



Chemical Industries (Colombo) PLC (CIC)

CIC.N - Rs. 69.00 ; CIC.X - Rs. 44.25

BUY

Financial Year	Group Turnover (Rs.Million)	Operating Profit (Rs.Million)	PAT (Rs.Million)	Earnings to Equity (Rs. Million)	EPS (Rs.)	EPS Growth (%)	PER (x) - Voting	PER (x) - Non Voting
2008	14,121.8	1,218.7	744.7	509.8	5.4	3.33	12.8	8.2
2009	15,683.4	899.8	474.5	407.6	4.3	(20.05)	16.0	10.3
2010E	17,746.7	1,324.6	778.3	585.8	6.2	43.72	11.2	7.2
2011E	19,583.8	1,465.9	808.6	620.5	6.5	5.92	10.5	6.8
2012E	21,623.9	1,623.1	1,044.8	819.2	8.6	32.03	8.0	5.1
2013E	23,884.3	1,798.2	1,272.8	1,010.8	10.7	23.38	6.5	4.1
2014E	26,390.4	1,993.2	1,481.6	1,184.5	12.5	17.19	5.5	3.5

CIC			
Reuters Code	CIC.CM		
Bloomberg Code	CIC.SL		
Share Price LKR			
	Voting	69.00	
	Non Voting	44.25	
Issued Share Capital (Shares)			
	Voting	72,900,000	
	Non Voting	21,870,000	
12 mth High/Low (Rs.)			
	Voting	71.25 / 30.50	
	Non Voting	46.25 / 20.00	
Average Daily Volume (Shares)			
	Voting	135,045	
	Non Voting	111,222	
Market Capitalisation Rs. mn			
	Voting	5,030	
	Non Voting	968	
Price Performance (%)			
	1 mth	6 mth	12 mth
ASPI	2.56	31.22	133.70
CIC.N	3.79	4.18	120.97
CIC.X	10.37	13.13	126.25

Executive Summary

Originally set-up as a Trading House for ICI - UK, CIC has pursued a policy of planned growth which has resulted in its diversification in to a number of fields over the years. The company is in to agriculture, paints and chemicals, pharmaceuticals, industrial raw material and packaging etc.

CIC Agri Businesses, the biggest contributor in terms of revenue and earnings to the group, comprises of companies that provide inputs to the agricultural sector. The construction sector is effectively CIC's paints and surface coatings business which is under the group's associate CIC Paints. CIC's quoted subsidiary Chemanex is a manufacturer and marketer of chemicals and industrial intermediates. Chemanex markets chemicals to the rubber industry and distributes and mixes paints made by CIC.

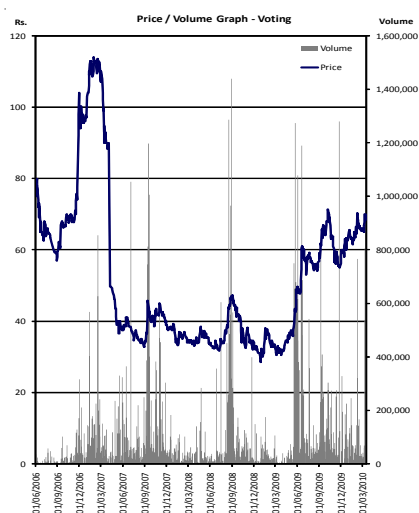
The group's revenue grew by nearly 11% during FY09, despite a 73% reduction in revenue from the construction segment as a result of the accounting treatment to CIC Paints which became an associate from subsidiary from 3QFY08. Revenue from the segment also declined consequent to double digit inflation which adversely affected the consumers' purchasing power.

Earnings to Equity for FY09 declined 20% as a result of an adjustment to its inventory of fertilizer which was written down by Rs. 496 million due to the decline in global commodity prices. Further, by the end of FY09, the GoSL owed over Rs. 900 million in subsidy to CIC, part of which, amounting

to Rs. 250 million for the period November 2008 to March 2009, was received in 3QFY10.

We expect CIC's revenue to grow at a 5 year CAGR of 11% and earnings to equity at 24% CAGR from FY09 with agriculture and livestock sector contributing to approximately 70% of the total turnover. The above forecasts exclude any refund from the GoSL in the form of the subsidy, therefore, any such disbursement will further boost earnings. The operating profit margin is expected to hover around 7% - 8% for the next 4 years from 6% in FY09 mainly due to the cost and scale advantage from retooling the value chain.

Earnings to equity for FY09 included a net gain on sale of investments of Rs. 245 million which comprises the gain from the sale of Commercial Leasing PLC and Dev Fern (Pvt) Ltd. For FY10E the group is expected to post Rs. 586 million excluding any refunds from the GoSL. At a price of Rs. 69, the voting share is trading at a P/E of 10.54x while the non voting counter trades at a multiple of 7 times, at a price of Rs. 44.25. With much of the growth seen from the North and East in the agriculture and paints sectors, we expect the long run to be more rewarding. We believe that prospects of steady growth demand a re-rating of the counter, with growth stemming from agriculture in the longterm and untapped potential in the North & East.



Background of the company

Chemical Industries Colombo diversified into many sectors since its inception in 1940s. Commencing with the manufacture of 'Alkathene' agricultural plastic pipes in the late 1940's and the marketing of a range of ICI paints manufactured locally by Paints and General Industries Ltd. In 1967, Chemical Industries Colombo is currently engaged in agriculture, paints and chemicals, consumer and pharmaceuticals, industrial raw material and packaging and etc.

CIC which started operations with an employee base of approximately 60 in 1964 has over 200 employees today excluding those at its subsidiaries and associate companies.

Segmental Profile

Agriculture

CIC Agri Businesses comprises companies that provide inputs to the agricultural sector and that includes Fertilizer, Seed, Agro Chemicals, Planting Material, Agricultural Machinery, Advisory Services, Animal feed etc, where it is dominated by fertilizer.

Fertilizer is a regulated business and the company supplies fertilizer to the tea plantation, coconut and paddy cultivation sectors. Fertilizer which is imported, is blended at two plants, branded as CIC Pohora and marketed island wide through a network of dealers. Agrochemicals is weighted towards weedicides with CIC's main product being Gramoxone.

Fertilizer is 60% of the total agriculture business. CIC supplies around 30% of the fertilizer requirement of the tea small holder sector. However, due to the risk and govt. regulations (Govt's policy of handling the paddy sector fertilizer distribution exclusively through the two Govt. corporations) and due to the high price of fertilizer (increase of at least 300% in the past two years - until up to latter part of 2008) the company is concentrating on other opportunities in agriculture.

Farms and Seeds Business

CIC has three farms at Thalawe, Higurakgoda and Pelwehera (Government farms) all acquired as 50 year leases. The farms play an integral part in the seeds business with Higurakgoda yielding almost 120 bushels of paddy seed per acre where the average country yield and production is approximately 80 bushels of paddy seed per acre.

The seed business is primarily engaged in the production of seed paddy. CIC has approximately 35% market share in seed business.

The farms make CIC the biggest seller of seed paddy in the country. It is conducting experiments at its paddy farms to grow exotic, indigenous varieties of rice with the aim of identifying exportable types that could find buyers in high-end, niche overseas markets. Long grained red rice is popular in US, Australia, UK but the company has taken the strategy of cautious expansion. The capacity of the export segment is 15 tons per day and it provides Rs.200m in turnover annually. The state of the art rice mill with a capacity of 3 tons/hr which was commissioned in December 2007 is another milestone in the lucrative rice market.

The farms also have livestock which enhance agricultural sustainability in addition to being a supplementary source of revenue.

The seeds segment yields approximately Rs.600m in turnover, Rs.40m in profit and



expected to grow at a rate of 20%.

Hatchery and Animal Feed

The company also supports the livestock industry with the rearing of poultry, buffalo and pigs. The output from the livestock is marketed under the brand name 'CIC Agri Produce' in leading super markets.

The state of the art chicken processing factory (Commenced in October 2007) processes 500 tons of chicken per month and the company is confident in making profits despite the price controls from consumer authorities and the increasing corn prices. And the company claims that to survive this vertical integration is a necessity.

CIC's animal feed business has grown after being acquired from Cargills in 2002. The feed mill came with a hatchery. The breeder farm and hatchery are on an 18.5 acre block of land in Waradala, Divulapitiya. The Feed business is 100% owned by CIC. CIC's poultry farm business is 75% owned, with the rest owned by a technical collaborator.

CIC has purchased two milking facilities worth of Rs.500 m in the Eastern province (Welikanda and Punani) with 25,000 lit/day milking capacity and 50tons/year milk production capacity and is expected to have a network of 5000 outgrowers in 3 years time. This is a joint venture between CIC Agribusiness and State owned limited liability company Mahaweli Livestock Enterprises (Pvt) Ltd.

The prospects for Sri Lanka's milk production is very positive with current annual consumption being a billion litres where the local production is a mere 20% while the remaining 80% is imported. The sector is expected to grow further. The company is also planning to enter into retail business from 9 outlets to 20 to covering the whole value chain.

Manufacturing of curd on a limited basis which is around 1000 to 1200 pots per day, is expected to be expanded by 25% by June 2009. The venture will also be expanding into a wide variety of dairy related products such as yoghurt, ice creams, sterilized and pasteurized milk, cheese which will be targeted at the upper end of the market. CIC is also using the farm infrastructure to grow maize and soya bean which will be converted to animal feed and the surplus will be sold in the local market.

Construction

The Sri Lankan paints market is sophisticated where most of the revenue comes from the premium category (i.e. Dulux) and the prices of paint is high relative to the regional prices. The domestic demand for paints is usually seasonal. Currently per capita consumption of paint in Sri Lanka is around one litre from approximately 0.5 litres a decade ago.

The construction business is effectively CIC's paints and surface coatings business which comes under the group's associate company CIC Paints. (which is now under Akzo Nobel Paints Lanka). CIC is into decorative, vehicle refinishing and industrial paints segments where 80% of the revenue comes from the decorative sector. CIC has about 40% market share with paints under the brand names like Dulux and Glidden targeting different income levels. Dulux is for the quality conscious higher income segment which brings in approximately 88% of revenue while Glidden is targeted at the lower income market. CIC also manufactures a range of acrylic and vinyl acetate emulsion polymers, which are key ingredients for emulsion paints.

Paints and General Industries manufacture the paint which they can contractually sell only to CIC. CIC has around 51% of the market. CIC's emulsion polymerization plant is fully owned by CIC. Most of the production of this plant is sold to Paints and General as the paint lattices necessary for the final product. The plant is classified as part of the Industrial Chemicals segment.

The paints industry is seasonal and due to the drop in construction and big investment projects along with the completion of post Tsunami construction and limitations on housing loans, the sector is significantly affected. However, when fresh investments and rehabilitation activities in the north and east commence there would be enormous scope for growth. Thus, in the longer run the sector looks lucrative.

Pharmaceutical and Consumer

The pharmaceutical business markets products from principals like Johnson & Johnson, Hilton Pharma and Solvay Pharmaceuticals and sells products from prescription drugs to diagnostic equipment to hospitals.

The consumer products division markets solar heaters, water storage tanks, paint brushes, adhesives, writing instruments and industrial safety products.

CIC has a 40,000 strong dealer network for their consumable and pharmaceutical products. CIC holds the agency for Johnson & Johnson which markets baby products under the soap, lotion, shampoo and cologne categories. 30% of revenue flows from principals like Johnson & Johnson, etc. The company follows the strategy of niche marketing.

Link Natural Products does about Rs.30-35m in revenue. Their flagship product is 'Samahan' a remedy for the common cold, but they also sell other healthcare products and cosmetics.

Chemmanex PLC

CIC's quoted subsidiary Chemmanex is a manufacturer and marketer of chemicals and industrial intermediates with six subsidiaries and four associates. Chemmanex markets chemicals to the rubber industry and distributes and mixes paints made by CIC.

Chemmanex exports Carboxy Methyl Cellulose which is used in detergent products by P&G and Unilevers. Chemmanex's main exports are to a P&G unit in the Philippines.

Chemmanex PLC sold its investment in Commercial Leasing PLC in 2008. The capital gain from this sale amounts to approximately Rs.129.5mn.

Industrial Raw Materials

The industrial raw materials segment consists of an emulsion polymerization plant for the paints business, adhesives for the packaging industry, rubber and leather chemicals and ingredients for food and personal products. The business competes with low priced Chinese products.

Financial Performance

The group's revenue grew by nearly 11% during FY09, despite a 73% reduction in revenue from the construction segment as a result of the accounting treatment to CIC Paints which became an associate from subsidiary from 3QFY08. Revenue from the segment also declined consequent to double digit inflation which adversely affected the consumers' purchasing power. However, earnings to equity declined 20% in FY09 albeit a capital gain of Rs. 245 million in the sale of its stake in Commercial Leasing PLC.



The largest contribution in terms of revenue for the year was seen from the agriculture and livestock segment amounting to 58%. Despite the price controls on rice the company entered the lucrative local rice market with the commissioning of the Rice Mill in December 2007. Overall, the Agri businesses which comprises of seed, agricultural inputs and feeds, have realized improved results in comparison to the previous year.

The construction sub sector experienced a 73% decline in revenue mainly as a result of the treatment of CIC Paints which has been removed from being a subsidy to an associate stake while subdued demand for housing and condominium projects also having an adverse effect on the paints market. The PBIT of the sector declined by 77% to reach Rs. 54 million on account of the lack of demand in the housing market, increased cost of Paints and labour costs associated with application. The Consumer & Pharmaceutical sector saw 5% increase in revenue during the year.

During FY09, CIC wrote off an amount equivalent to Rs. 496 million as fertilizer prices declined drastically by around 60%. The situation was further aggravated by the delay in the payment of the subsidy by the GoSL which has accumulated to Rs. 900 million. A part of this amount (Rs. 250 million) was received in 3QFY10 in respect to the period from November 2008 and March 2009.

Earnings Outlook

The company is exploring the possibility of exporting rice to the European market following an initial export of 11 metric tons earlier in 2008. The company has also made new sourcing arrangements for the vegetable seed business and is planning to aggressively compete in the poultry industry despite the corn crisis faced by CIC feeds. With the expected revenue flow from the new milking facilities in the Eastern province and the benefits from commencing chicken processing facility (which means CIC will own the whole value chain in hatchery and animal feed) it is expected that revenue from the Agriculture would grow by approximately 16% in FY10E and 10% yoy from thereon.

The construction sector is evidently on a decline, but soon there will be new developments in the North and East with the victory on the war front and also the company's new initiatives on cost cutting has the propensity of at least a marginal growth in the short run (in the long run the sector is expected to grow at a faster pace). The chemical and pharmaceutical sector's revenue from principals like Johnson & Johnson and others is expected to be steady and grow along with an increase in domestic income.

The group earnings have been heavily reduced due to high finance costs. With the decline in interest rates, we expect the burden to fall but still have a significant impact on earnings. By the end of FY09, the group had Rs. 1,868 million worth of short term borrowings and Rs. 2,135 million as Bank overdraft.

At a price of Rs. 69, the voting share is trading at a P/E of 10.54x while the non voting counter trades at a multiple of 6.8 times, at a price of Rs. 44.25 based on FY11E earnings. Further, we expect in FY10E the agriculture and livestock segment to account for 71% and 64% of revenue and operating profits respectively, while pharmaceutical and consumer segment to generate 17% and 16% of the same. With much of the growth seen from the North and East in the agriculture and paints sectors, we expect the long run to be more rewarding. We believe that prospects of steady growth demand a re-rating of the counter, with growth stemming from agriculture in the longterm and untapped potential in the North & East. We recommend **BUY**.



Profit and Loss Account							
For the year ended 31st March	FY2008	FY2009	FY2010E	FY2011E	FY2012E	FY2013E	FY2014E
Revenue							
Construction	2,856.4	771.5	687.7	825.2	990.3	1,188.3	1,426.0
Agriculture & Livestock	7,781.5	10,927.5	12,637.5	13,901.2	15,291.4	16,820.5	18,502.5
Industrial Raw Materials	769.0	938.9	998.7	1,098.5	1,208.4	1,329.2	1,462.1
Packaging	362.4	485.0	508.7	559.6	615.6	677.1	744.8
Consumer & Pharmaceutical	2,513.7	2,650.3	3,006.6	3,307.3	3,638.0	4,001.8	4,402.0
Others	84.4	80.3	81.6	89.8	98.8	108.6	119.5
Intra group sales	(245.6)	(170.1)	(174.1)	(197.8)	(218.4)	(241.3)	(266.6)
Net revenue	14,121.8	15,683.4	17,746.7	19,583.8	21,623.9	23,884.3	26,390.4
Operating Profit							
Construction	235.9	54.2	88.3	106.0	127.2	152.6	183.1
Agriculture & Livestock	629.5	521.8	853.5	938.8	1,032.7	1,136.0	1,249.6
Industrial Raw Materials	64.9	24.6	81.1	89.2	98.2	108.0	118.8
Packaging	45.0	70.5	73.9	81.3	89.4	98.4	108.2
Consumer & Pharmaceutical	230.5	214.4	213.3	234.6	258.0	283.9	312.2
Others	12.9	14.3	14.6	16.0	17.6	19.4	21.3
	1,218.7	899.8	1,324.6	1,465.9	1,623.1	1,798.2	1,993.2
Other Income	131.8	414.0	522.0	220.4	252.4	288.7	329.7
Other expenses	(105.2)	(99.9)	(103.9)	(108.1)	(112.4)	(116.9)	(121.6)
Financing costs	(438.3)	(734.6)	(690.6)	(495.3)	(328.4)	(198.1)	(124.5)
Share of profits from Associate	261.4	264.5	167.6	184.3	202.8	223.0	245.3
Profit Before Tax	1,068.3	743.7	1,219.8	1,267.3	1,637.4	1,994.8	2,322.2
Taxation	(323.6)	(269.2)	(441.5)	(458.7)	(592.7)	(722.0)	(840.5)
Profit after Tax	744.7	474.5	778.3	808.6	1,044.8	1,272.8	1,481.6
Minority Interest	(234.9)	(66.9)	(192.4)	(188.1)	(225.5)	(262.0)	(297.2)
Earnings to Equity Holders	509.8	407.6	585.8	620.5	819.2	1,010.8	1,184.5
Balance Sheet							
As at 31st March	FY2008	FY2009	FY2010E	FY2011E	FY2012E	FY2013E	FY2014E
ASSETS							
Non Current Assets							
Property, Plant and Equipment	3,916.4	4,072.6	4,277.1	4,466.9	4,641.1	4,799.1	4,939.9
Capital Work in progress	102.8	52.4	52.4	52.4	52.4	52.4	52.4
Investments in Equity Accounted Investees	920.1	493.7	543.1	597.4	657.1	722.8	795.1
Other Long term investments and others	94.0	173.2	177.7	182.5	187.9	193.8	200.2
	5,033.3	4,792.0	5,050.3	5,299.2	5,538.5	5,768.1	5,987.7
Current Assets							
Inventories	2,808.5	3,287.1	3,714.6	4,094.1	4,515.6	4,982.6	5,500.4
Trade Receivables	3,572.5	4,159.7	4,595.6	4,961.1	5,368.7	5,821.9	6,325.8
Other Receivables	447.2	864.4	978.1	1,079.3	1,191.8	1,316.4	1,454.5
Assets classified as held for sale	-	78.8	78.8	78.8	78.8	78.8	78.8
Cash in hand and at bank	226.1	760.2	500.0	500.0	500.0	500.0	500.0
	7,054.3	9,150.2	9,867.1	10,713.3	11,654.9	12,699.7	13,859.5
TOTAL ASSETS	12,087.6	13,942.2	14,917.4	16,012.6	17,193.5	18,467.8	19,847.2
EQUITY & LIABILITIES							
Equity attributable to Equityholders of the company							
Stated capital	1,008.5	1,008.5	1,008.5	1,008.5	1,008.5	1,008.5	1,008.5
Capital reserves	603.6	583.5	583.5	583.5	583.5	583.5	583.5
Revenue reserves	878.6	878.6	878.6	878.6	878.6	878.6	878.6
Retained earnings	1,807.6	2,084.5	2,528.1	3,006.4	3,683.5	4,552.1	5,594.4
	4,298.3	4,555.0	4,998.7	5,477.0	6,154.1	7,022.7	8,065.0
Minority Interest	1,081.8	1,095.4	1,192.3	1,275.3	1,385.3	1,520.1	1,677.5
	5,380.1	5,650.4	6,191.0	6,752.3	7,539.3	8,542.8	9,742.4
Non Current Liabilities							
Long term loans & borrowings	544.2	479.3	503.5	433.5	328.5	223.5	118.5
Retirement benefit obligations	203.2	245.5	290.0	337.2	387.3	440.4	496.7
Others	179.6	183.7	230.0	263.3	301.7	346.0	397.0
	927.0	908.5	1,023.5	1,034.0	1,017.5	1,009.9	1,012.1
Current Liabilities							
Trade payables	2,750.5	2,904.3	3,224.9	3,556.6	3,924.8	4,332.7	4,784.5
Short term loans & borrowings	578.5	1,867.9	1,952.2	1,661.8	1,247.8	926.0	673.5
Income tax payable	119.8	118.9	130.8	143.9	158.3	174.1	191.6
Accruals and other payables	370.5	356.9	410.5	472.0	542.8	624.3	717.9
Bank overdraft	1,961.2	2,135.2	1,984.5	2,391.9	2,762.9	2,858.0	2,725.2
	5,780.5	7,383.3	7,702.9	8,226.2	8,636.6	8,915.1	9,092.7
TOTAL EQUITY & LIABILITIES	12,087.6	13,942.2	14,917.4	16,012.6	17,193.5	18,467.8	19,847.2



Cashflow Statement	FY2008	FY2009	FY2010E	FY2011E	FY2012E	FY2013E	FY2014E
For the year ended 31st March							
Profit before Interest and tax	1,245.2	1,213.8	1,742.7	1,578.2	1,763.1	1,969.9	2,201.3
Adjustments for :							
Depreciation of Property, Plant and Equipment	229.9	281.4	295.5	310.2	325.8	342.0	359.1
Others	101.2	588.5	177.0	177.7	178.6	179.5	180.5
Operating profit before working capital changes	1,576.3	2,083.8	2,215.2	2,066.2	2,267.5	2,491.5	2,740.9
Working Capital changes	(848.4)	(1,963.2)	(949.6)	(259.2)	(191.6)	(327.3)	(444.6)
Cash generated from operations	727.8	120.5	1,265.6	1,807.0	2,075.9	2,164.2	2,296.3
Interest paid	(438.3)	(734.6)	(690.6)	(495.3)	(328.4)	(198.1)	(124.5)
Retirement benefit paid	(29.5)	(12.6)	(10.0)	(10.0)	(10.0)	(10.0)	(10.0)
Income tax paid	(392.6)	(284.5)	(441.5)	(458.7)	(592.7)	(722.0)	(840.5)
Net cash inflow / (outflow) from operating activities	(132.6)	(911.2)	123.5	843.0	1,144.8	1,234.0	1,321.3
Cashflow from investing activities							
Addition to Property, Plant and Equipment	(1,009.6)	(473.6)	(500.0)	(500.0)	(500.0)	(500.0)	(500.0)
Others	(123.4)	780.4	11.1	12.7	14.5	16.5	18.8
	(1,133.0)	306.7	(488.9)	(487.3)	(485.5)	(483.5)	(481.2)
Cashflow from financing activities							
Dividends paid	(118.5)	(142.2)	(142.2)	(142.2)	(142.2)	(142.2)	(142.2)
Proceeds from rights issue	-	-	-	-	-	-	-
Long term loans received	300.6	586.9	539.4	100.0	100.0	100.0	100.0
Long term loans repaid	(10.0)	(651.9)	(430.9)	(460.5)	(619.0)	(526.7)	(457.6)
	172.2	(207.1)	(33.6)	(502.6)	(661.1)	(568.9)	(499.7)
Net increase in cash and cash equivalent	(1,093.4)	(811.6)	(398.9)	(146.9)	(1.9)	181.6	340.4
Balance at the beginning	(917.0)	(2,010.4)	(2,822.0)	(3,221.0)	(3,367.9)	(3,369.8)	(3,188.2)
Balance at the end	(2,010.4)	(2,822.0)	(3,221.0)	(3,367.9)	(3,369.8)	(3,188.2)	(2,847.9)

