

AACT – RO 0.238

MSM – 4870.060

25<sup>th</sup> February 2009

Recommendation	Target
Buy	0.379

### Investment rationale

During the FY2008, the company achieved an outstanding sales growth of 35%. The revenue for FY2008 reaching RO11.869 mn, beating almost all analyst expectations. As of February 2009, the company has a healthy order book, same as of FY2008. The company's focus on local market was highly successful in generating the top line. The contribution from local market in FY2008 was 60% to the total revenue by value as well as volume and the market share of the company increased to nearly 50% in local market.

The company is one of the **Low cost producer** and easy access to the export markets. We expect the growth to continue because of the huge gap between supply and demand of ceramic tiles in GCC region.

The growth of the company has been steady throughout the years and expected to move with the increased Government expenditure on tourism and infrastructure development. Al Shams, with its product quality and expansion will be able to cater the required 70% of the Omani demand which shows a growth of 12-13% annually, thus benefiting from the domestic demand growth and import gap.

We believe that the **addition of new production** line will increase the company's control over the market and the cost as well. As the capacity utilization imperative will drive pricing behaviour.

We expect a CAGR of 13% over 2009-2011. The stock is trading at P/E of 6.3x and 5.5x of FY09 and FY10 respectively.

Given the entry of new players into Oman's real estate sector as well as the integrated tourism projects with a favorable macro picture, we have valued the stock at RO 0.379. We recommend investors to buy the stock at current price with a target price of RO 0.379, for 12 months, which carries an upside of 59% from the present market price.

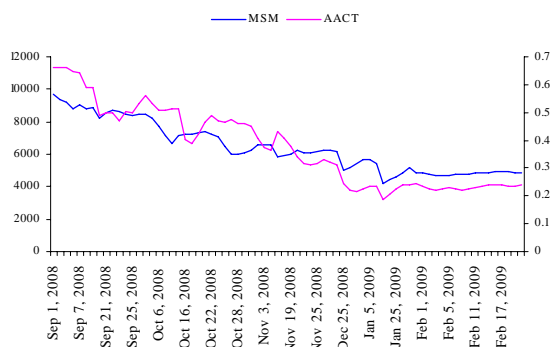
Key Figures	2008A	2009E	2010E	2011E
Net Sales	11,869.9	13,500.0	15,200.0	17,000.0
Operating Profit	3,981.3	4,701.6	5,379.9	6,118.9
EBITDA	4,755.1	5,498.6	6,200.8	6,964.4
Net Income	3,567.2	4,212.6	4,820.3	5,482.5

Key Ratios	2008A	2009E	2010E	2011E
NPM(%)	30%	31%	32%	32%
ROE(%)	26.4%	19.1%	15.0%	12.9%
ROA	20.2%	15.9%	13.3%	11.6%

Valuation	2008A	2009E	2010E	2011E
EPS	0.032	0.038	0.043	0.049
P/E(x)	7.5	6.3	5.5	4.9
P/BV(x)	2.0	1.2	0.8	0.6

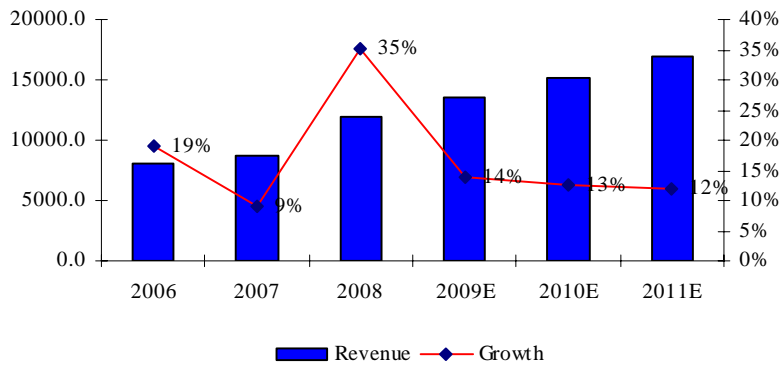
Basic Details		
Market Price	0.238 52Wk high	0.749
Shares O/S (In,000)	111,891 52Wk low	0.175
Market Cap	26630.06 YTD Change	26.35%
MSM Ticker	AACT Bloomberg Reuters	AACT OM AACT. OM

### Stock performance last 6 Months



### Financial Analysis

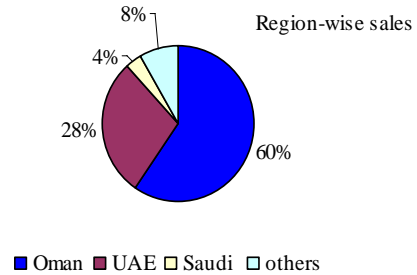
During the year 2007, the company registered gross revenue of RO 8.773 mn and a net profit of RO 2.315 mn signifying a 30% profit growth over the previous year. The company produced 6.18 Million Sq Ft of tiles in FY 2007. The Company has the benefit of using local raw materials and new technologies successfully, thereby deriving significant cost advantages.



The year 2008 has been remarkable and outstanding for the company. The top line as well as the bottom line was in line with our previous estimates. The company achieved revenue of RO 11.87mn, selling 7.11 mn sqm of ceramics. The new production line added produced 25% of the capacity. The sales growth was driven by basically from the local market.

Compared to FY2007 when the company sold only 2.2 mn Sqm in local market, the year 2008 witnessed a huge demand growth from the local market. The company was bale to sale 4.34 mn sqm of ceramics in the local market. Thus the company has gained and acquired the local market share by almost 50%.

Going forward, we believe the sales to export market to remain in tact; the company will be able to push the sales of UAE market to Saudi market, which is comparatively huge. Also in UAE market, the 70% of the sales of the company comes from the distributors, where as only 30% from the contractors.



The company has 15-30 dealers in Oman. In UAE, the company sales through 15-20 dealers and 10-12 contractors.

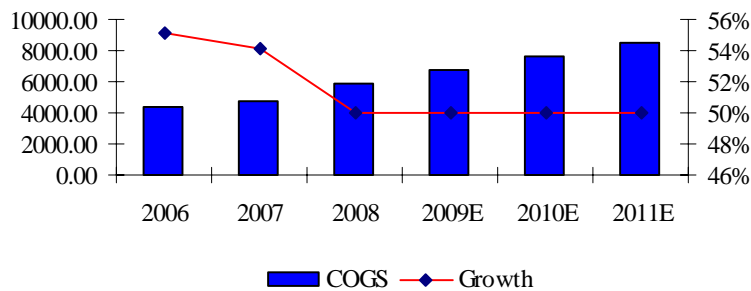
In the Saudi market, which is the largest market in the GCC for ceramic tiles, the company has 5 key distributors, those are large in size to absorb any further push of sales. Also with the capacity expansion, the company would try to capture the gap between the

domestic produced and import market. The company has its brand equity in the low cost tiles only. And it's planning to have a co branding arrangement with Italian tile producer.

### Cost and Expenses

The company enjoys the benefit of low cost because of the reach to the raw materials. The raw material required for ceramics are Clay, Silica and limestone or Sand. So the most important thing is that the basic raw material is available within 200 Km diameter of the manufacturing facility. Thus the company enjoys the advantage of cost efficiency in procuring raw material.

The cost of production accounts for 50-55% of the total sales. The company has managed to maintain the cost level. The fixed cost is around 40% of the total cost.



The major concern here is the easy and sufficient availability of natural gas, which account for 5% of the total cost, whereas the total energy cost accounts to 8%, including electricity and gas.

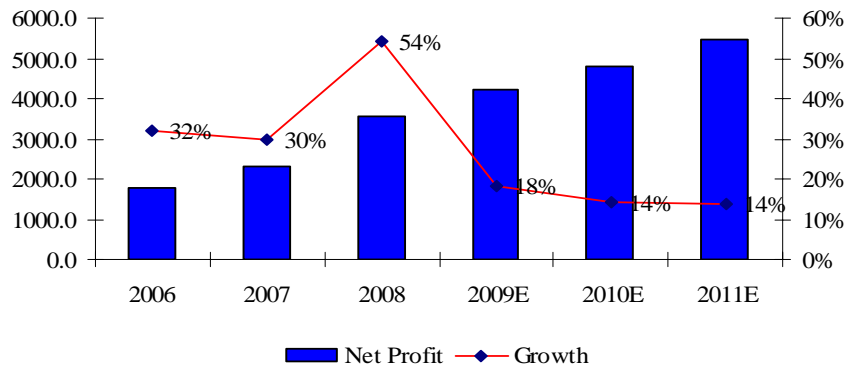
The supply of gas is not a constraint for the company, as the company has an agreement till 2022. So in the short term, supply of gas is not a concern. The leasing agreement for the mines is also stable and renewed for next 15 years.



**Profitability**

The Profit before tax for FY08 was RO 3.981 mn , which increased by 70% over 2007. The growth was derived by the high and consistent realization per unit sales as well as the high oil price, leading to the investment boom.

The Net Profit achieved the company for FY08 reached at RO 3.56mn, growing by 35% for on a year on year basis.



The company has been able to manage the profitability margin by prudently keeping the cost under control. As of today, there has been no sign of decrease in realization per unit.

	2004	2005	2006	2007	2008
Sales Volume( mn Sqm)	3.49	5.01	5.91	6.18	7.11
Sales(RO mn)	5.00	6.76	8.05	8.77	11.87
Avarage realization / unit	1.43	1.35	1.36	1.42	1.67
Net Profit	1.33	1.38	1.78	2.37	3.56
Net Profit Margin	27%	20%	22%	27%	30%

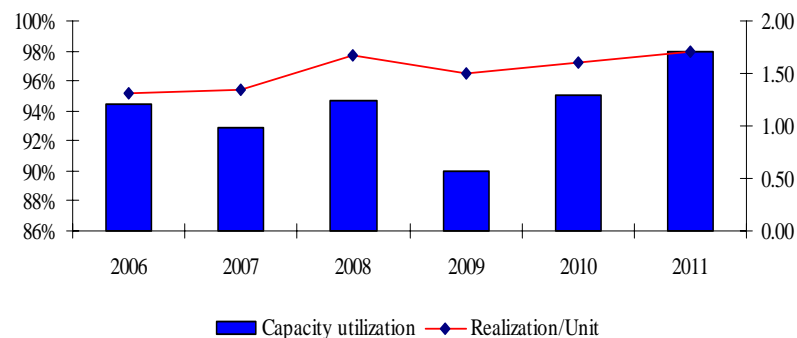
### Capacity utilization & Expansion plan

Earlier till the third quarter of 2008, Al Anwar Ceramics was operating with two production lines with a capacity of about 7 million Sq. metres per annum. The company has added a new production line which gives an additional capacity of 3 million Sq. mtr per annum, thus taking the total capacity close to 10 million Sq. Mtrs per annum. With new firing line, the company has emerged as one of the largest producers in the GCC region.

The company plans to expand to 16 mn sqm in medium term.

At present the factory and office premises occupy only 20% of the total leased area. So given the opportunity, on a requirement basis, there is huge scope for expansion. As acquiring land will not be a problem.

The company uses both the dry as well as the wet process of producing ceramic tiles. Two of the lines are being engaged with dry process, which gives the company better cost control and efficient realization on output.

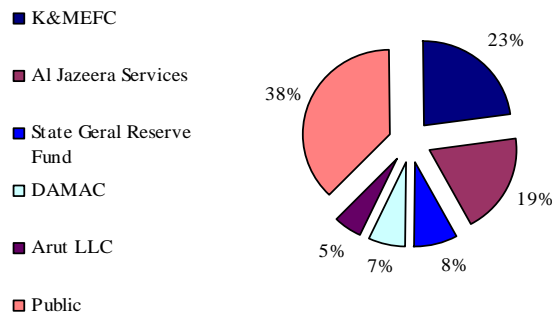


Currently the company is running utilising almost 100% of its capacity. As we believe the capacity utilization imperative will drive pricing behavior. The ceramic tile manufacturing Industry being a capital intensive one, the overall cost for the setting up of the new facility would be higher. We estimate that setting up a new production line requires a minimum fixed cost of Ro 5 mn. And given the demand supply gap in GCC region, running with full capacity would give the company economies of scale.

### Company overview

Al Anwar Ceramic Tiles Co (AACT) was established in 1997 by a group of 11 local investors led by Al Anwar Industrial & Trading Co. SAOG, Oman & Emirates Investment Holding Co. SAOG. The other founding members include the Oryx Joint Investment Account and National Aluminium Products Co. SAOG. The start up capital was RO 1.8 mn and a capacity of 3 mn Sqm per annum.

The company is engaged in the activity of producing glazed ceramic floor and wall tiles, in collaboration with an Italian company, under the brand name of ‘Al Shams’. The basic raw materials utilized in the production of tiles such as silica sand, shale and limestone are sourced from within a 200-km radius of the plant.



AACT is the dominant manufacturer of ceramic tiles in Oman, but faces competition from products imported from other countries in the GCC/Mid-East, Africa, South-East Asia and Europe.

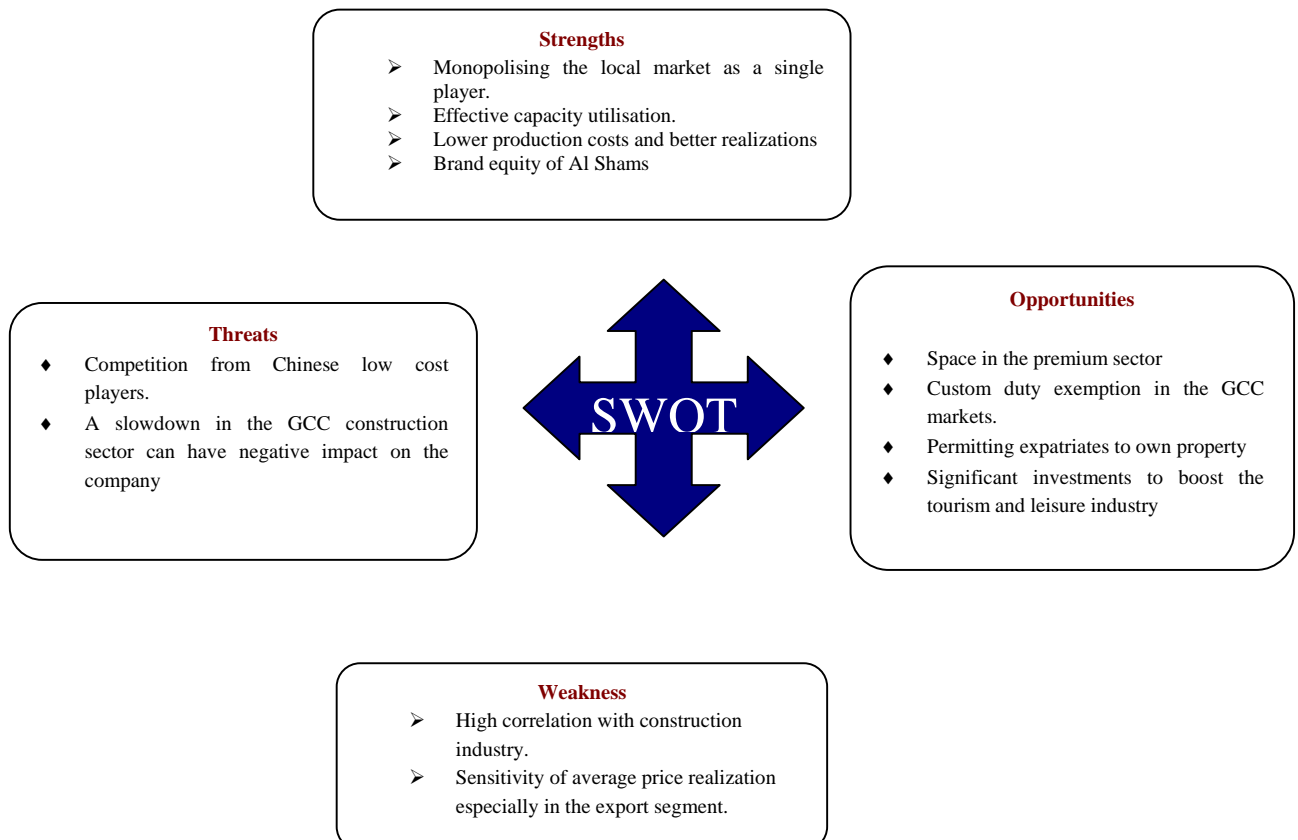
## The industry

The ceramic tile market in the region is estimated at about 145 Million sq. Mt. pa Constituting 4% of the global market. The industry has registered a CAGR of 14% (2000-2008) making it one of the fastest growing markets in the world.

Though currently the GCC tile market constitutes only 4% of the world markets the strong construction growth fuelled by the opening of the real estate sector to foreign investments coupled with the high liquidity in the economies will provide further impetus to the industry.

The GCC region is catered by the local players by 50% of the demand and the rest by imports. So, this provides a huge opportunity for local manufacturers to fill the gap providing in time delivery and quality products.

## SWOT Analysis



### **Local Market**

Omani market is driven by the demand from retail segment only. The mid-segment retail product forms more than 70% of the market and this is being catered by local manufacturers Al Anwar Ceramics and Al Maha Ceramics. The mid-segment retail product forms more than 70% of the market and this is being catered by local manufacturers Al Anwar Ceramics and Al Maha Ceramics. The premium product which forms around 10% of the overall market is catered by western players. The rest of the market, around 10-20% being catered by low cost Chinese products.

### **Favourable demographic**

The total GCC population of around 30 million people is expected to double by 2050. Further favourable demographic factors such as 70% of the total GCC population being below 30 years of age, increasing nuclear families and higher purchasing power have created a surge in demand for user industries.

### **Supply deficiency creates opportunity**

The current boom in the end user industries has triggered exponential demand growth in the ceramic and tile market. Although the GCC manufacturers have stepped up production, more than 35-40% of the demand is currently met by imports. The major countries that sell their products in the GCC are Italy, Spain, China, India, Indonesia and Iran.

### **Outlook**

There has been a supply gap in the region which is estimated between 30 million to 40 million square metres. This leaves a huge opportunity for all the players in the GCC to capitalise on.

The Construction Industry in the GCC continues to witness very satisfactory growth and the medium term demand view remains optimistic.

We expect growing consumption for the company's products. However increased supplies and price competition from around the world, particularly China is a Iso a concern. So while the demand grows, so does supply. Instead of pricing , cost of production remains the key to profitable growth.

Since there is no company with a similar business in Oman, we compare companies in the region and observe that AACT is trading at a significant discount to its peers.



## Valuation

We initiated our valuation considering the market return to be 15% for the year and the terminal growth for the company at 1%.the new issue of bonus shares have been taken in to consideration. With the below mentioned assumptions, we reached at the intrinsic value of RO 0.379, which have an upside of around 60% from the present market price.

### DCF Assumptions

Risk Free rate	4.5%	Market cap	27886.8
Risk Premium	10.5%	Debt	1064
Beta	1.26	Cost of debt	10.0%
Cost of Equity	17.1%	Market Returns	15.0%
WACC	16.8%	Terminal growth rate	1%

Total discounted cash flows	<b>55,393.4</b>
Less Debt	(1,126.8)
Add cash	1,279.1
Add Investments	0.0
Less Minority Interests	0.0
Equity Value	55,545.7
Shares in issue	111,891.000
DCF per share	<b>0.379</b>
Share Price	0.238
Upside/(Downside)	<b>59.2%</b>

**Ratio analysis**

<b>Valuation &amp; Return Metrics</b>	<b>2006A</b>	<b>2007A</b>	<b>2008A</b>	<b>2009E</b>	<b>2010E</b>	<b>2011E</b>
P/E(x)	9.5	7.4	7.5	6.3	5.5	4.9
P/BV(x)	1.9	1.5	2.0	1.2	0.8	0.6
ROE	20.4%	20.9%	26.4%	19.1%	15.0%	12.9%
ROCE	17.9%	19.3%	24.6%	18.4%	14.8%	12.8%

<b>Growth Rates and Margins:</b>	<b>2006A</b>	<b>2007A</b>	<b>2008E</b>	<b>2009E</b>	<b>2010E</b>	<b>2011E</b>
Revenue Growth	19.0%	9.0%	35.3%	13.7%	12.6%	11.8%
EBITDA Growth	17.8%	22.2%	56.3%	15.6%	12.8%	12.3%
EBITDA Margin	30.9%	34.7%	40.1%	40.7%	40.8%	41.0%
EBIT Margin	22.6%	26.8%	33.5%	34.8%	35.4%	36.0%

<b>Credit Statistics:</b>	<b>2006A</b>	<b>2007A</b>	<b>2008E</b>	<b>2009E</b>	<b>2010E</b>	<b>2011E</b>
EBITDA /Net Interest Expense	1.4	1.3	1.2	1.2	1.2	1.1
EBITDA-CapEx /Net Interest Expense	1.5	1.4	2.6	1.2	1.2	1.2

**Key Financial statements**

<b>INCOME STATEMENT</b>	<b>2005A</b>	<b>2006A</b>	<b>2007A</b>	<b>2008A</b>	<b>2009E</b>	<b>2010E</b>	<b>2011E</b>
	<b>OMR mn</b>	<b>OMR mn</b>	<b>OMR mn</b>	<b>OMR mn</b>	<b>OMR mn</b>	<b>OMR mn</b>	<b>OMR mn</b>
Revenue	6767.20 #	8050.00	8774.00	11869.93	13500.00	15200.00	17000.00
Other income	0.00	0.00	0.00	0.00	0.00	0.00	0.00
<b>Total Turnover</b>	<b>6767.20</b>	<b>8050.00</b>	<b>8774.00</b>	<b>11869.93</b>	<b>13500.00</b>	<b>15200.00</b>	<b>17000.00</b>
% Growth		19%	9%	35%	14%	13%	12%
Cost of sales	4028.36	4433.24	4747.37	5935.40	6750.50	7600.56	8500.63
COGS % of sales	60%	55%	54%	50%	50%	50%	50%
<b>Gross Profit</b>	<b>2738.84</b>	<b>3616.76</b>	<b>4026.63</b>	<b>5934.53</b>	<b>6749.50</b>	<b>7599.44</b>	<b>8499.37</b>
Gross Profit Margin	40%	45%	46%	50%	50%	50%	50%
Other income	4.099 0	13.157	96.3	80.114	76.1083	57.081225	77.0596538
<b>Operating Expenses</b>							
General and administration expenses	587.65	742.10	837.27	1161.25	1219.31	1341.24	1475.37
Selling & Distribution Expenses	641.43	976.44	887.65	848.45	890.87	935.42	982.19
Net Interest Expense	76.053 0	65.655	13.312	23.677	13.8	0	0
Directors's Salary	0 0	28	36	0	0	0	0
<b>Total Operating Expenses</b>	<b>1305.13</b>	<b>1812.20</b>	<b>1774.23</b>	<b>2033.38</b>	<b>2123.99</b>	<b>2276.66</b>	<b>2457.56</b>
<b>Profit Before tax</b>	<b>1437.81</b>	<b>1817.72</b>	<b>2348.70</b>	<b>3981.26</b>	<b>4701.62</b>	<b>5379.86</b>	<b>6118.87</b>
EBIT Margin	21%	23%	27%	34%	35%	35%	36%
Tax	(26.00)	(35.00)	(33.00)	(414.07)	(488.99)	(559.53)	(636.39)
<b>Net Income</b>	<b>1411.81</b>	<b>1782.72</b>	<b>2315.70</b>	<b>3567.19</b>	<b>4212.63</b>	<b>4820.33 #</b>	<b>5482.48</b>
NI Margin	21%	22%	26%	30%	31%	32%	32%



Balance Sheet	2005A	2006A	2007A	2008E	2009E	2010E	2011E
	OMR mn	OMR mn	OMR mn	OMR m	OMR m	OMR m	OMR m
<b>Assets</b>							
Cash and bank balances	64.3	811.9	589.7	1,279.1	9,139.7	18,116.3	27,983.4
Inventories	1,802.9	1,615.4	1,415.1	2,164.4	2,461.6	2,771.6	3,099.8
Trade receivables	2,068.1	2,405.2	1,847.2	2,587.9	2,717.3	2,853.2	2,995.8
Other receivables	82.2	103.1	346.7	178.3	533.5	600.6	671.8
Financial assets held - to - maturity	0.0	0.0	3,425.2	107.9	0.0	0.0	0.0
<b>Total Current Assets</b>	<b>4,017.5</b>	<b>4,935.6</b>	<b>7,623.8</b>	<b>6,317.6</b>	<b>14,852.1</b>	<b>24,341.7</b>	<b>34,750.8</b>
Property, plant and equipment	7,029.0	6,614.5	6,233.4	11,341.2	11,681.5	12,031.9	12,392.9
Financial assets available - for - sale	0.0	0.0	74.2	22.9	0.0	0.0	0.0
<b>Total Assets</b>	<b>11,046.5</b>	<b>11,550.1</b>	<b>13,931.4</b>	<b>17,681.7</b>	<b>26,533.5</b>	<b>36,373.6</b>	<b>47,143.6</b>
<b>Liabilities and Shareholders Equity</b>							
<b>Current Liabilities</b>							
Current maturities of Government soft loans	725.0	308.3	308.3	308.3	308.3	0.0	0.0
Trade and other payables	1,096.8	1,000.4	1,255.9	2,404.6	2,734.8	3,079.2	3,443.8
Taxation	298.1	0.0	0.0	342.1	359.2	377.2	396.0
<b>Total Current Liabilities</b>	<b>2,120.0</b>	<b>1,308.7</b>	<b>1,564.3</b>	<b>3,055.0</b>	<b>3,402.3</b>	<b>3,456.4</b>	<b>3,839.8</b>
Non -current maturities of Government soft loans	1,443.7	1,023.0	793.8	485.6	308.3	0.0	0.0
Deferred Government grant	304.9	210.3	131.0	131.0	131.0	0.0	0.0
Employee End Service benefits	90.0	102.9	145.0	201.8	246.3	301.9	371.5
Deferred tax liability	149.0	184.0	217.0	289.0	361.2	451.5	564.4
<b>Total Liabilities</b>	<b>1,987.6</b>	<b>1,520.2</b>	<b>1,286.8</b>	<b>1,107.4</b>	<b>1,046.9</b>	<b>753.4</b>	<b>935.9</b>
Share capital	3,187.8	5,738.0	7,172.6	8,607.1	8,607.1	8,607.1	8,607.1
Legal reserve	590.3	768.6	1,000.1	1,356.8	2,100.0	2,310.0	2,541.0
Retained earnings	610.6	780.1	353.7	3,564.1	7,776.8	12,597.1	18,079.6
Proposed bonus shares/Dividend	2,550.2	1,434.5	2,510.4	0.0	3,600.5	8,649.6	13,140.2
Fair value reserve	0.0	0.0	43.6	(8.8)	0.0	0.0	0.0
<b>Total Equity</b>	<b>6,939.0</b>	<b>8,721.2</b>	<b>11,080.3</b>	<b>13,519.2</b>	<b>22,084.3</b>	<b>32,163.8</b>	<b>42,367.9</b>
<b>Total Liabilities &amp; Shareholders' Equity</b>	<b>11,046.5</b>	<b>11,550.1</b>	<b>13,931.4</b>	<b>17,681.7</b>	<b>26,533.5</b>	<b>36,373.6</b>	<b>47,143.6</b>

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