



SHUAACAPITAL_{PSC}

Arabian Pipes Company (2200.SE)

Cashing in on an Oil & Gas Infrastructure Boom

Equity Research

Initiation Coverage

May 28th, 2008

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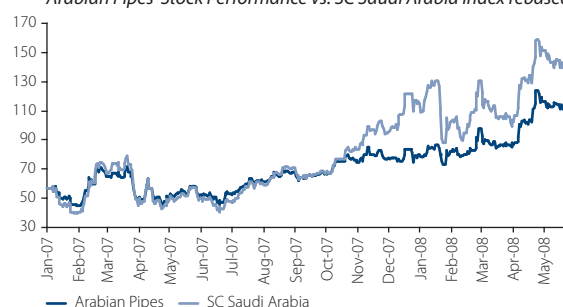
Current Price:	SAR 107.00	Country:	Saudi Arabia
Fair value Target:	SAR 155.00	Sector:	Industrial/Pipes
Recommendation:	BUY	Exchange:	Saudi Stock Exchange (Tadawul)

- Arabian Pipes Company (APC) is the largest manufacturer of medium range High Frequency Welded (HFW) steel pipes in the Middle East (ME) with a total production capacity of 160,000 tons per annum (tpa) in 2007 and expected to reach 780,000 tpa by Q4 2011. Increased oil and gas exploration and associated O&G infrastructure construction spending globally have given the steel tubing and pipes industry a major boost. The Middle East represents a significant share of anticipated demand for steel pipes over the next five years, from which APC should be a major beneficiary.
- APC benefits from long term supply contracts with Saudi Aramco and Oman Oil Company, which represent the primary revenue anchor for the pipe producer. The company's strategy going forward includes retaining and extending of these contracts, as well as diversifying its customer base by targeting other regional oil majors as well as low energy infrastructure markets.
- Given APC's significant investments in new capacity to meet strong current and anticipated demand for steel pipes in the GCC and the rest of the Middle East, we expect the company's market share of production in the region to expand drastically from around 15% to over 50% by 2012. As a result we expect APC to witness very strong 42% CAGR in revenues over our forecast horizon and a net profit CAGR of 46% over the same period. Net profits for 2008 are expected to grow at a lower rate of 20%, coming in at SAR 153 mn on total revenues of SAR 808 mn.
- APC's strategic location in the heart of resource rich GCC at a time of significant growth in the sector's CAPEX, especially related to oil and gas transportation infrastructure, are key drivers of the company's growth and profitability going forward. Its strong alliance and successful track record with Saudi Aramco opens up the likelihood of significant new supply contracts with other oil majors in the region. The company's planned capacity expansion as well as its technical know-how and timely delivery are core to the growth and value realization anticipated for the company over the next five years. We initiate coverage on APC with a BUY recommendation based on a target price of SAR 155.00 per share, implying 45% upside potential over the latest market price of SAR 107.00 per share.

Year	Net Profit (SAR '000)	BV (SAR '000)	EPS (SAR)	BVPS (SAR)	Return on Equity	EBITDA Margin	P/E (x)	P/BV (x)	EV/EBITDA (x)
Dec-10	473,125	1,289,587	15.02	40.94	36.7%	27.8%	7.12	2.61	8.85
Dec-09	370,229	982,056	11.75	31.18	37.7%	27.8%	9.10	3.43	10.51
Dec-08	153,297	741,407	4.87	23.54	20.7%	26.5%	21.99	4.55	19.88
Dec-07	125,580	641,764	3.99	20.37	19.6%	24.7%	26.84	5.25	25.93

52-Week high	115.50
Number of shares ('000)	31,500
Free float	44%
Market Cap (SAR ' 000)	3,370,500
Market Cap (USD ' 000)	898,800

Arabian Pipes Stock Performance vs. SC Saudi Arabia Index rebased



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Investment Highlights

- Arabian Pipes Company (APC) is the largest manufacturer of medium range High Frequency Welded (HFW) steel pipes in the Middle East (ME) with a total production capacity of 160,000 tons per annum (tpa) in 2007 and expected to reach 780,000 tpa by Q4 2011. The company has two production facilities; one in Riyadh's Industrial City with a total production capacity of 160,000 tpa of small diameter pipes, and expected to reach 400,000 tpa in 2011, while the second, currently under construction, is located in Jubail Industrial City with total production capacity of 380,000 tpa.
- Steel pipes are considered arteries of any country's energy infrastructure, as well as the safest and cheapest way to transport energy products. Increased oil and gas (O&G) exploration and associated O&G infrastructure construction spending globally have given the steel tubing and pipes industry a major boost. The Middle East represents a significant share of anticipated demand for steel pipes over the next five years, with the GCC alone expected to add 21,000 km, or 14% of anticipated global additions, to its pipeline network.
- Given APC's significant investments in new capacity to meet strong current and anticipated demand for steel pipes in the GCC and the rest of the Middle East, we expect the company's market share of production in the region to expand drastically from around 15% to over 50% by 2012, while the company's product mix is diversified from the current production of only small diameter pipes, to include large diameter and spiral pipes. Despite the massive increase in production capacity, we anticipate that regional demand will remain in line with supply over the forecast period, and that prices will remain firm.
- APC benefits from long term supply contracts with Saudi Aramco, the largest oil major in the region and arguably the producer with the most stringent quality standards, as well as with Oman Oil Company. These contracts represent the primary revenue anchor for the pipe producer. The company's strategy going forward includes retaining and extending of these contracts, as well as diversifying its customer base by targeting other regional oil majors including in gas rich Qatar as well as targeting low energy infrastructure markets such as Iraq. Possible risks arise from current customer concentration as well as from the spiraling cost of steel, which represents between 65-70% of production costs.
- We expect APC to witness very strong 42% CAGR in revenues over our forecast horizon, underpinned by aggressive new capacity coming on line. Although steel price appreciation may result in some intermittent margin pressure, we believe that APC will actually achieve an expansion in margins over our forecast horizon, resulting in a net profit CAGR of 46% over the same period. Net profits for 2008 are expected to grow at a lower rate of 20%, coming in at SAR 153 mn on total revenues of SAR 808 mn.
- APC's strategic location in the heart of resource rich GCC at a time of significant growth in the sector's CAPEX, especially related to oil and gas transportation infrastructure, are key drivers of the company's growth and profitability going forward. Its strong alliance and successful track record with Saudi Aramco is evident in a five year supply contract, and promises a solid and stable base for growth. It also opens up the likelihood of significant new supply contracts with other oil majors in the region. The company's planned capacity expansion, of which significant CAPEX outlay has already occurred, as well as its technical know-how and timely delivery are core to the growth and value realization anticipated for the company over the next five years, and should result in significant market share gains, as well as a more robust barrier to entry for other producers.
- We initiate coverage on APC with a Buy recommendation based on a target price of SAR 155.00 per share, implying 45% upside potential over the latest market price of SAR 107.00 per share. Our target price per share is based on two valuation methods, Discounted Cash Flow method (DCF), which has yielded a target price of SAR 158.94 per share and Price Earnings (PE) relative valuation, which has yielded a fair value of SAR 145.87 per share based on FY09 earnings. We assign an average weight for our DCF value of 70% and 30% to our relative valuation.

Steel Pipe Industry: Flowing Success

Introduction

***Pipes, critical
component of energy
infrastructure...***

Steel pipes, long and hollow tubes, are considered arteries of any country's energy infrastructure, as well as the safest and cheapest way to transport energy products. Pipelines are the most common method to transport large quantities of oil and natural gas over land. They can also be utilized as a protection for electrical wires, in addition to agriculture industries as a mean of irrigation and drainage activities. As opposed to railroad or other land-based transportation, pipelines have lower average cost per unit and higher capacity. Investments in pipelines are highly correlated to investment in general oil and gas infrastructure, and therefore represent a key play on overall growth in the sector.

***...received a major boost
from rising O&G spend***

Rising crude prices and depleting oil reserves have led to increased exploration and production efforts. The consequent investments in Oil and Gas (O&G) exploration and rising construction spending globally have given the steel tubing and pipes industry a major boost. The overall demand for oil and other energy sources, as well as inequitable distribution of supply sources, is a key driver for growth in demand for steel pipes to transport oil and gas from global sources of supply to global sources of demand. The favourable relative economic qualities of pipelines ensure that they will always be an integral link in the world's oil and gas supply network.

This report seeks to analyze the market dynamics and outlook for steel pipes in the region, and its impact on Saudi Arabia based Arabian Pipes Company (APC), the Middle East's largest producer and potentially the biggest beneficiary from the anticipated growth in demand.

Company Overview

Background

APC is the largest producer of HFW steel pipes in ME

APC is the largest manufacturer of medium range High Frequency Welded (HFW) steel pipes in the Middle East (ME) with a total production capacity of 160,000 tons per annum (tpa) in 2007 and expected to reach 780,000 tpa by Q4 2011. APC was established in 1991 and commenced production in 1995, soon becoming a major supplier of welded pipes in Saudi Arabia and the ME. Since oil, gas, and petrochemical sectors are considered the primary market for the company's products, its target market includes oil rich countries such as UAE, Kuwait, Qatar, Nigeria, Iran, North African countries and other international markets.

With two strategically located plants in KSA

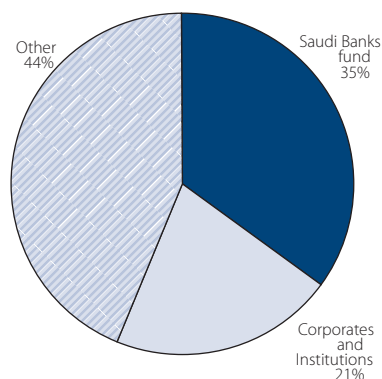
Currently, APC has two production facilities; one in Riyadh's Industrial City with a total production capacity of 160,000 tpa of small diameter pipes ranging from 6 - 20 inches and expected to reach 400,000 tpa in 2011. Riyadh's plant is located on a total area of 228,000 sq. meters. The second plant, currently under construction, is located in Jubail Industrial City with total production capacity of 380,000 tpa, split between 300,000 tpa of large diameter pipes (16-48 inch) and 80,000 tpa of spiral pipes. Large diameters capacity is expected to come on board in Q4 2008, while spiral pipes capacity expansion is expected to take place in Q4 09. The Jubail plant's location on the Arabian Gulf makes it an attractive export oriented base for targeting other GCC markets.

APC capitalizes on an extensive network across the ME for distribution of the company's products. APC's main distributors are located in the GCC (Kuwait, UAE, and Qatar), Egypt, Syria, and Jordan.

Shareholder Structure

APC total paid in capital is SAR 315 mn distributed over 31.5 mn shares with par value per share of SAR 10. Corporate and financial institutions are the largest shareholder in Arabian Pipes with a combined holding stake of 56%.

Arabian Pipes Shareholders

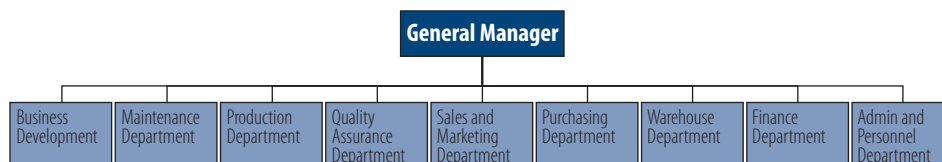


Source: Zawya

Organization Structure

APC currently employs 450 employees, 90% of whom are based in the company's manufacturing facilities and the remaining employees in the company's head office in Riyadh.

Arabian Pipes Organization Structure



Group Structure

APC holds a 5.6 % stake in Saudi-based, Taqa

Arabian Pipes holds a 5.6 % stake in Industrialization and Energy Service Company (Taqa), a Saudi-based company established in 2003 to provide services for the O&G industry including exploration and drilling of oil and gas, conducting geophysical surveys, manufacturing of pipes, and ensuring water supply. In FY 06, Taqa recorded a net profit of SAR 129 mn versus SAR 67 mn in FY 05, 92% y-o-y increase. In December 2007, Taqa named Samba Financial Group as the lead manager for an initial public offering expected to take place by the end of 2008. APC books profit from Taqa under the cost method.

And a 50 % stake in Arabian Yadong Coating Company

Additionally, APC holds a 50 % stake in Arabian Yadong Coating Company Ltd. Saudi based Arabian Yadong Coating Company, a joint venture between Arabian Pipes and Yadong Coating International, was established in 2002 to cater to the needs of the local as well as the regional market. The coating mill is capable of coating steel pipes size from six inches up to 48 inches in diameter, and different length. During 2007, Yadong Coating recorded a net profit of SAR 4.3 mn, where SAR 2.1 mn were booked in APC books under the equity method.

Steel Pipes in APC's Portfolio

Generally, there are several different types of steel pipes, all with different chemical compositions. Steel pipes can be designed and fabricated to any length and strength for specific applications in automotive, petrochemicals, power, fertilizer, refinery, construction and manufacturing industries.

APC production line manufactures pipes for the following applications:

- Line pipes application
- Structural application
- General purpose application, and
- Casing applications primarily related to all oil, gas and water well casings.

Line Steel Pipes

***O&G transportation
accounts for 60%
of demand for
line steel pipes***

Line steel pipes are long distance pipelines utilized for transportation of flammable liquids and gases. As seamless line pipes do not have any welding or joints they are used for construction of long distance pipelines for high pressure flammable liquids and gases, nuclear station pipelines, heating system pipelines, and also general-purpose pipelines. Toughness requirements for line steel tubes are obviously more stringent than tensile property requirements. The strategic importance of oil and gas transportation, accounting for 60% of demand for these pipes, has led to a strong focus on enhancing the domestic production capacity of line steel pipes.

Standard Steel Pipes

Standard Steel Pipes, are circular welded non-alloy steel pipes with an average diameter of 16 inches. These pipes are utilized for low-pressure transportation of water, steam, natural gas, and other liquids and gases in plumbing and heating systems, air conditioning units, automatic sprinkler systems, and other related uses. Standard steel pipes and tubes may also be used for light load-bearing applications, such as for fence tubing; as structural pipe tubing used for framing to support members, and for reconstruction or load-bearing purposes in the construction, shipbuilding, trucking, farm equipment, and related industries.

Structural Steel Pipes

Structural steel pipes come in various shapes with circular, square and rectangular cross-sections and are used for drainage pipe, small bridges or numerous other construction or industrial applications. The application ranges from culverts, sub-drains, sewers, service tunnels, etc., for general construction and engineering purposes. These pipes are generally used where plant-fabricated pipes cannot be installed, are not big enough or do not have the strength to support the loads imposed on them.

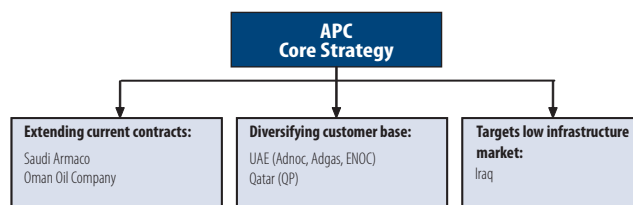
Plumbing Tubes

Plumbing refers to a system of pipes and fixtures installed in a building for the supply & distribution of potable water, and for the removal of waterborne wastes. Plumbing differentiates itself from water and sewage systems, in a way that a plumbing system serves to a single building, while water and sewage systems serve a group of buildings or a city.

Strategy

We believe that Arabian Pipes' core growth strategy rests on the followings:

- Extending current long-term supply contracts to key clients
- Diversifying customer base to seek more long-term contracts
- Targeting markets with low energy infrastructure to build its regional presence



Source: SHUAA Capital

Extending Current Contracts

Contracts with Saudi Aramco and Oman Oil represent the core revenue stream of APC

Saudi-based APC enjoys an inherent location advantage given the current production and proven oil reserves in Saudi Arabia (66 years). According to British Petroleum statistical annual book, proven oil reserves ratio in the ME is close to 79.5 years. This proven reserve is expected to boost the exploration and drilling activities in the near future, which, in turn, should boost the demand for pipes to transmit the oil reserves to various target destinations. Taking into account the industry potential and capacity expansions underway at APC, we expect the company to extend its current contract with Saudi Aramco and Oman Oil Company. APC has signed five years supply contract with Saudi Aramco running to 2011 and four years supply contract with Oman Oil Company running to 2010. These two contracts represent the core revenue stream of the company at this stage.

Diversifying Customer Base, underpinned by track record

Qatar is considered the world's largest producer of Liquefied Natural Gas (LNG). The state owned company, Qatari Gas, targets to be the world's largest producer of LNG by 2010. Despite Qatar's plan to supply the entire GCC with gas network, the efforts are limited to the undersea Dolphin pipeline, majority owned by the UAE, connecting Qatar to Abu Dhabi. The lack of pipelines offers a solid opportunity for APC to transport the abundant energy reserves from Qatar to the rest of the GCC. Other opportunities in the region abound, and penetration into any of the major National Oil Companies (NOC) or National Gas Companies (NGC) as an approved supplier carries significant upside potential for sales, especially in light of planned production boost.

Qatar's plan to supply the entire GCC with gas network offers solid opportunity for APC...

We believe that APC's ability to secure a long-term supply contract with Saudi based Aramco, the world leader in crude oil production, and Oman Oil Company, underpins its technical strength and know-how. APC enjoys approval from leading exploratory entities to supply them with its product. Among the top of the list are, Aramco, Shell Global Solution, Abu Dhabi National Oil Company (ADNOC), Canadian Nexen Petroleum, and Egyptian General Petroleum Corporation (EGPC). Additionally, APC has attained large contracts to export steel pipes from major global companies illustrating APC's ability in utilizing the latest technology and high technical specification in this field.

Regional Presence Targets Low Energy Infrastructure Markets

We expect APC to eye markets with limited energy infrastructure while firming its regional expansion plans. The Iraqi market is considered one of the most promising markets in the region given its abundant energy reserves ratio and limited energy infrastructure. Iraq's total oil production at 1,999,000 barrels per day (b/d) represents approximately 8% of the ME total production. More importantly, the proven reserves in Iraq are unidentified due to the current political situation in the country, and hence significant future prospecting and exploration activity is virtually guaranteed in case of stability.

SWOT Analysis

Strengths	Weakness
- Strategic alliance with ARAMCO and Oman Oil Company. - APC's track record and technical know-how create high entry barriers, as well as opportunity to secure further contracts with other NOCs and NOGs.	Bargaining power of suppliers. HADEED provides APC with 60% of its required steel volume while the other 40% are imported.
Opportunities	Threats
- Presence in the hub of oil and gas exploration activities - Rising oil and gas exports from Saudi Arabia and the GCC to the world offers an optimal business environment for APC	- Fall in crude oil prices, will slow demand for pipes. - Sharp rise in flat steel prices will negatively impact pipes players margins

Source: SHUAA Capital

Key Risks

Drop in Crude Oil Prices

High oil prices likely to keep demand for steel pipes robust

Empirical evidence depicts strong positive correlation between oil prices and exploration expenditures. The current high level of oil price per barrel has boosted the overall exploration expenditures, which in turn has a direct positive impact on demand for pipes. We believe oil prices will continue to hover near USD 100 per barrel based on current demand level underpinned by solid demand from China and India, which is expected to offset the weaknesses of the US market. The current tight supply along with geopolitical risks in various supply countries, including the ME, is putting upward pressure on the oil prices, and hence is likely to keep demand for steel pipes robust for the foreseeable future.

Unprecedented Increase In Steel Prices

Steel output to grow by 10 mtpa in coming three years

Given the fact that steel represents approximately 65%-70% of steel pipe cash cost, sharp increase in steel prices will negatively impact the overall operating margins and profitability for pipes players. However, we believe capacity expansion by global players; most likely will put pressure on realizations. Mega steel projects currently undertaken by GCC countries are expected to boost the steel output by 10 million tons per annum (mtpa) during the coming three years. Also, most steel pipes supplied by APC are adjusted for factor cost inflation, and the company has to-date been able to pass on most steel price appreciation to its customers.

Concentrated Customer Base

APC's revenue stream is generated through contract undertaken from its two main customers, Saudi Aramco and Oman Oil Company. We believe that this concentration in the customer base is a key risk for APC, although it also represents a very high quality revenue anchor.

Global Industry Overview

ME to account for 56% of total CAPEX on pipelines between 2007-2011

The rise in energy demand has led to chronic need for energy infrastructure in the form of pipelines, terminals, and ports. Globally, there is around 2 mn km of oil and gas pipeline and expected to increase significantly with ambitious expansion plans already underway. UK energy research group, Douglas Westwood, expects a 28% increase in total capital expenditure (CAPEX) on pipelines between 2007 and 2011. The table below depicts the global pipeline construction projects in 2007.

Global pipeline projects

Global Pipeline construction projects	Number of projects	Length (km)	Regional Share
North America	189	57,920	23.5%
Latin America	39	34,279	13.9%
Europe	62	33,822	13.7%
Africa	28	11,610	4.7%
Middle East	92	21,541	8.7%
Asia	90	81,736	33.2%
Australia	11	5,566	2.3%
Total	511	246,474	100.0%

Source: Simdex

Continuous welded pipes & tubes market to exceed 12.1 mt by 2009

Construction of oil and gas pipelines, in turn, fuels demand for new and replacement steel tubes. Hence, seamless pipes & tubes market in the O&G sector is expected to rise by more than 3.6 mt by 2009 as compared to the year 2006. Continuous welded pipes & tubes market is projected to account for more than 12.1 mt by the year 2009. In the other non-energy steel tube and pipe markets, such as mechanical, precision and structural, producers continue to benefit from ongoing strength in the steel construction markets; however, demand may be less buoyant than in the energy markets.

Demand Dynamics

Demand from planned pipelines capacity to exceed USD 60 bn

Soaring oil prices underpinning exploration activities in O&G sector make the demand projections for pipe industry rather evident. According to Pipelines and Gas Journal, the planned pipelines projects in different part of the world are estimated to exceed 161,000 Km as opposed to 80,500 Km during the period 2003 -2005. Assuming 250 tons per Km, translated to an expected global demand for steel pipes approximately of 40 mtpa and average selling price of USD 1,400 per ton, we estimate the demand from the planned pipelines capacity to exceed USD 60 bn. As world population grows, the global demand for liquid energy increases. Liquid energy includes oil, natural gas, and coal.

Demand Drivers

IEA forecasts growth of 57% in global energy demand by 2030

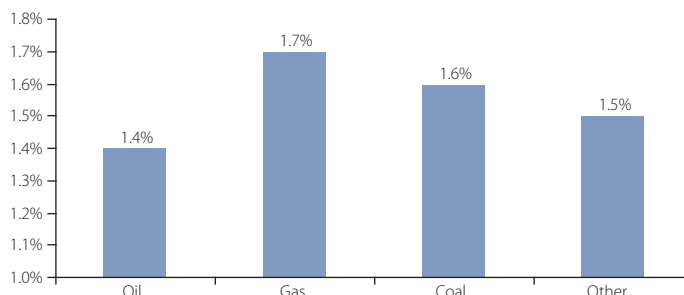
Rising Energy Demand

The developed world's insatiable thirst for energy and emergence of the industrial powerhouses of China and India, are the major catalysts of growth in demand for energy. Exxon-Mobil estimated that the global energy demand would increase by a CAGR of 1.6% annually to 2030, where oil, gas, and coal will represent approximately 80% of the global energy demand. International Energy Agency(IEA) forecasts growth of 57% in global energy demand by 2030 with demand for oil increasing from 36 mn b/d in 2006 to 95.8 mn b/d in 2012, and 117 mn b/d in 2030.

In addition to USD 22 trillion investment in energy-supply infrastructure

The increased demand has warranted increasing exploration and procurement activities creating, in turn, a demand for pipes. Further, demand and supply mismatch in countries means more energy trade and more pipes to transport it. IEA estimates that USD 22 trillion in investment will be needed in energy-supply infrastructure by 2030. The oil sector alone needs USD 5.4 trillion.

Average annual growth rate for Global energy demand 2000-2030



Source: Exxon-Mobil Statistical yearbook

In the face of falling oil reserves to production ratio

Oil reserves have increased by a CAGR of 2% during the period 1986-2006. However, the world's oil reserves to production ratio (R&P) reached 40 years as opposed to 41 years in 1996. Reserves to production ratio represent the outstanding reserves at the end of any year divided by the production in that year. The result is the period of time that those remaining reserves would last if production were to continue at that rate. The table below depicts the proven oil reserves during the period 1986-2006.

Proven Oil Reserves

Proven Oil Reserves in bn barrels	1986 Actual	1996 Actual	2005 Actual	2006 Actual	2006 *R/P (years)
North America	101.60	89.30	60.70	59.90	12.00
South and Centre America	64.60	90.80	103.20	103.50	41.20
Europe	76.80	82.60	145.20	144.40	22.50
Middle East	536.70	672.20	742.70	742.70	79.50
Africa	58.00	74.90	117.20	117.20	32.10
Asia Pacific	39.70	39.20	40.50	40.50	14.00
World	877.40	1,049.00	1,209.50	1,208.20	40.50

Source: British Petroleum Statistical yearbook

*Reserves to production ratio

Natural gas is the fastest growing segment in world primary energy

And Where Demand for Natural Gas Is Expected To Outperform Other Energy Sources

As the world's energy consumption continues to grow amidst rising prices, demand for alternative energy sources is bound to increase. According to IEA, natural gas is not only a cheaper and more environmentally friendly option but also the fastest growing segment in world primary energy. The strongest growth will come from emerging economies with projected average increase of 4.1% per annum. India alone is expected to record an annual growth of 5.1% between 2002-2025 taking its gas consumption to 2.6 tr cubic feet in 2025.

In 2005, the share of natural gas represented approximately 24% of the global energy pie as opposed to 20% in 1986. The rising share of natural gas in the global energy consumption pie will further drive the need for pipes as 69% of the global natural gas supply would be distributed through pipes.

69% of global natural gas supply distributed through pipes

Natural Gas Proven Reserves

Natural Gas proven reserves Trillion cubic meter	1986 Actual	1996 Actual	2005 Actual	2006 Actual	2006 * R/P (years)
North America	10.26	8.41	7.83	7.98	10.6
South and Centre America	4.24	6.06	6.85	6.88	47.6
Europe	47.22	63.55	64.30	64.13	59.8
Middle East	30.41	49.31	72.49	73.47	40.8
Africa	7.40	10.17	14.08	14.18	78.6
Asia pacific	8.14	10.40	14.66	14.82	39.3
World	107.67	147.90	180.21	181.46	63.3

Source: British Petroleum Statistical yearbook

*Reserves to production ratio

Natural gas enjoys extended proven reserves ratio

Natural gas' global proven reserves enjoy an extended life cycle of approximately 63 years as compared to 40 years for proven oil reserves, indicating that natural gas is poised to be the optimal alternative energy sources, at least, for the coming 50 years. ME stands approximately on 40% of the global proven reserves of natural gas, where Qatar holds the largest portion. However, the lack of pipelines limits access to this huge reserve presently, the additional demand for natural gas in the long-run will increase the need for steel pipes to distribute the abundant natural gas.

ME stands on around 40% of the global proven reserves of natural gas

Tightening refined product market

During 2006, world refined oil production stood at 79.34 mn b/d, barely ahead of global consumption of 78.25 mn b/d. This tightness in the global refined market is bound to enhance the demand for new oil fields.

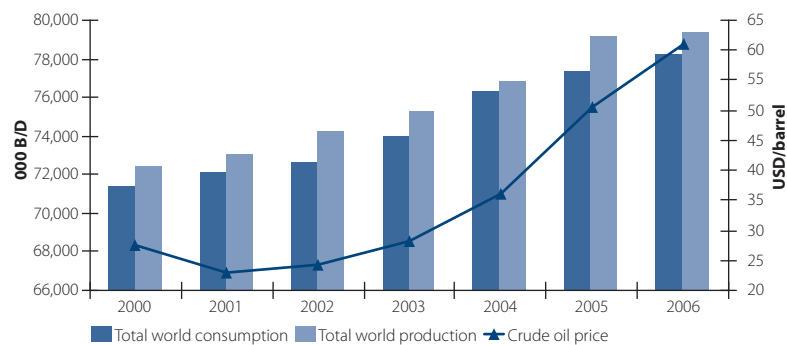
World production and consumption of refined products

Barrels (000) Per Day	2003 Actual	2004 Actual	2005 Actual	2006 Actual
Production	75,277	76,869	79,225	79,346
Consumption	73,945	76,351	77,352	78,254
Surplus/Deficit	1,331	514	1,873	1,124

Source: OPEC

The chart below depicts the impact of the supply tightness in the global refined oil market on global oil prices, which have increased from an average of USD 28.10/barrel in 2003 to an average of USD 75.54/barrel in 2007, a CAGR of 28%. Currently oil prices are trading above USD 130/barrel. Given the high degree of correlation between oil prices and rig count, the positive prospects for pipe industry are on firm footing in the current scenario of sustained high oil prices.

Global refined oil market



Source: OPEC

**28% increase in CAPEX
on pipelines between
2007 and 2011**

Upswing in Capex on Pipelines

All the above factors clearly indicate an increased need for exploration of new oil fields implying higher capital expenditures for major oil companies worldwide, which, in turn, underpins the demand for pipes. UK energy research group, Douglas Westwood, expects a 28% increase in total capital expenditure (Capex) on pipelines between 2007 and 2011. It also says that the Middle East (ME) Asia Pacific will drive this growth on the back of high investment levels in both production and processing of oil and gas, estimating 56% of the total Capex to take place from the ME and Asia Pacific region.

**Underpinned by need
to replace old pipes and
privatization of oil sector**

While increased drilling rates, new pipeline projects, and strong energy prices imply a guaranteed demand and a bullish outlook on pipes, the pressure to realize cost efficiencies among O&G companies is also contributing to increased demand by driving these manufacturers to upgrade their infrastructure. Further, the demand for pipes is expected to come not only from the large demand anticipated for new pipes but also from the large number of pipelines that had been laid in the 1960's and 1970's and are long due for replacement. Privatization of oil exploration sector too, is likely to boost demand.

The table below depicts capital and exploratory expenditures for major global oil companies during the period 2002-2006, including the transportation expenditures as pipes and tubes represent the lion's share. During the period 2002-2006, transportation expenditures represented approximately 2%-3% of the total expenditures for global oil majors and we have assumed the same ratio for the GCC major oil companies.

Capital and exploratory expenditures for major global oil companies

Capital and exploratory expenditures For major oil companies (USD Millions)	2002 Actual	2003 Actual	2004 Actual	2005 Actual	2006 Actual
British Petroleum	13,321	13,986	14,408	14,149	17,231
Exxon Mobil	13,955	15,525	14,885	17,699	19,855
Total	9,191	8,740	10,812	13,928	14,886
Royal Dutch/Shell	22,362	12,252	13,209	15,916	23,096
Chevron	9,255	7,363	8,315	11,063	16,611
Total exploratory expenditures	68,084	57,866	61,629	72,755	91,679
Transportation expenditures	1,632	1,100	1,329	2,150	3,175
Transportation expenditures/Exploratory expenditures	2.4%	1.9%	2.2%	3.0%	3.5%

Source: OPEC statistical book 2006

Steel tubes and pipes industry estimated at USD 70 bn by end-2007

Supply

The global steel pipes market was relatively balanced during the past couple of years with supply meeting demand near the range of 80,000 mtpa. According to the International Trade Centre, the steel tubes and pipes industry size is stated to be near the range of USD 70 bn by the end of 2007 as opposed to USD 25 bn by the end of 2001, recording a CAGR of 23%. The table below depicts the major exporting and importing countries for tubes and pipes.

Tubes and Pipes major exporting countries

Exporters USD (000)	2001 Actual	2002 Actual	2003 Actual	2004 Actual	2005 Actual
Germany	3,292,406	3,372,469	3,738,619	5,191,721	6,621,593
Italy	2,524,392	2,708,863	3,169,414	4,685,382	5,531,479
Japan	2,961,406	2,918,276	2,966,837	3,695,542	5,052,480
China	887,535	974,320	1,344,452	2,327,560	4,087,668
United States of America	1,967,688	1,903,972	1,962,964	2,590,734	3,374,249
Other	13,600,177	14,350,354	16,190,980	22,813,814	28,874,479
Total	25,233,604	26,228,254	29,373,266	41,304,753	53,541,948

Source: International Trade Center

Tubes and Pipes major Importing Countries

Importers (USD 000)	2001 Actual	2002 Actual	2003 Actual	2004 Actual	2005 Actual
United States of America	3,660,120	3,293,066	3,197,728	5,093,657	7,404,144
Germany	1,735,399	1,626,099	1,963,549	2,828,244	2,865,779
China	799,490	1,206,907	1,173,682	1,874,848	2,674,355
Canada	1,238,738	1,128,670	1,345,611	1,758,925	2,526,859
France	1,052,996	1,157,332	1,360,431	1,798,924	1,973,237
United Kingdom of Great Britain & Northern Ireland	1,099,492	940,871	1,103,723	1,439,190	1,719,378
Other	15,647,369	17,816,180	19,228,542	26,510,965	34,378,146
Total	25,233,604	26,228,254	29,373,266	41,304,753	53,541,948

Source: International Trade Center

However, supply is likely to exceed total demand by 2010 on the back of excessive production from China.

The China Factor

Supply is likely to exceed total demand by 2010 due to excessive production from China

In order to illustrate more clearly the dynamism of the Chinese market, it is helpful to make a comparison of the percentage growth rates in steel pipes production. While steel pipe production worldwide increased overall between 2002 and 2006 by total of 45%, according to the Steel Tube Manufacturers Association, China registered an increase of 142%. Excluding China from the equation, worldwide steel pipe production has risen by just 19% in the last five years. Further, China Iron and Steel Industry Development Policy has outlined plans to create by 2010, two 30 mn ton annual capacity producers and several "internationally competitive" companies at the 10 mn ton level.

Global Players

Given that steel is the main raw material for steel pipes, major players dominating the global steel pipes & tubes market are the global steel players. These include Arcelor-Mittal, Thyssenkrupp, Voestalpine, Evraz Group, and Northwest pipe.

Regional Market Overview

**ME will need to invest
USD 18 bn in next five
years in new pipelines**

The regional pipe industry has been riding a steep demand curve backed by huge planned outlays on O&G infrastructure by most regional governments. According to the IEA, the ME alone will need to invest around USD 18 bn in the next five years in new pipelines and associated infrastructure ensuring high volume to weight ratio.

Supply

**APC accounts for 40%
of the regional current
announced capacity**

APC is the largest producer of steel pipes in the GCC and North Africa, producing approximately 40% of the total current announced capacity in the region. Total steel pipes capacities in the GCC and North Africa, stands approximately at 1.14 mtpa as of 2008. Saudi Arabia produces approximately 60% of the total regional capacity. The table below shows the expected pipes capacity based on the company's announcements by 2011.

Major steel producers in the region

Company	Country	Year of Establishment	Capacity in 2011 (Tons)
Arabian Pipes	Saudi Arabia	1995	780,000
Gulf International Pipe Industry	Oman	2007	250,000
Saudi Steel Pipes-Al Anabeeb	Saudi Arabia	1980	160,000
Kuwait Pipes-KPIOS	Kuwait	1966	130,000
Al Nasr Steel Pipes and Fittings	Egypt	1962	100,000
Jordan Pipes Manufacturing	Jordan	1968	40,000
Total			1,460,000

Source: Zawya & Company disclosures

Demand

Middle East countries account for about 34 % of the total global demand for pipes as demand is directly related to investment and growth in the O&G sector, planned projects and government initiatives. With oil prices near all time high in the face of robust worldwide and regional demand, the regional governments have drawn ambitious plans to expand and upgrade their facilities. Also, the global demand supply imbalance is very much in favour of ME pipe manufacturers.

Increased regional requirements with new dispersed settlements

**Creation of new
growth nucleus
adding to demand**

Flushed with oil money and trying hard to accomplish balanced and sustainable growth, diversified away from oil, GCC nations have been creating dispersed growth centres or economic cities to initiate fresh growth cycles and link them to generate higher momentum. Consequent, channelling of petrodollars to develop new industries such as manufacturing and real estate, by boosting demand for power and water, is creating new demand for pipes.

According to the World Energy Council, KSA, Kuwait, the UAE and three other Gulf countries need to invest up to USD 100 bn over the next decade to meet the growing energy demand. Investment in electric power projects in the GCC is expected to reach USD 45.6 bn over the next ten years, with UAE and Saudi accounting for the majority of the projects.

Pipeline Network

In 2006, the total pipeline network in the GCC was about 27,273 km, with crude oil network representing 58% and gas representing 32%. Saudi Arabia holds the largest crude oil network (7,187Km), while Iran has the largest gas network (9,619Km). The current pipe network is valued at approximately USD 9.54 bn, representing around 17 % of the global industry size (assuming pipeline demand of 250 Tons/Km and average selling price of USD 1,400/ton). The table below depicts the pipelines network in the GCC.

**GCC current pipe network
around 17 % of the
global industry size...**

Pipeline network in the GCC

Current pipeline network in the GCC (Km)	Crude Oil	Gas	Total
Saudi Arabia	7,187	NA	7,187
Iraq	7,219	171	7,390
Kuwait	262	196	458
Qatar	177	491	1,262
UAE	597	760	1,357
Iran		9,619	9,619
Total	16,036	11,236	27,273

Source: OPEC annual statistical bulletin

Additional 21,000 Km expected to come in place

**...and expected to add
more than 21,000 km
during next five years**

The unprecedented record highs in oil prices are expected to underpin exploration activities searching for further energy reserves and, consequently, energy infrastructure including pipelines to transmit oil and liquefied gas to target destinations. The GCC is expected to add more than 21,000 km during the coming five years to its current pipe network, approximately 14 % of the global planned pipeline network of 161,000 km. The additional pipeline networks in the GCC is expected to deliver a planned demand of steel pipes around 5.3 million tons during the coming five years which is equivalent to USD 7.2 billion.

Expected Demand for Steel Pipes in the GCC

Expected demand for pipes in the ME	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate	2012 Estimate	Total
Pipeline (Km /year)	3,978	4,300	4,408	4,451	4,440	21,575
Pipeline demand/KM (Tons)	250	250	250	250	250	250
Expected demand for pipes (Tons)	994,375	1,075,000	1,101,875	1,112,625	1,134,878	5,345,650

Source: SHUAA estimates

Capital expenditures for major exploration companies in the GCC

**Supply to marginally
surpass demand in the
GCC... assuming capacity
additions remain on track**

Aramco is the only company in the GCC that announced its capital expenditure figure of USD 90 bn, representing approximately 5%- 5.5% of Saudi Arabia's GDP, to be expensed over the coming five years.

**Prices to stay firm as major
projects scour to secure long
term and stable supply**

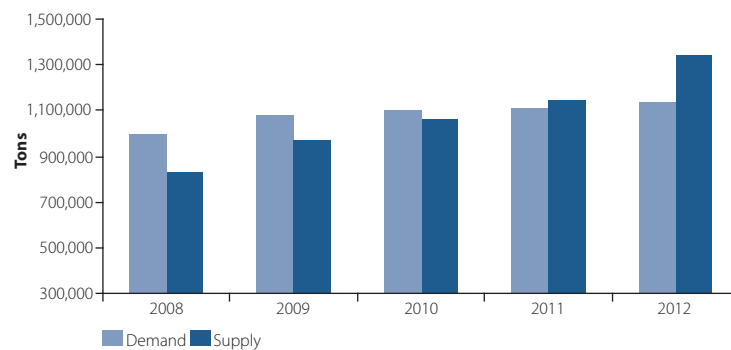
Given the announced pipes capacity in the region that is expected to reach 1.3 mtpa in 2012, and our outlook on the expected demand figure for steel pipes, supply could marginally surpass demand for steel pipes by year 2011/2012. However, we do not expect much softness in prices as major projects scour to secure long term and stable supply. In addition, the supply figures assume production capacity additions are achieved on time, at a time where major project completion delays have become the norm due to contractor capacity shortages. The table and chart below show our outlook for the expected demand and supply balance.

Steel Pipes Supply and Demand balance

Tons	2008	2009	2010	2011	2012
*Supply	828,750	972,400	1,060,800	1,140,700	1,343,000
Demand	994,375	1,075,000	1,101,875	1,112,625	1,134,878
Surplus/Deficit	-165,625	-102,600	-41,075	28,075	208,123

Source: SHUAA Capital

*Average supply

Outlook on Steel pipes supply and demand balance

Source: SHUAA Capital

Major exploration companies in the GCC

The following section depicts an overview of major exploration companies in the GCC which represent APC's core customers at this stage. In 2006, APC signed a five-year supply contract with Saudi Aramco, its largest customer, and a four-year supply contract with Oman Oil Company (OOC), the second largest customer for APC. Given the abundant natural gas reserves in Qatar that are expected to press the need for enhanced gas infrastructure, this section also covers Qatar Petroleum as one of APC's major prospects at this time.

ARAMCO

Saudi Aramco, the world's largest oil producing company....

Saudi Aramco, the world's largest oil producing company, commenced its operation in 1933, shortly after Saudi Arabia was unified and the Government granted a concession to Standard Oil of California. Later, several other major oil companies joined standard Oil of California, the parent company of Chevron, and the venture came to be known as Aramco - the Arabian American Oil Company.

The company, world leader in crude oil production, owns and operates an extensive network of refining and distribution channels for gas processing and transportation that fuels Saudi Arabia's industrial sector. Aramco business model is segmented along the following operational areas:

- Oil exploration - focused on finding oil and gas fields deep underground
- Oil operations – covers the pipe network totaling more than 1.5 mn sq km
- Refining, supply, and distribution

..has signed a five years agreement with APC

Aramco is a strategic and the most important customer for APC with the latter having signed a five-year agreement, ending 2011, to supply Aramco with required steel pipes.

Aramco's Pipe Network

Saudi Aramco operates more than 145,000 Km of petroleum pipelines throughout KSA

Saudi Aramco operates more than 145,000 Km of petroleum pipelines throughout Saudi Arabia, including two major petroleum pipelines, West Crude Oil Pipeline (Petroline), and Abqaiq-Yanbu natural gas liquids (NGL) pipeline.

- Petroline

Petroline has total length of 1198 Km producing 5 mn bbl/d. East Petroline has been operated by Aramco since 1984 and is mainly used to transport Arabian Light and Super Light from Abqaiq refineries in the Eastern Province to Red Sea terminals (Yanbu) for export to European markets.

- Abqaiq-Yanbu natural gas liquids pipeline

Running parallel to Petroline is the 290,000 bbl/d Abqaiq-Yanbu natural gas liquids (NGL) pipeline, which serves Yanbu's petrochemical plants. A USD 500 mn contract to install three NGL pipeline loop line on the Shedgum-Yanbu section of the trunk line, when

And has announced construction of more than 830 miles of new pipelines

completed in 2008, will increase capacity to 555,000 bbl/d (SHY-1 expansion). Additionally, there are six smaller pipelines that make up the Uthmaniya-Abqaiq pipeline complex. To support increased export capacity, Aramco has announced construction of more than a total of 830 miles of new oil, natural gas and NGL pipelines of varying sizes and lengths by 2009. The biggest development will extend to the 1.2 mn bbl/d Khurais redevelopment, which will require a 400 – 500 mile network in the Eastern Province. The Manifa development has a planned installation of 221 miles of pipeline (gas and crude/condensate).

Aramco's major pipes projects executed by APC

Project Title	Service type	Length (Km)
Dahran - Riyadh Product Pipeline	Products- On-shore	463
Shayba Flow lines Requirements	Crude- On-shore	86
Riyadh- Qassim Product Pipeline	Products- On-shore	198
Northern Area Off-shore Lines	Crude- Off-shore	24
MPPD Requirements- 1997	Crude- On-shore	91
Shayba Flow lines Requirements	Crude- On-shore	23
Khuff Gas Projects	Sour Gas - On-shore	15
Southern Area Flow lines- MPPD	Crude- On-shore	61
Southern Area Flow lines- MPPD	Crude- On-shore	243
MPPD Requirements- Injection	On-shore	9
MPPD Requirements- 1999	Crude- On-shore	565
Northern Area Pipeline Projects	Crude- On-shore	64
Southern Area Flow lines- MPPD	Crude- On-shore	171
Haradh- Abqaiq Condensate Line	Condensate- On-shore	100
Southern Area Flow lines- MPPD	Crude- On-shore	152
Abqaiq – Main Oil Flow Lines	Crude -Onshore	6,500

Source: Arabian Pipes Company

**Aramco to invest
USD 90 bn to raise
production capacity**

Aramco's announced CAPEX bill of USD 90 bn

On February 2008, Saudi Aramco announced its intention to invest approximately USD 90 bn in upstream and down stream projects in Saudi Arabia and around the world. According to the company, these projects would add about three million bbl/d to be used in raising the country's production capacity and offsetting the natural decline in some oil fields.

Oman Oil Company

**OOC as a government
owned commercial
company is an ideal
partner for APC**

Oman Oil Company (OOC), established in 1992 and fully owned by the Government of the Sultanate of Oman, is considered the government's investment arm for petroleum and petrochemical projects eyeing investment opportunities both inside and outside of Oman. Accordingly, OOC develops partnerships with private sector companies to pursue the development of gas-based industrial projects and other downstream energy and energy related projects. OOC position as a government owned commercial company makes it an ideal partner for companies looking to invest in the energy sector in Oman, where oil and petroleum sector is considered the main contributor to GDP. OOC has pursued commercial ventures beyond the Omani borders to diversify revenue sources for the Government of Oman. Currently, the company is involved in upstream energy projects in Kazakhstan and Caspian Sea. In 2006, APC has signed a four-year supply contract to supply OOC with their pipes requirements.

Qatar Petroleum Company

**QP produces more
than half of Qatar's
total oil output**

Qatar Petroleum Company (QP) is an important industry player as it accounts for the largest portion of Qatar's national income. In the crude oil business, QP produces more than half of Qatar's total oil output, with the rest generated by international companies

operating under production-sharing agreements covering oil fields. The current total oil output of 850,000 bbl/d is expected to reach one million bbl/d by the end of 2009. Furthermore, QP also stands to benefit from Qatar's status as the world's largest liquefied natural gas producer and exporter with total production capacity of 30 mtpa. The expansions in natural gas projects are expected to take the LNG capacity in Qatar to 77 mtpa by 2010 – imparting a huge demand push to steel pipes in the GCC.

The tables below depict the major oil pipelines expected to take place in the GCC during the coming period.

Oil pipelines in the GCC

Major Oil pipelines projects in the GCC	Country	Cost (USD mn)	Start date	End date
KOC - Flow Lines Upgrade - Eastern & Southern Fields	Kuwait	82	30-Sep-05	30-Sep-09
KOC - Flow Lines Upgrade - Northern Fields 1	Kuwait	100	29-Aug-05	30-Sep-09
KOC - Flow Lines Upgrade - Western Fields	Kuwait	55	30-Sep-05	30-Sep-09
New Doha International Airport (NDIA) Project - Phase 1 - Fuel Systems	Qatar	100	1-Nov-06	1-Nov-08
Aramco - Khurais Full Field Development - Pipelines Package 2	Saudi Arabia	500	15-May-06	31-Dec-08
Aramco - Khurais Full Field Development - Pipelines Package 3	Saudi Arabia	500	15-Jun-06	31-Oct-09
Renovation & Expansions of Al-Khafji South Jetty; Dredging & Widening of Access Channel	Saudi Arabia	30	28-Jul-05	30-Dec-07
Aramco - Khurais Full Field Development - Pipelines Package 1	Saudi Arabia	500	15-May-06	1-Jul-08
Inter Refineries Pipeline (IRP) – Pipelines	United Arab Emirates	400	26-Mar-05	30-Dec-07
Inter Refineries Pipeline (IRP) – Terminal	United Arab Emirates	400	26-Mar-05	30-Dec-07
KOC - Gathering Center 16 (GC 16) - Gas Compression	Kuwait	80	7-Feb-08	30-Dec-10
KOC - New Crude Storage Tanks	Kuwait	1,000	1-May-08	30-Jun-10
Aramco - Manifa Field Development - Onshore - Central Processing - Package 1 (Water Injection)	Saudi Arabia	1,500	1-Mar-08	30-Dec-11
Aramco - Manifa Field Development - Onshore - Downstream Pipelines	Saudi Arabia	1,000	1-Mar-08	30-Dec-11
Aramco – Saudi Bahrain (New Arabia) Oil Pipeline	Saudi Arabia	300	1-Nov-08	1-Apr-10
Total cost for oil pipelines projects in the GCC		6,547		

Source: SHUAA Capital

Major Gas pipelines projects in the GCC	Country	Cost (USD mn)	Start date	End date
PDO - Saih Nihayda Sur Gas Pipeline	Oman	400	30-Apr-07	30-Dec-08
Nakilat - Q-Flex LNG Carrying Vessels	Qatar	220	5-Apr-07	1-Jan-10
Nakilat - Q-Max LNG Carrying Vessels	Qatar	280	5-Apr-07	1-Jan-10
Nakilat OSG – Q-Max LNG Carrying Vessels	Qatar	80	5-Apr-07	1-Jan-10
Nakilat Pronav - Q-Max LNG Carrying Vessels	Qatar	80	5-Apr-07	1-Jan-10
RLC - Storage Tanks	Qatar	200	1-Apr-06	15-Feb-09
Aramco - Hawiyah NGL Recovery Scheme - Pipeline Package 1	Saudi Arabia	200	31-May-05	30-Sep-08
Aramco - Hawiyah NGL Recovery Scheme - Pipeline Package 2	Saudi Arabia	300	31-Oct-05	30-Sep-08
Aramco - Juaymah to Jubail Ethane Pipeline	Saudi Arabia	50	19-Dec-05	30-Oct-07
Aramco - Khurais Full Field Development - Downstream Gas Line	Saudi Arabia	100	30-Nov-06	30-Dec-08
Aramco - Khursaniyah Pipeline Project - Upstream & Downstream Pipelines	Saudi Arabia	150	12-Nov-05	31-Dec-08
Gasco - Habshan Gas Expansion Phase 1 – Pipelines	United Arab Emirates	52	15-Aug-06	31-Jul-08
KOC - Gas Booster Station 160 (BS 160)	Kuwait	1,000	1-Feb-08	30-Dec-10
OGC - Nimr Salalah Gas Pipeline	Oman	200	26-Aug-08	31-Aug-11
QP - Ras Laffan Pipeline Network	Qatar	60	30-Jun-08	30-Jun-09
QP - Ras Laffan to Mesaieed Gas Pipeline	Qatar	150	30-Jun-08	31-Dec-10
Aramco - Manifa Field Development - Onshore - Central Processing - Package 4 (Gas Processing)	Saudi Arabia	3,000	1-Aug-08	30-Jul-11
Shedgum Juaymah Gas Pipeline	Saudi Arabia	200	30-Oct-07	30-Nov-08
Abu Dhabi Gas Distribution Network (Gas Grid)	United Arab Emirates	300	1-Aug-08	30-Sep-11
DEL – Taweelah Qidfa Gas Pipeline	United Arab Emirates	300	30-Aug-08	30-Jun-09
Total cost for gas pipelines projects in the GCC		7,322		

Source: SHUAA Capital

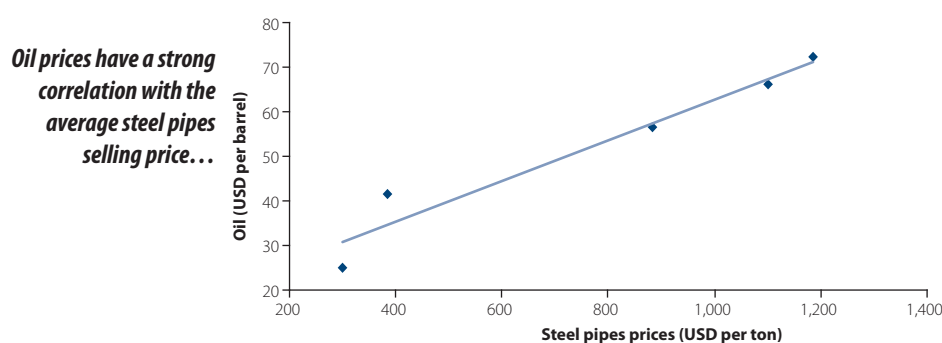
Prices and Feedstock

Pipes prices are mainly driven by raw material costs, quality requirements, geographical and geopolitical location, and delivery capability.

Pipes prices

The increase in oil prices has a strong correlation with the average steel pipes selling price per ton ($R^2 = 0.92$). The chart below depicts our utilized regression analysis model between the average oil price per barrel and the average selling price of steel pipes as per APC statistics for the past five years.

Relation between oil price and average steel pipes prices



Source: SHUAA Capital

Selling price per ton to increase by CAGR of 6% throughout our forecast horizon

Given the said strong relation, we utilized a regression analysis model to estimate the expected average steel pipes selling price per ton during the period 2008-2012. During 2007, APC average selling price was near the range of USD 1,185 per ton, and we expect the average selling price per ton to increase by a CAGR of 6% throughout our forecast horizon (2008-2012).

Outlook on average steel pipes prices

USD	2006 Actual	2007 Actual	2008 Estimate	2009 Estimate	2010 Estimate
Oil price per barrel	66.11	75.16	100.00	95.00	90.00
Steel pipe prices per ton	1,100	1,185	1,450	1,590	1,548
Steel Pipes Price Change	25%	8%	22%	10%	-3%

Source: OPEC Statistical book & SHUAA Capital estimates

Raw Materials

Steel represents 65%-70% of the total cost of steel pipe

The primary raw material in production of pipes is steel, representing approximately 65%-70% of the total cost. Steel is primarily made of iron ore; other metals that may be present in the alloy include aluminium, manganese, titanium, tungsten, vanadium, and zirconium. During the past five years, pipes and tubes industry utilized approximately 10% of global steel exports. In 2005, pipes and tubes utilized approximately 31 million metric tons (mmt) of the world crude steel exports (331.9 mmt). In 2006, global steel production was 1,244 mmt, with China considered as the major steel producing country with a total production capacity of 422 mmt, representing 34% of the global production.

Major steel producing countries

Country (mn metric tons)	2005 Actual	2006 Actual
China	355.8	422.7
Japan	112.5	116.2
United States	94.9	98.6
Russia	66.1	70.8
South Korea	47.8	48.5
World	1,141.9	1,244.2

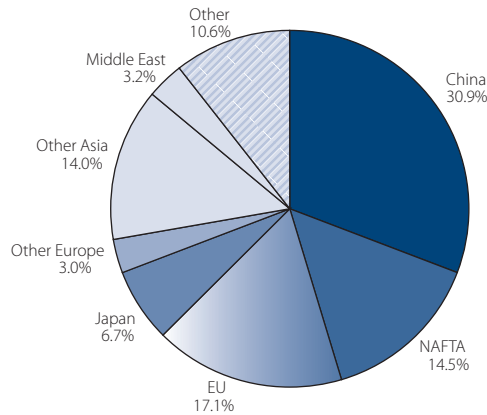
Source: International Iron and Steel Institute (IISI)

Consumption

**China represents
31% of global
consumption**

In 2006, global steel consumption was 1,113 mmt as opposed to 1,026 mmt in 2005. China is considered to be the highest steel consuming country, representing approximately 31% of global consumption level.

Steel consuming country by region in 2006



Source: International Iron and Steel Institute (IISI)

Exports and Imports

World steel exports in 2005 were 331.9 mmt, where Japan is the largest net exporting country with total net exports volume of 26.8 mmt, followed by Ukraine and Russia with 26.3 mmt. USA is the largest net importing country with an import volume of 20.8 mmt.

Major exporting and importing countries in 2006

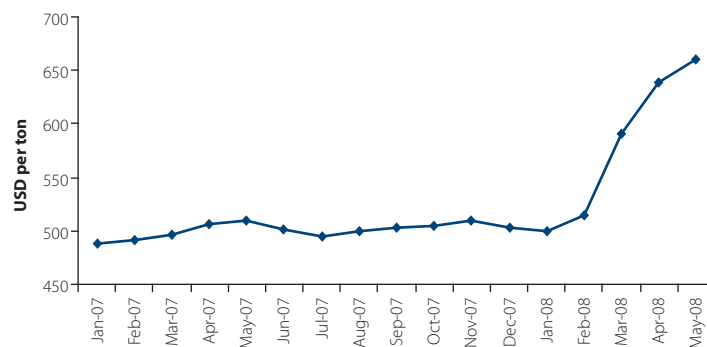
Country	Net Exports	Country	Net Imports
Japan	26.8	USA	20.8
Ukraine	26.3	Thailand	10.4
Russia	26.3	Iran	6.9
Brazil	11.8	UAE	5.4
EU	10.7	Spain	4.6

Source: International Iron and Steel Institute (IISI)

Coil Prices

Coils and billets are considered to be the initial link in the pipe production process. While, billet is considered the main raw material for the large dimension pipes, coil is the main raw material for the small and medium diameter pipes. Coil and billet steel prices have moved up from USD 487 per ton in January 2007, to USD 660 per ton in May 2008.

Coil price



Source: Bloomberg

Analysis and Forecasts

Production and Utilization rates

APC production capacity expected to reach 780,000 tpa by 2011...

APC has two production facilities; the first, located in Riyadh's second industrial city, has a current production capacity of 160,000 tpa producing small and medium diameter steel pipes ranges from 6-20 inch. Riyadh plant is expected to increase its capacity by additional 280,000 tpa as of Q4 2011, bringing the overall production capacity in Riyadh facility to 400,000 tpa. The second production facility is located in Jubail Industrial City with a total production capacity of 380,000 tpa split between large diameter steel pipes ranging from 16-48 inch (300,000 tpa) and spiral steel pipes (80,000 tpa). Large diameter steel pipes are expected to come on board in Q4 08 while spiral pipes in Q4 09. The location of Jubail plant on the Arabian Gulf makes it an attractive export base to other GCC markets. Accordingly, as of 2011, APC total production capacity is expected to reach 780,000 tpa where 400,000 tpa are expected to come from Riyadh plant, small diameter pipes, while the remaining 380,000 tpa are expected to be delivered from Jubail plant, large diameter pipes.

Production capacity and utilization rate

Production capacity (tons)	2006 Actual	2007 Actual	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate
Riyadh	160,000	160,000	160,000	160,000	160,000	400,000
Jubail	0	0	300,000	380,000	380,000	380,000
Total	160,000	160,000	460,000	540,000	540,000	780,000
Utilization rate	90%	90%	90%	90%	90%	90%

Source: Arabian Pipes Company

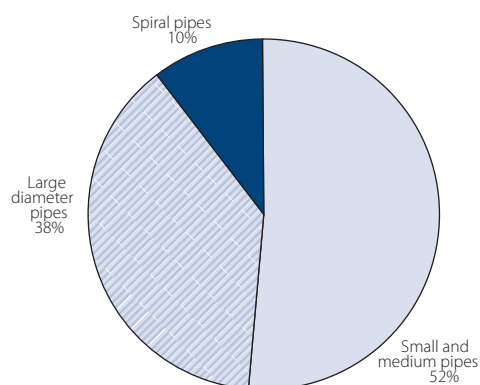
Outlook

Product Mix

...with more diversified product mix

APC is expected to deliver a diversified product mix by 2011 as opposed to the current situation where most of the production is of small diameter pipes. The chart below, depicts APC expected product mix in 2011.

Arabian Pipes production mix in 2010



Source: Arabian Pipes Company

Sales

Given the nature of the business as a job order production, we can consider APC's actual production figure to be its actual sales volume. The table below depicts APC expected sales volume during the period 2008-2012.

Expected sales volume & market share in GCC for 2008-2012

Sales Volume (tons)	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate	2012 Estimate
Demand	994,375	1,075,000	1,101,875	1,112,625	1,134,878
Sales	148,750	292,400	380,800	460,700	663,000
Market share	15%	27%	35%	41%	58%

Source: SHUAA Capital

As can be seen from the above table, we expect APC to achieve solid gains in its market share of upcoming regional production. Our bullish outlook is underpinned by the aggressive capacity expansion planned to match expected increase in the pipe industry's market size.

Prices

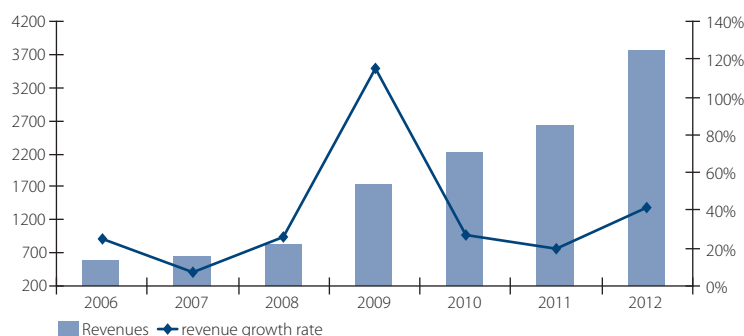
Average selling prices for Arabian Pipes witnessed an increase from an average of USD 880 per ton in 2005 to an average of USD 1,200 per ton in 2007, a CAGR of 16%. Our regression analysis model depicts that average selling price for APC throughout our forecast period will be within the range of USD 1,400-USD 1,600 per ton.

Revenues

APC's revenues to increase by a CAGR of 42% during 2008-2012, underpinned by upcoming capacity

During the period 2003-2007, APC recorded revenue CAGR of 43%, illustrating the strong demand for pipes underpinned by oil prices soaring from an average of USD 30 per barrel in 2003 to USD 100 per barrel, a CAGR of 35%. In 2007, APC recorded total revenue of SAR 639 mn as opposed to SAR 593 mn in 2006, on the back of rising demand and appreciating average selling price. During the coming period (2008-2012), we expect APC to increase its revenues by a CAGR of 42% underpinned by aggressive capacity expansions. In 2008, we expect APC to record total revenues of SAR 808 mn, up 26 % y-o-y.

Revenues outlook (SAR mn)



Source: Arabian Pipes Company and SHUAA Capital estimates

Margins and Profitability

Coil and billet are the main input in APC's production chain and they are considered the main reason for volatility in the company's margins. The chart below depicts the variability in APC's gross profit margin since Q1 04.

Gross profit margins volatility



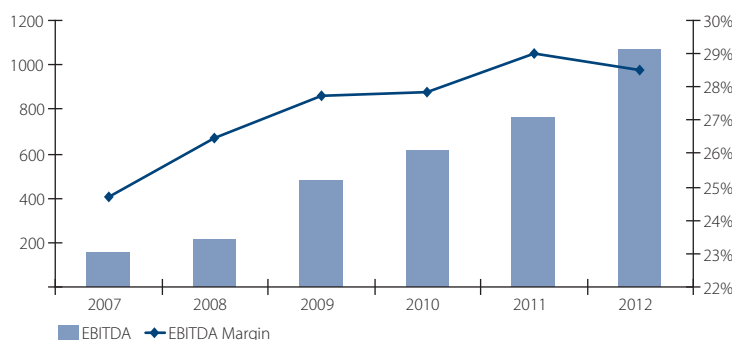
Source: Arabian Pipes Company

APC secures around 40 % of its required raw material from the local Saudi market while the remaining amount is imported from global suppliers through annual supply contracts reflecting global prices. Currently, APC produces small and medium diameter pipes where coil is the main input, while large diameter pipes require billet as it is difficult to handle coil in large diameter pipes. APC secures coil, raw material for the small and medium pipes from Hadeed, a Saudi based steel manufacturer company that is fully owned by Saudi Basic Industries Corporation (SABIC).

APC's average EBITDA margin to expand slightly in 2009

During Q1 07, when average coil price was close to USD 563 per ton APC recorded an EBITDA margin of 22%. During Q4 07, average coil prices increased to USD 619 per ton causing a 600 bps drop in APC's quarterly EBITDA margins to 16%. Going forward, we expect APC's average EBITDA margin to expand slightly in 2009 over our average expected margin of 2008 as the company is expected to introduce large diameter pipes to its sales portfolio, which enjoy higher margin than small and medium sized diameter pipes. The chart below depicts our outlook on APC EBITDA margins.

EBITDA Margins Outlook (SAR mn)



Source: SHUAA Capital

Capital Expenditures

APC to spend SAR 1.5 bn during the coming five years

We estimate APC's capital expenditure to sum up to SAR 1.5 bn during the period 2008-2012, (assuming average SAR 2,500 per additional ton of capacity). The table below depicts our expected CAPEX figure during the period 2008-2012.

Outlook on Capital Expenditures

Capital Expenditures SAR (000)	2006 Actual	2007 Actual	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate	2012 Estimate
Capital expenditures	85,334	74,808	185,348	255,077	342,563	392,382	350,729

Source: SHUAA Capital

Leverage

As of December 2007, APC's total interest bearing debt was SAR 748 mn with short-term debt representing the lion share (80%) - mostly to finance working capital on the back of rising raw material costs. The company's current net debt to equity ratio and EBITDA to net debt stand at 1.17x and 0.21 respectively.

Net Profit

Net profit to increase by a CAGR of 46% through forecast period

During the period 2004-2007, APC's net profit increased by a CAGR of 54% - from SAR 34 mn in 2004 to SAR 126 mn in 2007. We expect APC to record a net profit of SAR 153 mn in 2008, up 20% y-o-y. Throughout our forecast period, we expect APC's net profit to increase by a CAGR of 46%, underpinned by upcoming capacity expansion and margins improvement.

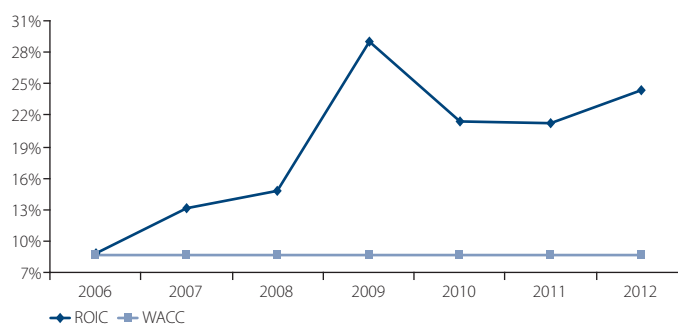
Dividends

APC announced a proposed cash dividend for 2007 of SAR 1.5 per share implying a dividend payout of 37.6% and dividend yield of 1.74 % as per the stock price of SAR 86.25 per share at the time of announcement. We estimate the company's dividend payout ratio to stand within the range of 35% per annum.

ROIC

During the preceding period (2006-2007), APC's ROIC witnessed a significant improvement from 9% to 13%. Throughout our forecast horizon, we expect gradual improvement in APC's ROIC underpinned by sustainable growth rate in the NOPLAT on the back of capacity expansions which is expected to be fully reflected on APC financials in 2009 and 2012.

Outlook on ROIC versus WACC



Source: SHUAA Capital

Valuation

Target price of SAR 155 per share implies 45% upside potential

We initiate coverage on APC with a Buy recommendation based on a target price of SAR 155.00 per share, implying 45% upside potential over the latest market price of SAR 107.00 per share. Our target price per share is based on two valuation methods, Discounted Cash Flow method (DCF), which has yielded a target price of SAR 158.94 per share and Price Earnings (PE) relative valuation, which has yielded a fair value of SAR 145.87 per share based on FY09 earnings. We assign an average weight for our DCF value of 70% and 30% to our relative valuation. In our relative valuation approach, we used FY09 earnings, as the APC new capacity is expected to be fully reflected on its financials by 2009.

Technical know-how and timely delivery core to growth and value realization

APC's strategic location in the heart of resource rich GCC at a time of significant growth in the sector's CAPEX, especially related to oil and gas transportation infrastructure, are key drivers of the company's growth and profitability going forward. Its strong alliance and successful track record with Saudi Aramco, the largest oil major in the region and arguably the producer with the most stringent quality standards, is evident in a five year supply contract, and promises a solid and stable base for growth. It also opens up the likelihood of significant new supply contracts with other oil majors in the region. The company's planned capacity expansion, of which significant CAPEX outlay has already occurred, as well as its technical know-how and timely delivery are core to the growth and value realization anticipated for the company over the next five years, and should result in significant market share gains, as well as a more robust barrier to entry for other producers.

Valuation methodology

SAR per share	Per share value	Weight
Discounted Cash flow	158.94	70%
Relative valuation	145.87	30%
Target value	155.00	100%

Source: SHUAA Capital

Taq's expected IPO holds further upside

As for its other investments, Taqa might go public in 2008, which we expected to be near the range of SAR 1.54 bn. During 2007, Taqa recorded a net profit of SAR 154 mn and we estimate the offering value based on ten times the recording earnings. If APC decides on selling its stake (5.63%), it is expected to record an investment gain of SAR 87 mn - adding around SAR 2.76 per share to our expected earnings estimate. If not, APC will benefit from being a shareholder in a downstream company. As TAQA introduces exploration and drilling services for O&G, it enhances APC's expected sales volume.

Discounted Cash Flow Valuation

Our DCF model is based on five year forecast period (2008-2013). The weighted average cost of capital is 8.59% based on cost of equity of 9.45% and cost of debt of 4.55 %. Our cost of equity is calculated based on the capital asset pricing model where our risk free rate is 4.5 %, market risk premium is 5% and a beta of 1. Our DCF model has yielded a target price of SAR 158.94, implying 49 % upside potential over the current market price of SAR 107.00 per share. However, It is important to note that the valuation of APC carries some risk due to:

- High dependency on terminal value.
- Free cash flows are expected to move into the positive territory by 2013 due to massive capital expenditures during the period 2008-2012. Management estimates the CAPEX figure to be around SAR 1.5 bn.

Sensitivity analysis

Perpetual Growth	2.00%	3.00%	4.00%	5.00%
WACC				
6.59%	179.65	242.80	354.71	607.40
7.59%	129.66	168.10	227.95	334.01
8.59%	95.44	120.83	157.27	214.02
9.59%	70.73	88.46	112.54	147.12
10.59%	52.17	65.08	81.91	104.77

Source: SHUAA Capital

Relative Valuation

We opted to run our relative valuation method based on FY09 estimated earnings, as APC new capacity is expected to be partially discounted in 2009. Our relative valuation approach has yielded a fair value for APC of SAR 145.87 per share implying 36 % upside potential to the current market price of SAR 107 per share. We utilized an average PE multiple and EV/EBITDA of 12.41x and 8.24 based on the following peers comparables.

Peer Comparison

Multiple comparables	Country	2009	
Company		PE	EV/EBITDA
Khartsizky Trubny	Ukraine	14.52	11.30
Trubnaya Metallurgic Kompaniya	Russia	7.06	4.89
Confab Industrial	Brazil	12.98	8.57
Corinth Pipe works	Greece	10.60	8.99
Tenaris SA	Italy	13.96	9.31
Tubacex SA	Spain	11.67	7.87
Vallourec SA	France	10.46	5.71
Northwest Pipe Company	USA	12.07	7.44
Valmont Industries	USA	18.38	10.05
Average		12.41	8.24
Arabian Pipes	Saudi Arabia	9.44	10.77
Relative Valuation		145.87	126.57

Source Reuters and SHUAA Capital

Financials

Income statement (SAR 000)

	2007 Actual	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate	2012 Estimate
Revenues	639,776	808,828	1,743,748	2,211,940	2,640,370	3,748,442
Cost of goods sold	445,359	542,263	1,172,527	1,496,472	1,756,150	2,529,828
Gross profit	194,417	266,565	571,221	715,468	884,220	1,218,614
Gross profit margin	30.4%	33.0%	32.8%	32.3%	33.5%	32.5%
SG&A	36,196	52,574	87,187	99,537	118,817	149,938
EBITDA	158,221	213,991	484,034	615,930	765,403	1,068,677
EBITDA Margin	24.7%	26.5%	27.8%	27.8%	29.0%	28.5%
Depreciation	11,588	16,137	18,362	20,846	23,694	26,959
Provision	-	-	-	-	-	-
EBIT	146,633	197,854	465,672	595,084	741,709	1,041,717
Interest expense	34,087	51,478	100,748	127,333	157,333	215,499
Interest income	-	-	-	-	-	-
Investment income	2,197	2,416	2,658	2,924	3,216	3,538
Dividends Income	6,750	6,009	6,910	7,946	9,138	10,509
Other non-operating income	7,066	2,426	5,231	6,636	7,921	11,245
Other non-operating expense	-	-	-	-	-	-
EBT	128,559	157,228	379,722	485,257	604,651	851,510
Taxes	3,013	3,931	9,493	12,131	15,116	21,288
Effective tax rate	2.3%	2.5%	2.5%	2.5%	2.5%	2.5%
EAT	125,546	153,297	370,229	473,125	589,535	830,222
Extraordinary items	34	-	-	-	-	-
Net profit after unusual items	125,580	153,297	370,229	473,125	589,535	830,222
Net Income	125,580	153,297	370,229	473,125	589,535	830,222
Net Income margin	19.6%	19.0%	21.2%	21.4%	22.3%	22.1%

Balance sheet SAR (000)

	2007 Actual	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate	2012 Estimate
Cash	5	8,088	17,437	22,119	26,404	37,484
Excess Cash	17,096	44,608	16,019	20,175	14,453	8,212
Accounts receivable	146,003	199,437	408,467	490,869	585,945	831,846
Inventory	642,424	690,828	1,434,338	1,754,767	2,059,266	2,966,483
Other current assets	6,003	7,684	16,566	21,013	25,084	35,610
Current Assets	811,531	950,645	1,892,827	2,308,944	2,711,151	3,879,636
Gross fixed assets	204,928	222,752	251,673	284,563	322,347	365,758
Accumulated depreciation	144,125	160,262	178,625	199,471	223,165	250,124
Net fixed assets	60,803	62,490	73,048	85,092	99,183	115,634
Projects under implementation	478,639	646,163	872,320	1,181,993	1,536,591	1,843,909
Long-term investments	123,314	125,730	128,388	131,312	134,528	138,065
Total assets	1,474,286	1,785,028	2,966,583	3,707,341	4,481,453	5,977,244
Due to banks	593,208	761,126	1,501,932	1,846,695	2,100,731	2,818,463
CPLTD	26,022	25,902	29,787	44,085	46,289	74,062
Accounts payable	26,278	44,570	96,372	122,998	144,341	207,931
Other current liabilities	53,008	56,618	122,062	154,836	184,826	262,391
Current Liabilities	698,516	888,215	1,750,154	2,168,614	2,476,187	3,362,847
Long term debt	129,508	148,935	220,423	231,445	370,311	555,467
Other long-term liabilities	4,498	6,471	13,950	17,696	21,123	29,988
Total liabilities	832,522	1,043,621	1,984,527	2,417,754	2,867,621	3,948,301
Paid in Capital	315,000	315,000	315,000	315,000	315,000	315,000
Legal and Statutory reserves	33,073	48,402	85,425	132,738	191,691	274,713
General reserves	98,942	144,931	255,999	397,937	574,797	823,864
Retained earnings	194,750	233,074	325,631	443,913	532,343	615,365
Total Equity	641,764	741,407	982,056	1,289,587	1,613,832	2,028,942
Total Liabilities & Equity	1,474,286	1,785,028	2,966,583	3,707,341	4,481,453	5,977,244

Financial ratios

	2007 Actual	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate	2012 Estimate	2013 Estimate
Growth ratio							
Revenues	8%	26%	116%	27%	19%	42%	10%
COGS	-5%	22%	116%	28%	17%	44%	10%
SG&A	9%	45%	66%	14%	19%	26%	79%
EBITDA	76%	35%	126%	27%	24%	40%	2%
Net profit	67%	22%	142%	28%	25%	41%	7%
Liquidity ratio							
Current ratio	1.16	1.07	1.08	1.06	1.09	1.15	1.62
Quick ratio	0.24	0.29	0.26	0.26	0.26	0.27	0.76
Cash ratio	0.00	0.01	0.01	0.01	0.01	0.01	0.01
Operating Working capital/current liabilities	1.09	0.96	1.01	0.99	1.02	1.08	1.06
Activity ratio							
Accounts receivable turnover	4.50	4.68	5.74	4.92	4.90	5.29	4.72
Accounts payable turnover	12.69	15.31	16.64	13.64	13.14	14.36	12.72
Inventory turnover	0.80	0.81	1.10	0.94	0.92	1.01	0.89
Accounts receivable days on hand	81	78	64	74	74	69	77
Accounts payable days on hand	29	24	22	27	28	25	29
Inventory days on hand	458	449	331	389	396	363	409
Profitability ratio							
Gross profit margin	30.4%	33.0%	32.8%	32.3%	33.5%	32.5%	32.8%
EBITDA margin	24.7%	26.5%	27.8%	27.8%	29.0%	28.5%	26.3%
SG&A to revenues	5.7%	6.5%	5.0%	4.5%	4.5%	4.0%	6.5%
Return on sales	19.6%	19.0%	21.2%	21.4%	22.3%	22.1%	21.6%
Return on equity	19.6%	20.7%	37.7%	36.7%	36.5%	40.9%	36.0%
Return assets	8.5%	8.6%	12.5%	12.8%	13.2%	13.9%	13.3%
Debt ratio							
Net debt to Equity	1.17	1.25	1.77	1.63	1.54	1.68	1.47
Net debt to market cap	0.22	0.28	0.51	0.62	0.74	1.01	1.08
EBITDA/Net debt	0.21	0.23	0.28	0.29	0.31	0.31	0.30
Interest coverage ratio	4.30	3.84	4.62	4.67	4.71	4.83	5.39
Investment ratio							
Outstanding shares	31,500	31,500	31,500	31,500	31,500	31,500	31,500
Market price	107.00	107.00	107.00	107.00	107.00	107.00	107.00
Enterprise value	4,102,138	4,253,766	5,089,186	5,450,430	5,846,975	6,772,796	5,169,164
Invested capital	1,301,596	1,562,436	2,709,239	3,411,843	4,163,048	5,587,426	4,455,020
Earnings per share	3.99	4.87	11.75	15.02	18.72	26.36	28.28
Book value per share	20.37	23.54	31.18	40.94	51.23	64.41	78.55
EBITDA per share	5.02	6.79	15.37	19.55	24.30	33.93	34.51
Dividends per share	0.00	1.70	4.11	5.26	8.42	13.18	14.14
Dividends payout ratio	0%	35%	35%	35%	45%	50%	50%
Price to earnings multiple	26.84	21.99	9.10	7.12	5.72	4.06	3.78
Price to book value multiple	5.25	4.55	3.43	2.61	2.09	1.66	1.36
EV/EBITDA	25.93	19.88	10.51	8.85	7.64	6.34	4.76
EV/IC	3.15	2.72	1.88	1.60	1.40	1.21	1.16

Free Cash flow	2007	2008	2009	2010	2011	2012
(SAR 000)	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
NOPLAT	143,197	192,908	454,030	580,207	723,166	1,015,674
Add: Depreciation	11,588	16,137	18,362	20,846	23,694	26,959
Change in working capital	(151,137)	(91,629)	(910,087)	(380,887)	(382,516)	(1,100,609)
Capital expenditures	(74,808)	(185,348)	(255,077)	(342,563)	(392,382)	(350,729)
Free Cash flow	(71,161)	(67,932)	(692,772)	(122,397)	(28,038)	(408,704)

Appendix

Technology of steel pipes

Different steel pipes are made through different technologies adding unique attributes to their basic properties such as toughness, flexibility and corrosion resistance. The section below depicts different technologies utilized in steel pipes manufacturing.

Galvanized Steel pipes



Galvanized steel pipes are pipes that are covered with a layer of zinc. For decades, designers, builders and consumers seeking long-term structural performance in the harshest of outdoor applications have turned to zinc-coated steel pipes. These pipes and tube, resistant to wind, humidity and road salts, are one of the most widely used building materials worldwide.

Seamless steel pipes



These pipes and tubing are manufactured by electrode vacuum melted quality steel. Seamless steel pipes and tube comes in different sizes and shapes including thin, small, and precise. Superior metallurgical characteristics, ultra high strength and corrosion-resistant properties makes seamless pipes perfect for the transmission of oil & gas and corrosive liquids.

Electric resistance welded steel pipes (ERW)



High performance ERW steel pipes possess high strength corrosion resistance, and high toughness, making ERW pipes the preferred pipes for transportation of oil and gas. Offering a wide range of size and quality specifications, these pipes have witnessed a tremendous increase in production driven by growing demand in the oil & gas industry, infrastructure and automobile usages. Arabian Pipes, the largest manufacturer of welded steel pipes in the Middle East (ME), has the only High Frequency Welded (HFW) mill in the ME to complement its anti-corrosion coating plant.

Welded steel pipes (WSP)



WSPs are used in all types of corrosive environments in chemical, metallurgical, energy, oil & gas, pulp & paper, ships, desalination, and food industries. WSPs come with improved design properties and offer much higher corrosion resistance than other conventional steel pipes.

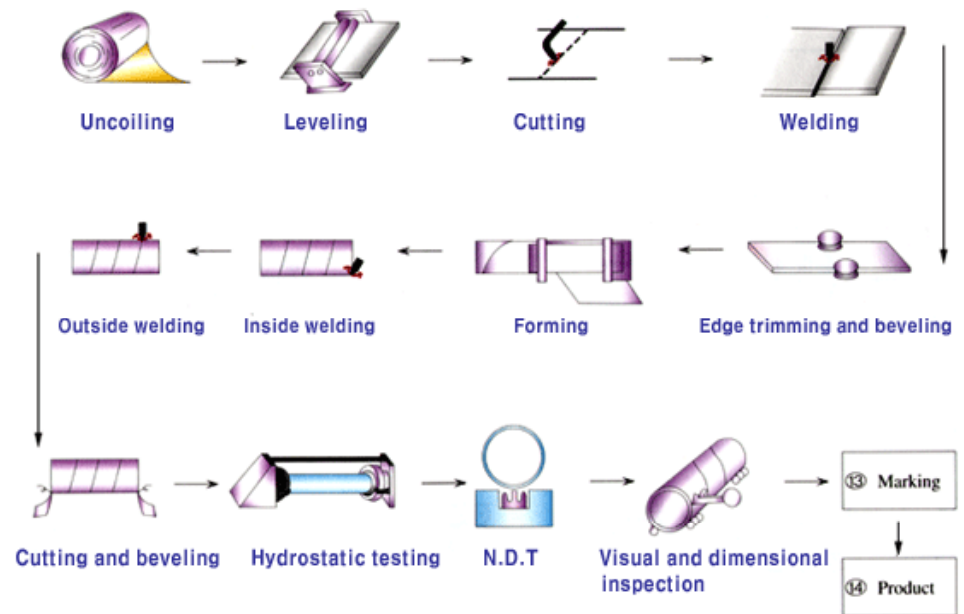
Production Process

Since the pipes used to drill wells are critical to operational integrity of the oil and gas industry, a meticulously designed and implemented production process is essential.

The production method for steel pipes involves the following three steps:

- Raw steel is converted into a more workable form
- Pipes are formed on a continuous or semi continuous production line
- Ready pipes are then cut and modified to suit specific customer needs.

Production Method for Steel Pipes

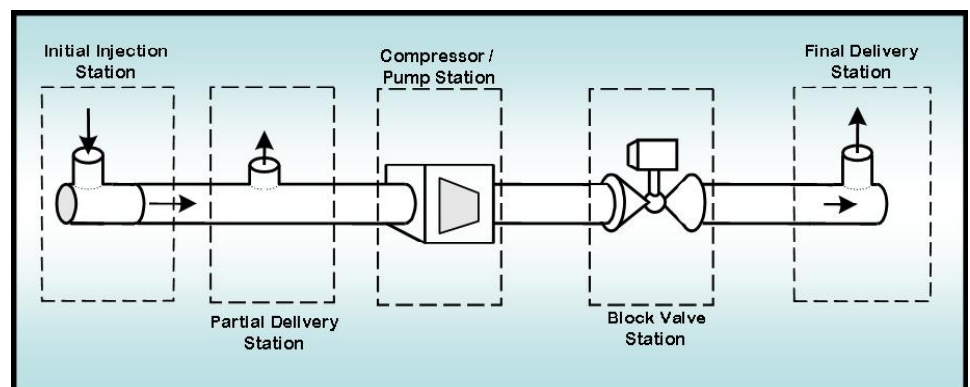


Source: Arabian Pipes

Pipeline components

The chart below shows the pipelines main components of the pipelines system.

Pipeline system



Source: Wikipedia

Initial Injection Station: The beginning of the system, where the product is injected into the line. Storage facilities, pumps or compressors are usually located at these locations.

Pump Stations: Pumps for liquid pipelines and Compressors for gas pipelines are located along the line to move the product through the pipeline.

Partial Delivery Station: These facilities allow the pipeline operator to deliver part of the transported product.

Block Valve Station: These are the first line of protection for pipelines. With these valves, the operator can isolate any segment of the line for maintenance work or isolate a rupture or leak.

Final Delivery Station: Known also as Outlet stations or Terminals, this is where the product will be distributed to the consumer. It could be a tank terminal for liquid pipelines or a connection to a distribution network for gas pipelines.

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