



OMAN REFRESHMENT COMPANY SAOG

Management Discussion and Analysis Report - 2019

Business activities of the Company

Oman Refreshment Company SAOG (“ORC/the Company”) is engaged in the business of filling and distribution of soft drinks, water, juices and trading in consumer packaged goods. It holds the franchise rights to produce, fill and distribute PepsiCo range of soft drinks and Aquafina water as well as trading in new edge beverages, Frito Lays range of snacks, Quaker range of Oat products, Eurocake bakery products and Froneri ice cream range (Nestle, Mondelez, Dell monte..) of products throughout the Sultanate of Oman. Further, it also produces and distributes juices under its own brand name “Topfruit”.

The company has acquired a new business line in October 2018 of Vending machines and hot drinks distribution in Sultanate of Oman through 100% share acquisition of Arabian Auto Vending Machine Company LLC.

The Company was established in 1975 as a joint stock company initially with small production and bottling facilities which were expanded from time to time as part of the business growth strategies to meet the growing market demand.

The company has purpose fit production & bottling plant as well as central warehousing facilities in Al Ghubrah, Muscat and 10 depots situated at Al Wafi, Ibri, Nizwa, Sohar, Salalah, Bukha, Buraimi, Hima, Musannah and Mudheibi that cater to the customers spread across the Sultanate of Oman.

The Company has 932 employees as at the current year end who are totally aligned with the Company’s business objective of delighting all stakeholders of the Company.

Overall Review

The company achieved a net profit after tax of RO 8,456,046 on a turnover of RO 63,765,515 during the year 2019 against a net profit after tax of RO 11,809,188 on a turnover of RO 76,024,055 in 2018, registering a decrease in the net profit after tax and turnover by 28.4% and 16.1% respectively.

During the year, ORC maintained highest Global standard of food safety for consumer through preventive and treat assessment tool certification including FSSC 22000 V4.1 and ISO 22000:2005 of Food Safety Management Systems (FSMS).

Forward-looking Statements

This report contains opinions and forward-looking statements, which may be identified by their use of words like “plans”, “expects”, “will”, “anticipates”, “believes”, “intends”, “projects”, “estimates” or other words of similar meaning. All statements that address expectations or projections about the future, including but not limited to statements about the company’s strategy for growth, product development, market position, expenditures, and financial results, are forward-looking statements.

Shareholders and readers are cautioned on the data and information external to the Company, that though they are based on sources believed to be reliable; no representation is made on their accuracy or comprehensiveness. Further, though utmost care has been taken to ensure that the opinions expressed by the management herein contain their perceptions on most of the important trends having a material impact on the Company's operations, no representation is made that the following presents an exhaustive coverage on and of all issues related to the same.

Further, the following discussion reflects the perceptions on major issues as on date and the opinions expressed herein are subject to change. The Company undertakes no obligation to publicly update or revise any of the opinions or forward-looking statements expressed in this report, consequent to new information, future events, or otherwise.

Operating Environment

The Sultanate of Oman economy during year 2019 was in testing phase where oil production was capped, and hydrocarbon production was lower. On other hand, non-oil economy expanded supported by on-going diversification in key sectors namely logistics, tourism, mining, fisheries etc. During mid of the year, new excise tax been implemented on selected products, which added momentum in non-oil revenue in 2019. The Government of Sultanate of Oman's impetus on creation of new jobs through selective spending on various infrastructure, tourism projects and oil & gas sector activities have helped economic momentum in 2018. Execution of major tourism projects, both in the Government and private sectors, are helping in the Government drive to promote inbound tourism. Growing trends of urbanisation, raising household income levels & consumerism and growing contribution of non-oil sector of the Omani economy have continued to spur the nation's economic growth in 2019.

The changing dynamics of employment environment in the Sultanate of Oman that include, inter alia, restricted employment of expatriates, shortage of skilled Omani workforce, the absence of a hire & fire ease policy and swift movement of the skilled Omani manpower from private sector to Government jobs are creating additional pressures on finding replacement of suitably qualified workforce besides the soaring recruitment & wage costs. The recent adoption of new excise tax on selected products including carbonated soft drink and energy drinks which are the key revenue driver of the company, have impacted the growth and resulted contracting revenue. The subsidy cancellation on fuel, electricity along with the raise in public charges and direct/indirect taxes are adding pressure on the manufacturing and distribution operation.

Since its inception, the Company has been playing a key role in the soft drinks & beverages business segment in Oman and has continued to be a leading player in this market. Besides the PepsiCo range of soft drinks, the Company's country wide distribution network had launched many other products in the "Beverages & Juices" sector over the years. The company's products, backed by its well-established customer relationships, enjoy loyal consumer patronage. The beverages market in Oman continues to grow with the growth of local population as well as the influx of expatriate manpower into the country to meet the requirements of growing economy and the diversity of market demand. On the food market, the rising demand for products with high quality and diversity of packaged goods combined with growing health conscious consumers offers a promising proposition for the food categories in which ORC operates particularly in the salty & sweet snacks segments. The recent introduction of work renewed brand by partnering with Froneri (Nestle and Mondelez) into the frozen desserts looks promising. The company has also embarked into a new category namely hot drinks introducing Lavazza coffee and expanding its vending business range across the sultanate. The company continues to thread carefully in its business expansion and product diversification and included dairy added flavored milk to cater to different consumer segments to meet the occasion based consumption needs and diverse consumer tastes.

Opportunities and threats

The company is a leader in the Omani beverages market and a prominent player in the snacks business segment. Besides the growing threat of competition within the Carbonated Soft Drinks (CSD) market for the company's products, the CSD market as a whole appears to be facing tough competition from dairy products, juices and other beverages. The recent adoption of new excise tax on selected products including carbonated soft drink and energy drinks which are the key revenue driver of the company, have resulted contracting revenue. With such in regulation and tax regime, the company have implemented revised price-pack-channel proposition to remain the choice of beverage of consumer. The change in consumer preference and rise of health conscious, the company has swiftly expanded its range of "Good for you" and "Better for you" propositions. While the company enjoys leadership position in the CSD market, it faces stiff competition from many players in the water, juice, snacks and ice cream segments. The company expects to widen its consumer base and strengthen its revenue base with the planned expansion of the food & beverages product portfolio.

Thanks to the successfully implemented new Human Resources policies and procedures in 2014 that included upgrading of pay structure benchmarked to the leading industry practices; and the performance based management culture in the Organisation, the Company is continuing to attract , develop & retain the best available local talent and with reasonable staff turnover mainly amongst local employees. On the other hand, the wages bill continued to raise on account of the changing job market dynamics that include reduced work week, minimum salary increments for local workforce, increased overtime pay and impact of extended leave of absence along the authorised public holidays amongst local workforce that is resulting in deployment of temporary local workforce at higher daily wages.

Volatile international prices of commodities, which are key input raw materials to the Company's products, may impact the current and future profitability. The Company keeps a close watch and attempts to mitigate this cost impact by entering into forward contracts on certain key raw and packing materials. Further, the Company is also watchful of the ongoing changes in the regional economic, specific to GCC through introduction of Selective Tax and Value Added Tax which may also severely impact its business performance and consequently its investment strategies.

On the other hand, stagnant consumer prices at multiple customer channels, raising trade margins pressure are severely affecting the "market driven offset mechanism" to absorb the impact of rising input & labour costs. The Company works closely with the respective authorities and other market players to address this issue for the overall benefit of the Omani consumers and economy.

The Company has well-defined marketing strategy, working in coordination with "PepsiCo" and its other partners, aimed at diversifying its revenue base by re-inventing its core products and expanding its product portfolio to cater to the diverse consumer preferences and tastes in careful co-ordination with other key principals.

As regards new investments into the business, the Company has continued expansion of its manufacturing, warehousing and logistics capacities at various business locations to improve operational & marketing efficiencies, as part of the objective to have purpose fit own premises for its distribution centres outside Muscat. The new PET line and Tetra line for still drinks have been commissioned during the year 2019. Further, the Company has also invested in strengthening its production capabilities during the current year to meet the performance & efficiency objectives. The

Company invests significantly & regularly on the upkeep of current production lines, warehousing compliant to the Oman regulations, company's distribution capabilities and marketing equipment, with the focus on improving operational efficiencies as well as increased customer reach. Through its subsidiary "Al Rawdah Integrated Trade & Investment Enterprises LLC", the Company is constantly exploring suitable new business growth opportunities.

Further, ORC has been following its established "green initiatives" to efficiently manage the both liquid and solid 'waste' generated during its production/bottling processes. Staff has been regularly trained in various Health, Safety and Environment (HSE) aspects with the focussed objective of strengthening HSE measures in the plant operations and various business locations that have shown tremendous benefits in safeguarding Company assets against unforeseen events and accidents. These measures have also proven to be effective with the tangible results demonstrated by improved scores in the unannounced audits conducted by independent international and local organisations.

The Company has been an active corporate citizen and regularly supports various initiatives focusing on environment preservation, education, social and suitability development. During the year 2019, the company has partnered with different CSR initiatives such as Beach cleaning event, support on Oman Science Festival through Ministry of Education (MOE), partnership and active contribution with Oman Football Association, support for events in Sultan Qaboos University (SQU) among others. The company is committed to pursue its CSR strategy in 2020 with the aim of positively impacting the communities across the Sultanate.

Furthermore, it has carried out numerous "learning and developmental" activities for its staff during 2019 with setting up a focussed "learning and development" team within its Human Capital Department and continues to invest in its human resources – both Omani and expatriate - by assessing & improving their professional & job skills in general and specifically to enhance the skills of individuals to ensure that they deliver the given responsibilities with efficiency and targeted productivity.

The Company is pro-actively carrying out the development of its Omani workforce to enable them move up higher in the organizational structure by sponsoring high potential employees to pursue their higher education. The Company had consistently maintained its staff Omanisation percentage above the legal requirement and continues to encourage & employ local workforce at every available opportunity. The Company is reaping the benefits of these measures in staff development & welfare, streamlining the human capital policies and practices in the declining staff turnover.

Financial and operational performance

Despite the economic challenges and excise tax implementation in June 2019, ORC continued its successful performance journey in 2019 with the help of innovative and intensified marketing strategies against the stiff market conditions such as the highly price-sensitive consumers, changing consumption habits, highly competitive Juice, Water and Snacks product segments, the Domestic and Overall sales volume has a de-growth at 13.8% and 13.7% respectively.

On the other hand, the rising operating costs especially the unpredictability in the volatile costs of input materials and employment continued to impact the operating margins, which to some extent withstood the pressure on the back of marginal sales volume growth and improving operational efficiencies. Further, the Company's selective and focussed investment strategy to improve

operational efficiencies across the organisation, together with the successes achieved in sourcing certain key input materials at competitive prices compared to the previous year helped in achieving good net profit during 2019.

Performance of various products

The company operates in the Beverages & Juices segment as well as importing & distributing food products. Following is the contribution of various products to the company's turnover, in terms of number of cases in thousands:

Product category	2019	2018	Variance (%)
Carbonated Soft Drinks	16,270	20,069	-18.9%
Water	3,591	3,822	-6.0%
Juices	2,232	2,107	5.9%
Food	1,605	1,547	3.7%
Ice Cream	102	75	36.0%
ORC domestic	23,801	27,620	-13.8%
Export	943	1,061	-11.1%
ORC	24,743	28,681	-13.7%

N.B.: The above is excluding Arabian Vending LLC sales

Financial highlights

	2019 RO	2018 RO	2017 RO	2016 RO	2015 RO
Revenue	63,765,515	76,024,055	77,851,117	77,223,438	77,063,509
Gross profit	25,582,660	31,530,131	33,696,542	32,250,370	31,534,270
Profit before taxation	9,935,665	13,895,500	12,682,631	11,725,614	10,909,492
Taxation	(1,479,619)	(2,086,312)	(1,866,049)	(1,403,582)	(1,309,347)
Net profit after taxation	8,456,046	11,809,188	10,816,582	10,322,032	9,600,145
Cash Dividend	2,500,000*	3,750,000	3,750,000	5,000,000	5,000,000
Net Equity	63,054,597	58,348,551	50,289,363	44,472,781	39,150,749

*proposed dividend for 2019 is subject to shareholders' approval at the ensuing AGM.

Conclusion

The Company shall continue to expand & diversify its products to appeal to the varying consumer needs through innovative products and strategies for wider consumer reach. The Company's growth plans will be driven by the success of its efforts in capitalising on the growth and diversity of the market demand with quality delivery of its product portfolio while simultaneously focussing on efficiency improvement, costs optimisation and suitable development of human capital to meet the growing business needs.

Having stated about the internal preparedness of the Company, it is also imperative not to underestimate impact, on its business performance, of the regional and local economic conditions and the various measures initiated by the Government authorities, such as fees & tax rate revision, proposed new taxes and pruning of subsidies, to mitigate the widening budget deficits on account of low oil prices. Though the near future presents an element of uncertainty in the general economic conditions of the region due to sliding oil prices, the company believes that it is well positioned in its business sector due to its cautious approach to selectively expand and introduce new products, while continuously driving internal efficiencies and improving market response time, on the back of its strong brand equity and established business relationships.
