

July 26, 2010

OMAN CEMENT (OCCO.OM)

12-Month Fair Value: RO 0.879

Last Close (26 July, 2010): RO 0.679

Recommendation: BUY - Risk Level: 3

- Our main theme of a drop in revenue coupled with an expansion in EBITDA margins for Omani cement companies is materializing. Oman Cement revenue for 2Q2010 was down 23.9% YoY to RO 13.2 million (7.4% lower than our forecast), while EBITDA margin expanded to 47.9% vs. our forecast of 47.3% and compared to 45.5% in 2Q2009. It is worth mentioning that the EBITDA margin for 2Q2010 is the highest in the last ten quarters. However, EBITDA declined almost 20% YoY to RO 6.31 million (6.5% lower than our forecast) during 2Q2010 mainly due to the significant drop in revenue.
- The decrease in revenue was almost entirely due to a 23.6% drop in cement sales volume to 420 thousand tons in 2Q2010 (499 thousand tons in 1Q2010) compared to 550 thousand tons in 2Q2009. According to management, this was mainly due to the cheap cement imports from the UAE. Domestic cement prices were almost flat at RO 31.4 per ton during the quarter (RO 31.3 during 1Q2010) in spite of the cheap imports. During 1H2010, revenue was down 18.9% to RO 28.8 million compared to the same period last year.
- We had highlighted in our last update (dated 7 April 2010) that we expect a further decline in domestic cement prices to RO 26 – 27 per ton for 2H2010. This seems to be the case as suggested by recent price cut by Oman Cement to those levels from the beginning of 2H2010. Our 2010 average domestic blended price forecast of RO 29 per ton assumes a softening in the average selling price to RO 27.7 per ton during 2H2010.
- The company's clinker imports fell 44.3% to 114 thousand tons of clinker during 2Q2010 compared to the same period last year. The company further benefitted from the lower prices of clinker imports (around RO 16 - 17 per ton in 2Q2010). Accordingly, due to lower clinker imports and absence of cement imports, EBITDA margin for 1H2010 significantly expanded to 47.2% (we expect 46.2% for 2010) compared to 36.2% during 1H2009.
- The company's cash flows and profitability were both boosted by a one-time government reimbursement of RO 7.34 million for earlier cement imports (the excess of cost over sales price of cement imported during 2007 and 2008). Due to the improved liquidity of the company, the management has decided reduce the borrowing to RO 13 million from the previously sanctioned amount of RO 20 million for financing the upcoming clinker line. We expect the new clinker line of 1.2 million tons per annum to be fully operational by beginning of 2011.
- Accordingly, net profit was up 71.3% to RO 11.2 million in 2Q2010 compared to the same period last year. Excluding the one-time government reimbursement, net profit would have plummeted by 27.5% YoY. Net profit during 1H2010 was up 63.6% to RO 18.3 million compared to the same period last year.
- Oman Cement continues to remain our top pick mainly due to: 1) doubling of clinker capacity from the 1.2 million tons per annum and hence absence of both clinker and cement imports going forward, 2) which should lead to EBITDA margin expansion (we forecast 46.2% in 2010), 3) the strong free cash flow/dividend story as the stock currently trades at a free cash flow (FCF) yield of 11.8% and 12.7% on our forecasted FCFs for 2011 and 2012 and 4) Adjusting for the company's current cash reserve (RO 34.7 million at the end of June 2010) and investment portfolio of RO 16.7 million, the stock is trading at PE of 8.3x on 2010 earnings.
- Given the results were in line, we maintain our 2010 earnings forecast and reiterate our fair value of RO 0.879 (upside potential of 29.5%) and hence our 'BUY' recommendation.

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Related Research

- [Oman Cement Analyst Comment - 25 April 2010](#)
- [Oman Cement Update - 07 April 2010](#)

RISK AND RECOMMENDATION GUIDE

RECOMMENDATION		UPSIDE (DOWNSIDE) POTENTIAL		
BUY		MORE THAN 20%		
ACCUMULATE		BETWEEN 5% AND 20%		
HOLD		BETWEEN -10% AND 5%		
REDUCE		BETWEEN -25% AND -10%		
SELL		LESS THAN -25%		
RISK LEVEL				
LOW RISK		HIGH RISK		
1	2	3	4	5

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