

23 May 2016

Heads up: Santova FY16 results – Diversification paying off

Share code:	SNV
Share price:	405cps
Market cap:	R630m
Year end:	Feb
Recommendation:	Buy

- **Overview:** Santova recently released positive full year results for their 2016 year end. The results were driven largely by three factors; i.) Recent acquisitions in the UK and Europe, ii.) Currency weakness across the group's blended exposure and iii.) Margin improvement in most of the business segments as a result of back office efficiencies and centralisation of shared services across the group.
- **About Santova:** Santova is an international, end-to-end trade solutions business with a geographic presence in South Africa, United Kingdom, Netherlands, Germany, Australia, Hong Kong and more recently in Ghana and Mauritius. The group's business model is capital light in that it does not own any transport assets or freight equipment, but rather connects customers to shippers and transporters while also supplying value added supply chain solutions, optimisation software, financial risk services and logistics solutions. The group has expanded offshore over the last few years from being a purely SA based business and aims to balance organic growth with bolt-on and strategic acquisitions.
- **FY16 financial highlights:** Revenue increased to R280m (+25% y-o-y), while normalised HEPS (NHEPS) improved to 34cps (+33% y-o-y). Net margins in the SA business improved to 13.9% from 12.8% in the prior period, despite trade volumes in SA declining by 5% y-o-y. Centralisation of back office functions and an improved operational performance offset the decline in volumes, allowing the SA business to show an increase of 16% in net profit after tax (NPAT), despite the macro headwinds. Both the UK and European segments also reported an increase in net margins to 21% (FY15: 18%) and 23% (FY15: 21%) respectively. Management guided that c.75% of the growth in NPAT for the period was due to organic growth while currency gains and acquisitions contributed 14% and 11% respectively.
- **Offshore strategy paying off:** The internationalisation of the business over the last few years has worked well thus far with the group benefitting strongly from *"the portfolio effect"*. The UK segment is expected to contribute c.35-40% of NPAT in the short to medium term, while SA's contribution will normalise at c.30% (FY15: c.40%) over the same period. Net margins and ROE's in the offshore segments are structurally higher than in the SA segment, due to the different funding and competitive dynamics in those regions. Management have guided that the focus going forward will be to capitalise on the integration of these international offices by rolling out their differentiated, cloud based, end-to-end supply chain IT platform across all Santova offices globally. The rollout of the IT platform is expected to be completed in the third quarter of the current calendar year and management expects the platform to be a key differentiator for the group in the international offices.
- **Forecasts and Valuation:** Based on our forecasts, Santova currently trades on a one year forward PE of 11.3x and a forward dividend yield of 1.4%. We expect Santova to deliver a three year annualised return of 12%. Critically, our assumptions include no changes to spot currencies over the forecast period and do not account for potential future acquisitions.
- **Investment case and recommendation:** Santova is a capital light, highly cash generative, scalable business operating in a highly fragmented industry and which is also diversified across geographies, currencies and industries. The business continues to internationalise thereby adding volumes and also allowing existing customers access to new trade routes. The management team appears to be relatively conservative and own c.15% of the business.

Notwithstanding the macro risks which the business faces, the economics of the business remains attractive. Although our base case expected return is 12%, the conservative assumptions baked in to our valuation gives us comfort to warrant a buy recommendation. Buyers attention is however drawn to the sensitivity of the expected return to currency fluctuations, assuming our base case

scenario materialises: a 10% stronger GBPZAR decreases our expected return by 4%, while a 10% stronger EURZAR decreases our expected return by 2%.

- **Risks to the recommendation:** Risks include (i) significant deterioration in trade volumes in the various geographies (ii) SA currency strength relative to the Pound and Euro, (iii) Britain leaving the European Union (“*Brexit*”) and (iv) increase in bad debts for the portion of the business where Santova finances customer orders.

Zaeem Kumandan

Investment Team

Nedbank Private Wealth

The analyst does not have a beneficial interest in the company	<input type="checkbox"/>
The analyst holds a direct beneficial interest in the company	<input checked="" type="checkbox"/>
The analyst holds an indirect beneficial interest in the company	<input type="checkbox"/>

This communication has been issued for internal purposes only by Nedgroup Private Wealth (Pty) Limited trading as Nedbank Private Wealth (“the Company”), and its subsidiaries, and is proprietary to the Company. If forwarded, distributed or transmitted to any person other than an employee of the Company, such transmission is for objective and general information purposes only and the information contained therein should not be relied upon by the recipient as financial advice. Any recipient seeking financial advice is strongly urged to contact an authorised representative of the Company. This communication may not be reproduced in whole or in part without the permission of the Company. The information contained herein has been obtained from sources which and persons whom we believe to be reliable but is not guaranteed for accuracy, completeness or otherwise. All opinions expressed and recommendations made are subject to change without notice. The portfolio holdings of the Company and its employees may from time to time include securities mentioned herein.