AL MAHA PETROLEUM PRODUCTS MARKETING COMPANY SAOG (MHAS.MSM)

Lower commercial fuel sales and drop in aviation fuel prices affect its Q1 2009 total sales while retail sales climb from addition of filling stations

RECOMMENDATION	:	**BUY**
CMP(14-JUN-09)	:	**RO 7.102**
TARGET PRICE	:	**RO 9.200**
VARIANCE	:	**29%**

FINANCIAL INDICATORS	Q1 2009
CMP (14-Jun-09) (RO)	7.102
MCAP (RO Mn)	49
P/E (TTM)	7.64
P/BV (Q1 09)	1.93
DIV YIELD (FY08)	7.0%
ROAE (TTM)	24.2%
ROAA (TTM)	13.8%
LT DEBT/EQUITY	-
CURRENT RATIO	1.29
OPERATING PROFIT MARGIN	3.7%
NET PROFIT MARGIN	3.3%
NET DEBT (RO Mn)	(8.14)
FCFE/SHARE (FY08)	1.659
FCFE YIELD	23.36%

Source: FINCORP Investment Research

INVESTMENT OPINION

Al Maha's Q1 2009 financial performance has been weak with total sales declining 27% while its EPS shrunk 43% YoY. Though retail sales have actually increased in Q1 2009 over Q1 2008 from the addition of ten new filling stations during April 2008 to March 2009, commercial and aviation fuel sales have dropped substantially. The slowdown in the economy that started in late 2008 has resulted in a stoppage of fuel consumption by a few of its commercial customers. The changes introduced in the sale of diesel to filling stations at border areas from an annual basis to a monthly basis affected its diesel sales growth. The sharp fall in aviation fuel prices in H2 2008 and the substantial reduction of Gulf Air's operations in Muscat adversely affected its aviation fuel sales.

Another setback was the recent change in the licensing fee structure for oil marketing companies from a fixed annual basis to a rate of 0.4% of total revenue which led to higher costs and lower net profit. We forecast a 17% decline in its 2009 sales to RO 159 million and a 20% decline in its EPS to RO 0.849. The sharp recovery in oil prices in 2009 however raises hopes for a pickup in economic activity in the quarters ahead which can improve Al Maha's commercial fuel sales. Aviation fuel sales are also likely to be higher going forward from higher oil prices. Taking these factors into account, the stock currently is trading at an attractive forward P/E multiple of 8.4x. Our target price for the stock is RO 9.200 which is 10.8 times its estimated 2009 EPS in line with the mean P/E multiple for the oil marketing industry.

COMPANY UPDATE

June 16, 2009

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BUSINESS MODEL

Al Maha Petroleum Products Marketing Company is the second largest oil marketing company by sales in Oman with a market share of 28%. It was earlier the marketing division of Oman Refinery Company LLC before it became an independent company in 1999. As of 2008, Al Maha has the largest filling station network among the three oil distribution companies at 156 as against Shell Oman's 132 and Oman Oil's 113. The company's main business segments comprise of retail, commercial and aviation fuel sales. It also sells lubricants of TOTAL, France under an agreement with TOTAL's local distributor.

Retail fuel sales,the largest business segment, posted a healthy growth of 19% during FY08 helped by higher demand and the launch of 10 new filling stations over the past 12 months. The company also provides value added services such as fuel cards, car washes and convenience stores ('Souk'). Convenience stores 'Souk' are run by Talal Zawawi Enterprises LLC and Al Maha receives a fixed annual fee till 2009 beyond which it may receive a share of Souk profits.

Commercial fuel sales segment grew by 5% in FY08. This segment is characterised by bulk sales of fuel to Ministeries, government agencies and corporates. Fuel is normally delivered by a contracted fleet of 67 heavy fuel tankers at customer locations. The Ministry of Electricity and Water, The Royal Air Force of Oman, The Ministry of Defence, ROP and PDO are key commercial customers of the company.

Aviation fuel sales is largely determined by air traffic at Muscat International Airport. Aviation fuels sales decreased 14% YoY in FY08 on account of a substantial reduction in Gulf Air's operations in Muscat International Airport as well as a sharp decline in international aviation fuel prices in H2 2008.

Q1 2009 PERFORMANCE

Total revenue for the company during Q1 2009 fell 27% YoY and 8% over Q4 2008 to RO 37.8 million. This was due to the introduction of fixed quota system for sale of diesel to filling stations located in the border areas (UAE), lower consumption from its commercial customers due to slowdown in the economic activity and declining prices of aviation fuel. Cost of sales dropped 8% sequentially due to lower quantities of fuel sold. Operating and other administrative expenses were 6% higher over Q1 2008 but 17% lower as against Q4 2008. Operating profit was 43% lower YoY, however the company was able to report a 6% higher operating profit over Q4 2008 at RO 1.4 million.

TABLE 1: FINANCIAL SNAPSHOT

	Q1 08	Q2 08	Q3 08	Q4 08	2008	Q1 09	QoQ %	YoY %
Revenue	51,755	52,558	46,260	41,085	191,658	37,782	-8%	-27%
Operating Profit	2,492	2,477	2,047	1,333	8,349	1,408	6%	-43%
Operating Profit Margin	*4.8%*	*4.7%*	*4.4%*	*3.2%*	*4.4%*	*3.7%*		
Net Profit	2,196	2,174	1,810	1,170	7,350	1,259	8%	-43%
Net Profit Margin	*3.9%*	*3.5%*	*3.7%*	*3.7%*	*3.7%*	*2.9%*		
EPS	0.318	0.315	0.262	0.170	1.065	0.182	8%	-43%

Source: Company Financial Statements

Sequentially, Al Maha's operating profit margin rose from 3.2% in Q4 08 to 3.7% in Q1 09 while net profit margin increased to 3.3% in Q1 09 from 2.8% in the last quarter of 2008.

The company's net profit fell by 43% YoY to 1.26 million in Q1 2009 as compared to RO 2.19 million in Q1 2008. The change in licencing fee structure for oil marketing companies from a fixed annual fee to a percentage share (0.4% of total annual revenue) in Q1 2009 resulted in higher licencing fees for the company.

As a result earnings per share for the quarter declined 43% YoY at RO 0.182 but was 8% higher than its EPS for Q4 2008. The company declared a cash dividend of 50% of its paid-up share capital for FY 2008 (RO 0.500 per share). This amounts to a payout ratio of 46.9% and a dividend yield of 7% at its last traded price of RO 7.102.

Property plant and equipment which accounts for 42% of the total assets increased 13% YoY on account of compeletion of the construction of the company's head office as well as the 10 new filling stations. The company has rented out a portion of its headquarters for an annual lease of RO 352,800. The company's accounts receivable which account for 32% of the total assets dropped 15.5% over the last quarter on account of lower sales.

Inventories of the company were 31.4% higher over Q4 08 at RO 3.64 million. Days sales of inventory is expected to be sharply higher in 2009 as a result of higher inventory and lower cost of sales.

Cash and Cash Equivalents amounted to RO 8.13 million at the end of Q1 09, 20% higher than in Q4 08.

The company is completely debt free as at March 31,2009 having retired all its outstanding debt obligations in November 2008.

The company has 6.9 million shares outstanding at the end of Q1 2009. Abu Dhabi based ABS Lubricants is the largest shareholder of the company having a 40% stake.

TABLE 2: SHAREHOLDING PATTERN

SHAREHOLDING PATTERN	2008	%	2007	%
Ordinary Shares				
ABS Lubricants	*2,760,000*	*40.0%*	*2,400,000*	*40.0%*

Source: Company Financial Statements

The company does not have any exposure to investments in the equity market. Retained earnings of the company reduced 12.7% in Q1 2009 to RO 15.02 million as against RO 17.21 million in Q4 2008.

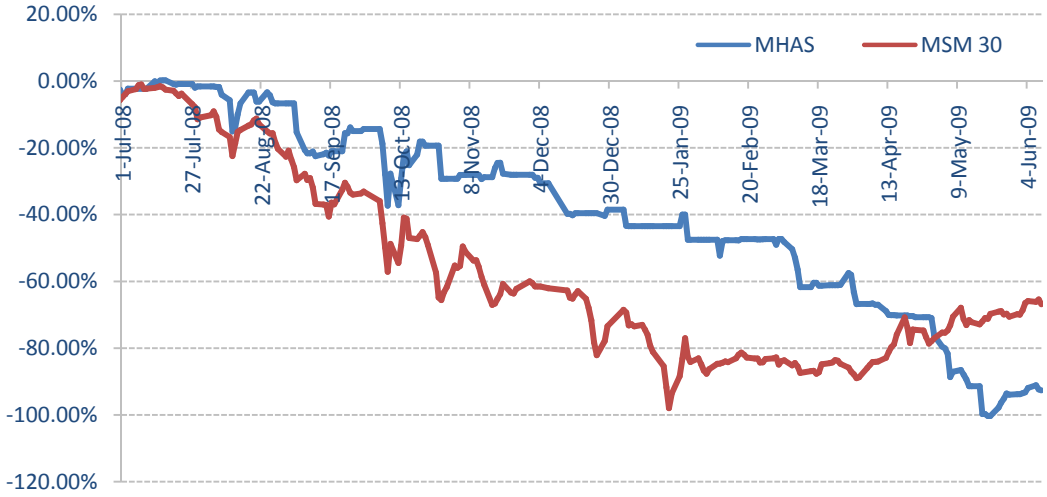
Book value per share amounted to RO 3.680 at the end of Q1 09 compared to RO 3.998 at the end of Q4 2008. The stock currently trades at a P/BV multiple of 1.93x.

TTM return on average equity dropped to 24.2% as against 29.3% in 2008 due to lower net profit in Q1 2009.

STOCK PRICE PERFORMANCE

The stock currently trades at P/E multiple of 7.64x its trailing 12 months earnings. As shown in the chart below, this stock has started to underperform the MSM 30 index since March 2009 along with its peers. Al Maha's stock has the highest 3-year beta of 0.95 as against Shell Oman's 3-year beta of 0.50 and Oman Oil's 0.69.

Figure1: Performance of MHAS vs MSM 30 Index - June 2008-June 2009



Source: MSM

VALUATION

DIVIDEND DISCOUNT MODEL

The company has increased its dividend payout ratio from 35% in 2007 to 47% in 2008. We assume the same payout ratio to be maintained in 2009 which works out to a dividend per share of RO 0.400 derived from an expected 2009 EPS of RO 0.849. We have used a long term earnings growth rate of 4% while the cost of equity works out to 10.68% (Table 3). The fair value of the stock works out to RO 5.993 which is 16% lower than its closing price on June 14, 2009 of RO 7.102.

TABLE 3

DIVIDEND DISCOUNT MODEL	
Average 3 year ROE	28.90%
Retention Ratio	50%
g	4.0%
k	10.68%
R_f	4.50%
R_m	11.00%
3 Year Beta	0.95
Dividend 2008	0.500
D_1	0.400
P_0	**5.993**

Source: FINCORP Investment Research

RELATIVE VALUATION

As seen in Table 6, the mean P/E multiple for the Oil marketing sector on a trailing twelve month basis is 9.89x. MHAS has the lowest P/E multiple 7.64x. Assuming an EPS of RO 0.849 for FY09 and a normalized P/E multiple of 12x, the fair value works out to be RO 10.188.

TABLE 4

PEER COMPARISON				
INDICATORS	MHAS	SOMS	OOMS	MEAN
P/E (TTM)	7.64	12.95	9.09	9.89
P/BV (Q109)	1.93	8.76	2.65	4.45
ROE (TTM)	24.21%	54.71%	28.36%	35.8%
Div Yield (FY08)	5.2%	6.4%	3.0%	4.9%
Div Payout (FY08)	46.9%	92.0%	35.7%	58.2%

Source: FINCORP Investment Research

DISCOUNTED CASH FLOW ANALYSIS

The company has recorded a 26.5% CAGR in revenue during 2005 to 2008 benefitting from economic expansion in the Sultanate. We expect the company's sales to decline 17% to RO 158.7 million in 2009 as a result of economic contraction. Our forecast of sales for the intermediate period between 2010 and 2013 is based on a moderation in growth rate from 12% in 2010 to 10% in 2013. EBIT margin is assumed to remain constant at 4% for the forecast period. Depreciation as a percentage of PP&E is assumed to be at 8-9%. Capex as a percentage of sales is assumed to be constant at 2.5%. Tax rate is held constant at 12%.

TABLE 5: FORECAST OF FCFF (RO Million)

	2006	2007	2008	2009E	2010E	2011E	2012E	2013E	Terminal Stage
Revenue	94,663	123,497	174,795	158,684	177,727	199,054	220,950	243,045	
EBIT Margin	3.8%	3.7%	4.4%	4.0%	4.0%	4.0%	4.0%	4.0%	
EBIT	4,014	6,126	9,132	6,347	7,109	7,962	8,838	9,722	
PP&E	10,098	11,752	16,324	19,800	21,780	23,958	26,354	28,989	
Depreciation	325	1,522	1,415	1,782	1,960	1,917	2,108	2,319	
Depreciation/PP&E	3.2%	12.9%	8.7%	9.0%	9.0%	8.0%	8.0%	8.0%	
Capex	2,578	2,895	6,012	3,967	4,443	4,976	5,524	6,076	
Capex/sales	2.7%	2.3%	3.4%	2.50%	2.50%	2.50%	2.50%	2.50%	
Change in Wcap	4,521	(2,194)	4,929	-	-	-	-	-	
Change in Wcap/sales	4.8%	-1.8%	2.8%	0.0%	0.0%	0.0%	0.0%	0.0%	
Tax Rate	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	
FCFF	(3,241)	6,211	(1,488)	3,401	3,773	3,947	4,362	4,798	
Discounted FCFF				3,232	3,241	3,063	3,059	3,040	47,363

Source: FINCORP Investment Research

TABLE 6: WACC

R_f	4.50%
R_m	11.00%
3 yr Beta	0.95
Cost of Equity	10.68%
Proportion of Equity	100%
Tax Rate	12%
WACC	**10.68%**

Source: FINCORP Investment Research

TABLE 7: FAIR VALUE COMPUTATION

Terminal Growth Rate	4%
Dis Terminal Value	47,363
Dis FCFF Explicit	15,634
Firm Value	62,997
Net Debt	(8,139)
Equity Value (RO '000)	71,136
Outstanding Shares ('000)	6,900
Fair value per share (RO)	**10.310**

Source: FINCORP Investment Research

Assigning a weightage of 50% to DCF and 25% each to DDM and Relative Valuation techniques, the Fair Value for Al Maha works out to RO 9.200 which is 29% higher than its last traded price of RO 7.102.

TABLE 8: Target price

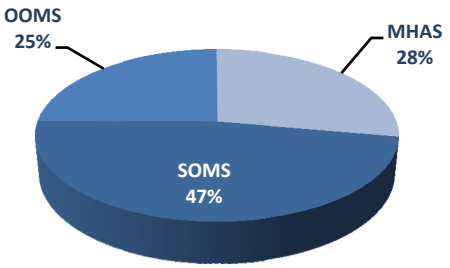
Method	Weight	Fair value
Dividend discount model	25%	5.993
Relative Valuation	25%	10.188
Discounted Cash flow	50%	10.310
Expected fair value per share (RO)		**9.200**

Source: FINCORP Investment Research

OMAN'S OIL MARKETING INDUSTRY OVERVIEW

As shown in Fig. 2 Shell Oman leads the oil marketing industry in Oman with a 2008 market share of 47% followed by Al Maha at 28% and Oman Oil at 25%. It is also the market leader in all of the individual business segments as shown in table 12. Under the retail segment, Shell reported sales of RO 157 million (48% of total sales) in 2008 while Oman Oil reported retail sales of RO 102 million (60% of total sales). Al Maha has the highest number of filling stations at 156 followed by Shell at 132 and Oman Oil at 113. In terms of sales per station too, Shell (annual sales of RO1.19 million per station) scores over Oman Oil (annual sales of RO0.903 million per station).*

Figure 2: Market Share (2008)



Source: Company Financial Statements

In terms of future growth, Al Maha is mainly focusing on improving its market share in the retail segment where. The company has been aggressive in opening more retail outlets along with providing good customer service/value added services as discussed earlier in its business model.

TABLE 9: 2008 SALES BREAKUP

	SOMS	OOMS	MHAS
Total sales (RO '000)	326,367	170,049	191,658
Number of stations (Retail)	132	113	156
Sales per station (Retail) (RO '000)	1,191	903	N.A.
3 yr Revenue growth	21%	24%	27%
3 Yr EPS growth	19%	25%	31%

Source: Company Financial Statements

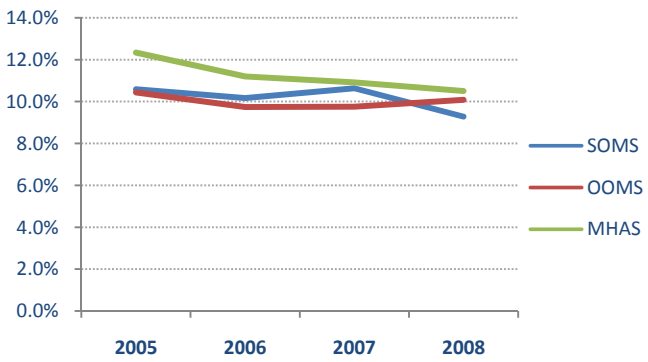
Al Maha's operating profit margin declined slightly in 2008 to 10.5% from 10.9% in 2007 while Oman Oil's OPM rose from 9.7% to 10.1% (Fig. 3). The industry's average operating margin is also close to 10%. In terms of Net Profit margin, Oman Oil has historically led the industry (Fig. 4). The Average net profit margin for the industry in 2008 was 4.7%.

TABLE 10: 2008 SALES BY SEGMENT

	SOMS	OOMS	MHAS
Retail	157,185	102,029	N.A.
Commercial	65,593	39,111	N.A.
Lubricant	60,317	17,005	N.A.
Aviation	43,272	11,903	N.A.
Total Sales	326,367	170,049	N.A.

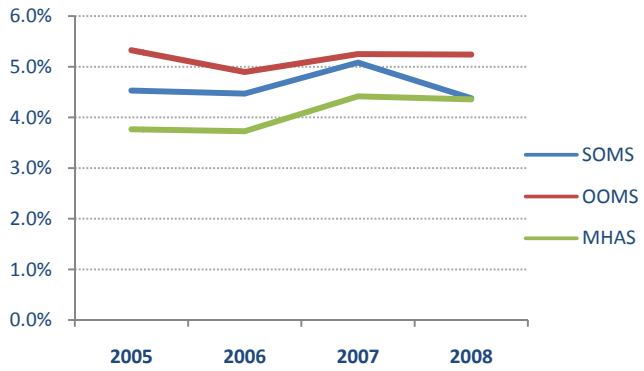
Source: Company Financial Statements

Figure 3: Operating Profit Margin



Source: Company Financial Statements

Figure 4: Net Profit Margin

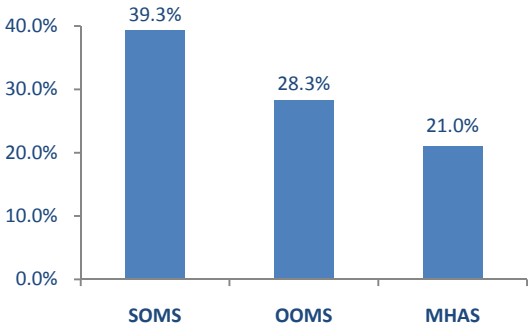


Source: Company Financial Statements

* The corresponding figures for Al Maha are not available in that company's financial statements.

Shell delivers the highest ROIC, ROE and economic spread (ROIC-WACC) as shown in Fig. 5, 6 & 7. Shell has steadily improved its ROIC from 34.7% in 2005 to 47% in 2008 whereas Al Maha's ROIC improved from 19.3% in 2005 to 31.7% in 2008. Shell's ROE in 2008 at 48% is much higher than that of its competitors – Oman Oil (32.6%) and Al Maha (29.4%).

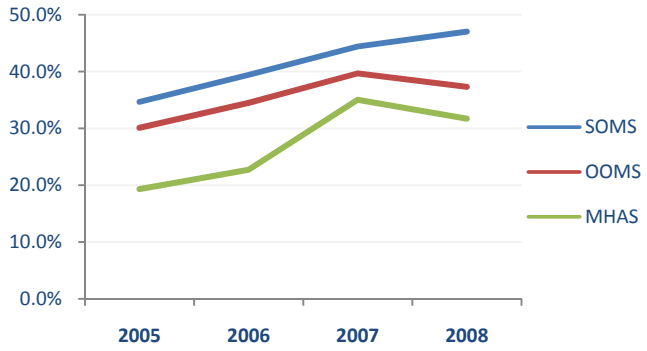
Figure 5: Economic Spread - FY2008



Source: Company Financial Statements

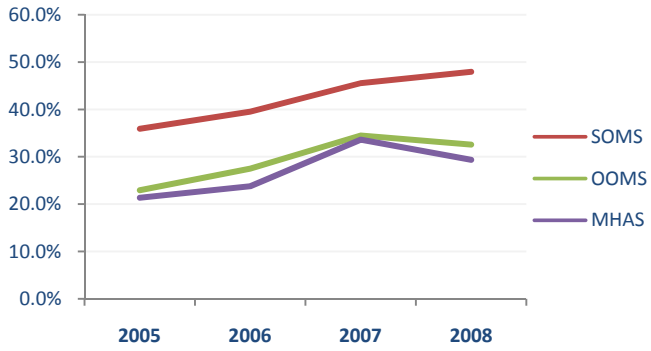
Weighted Average Cost of Capital was the lowest for Shell at 7.7% as against 9% for Oman Oil and 10.7% for Al Maha in 2008. As a result, Shell's economic spread at 39.3% is way above that of its competitors which explains its premium valuation (highest P/E, highest P/BV) in the market.

Figure 6: ROIC



Source: Company Financial Statements

Figure 7: ROE



Source: Company Financial Statements

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