loans with great care, and are much more conservatively approaching the market,” Harris says. “Loans are going to better customers with better credit. It’s the companies with marginal quality credit that will suffer.”

Harris’ advice to coaters is to build market share in emerging sectors, such as nanotechnology or green finishing. “Coatings that have environmentally favorable, low VOCs, can be UV-cured or are waterborne—essentially coatings that have a more benign impact on the environment—are where the market is shifting.”

He cautions that the change isn’t happening overnight. In fact, he says, it’s slower than some might think. But as the technology for green coatings improves, it will become necessary for both chemical suppliers and coaters to be well-positioned in that market.

Harris also advises coaters to continue to pass on both raw material price increases—and savings—to customers, and to expect their coating suppliers to do the same. Although some commodities, like crude oil and titanium dioxide, have seen sharp declines recently, others are up, and the days of suppliers and coaters being the shock absorbers for the industry’s price volatility are over.

A LITTLE PERSPECTIVE

By many accounts, the nation’s recession is expected to last 18 months to two years. Although manufacturing and, by extension, coating, may lag behind other indicators and emerge a little later, time invested in improving your business, ramping up customer service, cutting out inefficiencies, seeking out emerging markets, training your workforce and

diversifying your offerings will be time well spent.

As Johnson put it: “Yes, we’re in a recession. But the root word of recession is ‘recess.’ Remember, that was a good thing when you were a kid. You were doing something and then you did something else for a little while to clear your mind and get you ready to go. I know it will be bad for a lot of people, but if this country can learn from its mistakes and take the time to clear its head, there’s a lot of opportunity for good.” ■

LEARN MORE

2003 Coating Job Shop Survey

It’s been five years since we last conducted this survey. To see how the industry and its concerns have evolved, go to: pfonline.com/articles/100305.html



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