

Oman Cement - Realisation sustained amid volume pressure

Closing Price: RO 0.539

Recommendation: Neutral

Fair Value: RO 0.575

Upside: 6.8%

Overall Results Review: Below our Estimates

Revenue marred by dip in sales volume on QoQ basis: After witnessing an upswing during Q1 2011 the sales revenue of Oman cement dropped by 9% YoY and 7% QoQ to RO 11.952 million in Q2 2011. Despite the company maintaining its realisation at RO 26/tonne, the inflow of cheap cement from neighboring peers impacted the sales revenue of the company. The total sales volume stood at 454k tonnes, an increase of 8% YoY and a decline of 8% QoQ.

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Production drops down moderately on QoQ: Owing to shut down of two kilns for major maintenance, rebricking and other minor operational issues, the company witnessed a drop in its clinker production from the existing Kiln 1 & 2 by 12% on QoQ to 227 MT. This in turn resulted in lower capacity utilization which stood at 75.6%. However, the production from its new line shot up during the quarter by 822% on QoQ basis to 173k MT. Cement production witnessed a modest decline by 6% to 459k MT as against 491k MT in Q1 2011.

Graph 1: Sales Vs Realization (RO/ ton)



Source: GBCM Research; Company Reports

Realisation sustains @ RO 26/tonne: With the intention of maintaining its market share, during 2H 2010 the company announced a price cut by 10%. The company witnessed a further fall in its realisation by another 6.9% to RO 26.2/tonne during Q1 2011 and has maintained the same during the quarter under review. It is noteworthy that the company has been able to maintain its realization despite volume pressure.

Gross margins jumps sequentially on lower clinker procurement: The company witnessed an improvement in the output of the new production line (*still under trail run*) due to which the import of clinker fell significantly during the quarter. However the company saw a rise in its employee and fuel & electricity costs, which increased by 25% and 55% on sequential basis. The recent measures taken by the company to improve the compensation package and other benefits (*FY11E Estimated impact of about RO 1.25 million*) has ultimately led to the increase in the employee costs.

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The fall in clinker procurement costs has mitigated the rise in the employee and fuel & electricity costs. The total cost of sales excluding depreciation stood at RO 6.049 million, declining 16.3% on QoQ basis. The company reported a Gross profit of RO 5.903 million a decline of 14% YoY and an increase of 5% QoQ. Gross Profit margins for the quarter stood at 49.4% as against 52.3% in Q2 2010 and 43.8% in Q1 2011

Other Income: The other income for the quarter stood at RO 431k which includes a bank interest of RO 268k and a Cumulative gain reclassified from fair value reserve on sale of available-for-sale- investments of RO 144k. This inturn had partially boosted the earnings of the company.

Higher depreciation and Interest costs knocks PAT margins: The commissioning of new plant and equipments viz, new clinker plant worth of RO 64.012 million, Gas station worth RO 1.945 million and Alternate cement transport worth RO 1.176 million had increased the depreciation costs during the quarter. The total depreciation costs for the quarter increased by 64.6% to RO 1.543 million from RO 938k in Q1 2011.

The term loan during the quarter increased to RO 11.773 million as against RO 7.666 million in Q2 2010 as the company had made a draw down to pay its supplier. The interest charges for the quarter stood at RO 152k as against RO 3k in Q1 2011. We believe this increasing trend to continue in the forthcoming quarters.

Apart from increase in employee and fuel & electricity costs, higher depreciation and interest costs knocked the net profit of the company during the quarter. PAT for the quarter declined by 32% YoY and 23% QoQ to RO 3.179 million. PAT margins contracted by 570 bps on QoQ and 910 bps on YoY to 26.6%.

Lowering Earnings for FY11E

Outlook and Valuations: In order to remain competitive in the market, Oman cement further announced a price revision in its selling prices at the beginning of the year. We believe this would help the company to retain or slightly improve the sales volume from its current levels; soaring cost of sales (excl depreciation) along with higher depreciation and interest costs are expected to take a hit on the earnings of the company going forward. During Q1 2011, the company announced its plans on modernizing its Plants & Equipments (*Modernization of the existing Pollution Control equipment of Line-1 and clinkerisation unit*) and the capex for the same would be about RO 14.3 million.

We have already factored in our model the above said concerns such as increase in cost of sales, higher depreciation and interest costs for 2011E and 2012E; At the sametime we continue to retain the realisation levels at RO 25/tonne for the next two years, on account of continuing cement dumping from the regional players despite local demand remaining intact (*Investment in Airports, Ports, Roads etc.,*). On this, we have estimated the company to report net profit of RO 14.306 million for FY11E and about RO 17.889 million for 2012E.

At the current market price of RO 0.535, the stock is trading at PE of 12.5X on FY11E EPS of RO 0.043 and about 10X of FY12E EPS of 0.054. We recommend a '**Neutral**' rating on the stock. Based on the DCF valuation model the revised fair value works out to **RO 0.575**, an upside of 6.8% from the current levels.

(Ratings and Fair value revised downwards on account of revision in our Earnings estimates for 2011E and 2012E. Post FY2010 results we had put Oman Cement ratings under Review; Last Report- GBCM Research: Oman Cement - FY2010 results - Initial View dated 16-Jan-11)

Particulars	1QFY11	1QFY10	%	2QFY11	2QFY10	%	H1 FY11	H1 FY10	%
Cement Sales (Vol)									
Total Cement Sales (in MT)	490,865	498,958	-1.62%	453,701	420,356	8%	944,566	919,314	3%
Cement Production (in MT)	491,019	495,133	-0.83%	459,534	419,567	10%	950,553	914,700	4%
Cement Sales (Val)									
Local (RO 000's)	13,128	15,157	-13.39%	12,177	13,004	-6%	25,305	28,161	-10%
Export (RO 000's)	194	580	-66.55%	337	239	41%	531	819	-35%
Less: Discount	462	104	344.23%	561	54	940%	1,023	158	548%
Total Cement Sales (RO 000's)	12,860	15,633	-17.74%	11,952	13,189	-9%	24,812	28,822	-14%
Net Realisation	26.2	31.3	-16.4%	26.3	31.4	-16.0%	26.3	31.4	-16.2%

Source: Company Reports, GBCM Research

Period Ended (RO 000's)	1QFY11	1QFY10	%	2QFY11	2QFY10	%	H1 FY11	H1 FY10	%
Sales	12,860	15,633	-17.7%	11,952	13,189	-9.4%	24,812	28,822	-13.9%
Total Expenditure	7,230	7,710	-6.2%	6,049	6,286	-3.8%	13,279	13,996	-5.1%
Gross Profit	5,630	7,923	-28.9%	5,903	6,903	-14.5%	11,533	14,826	-22.2%
GPM (%)	44%	51%		49%	52%		46%	51%	
Admin & general expenses	690	695	-0.7%	801	542	47.9%	1,491	1236.645	20.6%
PBIDT	4,940	7,228	-31.7%	5,102	6,361	-19.8%	10,042	13,589	-26.1%
OPM (%)	38%	46%		43%	48%		40%	47%	
Depreciation	938	880	6.6%	1,544	989	56.1%	2,482	1,869	32.8%
Other Income	1,115	1,388	-19.7%	431	458	-5.9%	1,546	1,846	-16.3%
EBIT	4,669	7,972	-41.4%	3,768	5,392	-30.1%	8,437	13,364	-36.9%
EBIT (%)	36%	51%		32%	41%		34%	46%	
Interest	-3	-2	50.0%	-152	-7	NA	-155	-9	1621.0%
Government Reimbursement					7,339			7,339	
PBT	4,674	7,970	-41.4%	3,623	12,724	-71.5%	8,297	20,694	-59.9%
Tax	523	852	-38.6%	444	1,557	-71.5%	967	2,409	-59.9%
PAT	4,151	7,118	-41.7%	3,179	11,167	-71.5%	7,330	18,285	-59.9%
PAT Margin (%)	32.3%	45.5%		26.6%	84.7%		29.5%	63.4%	

Source: Company, GBCM Research

Income Statement (RO 000's)	2007	2008	2009	2010	2011E	2012E
Revenue	50,010	63,522	68,284	51,879	46,098	48,058
Gross Profit	23,758	17,437	29,275	26,218	22,398	26,719
EBITDA	24,441	18,077	30,600	26,731	22,203	26,394
PBT	19,696	14,108	27,363	28,205	16,165	20,213
Tax	-2,426	-1,567	-3,131	-3,167	-1,859	-2,325
PAT	17,270	12,540	24,232	25,038	14,306	17,889
EPS	0.052	0.038	0.073	0.076	0.043	0.054

Source: Company Reports, GBCM Research

Balance Sheet (RO 000's)	2007	2008	2009	2010	2011E	2012E
Fixed assets	44,633	59,430	91,793	99,502	108,321	116,930
Current assets	31,837	42,069	24,187	40,515	30,960	24,969
Total assets	134,265	132,987	153,480	172,248	177,414	181,224
Share capital	33,087	33,087	33,087	33,087	33,087	33,087
Shareholders Equity	119,765	117,931	135,938	148,520	149,689	156,527
Creditors and accruals	4,283	7,123	4,889	7,708	7,792	7,015
Current liabilities	7,734	9,320	8,451	12,596	12,118	11,340
Total liabilities	134,265	132,987	153,480	172,248	177,414	181,224

Source: Company Reports, GBCM Research

Key Ratios	2007	2008	2009	2010	2011E	2012E
Margins (%)						
GPM (%)	48%	27%	43%	51%	49%	56%
NPM (%)	35%	20%	35%	48%	31%	37%
Per Share Ratio (In RO)						
EPS	0.052	0.038	0.073	0.076	0.043	0.054
Book Value	0.362	0.356	0.411	0.449	0.452	0.473
Multiples (X)						
PE	10.3	14.2	7.4	7.1	12.5	10.0
PBV	1.5	1.5	1.3	1.2	1.2	1.1
Profitability Ratio (%)						
RoE	14%	11%	18%	17%	10%	11%
RoA	13%	9%	16%	15%	8%	10%
Leverage Ratios						
Current Ratio	4.1	4.5	2.9	3.2	2.6	2.2
Working Capital Ratios (In days)						
Debtors turnover	44	41	27	39	55	55
Creditors turnover	60	56	46	110	120	120
Inventory turnover	60	121	72	134	150	150
Cash Cycle	45	105	54	64	85	85

Source: Company Reports, GBCM Research estimates

Stock Rating Methodology:

Buy - Upside more than 20%

Accumulate - Upside between 10% and 20%

Neutral - Upside or downside less than 10%

Reduce - Downside between 10% and 20%

Sell - Downside more than 20%

Not Rated - Stocks not in regular research coverage

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