Between Europe and a hard place

Turkey wants a leading chemicals industry, but the task is daunting, say **Agostina da Cunha** and **Sulaiman Hakemy** of **Global Business Reports**

Much like the Turkish economy as a whole, the Turkish chemicals sector has seen significant and positive development and modernisation in the last few decades. It has gone from being a relatively minor producer of basic and intermediate inputs to an attractive M&A market, capable of competing on the world stage.

Internally, chemicals play a big role in the economy. As of last year, the chemicals sector accounted for 6% of Turkey's manufacturing and its exports overtook the automotive industry to generate nearly €10 billion, up from €1.6 billion ten years before. The Turkish regulatory environment is swiftly catching up with Europe's, the government and private sector have created institutions to attract foreign business and Turkish companies are reaching a sufficient scale to look outward.

The global chemicals industry has also changed considerably. Feedstock producers like the Gulf states and Brazil and the behemoth developing markets of India and China, are becoming increasingly dominant players. Growing links between these countries result not only in a parallel value chain to those of the past, but also a very large, partially self-reliant sales market in the global South.

These changes can leave Turkish chemicals firms, many of which are family enterprises passed down through generations, in awkward and unfamiliar territory. Turkey produces little of its own feedstock and is caught between emerging producers in the East and well-established, highly sophisticated incumbent producers to the West.

Along with competition, geographical and commercial proximity to Europe have brought the Turkish chemicals industry at least one valuable asset: the impetus for change. The introduction of REACH in the EU in 2006 marked a turning point.

"Whereas Europe had a long history of frequent and strict regulation, in Turkey REACH came like a tsunami wave," says Melih Babayiğit, founder of **CRAD**, a regulatory consultant. "We knew the first echoes of REACH in 2006 were an indication of further regulations to come; there is a domino effect for eagerness to regulate now."

The demand to jump on board with European regulatory standards has been further fuelled by the Turkish government, which has vowed to increase exports of sophisticated, environmentally friendly and higher value-added chemicals by 2023, the 100-year anniversary of the Turkish Republic. Homegrown industry leaders such as **Kalekim**, the chemical arm of Kale Group, have responded to the call by ensuring that every product, whether or not for sale in European markets, is REACH-compliant.

Labour and overheads are cheap, so Turkish manufacturers have, in principle, a choice. They can use low costs to establish themselves in export markets on the basis of price, or attempt to upgrade the quality of production and focus on high value-added, specialty chemicals. As many senior manufacturing executives have pointed out, however, the sheer scale at which China operates and its ability to secure large feedstock contracts from nearby regions mean that Turkey will not be able to compete on the basis of low prices.

The government has recognised this. Nihat Ergün, minister of science and technology, has stated that for the chemicals industry to contribute adequately to reaching Turkey's target of €375 billion in exports by 2023, there is a need for restructuring, with "higher value-added production systems and products".

Turkey, it seems, is committing itself to upgrading. Increasing partnerships among its larger firms and global giants, such as a recent joint venture between **Aksa** and **Dow Chemical**, will prove instrumental in moving the industry in that direction.

As Turkish companies pick up sufficient mass and capability, they can take advantage of one of Turkey's greatest economic strengths: its location. Even smaller producers, such as **Kazancı**, a water treatment chemicals manufacturer, have started expanding to Africa and the Middle East. They can take advantage of a host of political, commercial and logistics networks that other sectors of Turkish society have already put in place in these regions.

In postwar Iraq, for example, Turkish investment quickly became synonymous with the construction industry, providing an excellent foundation for Turkish industrial chemicals and paints manufacturers to move in. Kalekim is a good example of a large Turkish player that looks to the Iraqi construction market as a good point of entry to the Arab world.

Soner Çetinkaya, Kalekim's vice president of operations, notes that such a strategy comes with challenges. "Kalekim keenly pursues opportunities in the Middle East," he says. "But the geopolitical issues associated with the region mean that we always operate with several doors open to hedge against risks."

Turkish distributors have an obvious advantage in the global chemical trade, though as Rüya Bayegan of the **Bayegan Group** has noted, it comes as a surprise to many in the industry. Bayegan's experiences provide a valuable lesson. The company has hinged its international growth on its ability to make deals eastward and westward.

The recent floundering of Bayegan's joint venture for a Turkey-based polypropylene plant with Advanced Petrochemicals of Saudi Arabia, however, illustrates the challenges of moving into large-scale production and securing feedstock at home. "Turkey will always be a raw materials importer and to be successful the chemicals industry must come to terms with that reality," says Rüya Bayegan.

When it does, it must isolate focus areas and develop a sectoral upgrading plan accordingly. A 'Strategy Document & Action Plan for the Chemicals Industry' revealed by the government in late 2012 is only a starting point for the task ahead. To achieve higher value, efficiency, and sustainability, Ergün has stated, Turkey will need to develop closer ties with energy-rich Russia, Saudi Arabia and Iran. India and China used this strategy with positive results but then they had much greater buying power than Turkey.

Nonetheless, whilst the Turkish chemicals industry still relies heavily on feedstock imports and has yet to transition to higher value-added products, it has now become one to be taken seriously. A process of coordinated modernisation between the government and the private sector is taking root and Turkish firms are gaining the necessary capability to exploit the country's strategic position at the seam of two continents. The only question that remains is whether Turkey can develop the necessary sectoral focus to generate value and the world-class capabilities it needs to compete with the giants at either flank.

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