

IM Profiles

Keramik Laufen

Restructured and ready to grow

by Marcus Saller, Assistant Editor



Ueli Roost (right), CEO, and Martin Hellweg (left), member of the executive board, Keramik Holding AG Laufen

Increased competitiveness in the European ceramic sanitaryware sector and sluggish market conditions in Europe's building industry have forced the main producers of bathroom products to re-think their business strategies. It is expected that this industry will soon be dominated by a handful of producers. Notably, the recent £253m. sale of Armitage Shanks to American Standard could mark the start of rapid consolidations in the European sanitaryware market. Keramik Laufen, one of the main players in the European sanitaryware arena, has made no secrets about its intentions to form strategic alliances. *IM* visited the Swiss sanitaryware producer in late February to find out more about the company's plans.

Europe — consolidation is top priority

With 8,850 employees, a total capacity of 13.5m. pieces and sales of SFr434 (58% of total group sales), *Keramik Holding AG Laufen*, a Swiss family controlled group, is among the five biggest producers of ceramic sanitaryware products in Europe.

What distinguishes Keramik Laufen from other European sanitaryware producers?

Ueli Roost, chief executive officer: "We are a dedicated bathroom ceramics producer. Laufen is the third biggest producer of ceramic sanitaryware in Europe in terms of sales and No. 2 in terms of capacity. In South America, we are No. 1 in both sales and capacity. Keramik Laufen is therefore very well positioned in mature and stable western European and US markets, and in growing, emerging markets in eastern Europe and Brazil."

Martin Hellweg, member of the executive board: "We strongly believe in continental strength. Nowadays, production should not be confined to local but continental markets. Some other competitors, primarily small-sized companies, however, still concentrate their production on individual countries. This, in our view, will not be sustainable in the future and is a key factor of the consolidation we are witnessing."

Keramik Laufen's European partners are Duravit of Germany and Sanitana of Portugal. How are these partnerships structured and where do you have joint ventures?

Mr Roost: "We have a minority stake of 25% in Duravit. Keramik Laufen and Duravit work together in markets where both companies complement each other, like in Austria and Switzerland. We also have a joint venture in Italy. In terms of eastern Europe, we are in the process of re-organising our operations. We also hold a 35% share in Sanitana. The Laufen Group and Sanitana are not integrated a great deal. Sanitana is very well positioned in the Portuguese market and also has good market shares in France. We may increase our stake in Sanitana in the future and fully integrate this company."

Restructuring as a measure of rapid expansion

In the early 1990s, Laufen emerged as an international producer of ceramic products with market shares in the ceramic sanitaryware, tiles, tableware and heavy clays industries on four continents. A period of rapid global expansion, however, led to a stretch in resources and a strong increase in debts, which limited the group's abilities to sustain a strategic position in four mature industries. In 1997, Laufen's new management decided that the group needed

to consolidate its financial and management resources more effectively to achieve a strong ROCE (Return on Capital Employed), improve its operational activities and gain a leading role in its markets.

In how far have you fulfilled your aim to restructure the company?

Mr Roost: "The portfolio restructuring programme has been completed. Of course, in some parts the fulfilment of this programme still needs to be consolidated, but the strategy to concentrate our business, as the Laufen Group decided 1½ years ago and which led to extensive divestments, has been fulfilled."

Extensive divestments

With the goal to consolidate its activities, Laufen identified ceramic sanitaryware as its core business and subsequently sold certain non-core business units, as the table below illustrates.

Laufen Fliesen GmbH, your previous German tile business made heavy losses before its divestment. Was this because it couldn't keep up with strong competition from Italy and Spain – the leading tile producing countries in Europe?

Mr Hellweg: "Generally, the European tile market does not have great profit margins. Therefore it didn't come by surprise how we positioned ourselves in this market. Surely, we were in a particularly difficult competitive situation. With production units in Germany and in the UK, our European tile business was not ideally positioned. Cinca, our previous tile unit in Portugal, on the other hand, operated on good margins. Portugal, along with Italy and Spain, are major tile producing countries. However, we did not find it meaningful to solely keep one single tile unit because we believe in continental growth. Thus we decided to completely divest our European tile business."

Looking at promising markets in eastern Europe

At present, overall demand of ceramic sanitaryware products in western Europe is heavily impacted by sluggish conditions in the construction industry. What are your strategies to compensate this decrease in demand?

Mr Roost: "It is our strength to be geographically diversified, with a presence not only in Europe but also in emerging markets which increases our chances of regional compensation.

Milestones in Keramik Laufen's history

- 1892 Tonwarenfabrik Laufen AG is founded for the production and sale of bricks and roof tiles
- 1925 The group enters the sanitaryware business with the establishment of Keramik Laufen AG, Switzerland
- 1932 Keramik Laufen starts to produce ceramic tiles
- 1952 The group enters Brazil
- 1967 The group enters the tableware business through the acquisition of Oespag, Austria
- 1970 The holding company KHO is founded
- 1982 High pressure casting technology is commercialised
- 1986 Issue of non-voting shares (PS) on the stock exchange
- 1994 Conversion of PS into voting shares
- 1997 A new strategic thrust is announced; Keramik Laufen identifies sanitaryware as its core business

We see further potentials in eastern Europe and the Americas where we want to increase our market share and thus generate growth for Keramik Laufen."

In which eastern European countries, in your opinion, is the greatest growth potential for sanitaryware products?

Mr Roost: "The greatest long-term potentials are in Russia but it is hard to say how long it will take to develop a lasting economy in this country. In the short-term, potentials are in the Czech Republic, Poland and also in Hungary."

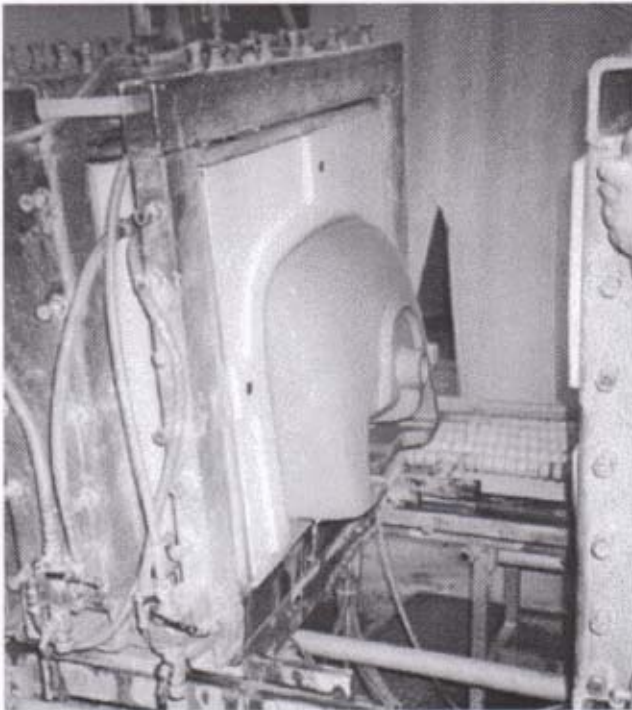
Mr Hellweg: "Overall, growth markets are in countries where people buy our products for the first time. There is a great potential for sanitaryware because at present only one third of the world's population use ceramic bathroom products. Of course, you're asking this question at a time where people have a critical attitude towards investments in emerging markets. In the long-term, however, this attitude may be different again. As mentioned before, Laufen managed to achieve a good balance between its participation in mature markets and in growth markets, and we intend to continue this way. It provides the right balance."

So, what are your concrete plans for eastern Europe?

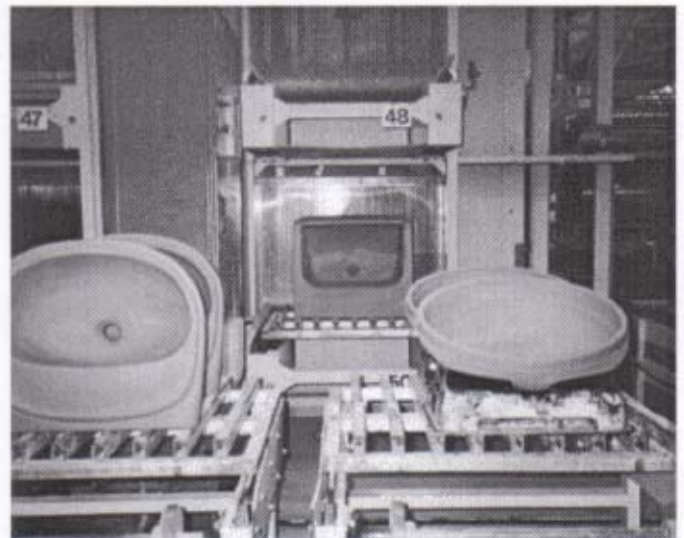
Mr Roost: "At present, we do not intend to expand further in this

Keramik Laufen's divestments of non-core assets

- Nov 1997 Laufen sells tableware division
- Jan 1998 Laufen divests its German tile business, Laufen Fliesen GmbH, to Deutsche Steinzeug Cremer & Breuer AG of Germany
- Sep 1998 Laufen announces sale of its heavy clay business. Tonwarenfabrik Laufen AG of Switzerland, Migeon SA and Bisch SNC of France and Tonwerk Kandern GmbH of Germany are divested to the Belgian-Austrian consortium Koramic/Wienerberger
- Sep 1998 Companhia Industrial de Ceramica SA (CINCA), Laufen's Portuguese tile business, is sold to Italy's Gruppo Ceramiche Ricchetti SpA
- Sep 1998 85% of UK-based tile wholesaler Bellegrove Ceramics PLC are sold to Cisa-Cerdisa SpA, Italy and the remaining 15% to Gruppo Ceramiche Ricchetti SpA, Italy. The two buyers are controlled by Italian Fincisa SpA



One of Keramik Laufen's pressure casting systems in operation: the pressure is released and a washbasin is separated from the mould



Washbasins entering a dryer at the company's Swiss sanitaryware plant

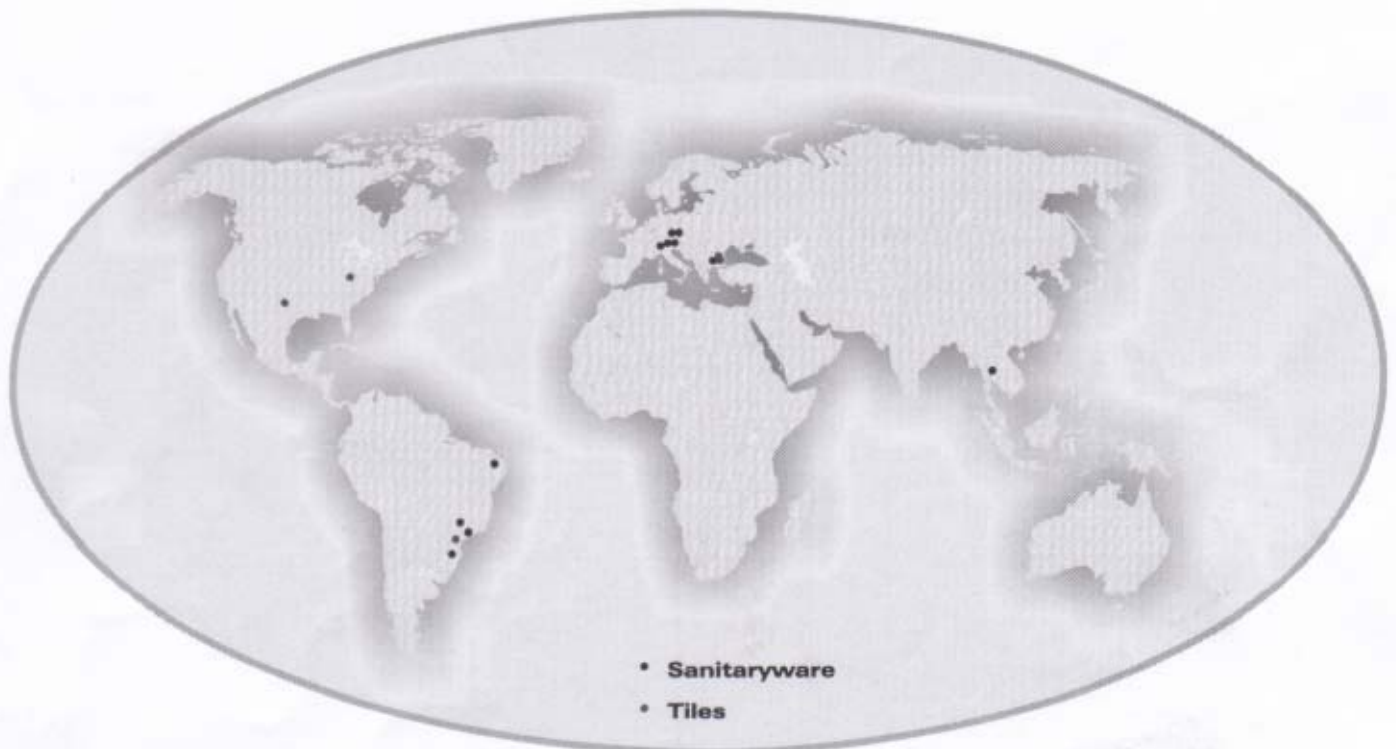
region. For the next two to three years, we see the greatest potential in optimising our existing operations in eastern Europe. With two production units in the Czech Republic and one unit in Bulgaria, Keramik Laufen is well positioned for growth potentials in Europe. We strongly believe in

continental sourcing which means that we aim to combine our operations to supply several markets from one production site. In the past production units primarily served domestic markets which did not bring about optimal cost structures."

Is there a danger that cheap products from countries such as Turkey will be dumped in western Europe?

Mr Roost: "Of course, especially as the trend to buy cheaper products and "do-it-yourself" is increasing in Europe. However, compared to the USA, where they have a completely different distribution and installation philosophy,

Keramik Laufen's global production sites



this trend is still relatively small in Europe."

Mr Hellweg: "I think we are well prepared for this change. Firstly, we have gained significant experience in the USA, selling to DIY and Home Centers. In the USA, we enjoy an excellent position in this segment. Secondly, as a leading sanitaryware player in Europe, we can and must be able to offer competitive products in all segments, including the DIY segment."

Pioneers in pressure casting

Keramik Laufen's plant in Laufen, Switzerland, hosts a number of high-tech facilities, ranging from CAD/CAM computing methods for the detailed design of various products, and high pressure casting technology to a fast dryer (5-6 hours per item) and a fast firing kiln. One part of this plant is fully automated, featuring a sophisticated barcode system which enables a computer to follow each item through the production process after the mould has been removed. In this way it can be determined where errors occur in the production line.

Keramik Laufen was the first company to commercialise a pressure cast system at its plant, and it has been successful to sell the know-how of this advanced production technology to other leading producers worldwide.

Which of your global operations use pressure casting?

Mr Hellweg: "Nearly all of our production units have pressure casting systems, including our four operations in Brazil. What you can achieve through pressure casting of washbasins cannot even be beaten by the low cost of labour in Brazil."

Consolidation efforts at full stretch

In February 1999, the European ceramic sanitaryware industry witnessed a further spate of consolidation when it became known that *Blue Circle Industries's* bathroom arm — consisting of UK-based *Armitage Shanks* and *Ceramica Dolomite* of Italy — was sold to *American Standard Inc.* This acquisition will enable *Ideal Standard*, a wholly owned subsidiary of the US-group, to strengthen its position in the European market.

When Blue Circle launched an auction for its bathroom division at the end of 1998, it did not come as a surprise that the name Laufen also appeared on the list of interested parties.

What were your main interests in Blue Circle's sanitaryware arm? Armitage Shanks, for example, has strong market shares in France and the UK.

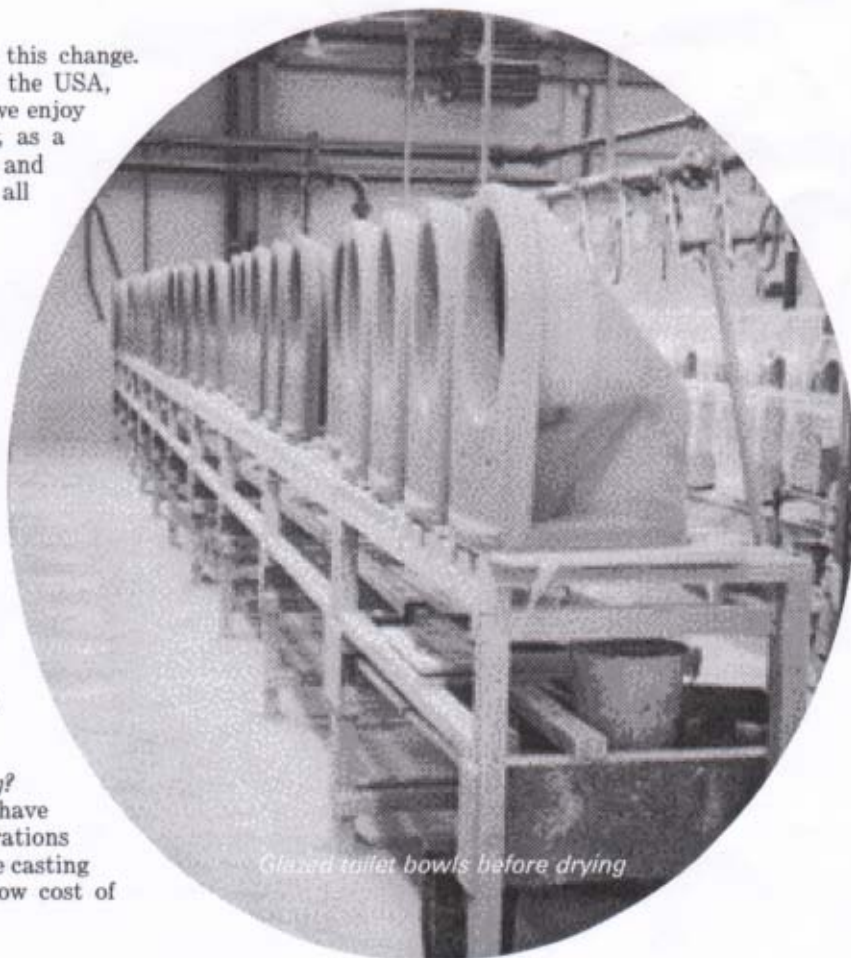
Mr Roost: "We are very convinced that the European sanitaryware industry will and has to consolidate. As we want to take part in this consolidation process, the offer of Blue Circle's sanitaryware arm presented a good opportunity for us, especially since it is very rare that one of the few major European producers is put up for sale. We were very interested in Blue Circle's operations in Italy, where we are a respected but still relatively small player, and in the UK, where we have no significant presence yet. We got out of this process because we felt that the suggested price for Blue Circle's bathroom division could not be justified."

Have you decided when the merger with another European sanitaryware producer should take place?

Mr Roost: "I don't want to set a deadline. All I can say is that we are currently working at full stretch on this subject."

Are you in discussions with other producers?

Mr Roost: "Discussions with other players happen all the time. As I already said, we don't make any secret about our intentions to take part in this consolidation process, in one way or the other."



Glazed toilet bowls before drying

Strategies for markets in the Americas

Besides Keramik Laufen's sanitaryware activities in Europe, the company also owns four sanitaryware production units and one tile unit in Brazil, and a further two tile businesses in North America.

Tiles — making a virtue out of necessity

In 1998, Laufen was able to maintain operating margins in its core business of sanitaryware in Brazil, but it suffered from margin erosions because of depressed markets in its tile business which have delayed the company's return to profitability. The devaluation of Brazil's currency further aggravated already stiff competition in the domestic tile industry.

Is there a possibility that you completely divest your tile business in the future?

Mr Hellweg: "We thought of divesting our tiles unit in Brazil last year. However, Brazil subsequently went straight into an economic turmoil, and it was simply not the right time to exit. Also, we first have to turn the operation around. We have a dedicated team in place that will make this turnaround happen. Of course, today, after the devaluation of the Real, Tiles Brazil has already become much more competitive. We have made a virtue out of necessity and integrate our tile business units in South and North America in terms of sourcing. Similar to the way we operate in the European sanitaryware market, it is also possible to serve the North American tile market with products from our Brazilian units. There is no reason to produce tiles for these markets outside the Americas because you can cover the whole product range — from low cost products to high quality product — from units within this region. In North America, home-centres are the fastest growing market for tiles with *Home Depot* as the biggest building products mass-merchandiser chain. Through our strong presence within this particular market we

will have the opportunity to keep pace with the aggressive growth rates of home centres which are now expanding into South America, where we welcome them as a professional client and partner. Tiles Brazil is now an important part of our Americas strategy for this industry. We seize an opportunity that arose out of the economic turmoil."

Sanitaryware — a market leader

Mr Hellweg: "With a market share of 52-53%, we are the leader in the Brazilian sanitaryware market. Our operation has reached a capacity of 8.1m. pieces per year, one wonders whether it might be feasible to export to other countries. For the next few months, we will primarily focus on our operative turn-around in Brazil. But in the second half of 1999, and naturally in the near future, we will be considering the possibility to gain a foothold in neighbouring markets with small, stable and strategic market shares — similar to our approach in Italy."

...and what about Asia?

During Laufen's rapid global expansion in the early 1990s, the company also tried to put its foot down in Asia and win market shares by building a sanitaryware plant in Thailand.

What were your original plans and strategies for Asia up to two years ago?

Mr Hellweg: "Quite frankly, in the past, Laufen not only tried to gain a foothold in too many industries but also to win market shares on too many continents. Our plant in Thailand is certainly a good basis for Asia and we might have good

opportunities when markets in this region recover. But Laufen's plans to expand into Vietnam and China within a period where we had market potentials in Europe and South America, were far too ambitious. We have a continental business which means that a strength on one continent, such as Asia, cannot make up for the possibilities we have by consolidating our existing businesses. Therefore, Laufen has dismissed the plans to penetrate into Asia beyond our Hong Kong presence and Thailand investment for the moment. Consequently we also discontinued our Vietnamese project to build a production unit and win market shares in this country."

What about China? American Standard, for instance, set other competitors an example by penetrating into China. And the company is now in the process to build another production unit in this country.

Mr Roost: "China has enormous production capacities in the ceramic sanitaryware sector. It is not very difficult to produce in this country but to distribute your products. It will therefore be interesting to see how successful American Standard will be in China. It is quite possible that other competitors will follow their example and expand into China. For Laufen, we have no plans for China at present. It is one of our main priorities to form a strategic alliance in Europe. Once we have developed our business from a strong position in this region, we can again see to bigger tasks."

Acknowledgment

The author would like to thank Keramik Laufen for the kind invitation to its Swiss headquarters and plant, its hospitality, and for the assistance in the production of this profile. 