Renaissance Capital

Analyst comment

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Tuesday, 30 June

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Barloworld 1H20 results – complex set of results with very little silver lining – 2H20 is set to be even tougher

Ticker: BAWJ.J
Rating: **BUY**
Target price: ZAR82
Current price: ZAR78

Barloworld released their 1H20 results this morning. Normalised HEPS was ZAc354 (1H19: 521), excluding the impact of BEE charges and IFRS16. Including these charges HEPS was ZAc268 (ZAc476) or a decline of 44%, compared with our full year estimate for a decline of 49%.

Bottom line: a complex set of results in our view, factoring in 1) the initial impact of COVID-19 (particularly car rental and motor trading); 2) the implementation of new IT system costs (which they refer to as Barloworld Business Systems), and 3) the implementation of the Khula Sizwe BEE transaction which included i) share based charges, ii) IFRS 2 charges and iii) initial rental charges [49 of 64 properties have been transferred]. The key drag on the result was from Automotive (both trading and car rental) as well as Logistics (which generated an operating loss) – in response management will reduce the headcount in both divisions. The only operational positive from the result was from Equipment Russia (operating profit +18%). All in all, with the full impact of COVID-19 still to come through, restructuring costs, tough trading conditions and uncertainty on the Tongaat Hulett Starch transaction, we believe it will be a difficult 2H20 for Barloworld.

Key points from the 1H20 results:

- Continued revenue declined 12.2%
- Continued operating margin declined 110bpts (-28%).
- No dividend declared in 1H20 and unlikely to pay a dividend at YE.
- Net debt to EBITDA 0.9x
- The Avis Fleet transaction has been put on hold. Avis Fleet and Avis Budget (car rental) will be integrated to unlock synergies.
- Cost saving austerity measures for FY20, once implemented is expected to save c.ZAR400mn.
- Retrenchment costs is expected to amount to between ZAR300-320mn when concluded. The focus will be a reduction of headcount in Automotive and Logistics (a 20-25% reduction in group headcount).
- No material updates provided on the Tongaat Hulett Starch and Mongolia transactions.
- Cash flow from operations was an outflow of ZAR372mn, which included a working capital outflow of ZAR2.3bn (as a result of higher receivables and inventory).
- Net debt was ZAR4.7bn, compared with ZAR582mn at FYE19, but in line with 1H19 at ZAR4.7bn – the working capital cycle tends to be more favourable in 2H.

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Distell: Pre-close trading statement reaffirms previous guidance - Neutral

Ticker: DGHJ.J
Rating: **BUY**
Target price: ZAR130.0
Current price: ZAR75.8

Distell reaffirmed its 15 May 2020 trading statement guidance of an up to 80% decline in FY20 HEPS and provided more detail on the revenue and volume sales on a per region basis. We believe that the cumulative revenues and volumes decline of 15.4% and 23.3% YoY, respectively, potentially translates into FY20 revenue of ZAR22.1bn and volumes of 549mn litres (a 8.3% and 9.6% miss to our forecast revenue and volumes, respectively). Distell guided to lenders relaxing debt covenants which gives further comfort that their solvency and liquidity measures should see it through this period. We continue to forecast a strong earnings recovery post the COVID-19 restrictions being lifted in its key regions. We view this announcement as neutral for Distell as it largely reaffirms the company's previous guidance. We have a BUY rating and ZAR130 TP on Distell.

COVID-19 update

Distell notes that it has recorded 58 infections across its South African operations. All affected individuals were placed into quarantine and given the appropriate support. This resulted in the closure of five distribution sites during the month of June, all of which have been re-opened and are currently operating at expected levels, after the necessary protocols were followed before the resumption of activities in accordance with regulations. Distell has generated around ZAR21mn from the sale of sanitisers and donated a total of 176,500 litres of sanitiser to various stakeholders (such as government, customers and their patrons as well as NGO's) in order to support the good hygiene efforts taken to curb the spread of the virus, especially in vulnerable communities.

Previously guided earnings decline reaffirmed

Distell issued a trading statement on 15 May 2020 guiding to FY20 HEPS declining by up to 80% YoY (FY19 HEPS: ZAR6.53) largely due to the impact of the COVID-19 restrictions in its sales regions. This translates into a c. 68% miss to our forecast (FY20E: ZAR4.06) and a c. 56% miss to the latest Thomson Reuters consensus of ZAR3.00. Distell remains confident that it should be able to satisfy export and local demand going forward as more productive capacity resumes, while noting that port constraints may provide a short-term headwind.

This guidance was reaffirmed because of the following factors:

- Restrictive trading conditions applicable to level 3 in South Africa and other operating regions.
- Potential increase in credit loss provisions for debtors and impairments to stock.
- Potential impact on valuations of minority holdings in specific African countries.

Trading conditions update

Distell provided more detail on trading conditions with cumulative revenues and volumes being down 15.4% and 23.3% YoY, respectively. We estimate potential FY20 revenue of ZAR22.1bn and volumes of 549mn litres which translates into an 8.3% and 9.6% miss to our forecast revenue and volumes respectively. The regional estimated performance is detailed below:

- Easing of export restrictions allowed approximately 54% (ZAR238mn) of a total orders of around ZAR440mn to be completed, largely due to port constraints and customer cancellations.
- Resumption of level 3 in South Africa resulted in an initial spike in demand which is expected to normalise. This resulted in cumulative revenues and volumes declining 18.3% and 25.6% YoY, respectively. We estimate that this translates into potential FY20 SA revenue of ZAR15.8bn and volumes of 426mn litres.
- The BLNS region saw a prolonged lockdown which resulted in cumulative revenues and volumes declining 14.9% and 20.4%, respectively, translating into potential FY20 BLNS revenue of ZAR1.7bn and volumes of 40mn litres.
- The Rest of Africa business proved more resilient with cumulative revenues up 2.3% but volumes declining 12.0%, translating into potential FY20 revenue of ZAR2.2bn and volumes of 44mn litres.
- The International business which saw travel restrictions impacting sales resulting in cumulative revenues and volumes declining 10.3% and 15.4%, respectively, translating into potential FY20 revenue of ZAR2.4bn and volumes of 36mn litres.

Solvency and liquidity position remain intact

Distell guides to solvency and liquidity remaining largely comfortable with the company being in a position to recover once trading patterns normalised. Over and above the additional facility and liquidity measures announced in its previous guidance, Distell further noted the following:

- Covenants (2.75x net debt/EBITDA) have been relaxed for the current period.
- Debtor collections have exceeded expectations, with vulnerable customers being supported through customised payment arrangements.
- Distell should announce the results of the sale of two wine farms (Alto and Plaisir de Merle) by its FY20 results presentation.

We still believe that the measures in place will ensure that Distell has enough liquidity to meet its short-term debt requirements by FY20.

Management will hold a pre-close conference call today at 2pm SA Time, registration link: https://www.diamondpass.net/7036012

Distell still expects to announce its FY20 results on or around 27 August 2020.

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China PMI / Kazakhstan follows Azerbaijan into lockdown / Arizona follows Sweden's interesting example

First the good news … China PMI for June was good .. about the 4th best monthly figure in a decade – supporting our view that domestic China will be one of the strongest stories in the 2Q20 global economy

New export orders were much improved, but would still count as shockingly bad in any normal year. Oddly these terrible figures did not correlate with Chinese export data in May though... so I'll be curious to see what Korean export figures show in June (out tomorrow). Apparently for the first 20 days, Korean trade figures were a bit better than May.

Meanwhile Kazakhstan's president has ordered his cabinet to prepare to re-impose full lockdown for 2-4 weeks. Kazakh coronavirus figures quoted on most websites don't look too bad – with active cases at 46 per 100k .. similar to Egypt and less than 2/3 of Canada (which is likely to see the EU travel ban lifted on it today). However, Kazakhstan emphasises only symptomatic cases in its data releases. China did this in 1Q20 and it was annoying because no-one else does – as far as I know. Taking data reported by journalists there, Kazakhstan's active cases are actually at 141 per 100k which would put it around 23rd in the world. Below France and Spain and they are easing policy (but they are also slow to report recovered cases). Kazakhstan would be below Russia or Saudi.

This would be only the second country to re-impose full lockdown after Azerbaijan which did it on 21st June.

It will be a hit to the economy in July 2020. I'll leave it to Sofya to judge how bit a hit.

I'm a little surprised because Kazakhstan is a pretty young country – but maybe the government thinks it can afford to do a full lockdown so why not.

Meanwhile Arizona – the worst state in the US for the virus spread and a place where the authorities have said we have to just learn to live with the virus – has now decided to close bars, gyms, cinemas and water parks. This is clearly not full lockdown like Azerbaijan where you can't leave your house for a max 2 hours without getting SMS permission first. It is a token effort (although goes further than Texas and Florida) which might slow the virus but will not supress it.

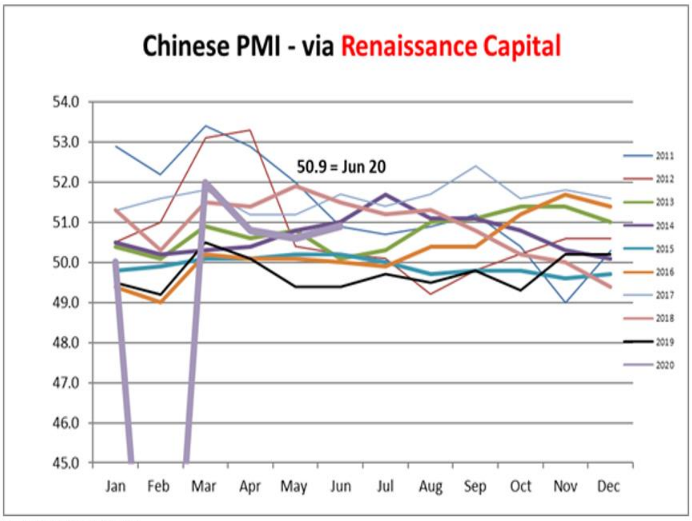
There are now 21 US states where the % of positive tests in the past week are above the cumulative figures. An incredible 24% of all tests in Arizona came back positive in the week and 15% of all tests since the virus began. A 1 in 4 chance of being diagnosed as positive if you get tested ! In New York or New Jersey it is a 1% chance.

The southern US states resisting a return to lockdown are probably looking to Sweden for inspiration. It is interesting that deaths in Sweden in the past week are running at around 200 compared to the peak of around 700 in April, despite a high number of active cases (in the top 10 globally by our estimates).

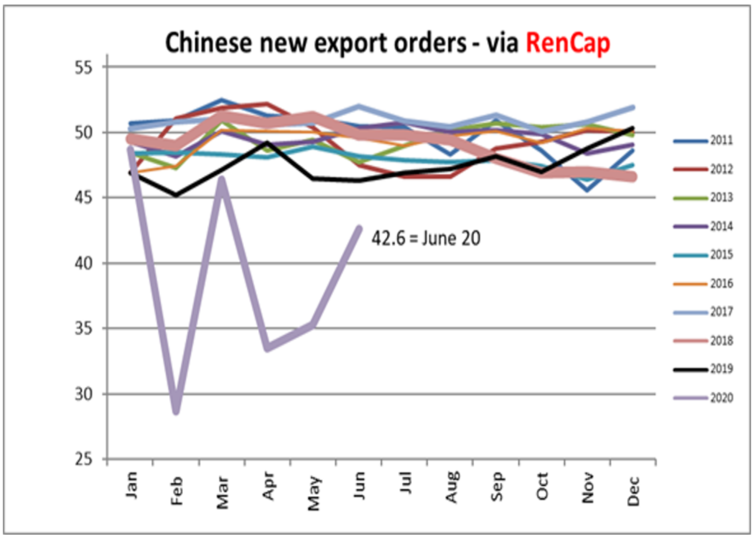
The improvement is obviously far less than Germany or Belgium or the Netherlands, and deaths per capita are 5 times higher than other Scandinavian countries (and above the US) – but Sweden is riding out the virus without ever imposing full lockdown.

As a last point – check Pakistan. Low income countries that drop lockdown are not recording many deaths – except in Latin America so far.

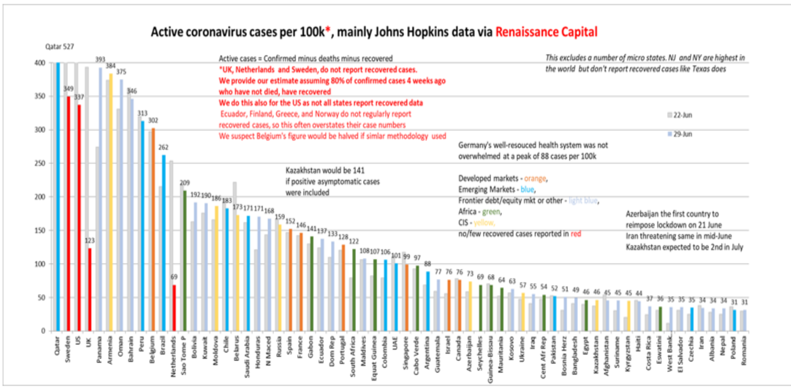
CONCLUSION: China data improving, Kazakhstan following Azerbaijan into lockdown is unexpected but we assume still not a harbinger of what we will see elsewhere … while southern US states are still not showing any serious commitment to suppress the virus. Supporting the economy remains more important.



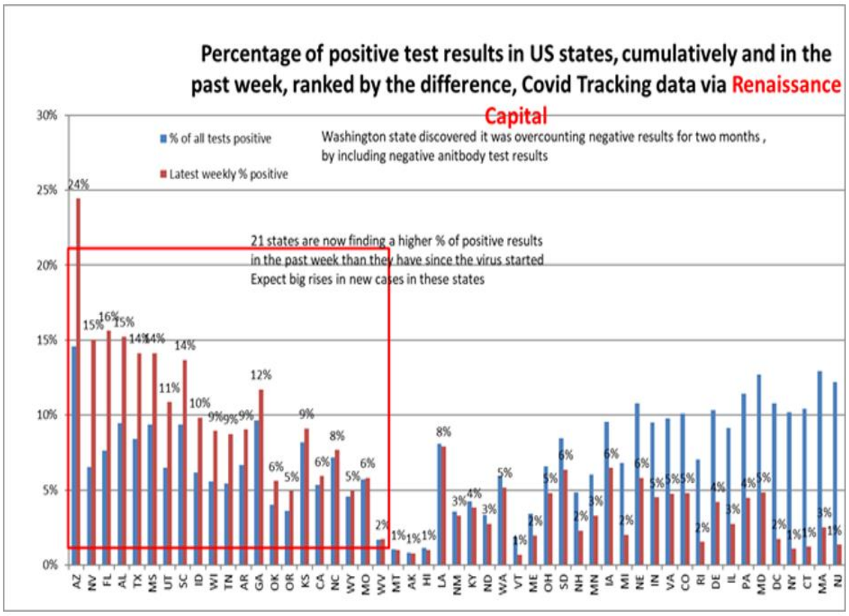
Source: Bloomberg



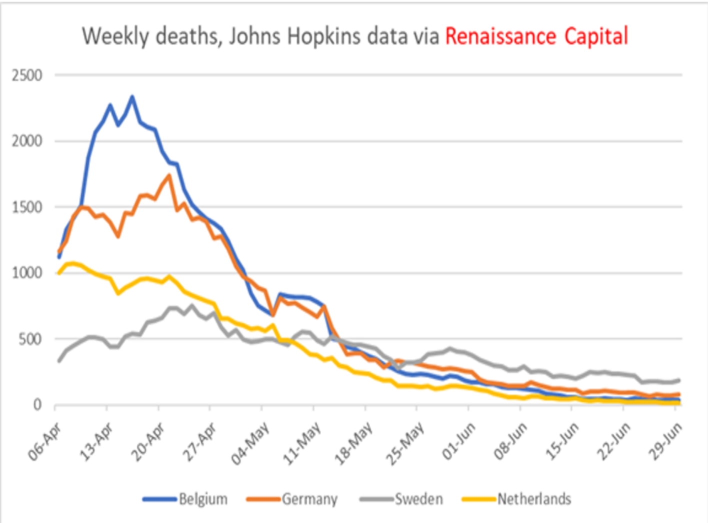
Source: Bloomberg



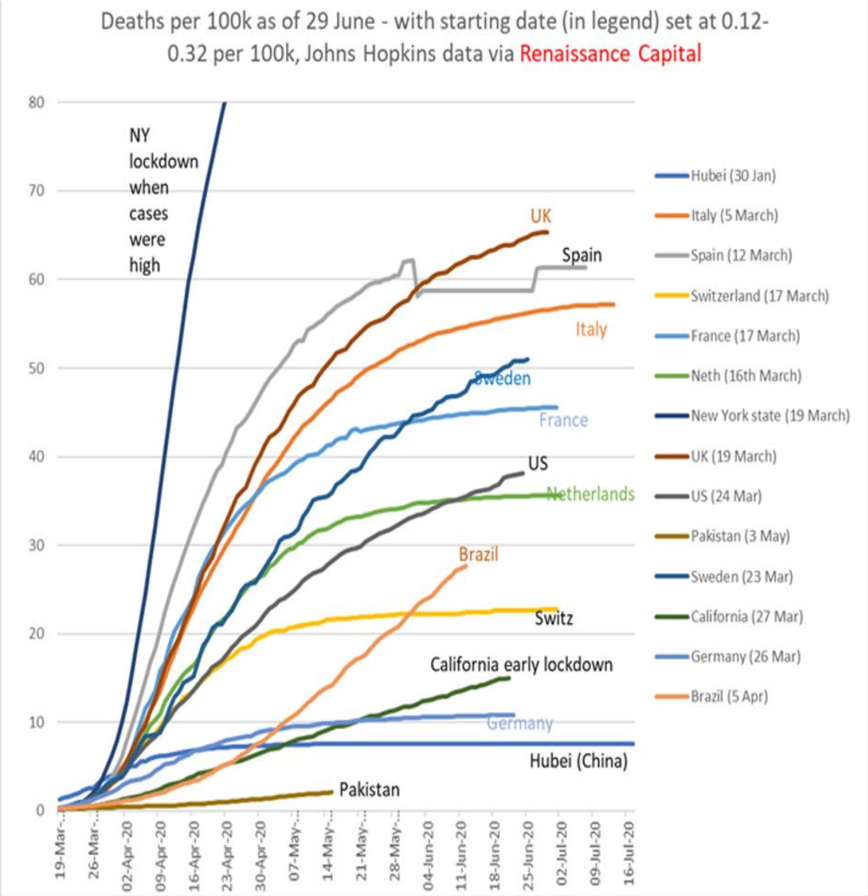
Source: Johns Hopkins



Source: Covid Tracking



Source: Johns Hopkins



Source: Johns Hopkins

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Resilient REIT pre-close update

Ticker: RESJ.J
Rating: **HOLD**
Target price: ZAR44.00
Current price: ZAR44.08

- Resilient REIT (RES) today provided a pre-close update for its financial year ending 30 June 2020. RES says it has offered COVID-19 rental relief (discount to normal rentals) amounting to R160m, and agreement has been reached with more than 90% of tenants about lock-down rentals. We believe our COVID-19 lockdown net rental impact allowance of -R170m looks reasonable.
- Trends it highlighted in its 8 May COVID-19 business update remain in place with non-metropolitan shopping centres trading better than those in metropolitan areas. Value retailers and conveniently located accessible retail centres have been favoured.
- Resilient's retail centres achieved comparable sales growth of -3.2% in the eleven months to May 2020, after increasing 4,7% for the eight months to February 2020. This implies that comparable sales had declined by 24% during the three months from March to May, a good performance in our view given the restrictions on trade during the lockdown.
- Vacancy levels remain low at 2.1% (from 1.9% at 31 Dec) and compares with our 2.0% forecast for FY20.
- RES says it terminated its last remaining cross-currency swap position. We estimate that the termination would have been done at a rand-Euro exchange rate of around 20 (the average prevailing exchange rate the past three months) compared with the 15.7 rand-Euro exchange rate of 31 December 2019. With the exception of the dollar-nominated debt funding its Nigerian properties (and debt in subsidiaries), RES now has no hard currency debt exposure left.
- Please see our May 2020 report for our detailed expectations and views. We have a ZAR44ps TP and **HOLD** rating on RES.

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EU lifts travel ban on Georgia, Morocco, Rwanda, Tunisia, Serbia

The EU lifted the travel ban – on exactly the countries we flagged yesterday (thank you FT subscription for being accurate).

They lifted it on 14 countries – of which five are in our universe – and below are the earnings they make from travel (ie tourism) in the balance of payments as a % of GDP. This is seriously good news for these countries, although we should caveat it for 3 reasons, 1) it requires EU people (or locals of these countries who live in the EU) to want to visit, 2) these are total travel receipts, not just the receipts from EU visitors and 3) the EU travel ban may yet get re-imposed. See below.

Three of those five were lucky – because the EU criteria says it is based on the number of cases in 2 weeks and per 100,000 people as of 15 June; stable or decreasing number of cases; overall response to COVID 19.

But Morocco cases have doubled in a week, Montenegro (also on the list below) has seen cases go up 4 times in a week, Rwanda saw record cases today and Serbia is seeing a bit of a surge too. Only Tunisia is no cause for concern. It's not clear whether the EU might take people off the list in the future.

Morocco flights should accept incoming flights around 10 July I think.

No reason I can see that Mauritius is not on the list. It should be.

This is bad news for Egypt and Turkey – people can choose Tunisia instead.

Global media only cares that the travel ban on the US is not lifted and that it might be lifted on China. I don't see this as game playing by the EU – their methodology makes a lot of sense, although it would have been wiser to include more recent data.

https://www.consilium.europa.eu/en/press/press-releases/2020/06/30/council-agrees-to-start-lifting-travel-restrictions-for-residents-of-some-third-countries/?utm_source=dsms-auto&utm_medium=email&utm_campaign=Council+agrees+to+start+lifting+travel+restrictions+for+residents+of+some+third+countries

Algeria

Australia

Canada

Georgia

Japan

Montenegro

Morocco

New Zealand

Rwanda

Serbia

South Korea

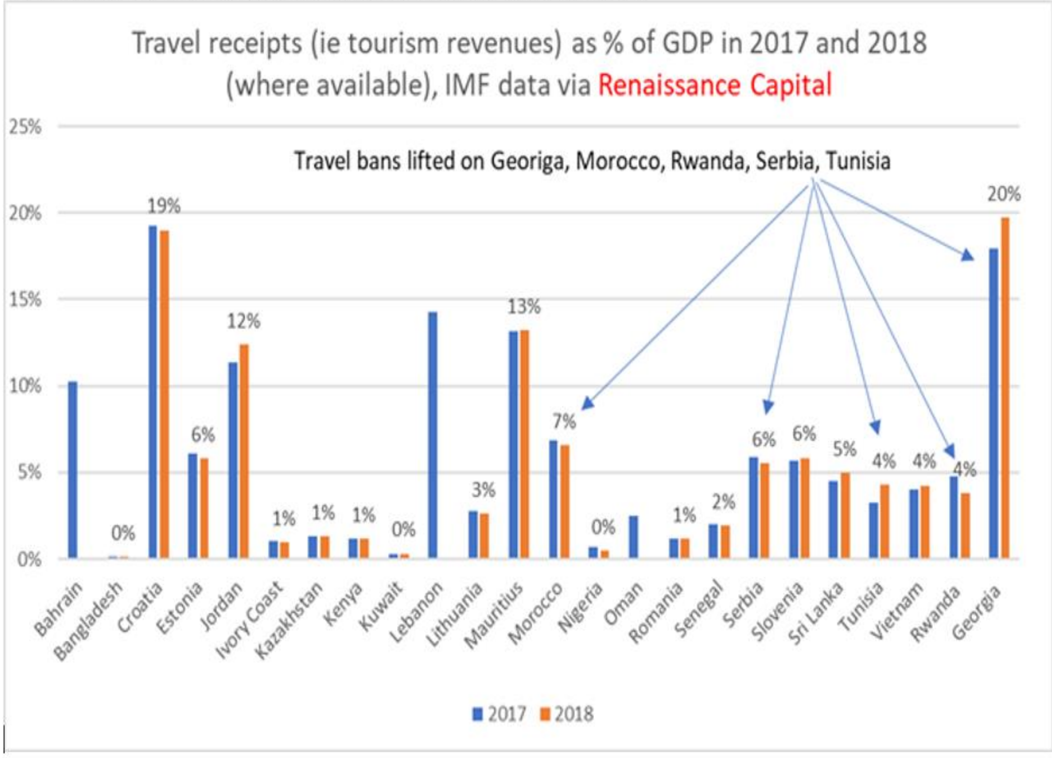
Thailand

Tunisia

Uruguay

China, subject to confirmation of reciprocity

Georgia, Morocco, Rwanda (the only one in SSA), Tunisia, Serbia



Source: IMF data, Rwanda central bank for 2018

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