



THE LUBRICANTS
DATABASE EXPERTS

OATS White Papers

10 June 2009

The GDP effect on lubricants demand

Apu Gosalia, Head of Strategic Marketing, Fuchs Petrolub AG.
Sebastian Crawshaw, CEO OATS.

It cannot have escaped anyone's attention that we are living, as Confucius might say, in "interesting" times. One of the key factors that makes the lubricants market interesting right now is the link between our industry and the movement in the Gross Domestic Product (GDP) of key nations across the world.

In Fuchs' home country, Germany, GDP is now forecast to fall 6% in 2009. Recent data showed Japan's economy shrank in the first quarter at its fastest rate since records began. Output contracted by 4% during the first three months of the year, or by 15.2% on an annual basis, as exports fell, according to official figures. *(Source: UK Cabinet Office cited by BBC).*

In the US real GDP is forecast to contract by 3.2% in 2009 as the financial crisis and the housing downturn take their toll on domestic demand. Slowing growth in the developed world will also curb US export growth in 2009. *(Source: EIU)*

So what has been the impact on Lubricants demand and what does the future hold for the industry?

The 2008 Out-turn

In 2008 globally lubricants demand slipped just 2%. But this hides a wide variation, both among countries and between the first and second half of the year.

In the first half of the year, we were approaching the end of the capital goods cycle. There were huge order books for Trucks and finance was freely available. Then the financial markets froze and orders for capital goods plummeted. Anecdotal evidence of 8-10% falls across the year, translate into a 16-20% fall in the second half of 2008.



THE LUBRICANTS
DATABASE EXPERTS

Table showing lubricants production in K/tonnes (source: Fuchs strategic marketing)

Region	2007	2008	Variance in %
North America	7,760	7,139	-8.0%
Latin America	3,395	3,417	0.6%
Western Europe	4,670	4,380	-6.2%
Central & Eastern Europe	5,060	5,102	0.8%
Middle East	1,855	1,867	0.6%
Africa	1,935	1,950	0.8%
Asia-Pacific	12,445	12,465	0.2%
WORLD	37,120	36,320	-2.2%

First Quarter 2009

In Europe, like the rest of the world, lubricants were badly hit. In Germany, lube demand fell around 35% January to March year-on-year. In Spain, where the construction industry has been seriously affected, lubricants demand dropped 33%. In other countries, the effect has been less severe but still significant: France down 20% for example, although according to the French it is the one European country not yet formally in recession!!

These figures appear even more gloomy when you take into account the fact that in Q1 2009 there were more working days than the previous year as Easter was later, although sometimes early results are smoothed out later in the year

	Domestic Lube demand (YTD March var 08-09)	Ending Lube stocks (var Dec 08 – Mar 09)
Germany	-34.2	-1.7
France	-19.7	-0.8
Italy	-32.8	n/a
USA	-21.1	-4.2
Japan	-29.1	-2.5

(Source: reported national lubricant statistics)



THE LUBRICANTS
DATABASE EXPERTS

What are the drivers? How sensitive is lubricants demand to GDP?

Even in the most stable economic climate, there are conflicting influences which affect the lubricants industry.

In “normal” times, for mature markets, there is a negative correlation between lubricants demand and GDP. As GDP improves, use of synthetic lubricants with improved drain intervals, combined with economic pressure to improve cost performance, results in longer drain intervals and a slow decline in lubricant volumes. For example, the table below shows eight years of German GDP growth but Lubricants consumption which declines in real terms.

	2000	2008
GDP Growth Index	100	121
Lubricant consumption	100	99

(Source: VSI)

In developing markets under ‘normal’ economic conditions, there is a positive correlation with GDP. This reflects improved standard of living and steady growth as industries develop and the vehicle parc and volume of use expands. Some sources have suggested that the Index of Industrial production is a more reliable measure with the lubricants industry showing a growth factor of 2:1 or even 3:1 relative to that Index.

Crisis times : The GDP effect

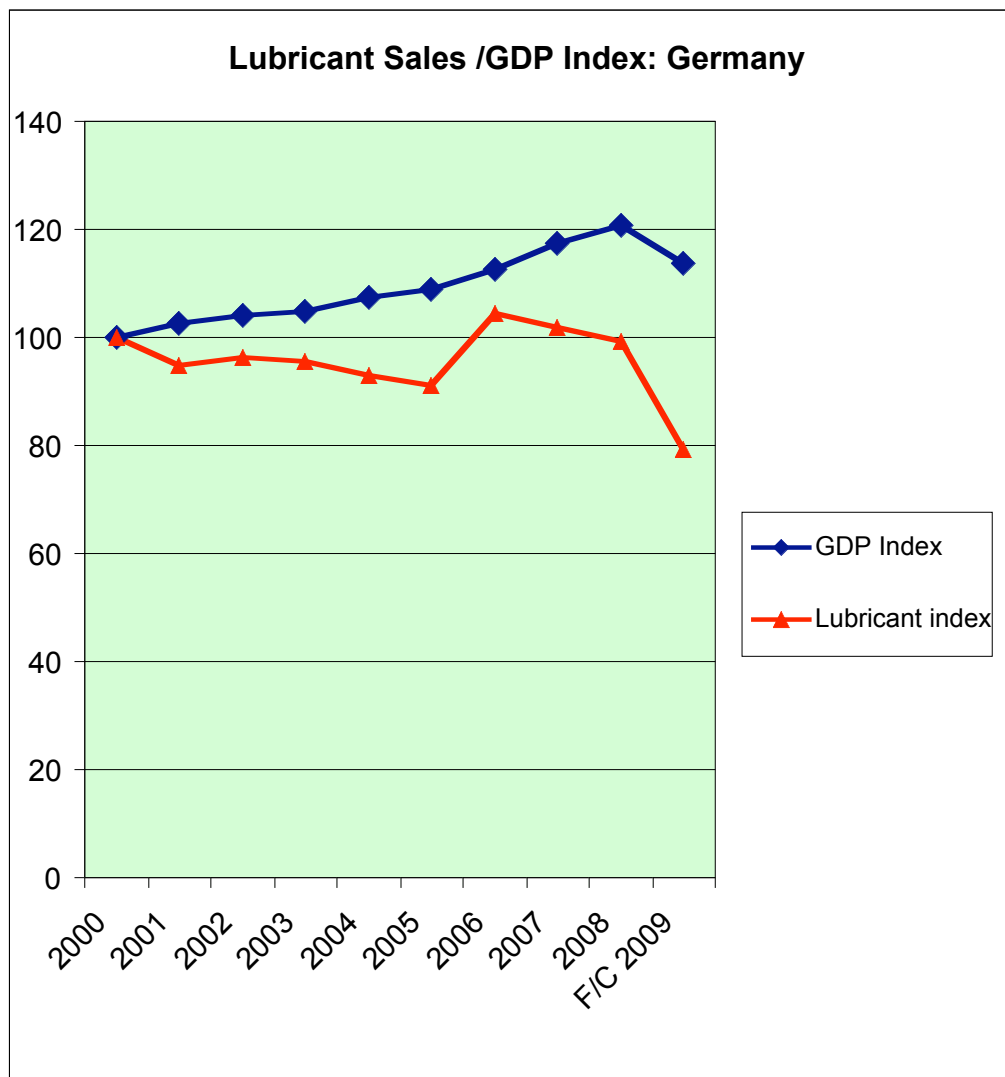
In times of crisis the dependency on the capital goods cycle and the reduction in journeys results in an exaggerated or geared response to GDP changes. Lubes demand appears to fall at between five and seven times the GDP downturn. So, has the current crisis highlighted a new empirical rule?

In Germany, as GDP fell 3.9 in Q1 2009, lubes demand plummeted 35%; in the US GDP dropped 3.5% with lubes demand down 22%.

From a sales perspective, the effect is the same. Projecting forward to the end of 2009 for Germany, with a predicted GDP shrinkage of 6%, year-on-year lubricant sales are likely to drop by 20%. Although not as steep as Q1, this is because conditions are expected to ameliorate in the latter part of the year and the first quarter effects are likely to average out.



THE LUBRICANTS
DATABASE EXPERTS



With many car plants being at a standstill or returning from an extended break, eg Honda in Swindon, John Deere and Mercedes, OEM lubricant demand has fallen much more sharply in Q1.

Equally there are fewer journeys being made, as factories need fewer deliveries. In the UK alone Q1 has shown 30,000 truckers currently out of work! The net result is a sharp fall in demand for commercial lubricants; while from a B2C perspective, rising unemployment and falling domestic income mean that people try to extend their oil change intervals.

In nearly all the key developed countries this effect is outweighing the impact of all other factors that usually influence lubricants demand and supply!



THE LUBRICANTS
DATABASE EXPERTS

De-stocking/re-stocking

Is there a possibility that the situation could actually be worse than it appears? We certainly hope not, but a good additional bellweather is trends in de-stocking and restocking?

At the end of 2008, following an initial sharp rise in the oil price and then Base oil prices, prices started falling rapidly and most lubricants businesses ran down their stocks.

Did this situation flatter the 2008 Q4 or 2009 Q1 figures? The picture is not yet clear. What is evident is that from early indications, stock levels have not altered greatly since end December 2008 compared with the end of March 2008. In fact, there is a small 3-5% increase in overall lubricant stocks.

Conclusion

Whatever stock figures emerge, and however the GDP/lube demand differential resolves itself, there is no question that the position for the overall lubricants industry remains challenging in the short to medium term. The critical question is when do we see the turn?

As the recession started in the US, "normal" theory may need to be turned on its head, with a revival of the lubricants market requiring an uplift in GDP. If this proves to be the solution, should we expect this in the final quarter 2009 or later? Currently, the jury is still out.

Sebastian Crawshaw/Apu Gosalia

10 June 2009