

Oman Cables - Earnings skid on high raw material prices

Closing Price: RO 1.021

Recommendation: Neutral

Fair Value: RO 1.080

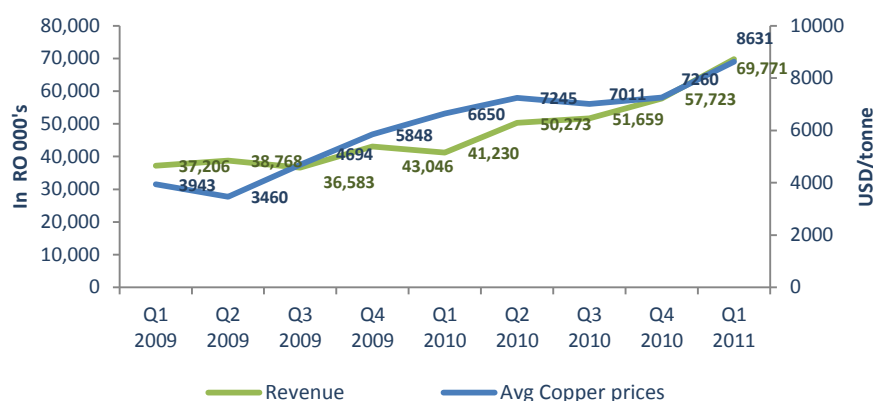
Upside: 5.8%

Cost pressure squeeze profit margins despite robust revenue

April 19, 2011

Higher demand pushes top line: Overall Group Revenue for Q1FY2011 has witnessed a significant upsurge to RO 69.771 million as compared to RO 41.230 million, a remarkable performance in last ten quarters. This was on the back of incremental volume and the prevailing commodity prices. The top line includes the subsidiary revenue of about RO 7.061 million. The company has disclosed that the demand in the local market continue to remain intact on the back of announced government projects. At the same time, the select export markets too have witnessed increase in demand, which is in line with the company's strategy.

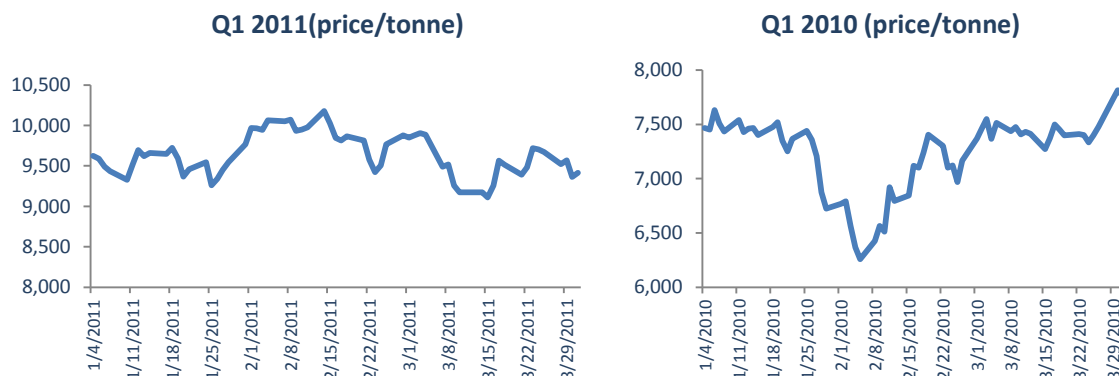
Quarterly Trend: Avg LME Copper Price Vs Revenue with quarterly lag



Source: Company Reports; Bloomberg (Copper - LME Spot); GBCM Research

During the quarter, LME copper futures averaged at about US\$9,633 per ton, which is 33.0% higher as compared to the average of US\$ 7,245 per ton in Q1 '10.

LME Copper prices Trend:



Source: Bloomberg (Copper - LME Spot); GBCM Research

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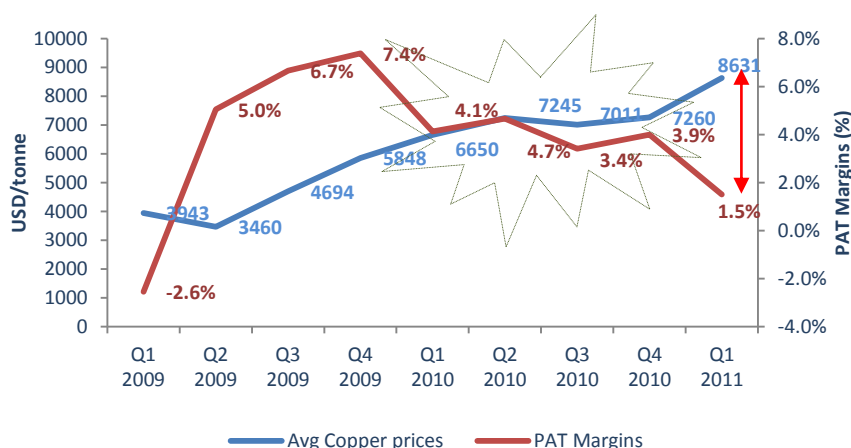
Margins fall on higher cost of sales: There was a considerable jump in the total cost of sales (incl. depreciation) of the company during the quarter by 76% to RO 66.492 million. This was on account of steep price increase on its key raw material Copper. At about 95% of sales, the costs of sales were higher by 385 basis points on YoY and by 366 basis points on QoQ.

Gross profit for the period ended march 2011 declined by 7% on YoY and 32% QoQ to RO 3.279 million. The gross profit margins of the company declined to 4.7% as compared to 8.5% in Q1 2010 and 8.4% in Q4 2010.

Increase in finance costs: Increase in raw material prices has resulted in increase in the working capital requirements of the company. The total borrowings stood at RO 56.275 million and the interest costs for the quarter swelled by 42.7% to RO 401K from RO 281K during the previous year.

PAT declines despite higher earnings: PAT for the quarter stood at RO 1.015 million a decline of 40% on YoY basis and 55% on QoQ basis. This was well below our estimate of RO 2.290 million. At the sametime, the PAT margins stood at 1.5% as against 4.1% in Q1 2010 and 3.9% in Q4 2010. However the company has blamed the intense competition from the increased number of manufacturers in the region is putting pressure on its sales prices which in turn had affected its earnings during the quarter.

Quarterly Trend: Avg LME Copper Price Vs PAT Margins (%) with quarterly lag

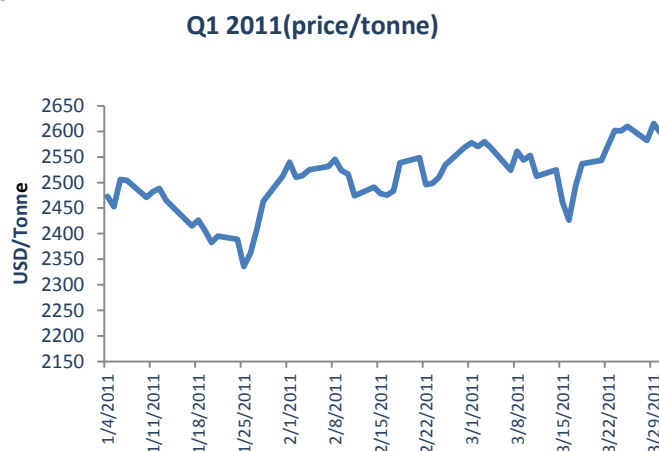


Source: Company Reports; Bloomberg; GBCM Research

The above chart shows that, if the prices of copper remain at \$7000-\$8000 levels per tonne, the company can maintain the net margins around 4% to 5%. As per our understanding, anything beyond that will squeeze the margins of the company. The average copper price during Q3 2010 was \$7,260/tonne and the company's net profit margin for the subsequent quarter (Q4FY10) stood at 3.9%. While the trend during Q1 2011 clearly indicates, with the copper prices scaling above \$8,000/tonne (during Q4FY10) the company is unable to maintain its margin, which is an area of concern.

Subsidiary performance during the quarter: The Company's subsidiary Oman Aluminium Processing Industries (OAPIL) posted revenue of RO 7.061 million during the quarter and a net loss of RO 68K. The company has stated that the recent unrest in Sohar has resulted in loss of production and sales for few days which in turn had affected the profitability of OAPIL. The company also claims that Oman Aluminium Processing Industries is well positioned with robust order book for the year.

LME Aluminium prices:



Source: Bloomberg; GBCM Research

Outlook: As per the company, the demand in the domestic market continues to remain positive due to the Government's investment on infrastructure programs and there has been a considerable improvement in few of its export markets, which is a positive sign. The order book position during the quarter has witnessed considerable improvement as compared to previous year.

The company also claims that the plant utilization has improved during this quarter for certain product lines, while the production capacity enhancement initiatives are in place in line with the expected demand.

Though the company is confident of increasing its top line, we expect the higher copper prices, the key raw material, will continue to daunt the margins moving forward (FY11E Estimated PAT margins at 3% levels). At the same time intense competition in the sector has also forced the company to reduce the selling price which in turn has impacted the margins. As mentioned above, a fall in the copper prices below \$8,000 levels would keep the margin at comfortable levels (FY10 PAT margin at 4%).

Factoring the Q1 2011 earnings along with the high volatility in the margins we have revised down the EPS estimates for FY 2011E to RO 0.090. We recommend a **'Neutral'** rating on the stock with the revised target price of **RO 1.080** (based on 12X of FY11E EPS). At current levels, the stock trades at a PE (FY10E EPS of 0.090) of 11.3X.

(Previous Rating- 'Neutral' with target price of RO 1.345, Last Report -GBCM Research-Oman Cables -FY2010 Earnings Initial View dated 24-Jan-11)

Oman Cables Industry: Q1FY11 Earnings Update

Profit & Loss Highlights (In RO 000's)	Q1 2010	Q1 2011	Var (%)	FY09	FY10	Var (%)
Revenue	41,230	69,771	69.22%	155,603	200,885	29.10%
Cost of Sales	37,705	66,492	76.35%	139,048	181,717	30.69%
Gross Profit	3,525	3,279	-6.98%	16,555	19,168	15.78%
GPM (%)	8.5%	4.7%		10.6%	9.5%	
EBITDA	2,211	1,521	-31.21%	9,573	10,432	8.98%
EBITDA Margin (%)	5.4%	2.2%		6.2%	5.2%	
Net Profit	1,701	1,015	-40.33%	6,625	8,074	21.86%
NPM (%)	4.1%	1.5%		4.3%	4.0%	
Balance Sheet Highlights (In RO 000's)						
Share Capital	8,970	8,970	0.00%	8,970	8,970	0.00%
Retained Earnings	24,763	27,837	12.41%	25,728	30,376	18.07%
Cumulative changes in fair values	478	397	-16.95%	-106	-891	740.57%
Total Equity	41,470	45,589	9.93%	41,510	46,899	12.98%
Term Loans	8,204	10,247	24.90%	6,780	10,247	51.14%
Bank Borrowings	40,563	56,275	38.73%	34,475	40,200	16.61%
Trade and Other payables	18,660	33,172	77.77%	14,301	31,405	119.60%
Total Current Liability	60,816	90,625	49.02%	50,931	74,081	45.45%
Total Equity and Liability	111,338	147,264	32.27%	100,068	132,046	31.96%
Fixed Assets	29,868	33,221	11.23%	27,993	33,079	18.17%
Total non-current assets	31,838	35,756	12.31%	30,071	35,566	18.27%
Inventories	31,881	46,779	46.73%	25,036	42,408	69.39%
Trade and other receivables	43,254	58,120	34.37%	40,864	49,945	22.22%
Cash and bank balances	3,626	3,978	9.71%	3,107	2,463	-20.73%
Total Current Assets	79,500	111,508	40.26%	6,997	96,480	1278.88%
Total Assets	111,338	147,264	32.27%	100,068	132,046	31.96%

Source: Company, GBCM Research

Income Statement Highlights

Profit & Loss A/c	2006	2007	2008	2009	2010	2011E
Revenue	125,718	217,445	304,377	155,603	200,885	264,691
Direct Cost	107,831	191,144	285,967	139,048	181,717	244,364
Gross Profit	17,887	26,301	18,410	16,555	19,168	20,327
GPM %	14%	12%	6%	11%	10%	8%
EBITDA	13,694	21,396	11,771	11,443	12,626	13,180
EBITDA margin %	11%	10%	4%	7%	6%	5%
Income Tax	1,296	2,066	818	907	1,271	1,099
Net Profit	9,538	15,134	6,132	6,625	8,074	8,058
NPM %	8%	7.0%	2.0%	4.3%	4.0%	3.0%
EPS	0.106	0.169	0.068	0.074	0.090	0.090

Source: Company, 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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