

Case Study: Jazeera Steel (Oman)

Jazeera Steel's Story

Jazeera Steel was founded by a prominent Omani industrialist in 1997 and incorporated as a public joint-stock company listed on the Muscat Stock Exchange in the same year. Combining Oman's low power costs with modern production lines sourced from the United States, Germany and Thailand, the company was well placed to serve the Gulf region's growing demand for steel tubing.

Ten years later, Jazeera Steel had grown into one of the largest producers of steel tubes in the MENA region, with four production lines covering a range of galvanized and ungalvanized tube products. The company had also obtained several standards certifications—including ISO 9001:2000 for general quality management and the American Petroleum Institute's (API) certification for oil and gas pipeline applications—earning it a reputation for reliability among regional players.

In 2007, Jazeera Steel was planning a major expansion of its operations into the steel bar market, but it faced high borrowing costs that made debt financing prohibitively expensive. To obtain capital for constructing the steel bar plant, the company sought an equity injection instead.



Kuwait-based Global Capital Management identified an opportunity to create value by funding Jazeera Steel's plant expansion through acquiring a majority stake in the company. From Global's perspective, the Gulf's steel industry was thriving amid growing infrastructure spending in the region and had not yet undergone consolidation. This presented ample opportunity for Jazeera Steel to grow organically. Moreover, with the addition of a steel merchant bar plant, Jazeera Steel would be poised to capture new segments of the market as it added differentiated and higher-margin niche products to its offerings. However, Global also saw several areas in which it could add value by drawing on its experience with other manufacturing portfolio companies to optimize Jazeera Steel's resource management and financial structure.

The Role Played by Private Equity

However, less than a year after Global's investment in Jazeera Steel, macroeconomic conditions as well as setbacks in the construction of the new steel rolling mill depressed revenues, raised costs, and led to operating losses. Jazeera Steel faced a collapse in world steel prices as construction demand dried up and its inventories grew to more than a year of sales; by early 2010, the company was under pressure to extend its credit lines.

To address Jazeera Steel's undercapitalization, Global tasked the company's finance department (which had previously focused mostly on accounting) with optimizing the company's capital structure and lowering its cost of borrowing. The result was substantial savings due to lower interest expenses; by negotiating Jazeera Steel's first credit lines with banks outside of Oman, the new Global-

appointed management team was able to reduce Jazeera's cost of debt by more than 200 basis points between 2010 and 2012.

Operationally, Global tackled rising inventories by implementing a new inventory management system modeled on just-in-time production, and reduced Jazeera Steel's working capital requirements by negotiating extended terms with new suppliers to shorten receivables days. Additionally, Jazeera Steel's new plant required significant modifications before it became operational. Construction on the new steel bar mill was both over budget and more than a year behind schedule. Global worked with management to bring the new plant online in 2010 and hired a consulting team to enhance the plant's performance, thus securing Jazeera Steel's entry into a critical new market segment. By 2011, the merchant bar plant had broken even on a profit and loss basis; today, the plant leads ▶

The Company



Jazeera Steel **حدید الحزیرة**

Essentials

Company: Al Jazeera Steel Products Co. SAOG (www.jazeerasteel.com)

Country: Oman

Sector: Manufacturing

Business focus: Steel tube and structural products

Size: Revenues of US\$237 million (2011); 688 employees as of July 2012

GP: Global Capital Management, a MENA-based private equity firm with a focus on GCC countries, Turkey, India and China (www.globalinv.net)

Date of investment: November 2007

Investment: US\$53.8 million for a 51% stake through a PIPE transaction

Impact Highlights

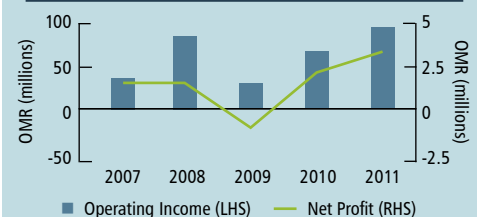
Global guided Jazeera Steel through a sharp contraction in the world steel market, reduced its borrowing costs by more than 200 basis points, and modernized resource management systems to decrease inventory stocks

With Global's support, Jazeera Steel salvaged a crucial factory expansion that had been behind schedule and over budget, nearly doubling the company's profits within four years of its acquisition

By introducing health and safety benchmarks tied to managers' key performance indicators, Global strengthened Jazeera Steel's accountability for workers' wellbeing

Global pursued dialogue with Jazeera Steel's labor union early on, creating an atmosphere of trust that later minimized factory shutdowns during civil unrest in 2011

Financial Performance



The Company View

“The contribution of Global Capital has outweighed our expectations. Global Capital has not only helped in the improvement of the performance of the tube mill and the commissioning of the merchant bar mill, but has also executed company-wide initiatives to strengthen the management team and improve reporting methods.”

“In any organization, success lies in clear communication. We are proud to say that we have a board which understands the company and gives free rein to employees to pursue innovations for its betterment.”

Bejoy John, Assistant General Manager, Finance, Jazeera Steel



Employee productivity



“We saw an excellent growth potential in Jazeera Steel through institutionalizing the company’s culture, implementing corporate governance initiatives, restructuring operations, and opening up new markets.”

Sulaiman M. Al-Rubaie, Partner, Global Capital Management

▶ all of the company’s units in year-on-year volume growth. To fully exploit growth opportunities in steel bar products, Jazeera Steel plans to add a second shift at the plant by the end of 2012 in order to begin round-the-clock production.

Beyond these localized efforts to keep Jazeera Steel capitalized and growing, Global also strengthened the company’s management culture by institutionalizing core business functions that Jazeera Steel had previously accomplished informally. In particular, Global’s team introduced an enterprise resource planning (ERP) system and separated financial accounts for different plants to better monitor each section’s profitability. Global also introduced best practices in monitoring costs; for example, detailed monthly forecasts were added to the company’s annual budget for greater precision.

On the corporate governance side, Global created a remuneration committee that replaced Jazeera Steel’s company-wide bonus system with a more

targeted system of KPIs that explicitly linked managers’ compensation to production, safety, and other performance targets. By adjusting managers’ incentives and allowing more granular assessments of performance at the individual and plant level, Global achieved labor productivity improvements of more than 45% (see graph).

Today, Jazeera Steel is one of the largest steel tube and bar product producers in the Gulf region, and its increasing competitiveness has propelled it into several new markets, such as Iraq and East Africa, while strengthening its footprint in the United States and Canada. Since Global’s investment, Jazeera Steel’s exports to North America as a share of total revenues rose from 5.7% in 2007 to 17.6% in 2011. Looking ahead, Jazeera Steel plans to expand through vertical integration; a planned joint venture in distribution slated to begin in late 2012 or early 2013 will allow it to sell directly end-users in second tier cities in Saudi Arabia.

Beyond the Bottom Line

Under Global’s leadership, Jazeera Steel has made strides in promoting the safety of its workers. Whereas previously employees sometimes flouted safety codes such as those governing helmet use due to Oman’s hot climate, Global insisted that Jazeera Steel hold itself to a higher standard than the lax safety environment prevailing in the surrounding industrial zone.

To ensure that health and safety were taken seriously, the remuneration committee added accident records to managers’ KPIs, thereby aligning managers’ incentives with the company’s responsibility for its workers’ safety. Global also installed new filters and ventilation equipment in order to further reduce ambient toxic chemicals beyond the levels required by law.

The company’s relationship with its employees’ labor union was also an early priority for Global. When operating losses in 2009 led to cuts in employee salaries, the resulting frictions with plant workers revealed the need for better lines of communication. Global instituted transparent production incentives to take the guesswork out of employee compensa-

tion, and included efficient interaction with the union as one of the KPIs on which managers were evaluated. Jazeera Steel also created an employee fund to cover workers’ uninsured injuries as well as costs for training and licenses—a fund to which Global’s board members contribute the entirety of their board fees.

In addition to worker safety, Global also improved the quality of employment at Jazeera Steel. Since the beginning of the partnership in 2007, the proportion of employees eligible for pensions has risen from 78% to 90%, even as total employment also rose by more than a third. While Jazeera Steel’s regular workforce grew by 9% per year since Global’s investment, salaries grew by 15%.

This outreach and stewardship of employees’ interests bore fruit in 2011; when labor unrest in Oman linked to the Arab Spring forced other firms to suspend production for several weeks, Jazeera Steel only experienced one day of plant shutdowns due to an active dialogue among the labor union, board members, and management.