

Paints and Coatings

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I N D U S T R Y P R O F I L E

1990-1991

PAINTS AND COATINGS

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FOREWORD

In a rapidly changing global trade environment, the international competitiveness of Canadian industry is the key to growth and prosperity. Promoting improved performance by Canadian firms in the global marketplace is a central element of the mandates of Industry, Science and Technology Canada and International Trade Canada. This Industry Profile is one of a series of papers in which Industry, Science and Technology Canada assesses, in a summary form, the current competitiveness of Canada's industrial sectors, taking into account technological, human resource and other critical factors. Industry, Science and Technology Canada and International Trade Canada assess the most recent changes in access to markets, including the implications of the Canada-U.S. Free Trade Agreement. Industry participants were consulted in the preparation of the profiles.

Ensuring that Canada remains prosperous over the next decade and into the next century is a challenge that affects us all. These profiles are intended to be informative and to serve as a basis for discussion of industrial prospects, strategic directions and the need for new approaches. This 1990-1991 series represents an updating and revision of the series published in 1988-1989. The Government will continue to update the series on a regular basis.

Michael H. Wilson
Minister of Industry, Science and Technology
and Minister for International Trade

Structure and Performance

Structure

The paints and coatings industry consists of manufacturers of paints, varnishes, lacquers, shellacs and stains. It includes two distinct subsectors — architectural and industrial — which are about equal in size in terms of value of shipments. On a volume basis, however, architectural coatings (also known as *trade coatings*) account for about 60 percent of production. The architectural coatings subsector depends heavily on the performance of the construction sector, whereas industrial coatings are linked closely to the automotive, major appliance and industrial equipment sectors.

Architectural coatings include interior and exterior house paints, primers, sealers, varnishes and stains. They are sold to contractors and the general public through retail and

wholesale outlets as well as direct to large commercial accounts. Of the retail portion, about 45 percent is sold through small hardware and decorator centres, 40 percent through large chains such as Canadian Tire, The Bay, Sears and Beaver Lumber (largely under private-brand labels) and the balance through company-owned stores.

Industrial coatings include automotive paints, can coatings, coil coatings, furniture finishings and road-marking paints. Most of these products are sold direct to the end user.

Paints and coatings are formulated products. The base material, known as the *binder*, is the film-forming ingredient that largely determines the performance characteristics of the coating. In the past, binders were natural products such as linseed or soybean oils. Today, to achieve higher performance, almost all binders are synthetic polymers, including high-volume resins such as alkyds, acrylics, vinyls, epoxies and urethanes, or lower-volume specialty resins such as

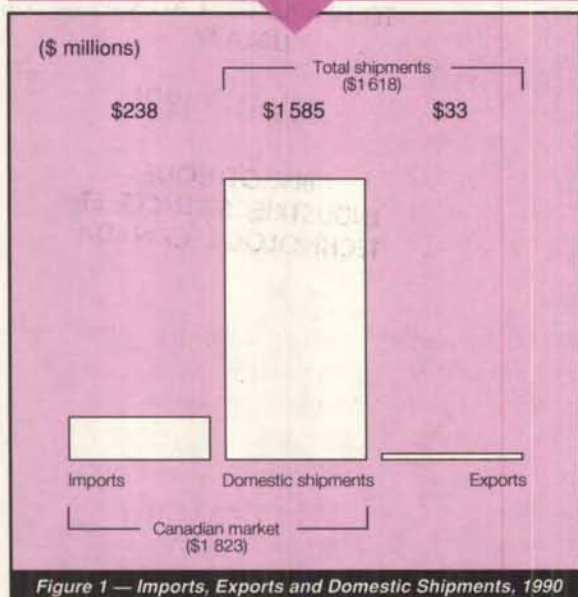


Figure 1 — Imports, Exports and Domestic Shipments, 1990

polyesters, phenolics and silicones. The binder is compounded with fillers to extend the product, pigments to impart colour and solvents to control viscosity. Small quantities of a large number of other chemicals, such as thickeners, biocides, plasticizers, dispersants, defoamers, ultraviolet absorbers, driers, emulsifiers and adhesion promoters, are added as required in each formulation.

In 1990, the industry consisted of about 150 establishments and employed approximately 8 400 people. There is some ownership concentration in the industry. About 7 percent of the firms, each employing more than 200 people, accounted for 40 percent of the value of shipments. Conversely, there is a large number of small participants in the industry; 70 percent of the establishments employ fewer than 50 people and account for an aggregate 20 percent of the value of shipments. About two-thirds of the larger firms are foreign-controlled. Most of the smaller firms are Canadian-controlled.

In 1990, industry firms shipped goods with an estimated value over \$1.6 billion (Figure 1). Exports totalled \$33 million, representing 2 percent of shipments. Imports were valued at \$238 million and accounted for 13 percent of the Canadian market.

On a regional basis, 87 percent of shipments originate in Ontario and Quebec, 12 percent in Western Canada, and 1 percent in the Atlantic provinces. While most of the larger manufacturers of industrial coatings are located in southern Ontario, some of the larger architectural coatings producers have plants in several provinces. Regional manufacturers of architectural paints serve local markets across the country in competition with national firms.

Chemical companies supply both domestic and imported raw materials to most of the industry. A few of the larger coatings manufacturers are vertically integrated, producing resins, either in Canada or elsewhere in their corporate network, for captive consumption. The degree of imported raw material content varies with the type of coating, reaching as high as 50 percent of the value of materials for some specialty coatings. Overall, an estimated 25 percent of materials used by the industry is imported.

Supply and demand fluctuations lead to periodic raw material shortages, the most recent being titanium dioxide during the mid-1980s. The worldwide supply of this important white pigment was so tight that paint manufacturers were put on allocation. However, the construction of new titanium dioxide capacity, coupled with decreased demand, alleviated the shortage by the end of the 1980s.

Performance

During the 1981–1982 recession, the industry gross domestic product (GDP) dropped far below the levels that had been achieved in the 1970s. The GDP did not surpass its pre-recession levels until 1987, and it still has not surpassed the historic highs that were recorded in the late 1970s. Between 1983 and 1988, the industry GDP in constant 1986 dollars grew at a real average annual rate of 7.3 percent. However, GDP declined in 1989 and again in 1990 so, when averaged over the 1983 to 1990 period, the real average annual growth rate drops to 2.5 percent.

The paints and coatings industry serves mature markets. New coating technologies typically displace older technologies with little increase in overall demand, a situation that is expected to continue. The performance of this industry is highly cyclical, closely following the business cycles of its major customers. The strong recovery from 1983 to 1989 reflected the general strength in all sectors of the manufacturing economy at that time, while the decline after 1989 coincided with the onset of a new recessionary period (Figure 2).

Between 1983 and 1990, the number of establishments remained nearly constant. Meanwhile, total employment increased in most years in order to satisfy the increased demand, indicating that the industry remains labour-intensive in nature.

International trade is predominantly with the United States. In 1990, some 92 percent of imports originated in the United States, while 95 percent of exports were shipped to that country. Most trade activity involves specialty and industrial coatings. There is comparatively little international commerce in architectural coatings, since these lower-value products cannot support high transportation costs.

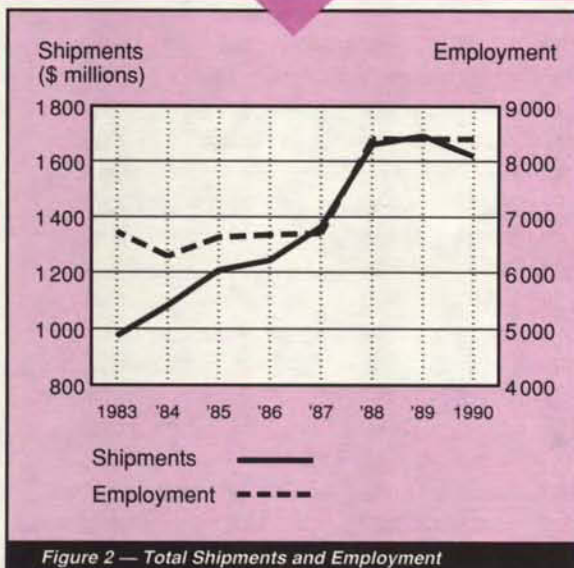


Figure 2 — Total Shipments and Employment

The problems faced by the Canadian industry, such as increasing raw material costs, fierce price competition for architectural coatings and relatively low growth and profitability, are similar to those of the coatings industries in other industrialized nations.

Strengths and Weaknesses

Structural Factors

A large portion of the industry is controlled by multinational firms. These firms had originally established plants in Canada largely because of the high Canadian tariffs on imported paints and coatings. In general, Canadian subsidiaries have tended to serve only the domestic market. Important factors affecting the competitiveness of the paints and coatings industry are the scale of manufacturing, raw material prices and transportation costs.

Canadian manufacturers generally operate on a much smaller scale than their U.S. counterparts. Canadian batches rarely exceed 15 000 litres, whereas in the United States batches of 45 000 litres are common. As a result, industry productivity is lower in Canada than in the United States. The implementation of the Canada-U.S. Free Trade Agreement (FTA) may provide Canadian manufacturers with the stimulus to focus on specific products and to seek expanded markets, thereby moving towards improved economies of scale.

Raw materials represent the most significant production cost, amounting to 50 percent of the value of shipments. By comparison, production labour and energy represent 7 and 1 percent, respectively, of the value of shipments.

A number of raw materials are imported, and some of those currently are dutiable. This, together with the higher unit costs for the smaller quantities in which they are purchased, means that raw materials cost an estimated 5 percent more in Canada than in the United States.

Transportation is another important cost factor. For architectural coatings, freight can represent as much as 10 percent of the selling price. Transportation costs have made it difficult for single-plant firms with a policy of national coverage to sell profitably in competition with regional manufacturers serving local markets. Industrial coatings are usually more profitable and the effect of transportation costs on the final price are not as significant. Furthermore, industrial coatings are often shipped in bulk to original equipment manufacturers, substantially reducing freight costs.

Trade-Related Factors

As of 1 January 1991, the duty on coatings imported into Canada from the United States is 3.7 percent. The duty on Canadian products entering the United States ranges from 0.7 to 2.4 percent, depending on the chemical composition of the product.

Canadian tariffs have offset some of the cost advantages that U.S. firms have had because of their larger production runs. Under the FTA, Canadian and U.S. tariffs on paints and coatings will be eliminated in five annual, equal stages ending 1 January 1993. In the more competitive environment of the 1990s, Canadian companies may need to specialize in order to achieve longer production runs. They may also need to add more high-technology products (with accompanying higher margins) to their product lines. Both these strategies will be easier to undertake if the companies can expand their markets beyond Canada's borders.

The Canadian tariff on products from countries having Most Favoured Nation (MFN) status is 9.2 percent. Canadian exports are assessed tariffs of 10 percent upon entering the European Community (EC) and from 4.6 to 6 percent when entering Japan.

Technological Factors

Although the manufacture of paints and coatings involves relatively simple processes, extensive knowledge and experience with the raw materials as well as their formulation and compounding is essential. Only a few companies perform research and development (R&D) in these areas in Canada. Most Canadian subsidiaries depend on their foreign parents to provide new technology. Other firms in the industry rely on the large resin producers to develop new polymer systems and guidelines for their use, then fine-tune the formulations themselves.



Environmental as well as health and safety considerations are motivating much of the ongoing technological development. For example, paints and coatings have been identified as significant sources of volatile organic compounds (VOCs). In combination with nitrogen oxides, VOCs are responsible for the buildup of ground-level ozone in populous regions of Canada. This ozone causes respiratory problems, vegetation damage and material degradation. A program is being developed by the Canadian Council of Ministers of the Environment to target the reduction of VOCs in coatings formulations and to limit emissions from plants manufacturing or using these products.

There has been a significant shift during the past 20 years in the use of formulations based on petroleum solvents to formulations based on water as the primary solvent. In addition to reducing VOC emissions, water-based formulations offer advantages such as lower cost, easier clean-up, less odour and faster drying. However, there are still applications where the necessary performance can be achieved only by using solvent-based systems. Research is continuing to further reduce solvent content while retaining its beneficial properties. Products such as radiation-curable and powder coatings contain little or no solvent but require specialized application equipment and are not suitable for use on all surfaces.

Other Factors

Several key federal and provincial legislative and regulatory regimes deal with the import, transport, storage, manufacture, use or sale of hazardous chemical substances or goods. These include the *Transportation of Dangerous Goods Act* (both federal and provincial regulations), the *Hazardous Products Act*, the *Occupational Health and Safety Act*, the *Canadian Environmental Protection Act* (CEPA) and the Workplace Hazardous Materials Information System (WHMIS).

The industry in Canada, as in many other countries, is experiencing increasing costs for compliance with environmental and safety regulations. Although these regulations reduce profitability in the short term, they also present manufacturers with an opportunity to develop safer replacement products and thereby gain a competitive advantage.

Through the Canadian Paint and Coatings Association, the industry works closely with government to ensure that its products and processes conform to legislative requirements. Due in part to this effort, there has been little negative impact on the industry from raw material restrictions (e.g., limitations on the allowable concentrations of mercury and lead) and environmental regulations. Recently, the association launched

a pilot paint recycling program, which involves the collection of waste paint for recycling by participating manufacturers.

The specification and selection of paints and coatings is facilitated through the use of qualified products lists maintained by the Canadian General Standards Board (CGSB). Products on the lists have been independently tested to ensure that they meet the requirements of the applicable CGSB standards, thus providing the purchaser with some assurance of product quality. New products are added at the request and expense of manufacturers, subject to a satisfactory assessment. Products previously listed are periodically retested to ensure that they continue to meet the requirements.

The Environmental Choice Program sponsored by Environment Canada establishes guidelines for selected products, including water-based and solvent-based paints. Products that satisfy the applicable requirements become eligible to display the EcoLogo symbol (three entwined doves forming a stylized maple leaf). Manufacturers are finding that the EcoLogo is a strong marketing tool among consumers who are becoming more environmentally aware.

An emerging, non-environmental issue relates to the cans used to package architectural paints. Increasingly, the four-litre can is in direct competition with U.S.-gallon cans, and the Canadian industry is facing some pressure to convert from the metric to the U.S. measure. The four-litre can is about 6 percent larger than the U.S.-gallon can but, since the selling prices are usually the same, the profit on a U.S.-gallon can is correspondingly higher. Some Canadian manufacturers believe that converting to the U.S. standard is necessary in order to compete in that market. However, others believe that there is a marketing advantage in offering more paint for the money and that the costs of converting machinery and relabelling to accommodate a different can size are not justifiable. Manufacturers who continue to use four-litre cans must either be successful in promoting their larger volume to gain market share or be prepared to accept lower profit margins than competitors using U.S.-gallon cans.

Evolving Environment

The paints and coatings industry in Canada and throughout the world is fragmented. There are many participants, many types of product and many markets to be served. In the past few years, there has been a worldwide trend towards ownership concentration of this industry through acquisition or merger. Acquisition has been used to gain access to new technology, allow rationalization of production facilities and provide immediate access to new regional markets. Global concentration within this industry has



resulted in a change in ownership for some subsidiary operations in Canada, and some rationalization has occurred.

Implementation of the FTA is not in itself strongly affecting profitability in the domestic market. Whereas the FTA does result in lowered raw material costs, the effect on profits is counterbalanced by lowered finished-product selling prices. The elimination of tariffs provides additional incentive for foreign-controlled firms to rationalize their operations on a North American basis. Rationalization allows plants to focus on a narrower product range and achieve the production volumes necessary to be internationally competitive.

Most multinationals already supplying the Canadian market through subsidiaries are expected to continue to do so in a free trade environment. According to industry representatives, the need for a warehousing/distribution centre in Canada as well as the increased costs of transportation and customer service would offset any benefit that might be derived from supplying Canadian customers from U.S. plants.

At the time of writing, the Canadian and U.S. economies were showing signs of recovering from a recessionary period. During the recession, companies in the industry generally experienced reduced demand for their outputs, in addition to longer-term underlying pressures to adjust. In some cases, the cyclical pressures may have accelerated adjustments and restructuring. With the signs of recovery, though still uneven, the medium-term outlook will correspondingly improve. The overall impact on the industry will depend on the pace of the recovery.

Competitiveness Assessment

Worldwide consumption of paints and coatings is not expected to grow significantly. New technological developments will continue to reorient the markets by displacing older products.

Since the Canadian paints and coatings industry is dominated by foreign-owned companies and the bulk of international trade is with the United States, most firms do not compete in markets outside North America. Indeed, very few Canadian-owned firms have manufacturing facilities in the United States or co-operative agreements with companies in that market. Although free trade narrows the price gap, product prices are expected to remain somewhat higher in Canada than in the United States because of the higher costs of transportation and provision of technical service.

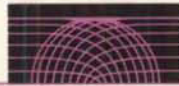
Despite the mature market for architectural coatings and the protection afforded by the cost of transportation, increased competition from the United States is occurring. The more

competitive environment is causing the industry to reassess its business strategy. Canadian-owned companies will have to improve their access to state-of-the-art technology, move to larger-scale production of a narrower product range and develop expanded export markets. The prospects for continued success and growth are best for Canadian producers who are able to expand their traditional markets by offering high-quality products at a competitive price.

Higher overall growth will occur in the industrial coatings subsector. Foreign competition in these products is expected to become more intense as companies assume a global business orientation. Much of this business is controlled by multinationals, whose subsidiaries in Canada have ready access to new technology. The FTA will probably encourage greater rationalization between foreign-owned plants in Canada and affiliated plants in the United States. The challenge for subsidiaries in Canada is to secure North American mandates for the manufacture of specific products.

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PRINCIPAL STATISTICS^a

	1983	1984	1985	1986	1987	1988	1989	1990
Establishments	148	151	145	145	131	151	150 ^b	150 ^b
Employment	6 725	6 291	6 630	6 677	6 763	8 404	8 400 ^b	8 400 ^b
Shipments (\$ millions)	975	1 081	1 207	1 243	1 364	1 660	1 692 ^c	1 618 ^c
GDP ^d (constant 1981 \$ millions)	265	307	340	299	333	341	342	309
(constant 1986 \$ millions)	373	432	480	427	482	532	505	456
Investment ^e (\$ millions)	15	19	23	43	31	29	37	53
Profits after tax ^f (\$ millions)	62	108	101	102	116	N/A	N/A	N/A
(% of income)	4.5	7.3	6.0	5.6	6.1	N/A	N/A	N/A

^aFor establishments, employment and shipments, see *Chemical and Chemical Product Industries*, Statistics Canada Catalogue No. 46-250, annual (SIC 3751, paint and varnish industry).

^bISTC estimates.

^cSee *Monthly Survey of Manufacturing*, Statistics Canada Catalogue No. 31-001, monthly.

^dSee *Gross Domestic Product by Industry*, Statistics Canada Catalogue No. 15-001, monthly. GDP in constant 1986 dollars has been used to calculate the growth rates contained in the text. Figures in constant 1981 dollars are included for comparison with other profiles in this series.

^eSee *Capital and Repair Expenditures, Manufacturing Subindustries, Intentions*, Statistics Canada Catalogue No. 61-214, annual. Repairs not included.

^fSee *Corporation Financial Statistics*, Statistics Canada Catalogue No. 61-207, annual.

N/A: not available

TRADE STATISTICS

	1983	1984	1985	1986	1987	1988 ^a	1989 ^a	1990 ^a
Exports ^b (\$ millions)	15	18	19	19	23	17	21	33
Domestic shipments (\$ millions)	960	1 063	1 188	1 224	1 341	1 643	1 671	1 585
Imports ^c (\$ millions)	111	149	173	184	233	191	218	238
Canadian market (\$ millions)	1 071	1 212	1 361	1 408	1 574	1 834	1 889	1 823
Exports (% of shipments)	2	2	2	2	2	1	1	2
Imports (% of Canadian market)	10	12	13	13	15	10	12	13

^aIt is important to note the data for 1988 and after are based on the Harmonized Commodity Description and Coding System (HS). Prior to 1988, the shipments, exports and imports data were classified using the Industrial Commodity Classification (ICC), the Export Commodity Classification (XCC) and the Canadian International Trade Classification (CITC), respectively. Although the data are shown as a continuous historical series, users are reminded that HS and previous classifications are not fully compatible. Therefore, changes in the levels for 1988 and after reflect not only changes in shipment, export and import trends, but also changes in the classification systems. It is impossible to assess with any degree of precision the respective contribution of each of these two factors to the total reported changes in these levels.

^bSee *Exports by Commodity*, Statistics Canada Catalogue No. 65-004, monthly.

^cSee *Imports by Commodity*, Statistics Canada Catalogue No. 65-007, monthly.



SOURCES OF IMPORTS^a (% of total value)

	1983	1984	1985	1986	1987	1988	1989	1990
United States	93	93	92	89	90	90	92	92
European Community	6	6	6	9	9	8	6	6
Pacific Rim	-	-	-	1	-	1	1	1
Other	1	1	2	1	1	1	1	1

^aSee *Imports by Commodity*, Statistics Canada Catalogue No. 65-007, monthly.

DESTINATIONS OF EXPORTS^a (% of total value)

	1983	1984	1985	1986	1987	1988	1989	1990
United States	84	85	83	82	87	84	87	95
European Community	2	2	4	6	3	7	3	1
Pacific Rim	3	2	6	4	5	2	3	1
Other	11	11	7	8	5	7	7	3

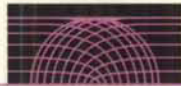
^aSee *Exports by Commodity*, Statistics Canada Catalogue No. 65-004, monthly.

REGIONAL DISTRIBUTION^a (average over the period 1986 to 1988)

	Atlantic	Quebec	Ontario	Prairies	British Columbia
Establishments (% of total)	4	25	53	7	11
Employment ^b (% of total)	2	25	63	4	6
Shipments ^b (% of total)	1	20	67	3	9

^aSee *Chemical and Chemical Product Industries*, Statistics Canada Catalogue No. 46-250, annual.

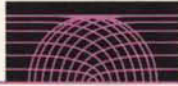
^bData shown for Atlantic and Prairie provinces are ISTC estimates.



MAJOR FIRMS

Name	Country of ownership	Location of major plants
BASF Canada Inc.	Germany	Brantford, Ontario Windsor, Ontario
Benjamin Moore & Co. Ltd.	United States	Toronto, Ontario Burlington, Ontario Montreal, Quebec Vancouver, British Columbia
Cloverdale Paint Inc.	Canada	Surrey, British Columbia Edmonton, Alberta
Color Your World Corp.	Canada	Toronto, Ontario Vancouver, British Columbia
Du Pont Canada Inc.	United States	Ajax, Ontario
General Paint Ltd.	United Kingdom	Vancouver, British Columbia
ICI Paints (Canada) Inc.	United Kingdom	Concord, Ontario Boucherville, Quebec
International Paints (Canada) Limited	United Kingdom	Baie-d'Urfé, Quebec Regina, Saskatchewan
PPG Canada Inc.	United States	Mississauga, Ontario
Para Inc.	Canada	Brampton, Ontario
Pratt & Lambert	United States	Fort Erie, Ontario
Prilco Inc. ^a	Canada	Etobicoke, Ontario
Selectone Paints Limited	Canada	Weston, Ontario
Sico Inc.	Canada	Beauport, Quebec Longueuil, Quebec Outremont, Quebec Rexdale, Ontario St. Catharines, Ontario
Valspar Inc.	United States	West Hill, Ontario

^aPrilco Inc. is the architectural coatings segment of the former DeSoto Coatings Ltd., acquired by Sico Inc. in 1991. Previously, the aerospace coatings segment of DeSoto had been sold to PRC Canada Inc., and the industrial coatings segment had been sold to Valspar Inc.



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