Sri Lanka Equities
CORPORATE UPDATE
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John Keells Stock Brokers (Pvt) Ltd.
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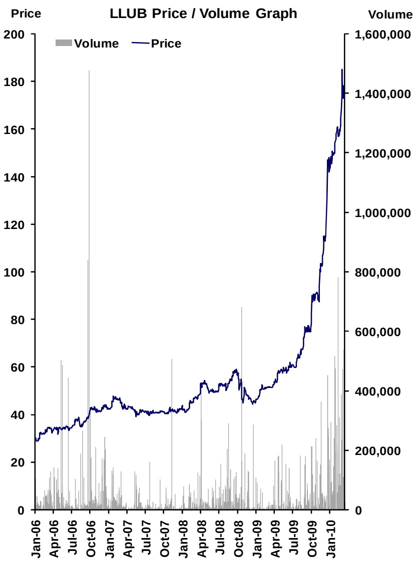
Chevron Lubricants Lanka PLC (LLUB)

Rs 173.00 **BUY**

LLUB			
Reuters Code			LLUB.CM
Bloomberg Code			LLUB.SL
Share Price LKR			173.00
Issued Share Capital (Shares)			120,000,000
12 mth High/Low (Rs.)			233.00 / 103.00
Average Daily Volume			48,295
Market Capitalisation Rs. mn			20,760
Price Performance (%)	1 mth	6 mth	12mth
ASPI	2.56	31.22	133.70
LLUB	9.80	123.20	235.90

Fiscal year	Net Profit (Rs m)	EPS (Rs)	EPS Growth (%)	PER (X)	ROE (%)	DPS (Rs.)
2007	1,078	8.98	33.58	19.26	58.8	12.50
2008	948	7.90	-12.06	21.90	44.1	10.50
2009	1,495	12.46	57.70	13.89	67.8	12.00
2010E	1,646	13.72	10.10	12.61	54.8	12.50
2011E	1,709	14.24	3.83	12.15	44.8	13.00
2012E	1,843	15.36	7.84	11.26	39.2	13.50



Chevron Lubricants controls approximately 70% of the local lube market, and LIOC follows with 15% in a market which now has 15 operators. Slower growth in 2009 meant that new vehicle registrations declined while consumers spent less thereby affecting lube volume growth. The firm said industry volumes fell 7% in 2009 which was the third consecutive year of declines.

Prices were cut by 10% aided by raw material prices falling in the first half of the year. Base oil (which is the main ingredient in lubricants) has historically had a strong correlation with crude oil prices, albeit with a lag of about six months. Despite the current rally in crude prices over the past six months, base oil remains well below its 2008 peak. If crude hovers at or above $80/bbl, base oil prices could start to rise once more.

Chevron Lubricants recorded an earnings growth of 57.7% to Rs.1.5bn despite a net revenue fall of 2.4% in FY09 on the back of favourable base oil prices and substantially higher gross margins. We expect LLUB to post an earnings growth of 10% to Rs.1,646m in FY10E and earnings of Rs.1,709m for FY11E. At 173.00, the counter trades at a PER of 12.6x FY10 earnings.

Over the past one year Sri Lanka's lubricant market has continued to post a slowdown in growth. The Sri Lankan lubricant industry lost its growth momentum over the last three years due to economic issues of the country. Last year's 7% fall in volumes, due to sluggish vehicle sales and lower usage of thermal power plants, needs to be seen in perspective against an annual average of 5% growth over the last 10 years. Currently the total local market value of lubricants and greases is around Rs. 11bn annually.

Currently operators who blend lubricants (both LIOC and Chevron have blending facilities) enjoy a tariff advantage of 7% compared to the previous 16.6%. These narrowing duty margins have encouraged importers. The 2 acre property where Chevron blends its products had its lease agreement extended for a further period of 5 years from July 2009 by the Government. Chevron was the owner of the sole blending plant (50,000 MT capacity at Kolonnawa), until 2007 when LIOC completed a 18,000 MT inside the China Bay tank farm area in Trincomalee.

Chevron expects newer markets in the former war zones of the North and East, with growth also coming from the rebuilding of infrastructure. Market growth in volumes should approach 6% per annum with growth of 4-5% in the vehicle segment and higher growth of 10-12% in the industrial segment. Demand for industrial lubricants tends to be driven by export activity as well as general economic growth with increased demand from sectors like thermal power distribution. While the industrial segment contributes 40% of Chevron volumes, 60% of the industrial segment consists of public sector organizations.

Export Markets

Chevron has expanded its operations overseas to Bangladesh and the Maldives in a small scale where exports amount to 10% of the company revenue. Revenue growth rates of above 10% were experienced in both Bangladesh and Maldives. The general economic downturn affected Chevron's export markets as well however, with the Maldives impacted by lower tourist volumes affecting transportation and Bangladesh volumes also suffering.

Despite this the broad outlook of the performance of Bangladeshi operations is very encouraging. Total demand in the Bangladeshi lubricant market is estimated at 150m litres. The market is extremely competitive with 6 established players in the market.

Chevron estimates it has approximately 10% of the lubricants market in the Maldives Although the size of the Maldivian market is only 3m litres per year, it has good profitability due to its high growth rate. Operations in Maldives were above expectations and the company is expected to replicate the strong market position that it enjoys in Sri Lanka.

Earnings

In FY09 LLUB registered an earnings growth of 57.7% to Rs.1.5bn resulting from favourable base oil prices and higher gross margins despite marginally falling turnover. Caltex has traditionally positioned itself as a premium player in the industry and with automotive volumes sensitive to issues like fuel consumption economies we expect them to continue to dominate the automotive sector. Industrial volumes should grow faster with infrastructure spending, the opening of fisheries and better performance of the export sector.

We expect earnings to increase by 10% to Rs.1,646m in FY10E and earnings of Rs.1,709m for FY11E. At 173.00, the counter trades at a PER of 12.6x FY10 earnings. With an effective dividend of Rs.12.00 the counter has a yield of 6.9%.

Income Statement Year ending 31st Dec	2007 Rs. mn	2008 Rs. mn	2009 Rs. mn	2010E Rs. mn	2011E Rs. mn	2012E Rs. mn
Revenue	8,654	8,900	8,691	9,733	10,561	11,458
Cost of Services	(6,368)	(6,774)	(5,595)	(6,424)	(7,076)	(7,677)
Gross profit	2,286	2,126	3,096	3,309	3,485	3,781
Other operating income	11	3	2	8	8	8
Selling and distribution	(369)	(455)	(548)	(569)	(618)	(670)
Admin expenses	(322)	(289)	(305)	(336)	(386)	(444)
Operating profit	1,606	1,385	2,245	2,412	2,489	2,675
Net finance cost	52	98	99	120	140	160
Tax	(580)	(535)	(849)	(886)	(920)	(992)
Net earnings	**1,078**	**948**	**1,495**	**1,646**	**1,709**	**1,843**

Balance Sheet As at 31st Dec	2007 Rs. mn	2008 Rs. mn	2009 Rs. mn	2010E Rs. mn	2011E Rs. mn	2012E Rs. mn
Fixed Assets						
PP&E	388	326	260	273	241	251
Non current receivables	27	23	34	34	34	34
Deferred tax asset		3	47	47	47	47
	415	352	340	354	322	332
Current Assets						
Inventories	1,144	1,696	1,429	1,606	1,743	1,891
Receivables and prepayment	741	1,033	868	1,071	1,162	1,260
Short term investments	388					
Cash and equivalents	183	90	1,394	1,822	2,479	3,079
	2,456	2,820	3,691	4,499	5,383	6,230
Current Liabilities						
Trade and other payables	600	657	1,099	1,168	1,267	1,375
Current tax liabilities	338	271	607	540	473	321
Borrowings	-	-	0	23	34	42
	938	928	1,706	1,731	1,774	1,738
Non Current Liabilities						
Deferred tax liabilities	13	-				
Defined benefit obligation	86	93	119	119	119	119
	99	93	119	119	119	119
Net Assets	**1,834**	**2,151**	**2,206**	**3,003**	**3,812**	**4,704**
Stated Capital	600	600	600	600	600	600
Reserves	1,234	1,551	1,606	2,402	3,211	4,104
Shareholder's Funds	**1,834**	**2,151**	**2,206**	**3,002**	**3,811**	**4,704**

Cash flow statement Year ending 31st Dec	2007 Rs. mn	2008 Rs. mn	2009 Rs. mn	2010E Rs. mn	2011E Rs. mn	2012E Rs. mn
PBT	1,658	1,483	2,344	2,532	2,629	2,835
Depreciation / Amortization	88	93	83	87	92	96
Net finance costs	(48)	(100)	(116)	(120)	(140)	(160)
Other	11	23	54			
Change in working capital	133	(836)	336	(378)	(295)	(399)
Cash from Operations	1,842	662	2,702	2,122	2,286	2,372
Finance costs paid	48	99	116	120	140	160
Income tax paid	(556)	(620)	(556)	(886)	(920)	(992)
Other	(3)	(5)	(13)			
Net Cash from Operations	**1,332**	**136**	**2,248**	**1,355**	**1,506**	**1,540**
Net PPE	(55)	(37)	(24)	(100)	(60)	(106)
Net Investments						
Other						
Net Cash from Investing	**(55)**	**(37)**	**(24)**	**(100)**	**(60)**	**(106)**
Borrowings	-	200	(200)	23	110	116
Dividends paid	(690)	(780)	(720)	(850)	(900)	(950)
Other						
Net Cash from Financing	(690)	(580)	(920)	(827)	(790)	(834)
Net increase in Cash	586	(481)	1,304	428	656	600

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