ARB Holdings Limited
Registration number: 1986/002975/06
Share code: ARH
ISIN: ZAE000109435
(“ARB” or “the company” or “the group”)

Unaudited interim results for the six months ended 31 December 2020

SALIENT POINTS

- Revenue up 5.3% to R1.49bn (2019: R1.42bn)
- Operating profit up 59.2% to R169m (2019: R106m)
- Net profits after tax up 28.9% to R109m (2019: R85m)
- Headline earnings per share (“HEPS”) up 25.9% to 41,12 cents (2019: 32.65 cents)
- In line with past practice, no interim dividend has been declared
- Cash generated by trading activities up 60% to R182m (2019: R114m)
- Net tangible asset value per share up 9.6% to 473.7 cents (2019: 432.4 cents)
- R305m cash on hand (2019: R85m)

The board of directors of ARB (the board) is pleased to present the group’s interim results for the six months ended 31 December 2020 (the period).

NATURE OF BUSINESS

ARB is an investment and property holding company that owns investments in related trading and distribution businesses. Major investment holdings include 74% of ARB Electrical Wholesalers, a level 2 BEE company that operates 20 electrical wholesale branches (June 2020: 22) throughout South Africa, and 60% of Eurolux, which imports and distributes light fittings, lamps and related accessories.

OVERVIEW OF THE PERIOD UNDER REVIEW

Key achievements during the period include significant improvements in operating profit and operating margin. The group’s financial position is robust and its cash flow has been resilient in challenging circumstances. These results demonstrate ARB’s ability to bounce back from adverse trading conditions, such as the Covid-19 lockdowns, and the ability of a highly experienced and skilled management team to reduce the costs of a largely fixed-cost business to maximise the operational leverage from an improvement in revenue and gross margin, resulting in enhanced returns to shareholders.

FINANCIAL REVIEW

The group delivered a strong performance for the period, increasing revenue by 5.3% to R1.49bn (2019: R1.42bn). This was largely due to ARB’s trading despite the effects of the pandemic.

Operating profit also showed substantial improvement, increasing by 59.2% to R169.2m (2019: R106.3m) at an operating margin of 11.3% of revenue (2019: 7.5%). The gross margin increased from 25.1% to 26.5%, mainly attributable to increased margins in both major trading divisions.

Whilst ARB experienced some challenges in its supply chain, both locally and internationally, as a result of the second wave of the pandemic, having stock available proved to be a significant factor in the group's success during this period. While the group, particularly the lighting division, was overstocked at the June financial year end, this proved to be beneficial, not only in terms of having stock on hand, but also because the stock had been acquired at favourable rand/US Dollar prices.

The group is committed to constantly reviewing its operating models and procedures to gain efficiencies and cost savings as market conditions change. Both divisions went through S189A retrenchment processes during the period and have frozen a number of vacant positions.

The new warehouse management system (WMS) at the Lords View distribution centre went live on 14 December 2020 but, as is to be expected, it will take time to settle down and then be optimised. It is estimated that this process will take another six months. The group has been consistent in advising the market that the real benefits of this system will only be effective after June 2021.

Shareholders have been regularly advised that the valuation of the liability of the put options of minority shareholders in Eurolux is volatile, and may increase or decrease significantly in the short term, mainly due to changes in the share price. The put option revaluations are reflected as a significant charge of R20.8m on earnings during the period (in the prior comparative period, this was an income of R6m); resulting in a combined negative change of R26.8m.

These put options are reflected as a current liability of R60m, an increase of 11% over the prior comparative period. This increase in the put option liability, and the associated charge to the income statement, is as a result of the improved earnings of the lighting division, and an increase in the valuation multiple to just over five. As explained previously, when operating profit increases, the put option valuation is likely to have a negative effect on earnings and vice versa. The CraigCor minority put option is exercisable from March 2023, and is reflected as a non-current liability.

The group's earnings per share (EPS) for the six months to December 2020 increased by 24.8% to 41.02 cents per share (2019: 32.87 cents). Headline earnings per share (HEPS) were up by 25.9% to 41.12 cents (2019: 32.65 cents).

The group has net cash on hand of R304.7m (2019: R84.9m), a substantial increase over the prior comparable period of 259%. Cash generation has been very positive during the last six months, partly as a result of the improvement in working capital management, particularly with regards to stock levels in the lighting division; exceptional debtors' collections in the electrical division; cost savings and efficiencies, and of the conscious decision not to pay a dividend at year end to retain cash reserves during the uncertainty of the Covid-19 pandemic.

Management in both divisions have been active in debtors' collections, which mitigated initial concerns about the recoverability of debtors. However, this remains a concern, more particularly in the electrical division, given potential new adverse trading conditions and the reluctance of credit insurers to grant sufficient cover to meet the anticipated increased exposure that will arise on normal supplies to customers.

Credit insurers have actively reduced or withdrawn cover on many of the group’s customers, and they have reduced the percentage of the cover from 90% to 75%, as well as increasing risk premiums substantially. This has predominantly affected the electrical division whose customers are more allied to the construction industry. The hardening of the credit insurance market has necessitated additional calculated credit risk in the electrical division, to support customers’ increasing needs. This has not resulted in any material losses, nor has it affected the IFRS 9 expected credit loss charge for the period.

Net interest received decreased by 0.2% to R2.7m (2019: R2.7m) as a result of the significant decrease in interest rates during the period, offset by increased cash from operations.

ARB continues to take all appropriate actions to protect staff; preserve cash; defend its balance sheet and minimise its operating costs given the current circumstances. All health and safety requirements for the management of people to prevent or restrict Covid-19 transmissions are adhered to in all ARB operations. The stringent adherence to rules for the protection of employees is now a way of doing business at ARB.

The group continued to honour all of its supplier payments on time and in full during this period.

DIVISIONAL REVIEWS

The group is currently organised into three operating divisions, and this is the basis on which the group reports its primary segmental information. Principal activities are as follows:

- **Electrical**: distributors of electrical products across three main categories: power and instrumentation cable; overhead line equipment, and low voltage products;
- **Lighting**: distributors of halogen, fluorescent and energy saving LED lamps; light fittings and electrical accessories, and
- **Corporate**: property investment; specialist IT services; strategic and technical consulting, and group head office companies.

Electrical division: revenue increased by 5.0% and operating profit up 60.9%.

The division comprises ARB Electrical Wholesalers, GMC Powerlines, ARB Global, CraigCor and CED. This division yielded a significant improvement in operating profit, mainly due to an improvement in the gross margin from trading, together with rationalisation and other cost-saving efforts, despite the lack of economic growth or infrastructure development in South Africa, and the lingering effects of Covid-19 and the associated lockdowns.

There was a robust improvement in sales of power cable during the period under review, although this is still below the level that the group is structured to supply due to the lack of infrastructure development in South Africa and increased competition from manufacturers.

The division also experienced supply constraints from local manufacturers during the period as a result of the pandemic and the lockdowns.

Overhead line product sales remain unsatisfactory due to the inconsistent spend by Eskom on electrification projects and the equally sporadic spend on general electrification projects, which have been further hampered as a result of Covid-19, particularly in restricting contractors' staff availability to execute on contracts. Eskom-related work is now a significantly smaller portion of this business, although ARB remains committed to, and is fully capable of, servicing this market when it regains momentum.

Low voltage sales, which have benefitted from the Connect model expansion in prior years, continue to improve and margins are being maintained on these products.

During the period, management undertook a number of right-sizing initiatives: closing two branches, retrenching surplus employees and freezing a number of vacant positions. Other initiatives included:

- assessing each branches footprint with a view to reducing excess space;
- simplifying systems to reduce staff requirements;
- emphasising staff costs and time management, and
- conducting a thorough review of all expenditure and eliminating non-productive costs.

The implementation of the WMS at the Lords View distribution centre in Midrand is also expected to bear fruit by streamlining processes and reducing costs in the future once it is fully and effectively operational.

This division's focus on working capital is commendable and the business remains cash generative.

Lighting division: revenue increased by 5.8% and operating profit by 94.9%
The division comprises Eurolux, Radiant and Cathay Lighting. Profitability improved substantially over prior years largely due to the effects of the rationalisation from the integration of the Eurolux/Radiant facilities in Johannesburg, which is now starting to reflect significant savings.

The restructuring of the division is now finalised, with the right-sizing of the business for the next normal resulting in a substantial reduction in the cost base. This included the rationalisation of the Johannesburg warehouses, retrenchments, and a reduction in contract workers. In addition, transport costs have been put out to tender, which should result in further savings.

While the lighting division was previously overstocked, this position has positively affected the results in the period, and also resulted in a slight increase in market share. The stock has been reduced by almost R90m and is more balanced than at the end of June 2020. However, given the long procurement lead times of this business, stock management will continue to be a major focus.

Corporate division: revenue decreased by 4.9% and operating profit increased by 2.9%
This division comprises the property portfolio and Xact ERP Solutions business. The results are lower than last year as a result of a reduction in rentals received during the lease renewals, but are in line with expectations as a result of Covid-19.

Xact ERP Solutions has generated additional revenue from the warehouse integration project, but this is reversed on the consolidation of the group results. It continues to develop a stand-alone identity relevant to its target market, and to show customer gains, but remains a small revenue and profit generator for the division.

CORPORATE ACTIVITY AND EXPANSION

Acquisitions remain part of the group's growth and expansion strategy and the board is cognisant of opportunities which present themselves. Potential to expand the product base in the electrical division are currently being evaluated, however the immediate focus is to ensure that the warehouse management system project implementation at the Lords View distribution centre is fully functional to generate the envisaged benefits and efficiencies, and to ensure that the integrated Eurolux and Radiant operation continues to runs optimally.

PROSPECTS
Even with the availability of vaccines globally, and the arrival of the first vaccines in South Africa in the first quarter of the 2021 calendar year, the duration and impact of the Covid-19 pandemic on our economy generally, and our customer base in particular, remains hard to determine. It is likely that the biggest challenge will be planning around any possible future waves of the pandemic. It appears that normality in markets and many aspects of daily life will only return in 2022, or thereafter. While the board indicated at the 2020-year end that it would take two to three years for life to normalise, ARB is cognisant of the fact that leading economists believe that it could take 48 months of growth just for the South African economy to revert to 2019 levels.

Fortunately, the return to Level 3 restrictions in December 2020 were not as restrictive from a business perspective, but certainly any Government, Eskom or large project work in South Africa has slowed down substantially, so the visibility for planning purposes remains low.

As mentioned, credit control is facing pressure from credit insurers, who are cutting cover limits, increasing co-insurance levels and charging increased premiums. The latter will aggravate the risk of credit loss to the group and could hamper revenue generation as ARB limits its credit risk exposure. However, the group remains committed to ensuring that it maintains sustainable operations capable of taking advantage of any short- or medium-term improvements in the South African economy.

Furthermore, the group has restructured its cost base to be profitable at these trading levels and this bodes exceptionally well for ARB in the short- to medium-term. ARB is strongly positioned to service the electrical needs of southern Africa, which will provide above average long-term growth and returns, as the continent increases its electricity generation and usage.

ARB has significant financial resources; geographical footprint; distribution capability and a well-established management team that can lead the business into the future.

The information in this report has been extracted from the unaudited condensed consolidated interim financial results, which have not been audited nor reviewed by the company's auditors. This short-form announcement is the responsibility of the directors of ARB.

This short-form announcement is only a summary of the information in the full announcement and does not contain full or complete details. Any investment decision by investors and/or shareholders should be based on consideration of, inter alia, the full announcement.

The full announcement has been released on SENS on 11 February 2020 and is available for viewing on ARB's website (https://arbhold.co.za/index.php/2013-06-04-06-33-35/results) and at https://senspdf.jse.co.za/documents/2021/jse/isse/ARH/ARH022020.pdf.

The full announcement is available for inspection at the offices of ARB (10 Mack Road, Prospecton, Durban, KwaZulu-Natal, 4133) and the offices of the Sponsor, Grindrod Bank Limited (Grindrod Tower, 8A Protea Place, Sandton, 2196), at no charge during normal office hours on business days from 12 February 2020 or may be requested by emailing info@arbhold.co.za.
11 February 2020

Sponsor Grindrod Bank Limited