Initiation of Coverage
13 April 2021

THE TRELLIDOR GROUP

Trellidor Holdings Ltd
Compounder with Yield & Tailwinds

Share Code: TRL – Market Cap: R333m – PE: 18.4x – DY: 2.3%

12m Target Price	**532cps**
Share Price	**345cps**
Implied Return	**54%**

Industrials | South Africa

Business Overview: Leveraging Product, Route-to-Market & Returns

- Trellidor's traditional business of customized manufacturing of security gates for a national, African and export network of franchisees remains strong while management's addition of innovative & complementary products (including Taylor blinds and shutters, and NMC) is logical and steadily gaining traction.
- The Group is cash generative and management's careful capital allocation into the acquisition of (some) the main regional franchisee, share buy-backs below fair value & degearing the Group's balance sheet while paying dividends should all add to the Group's financial performance and shareholder returns.

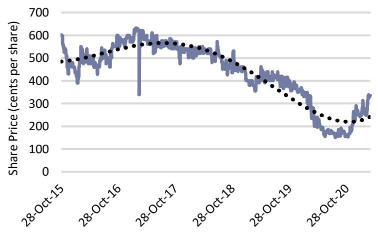
Macro Environment: Home Improvement Tailwinds

- While high domestic real rates had depressed residential property and home improvement markets, the South African Reserve Bank's strongly accommodative monetary response to COVID-19 has reversed this trend with exciting implications.
- Building materials, home improvement sales and the residential property markets have all positively responded to this and, in many instances, are trading at-or-above their pre-COVID levels.
- Despite numerous domestic & global macro risks remaining, Trellidor should be a beneficiary of these home improvement & residential property market tailwinds.

Forecast, Valuation and Implied Return: Undervalued & Yielding

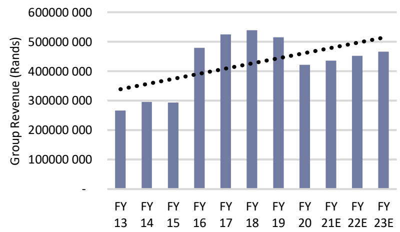
- Given a reasonableness check against our implied EV/EBITDA regression, our DCF Model indicates that Trellidor is worth c.442cps or a c.8.8x PE and c.4.4x EV/EBITDA against our expected FY 21E earnings. These valuation metrics appear quite undemanding of a Group with a 5-year average ROE of >20% and a Free Cash Flow/EV Yield just shy of 18%.
- Rolling 442cps forward by our CoE, we arrive at a 12m TP of 532cps implying a 54% return from the current share price.
- Even if the market never fully reflects this valuation, it is worth noting that the share's attractive c.6.0~7.0% Dividend Yield also makes this compounder a good yield play.

Trellidor – Share Price Since Listing



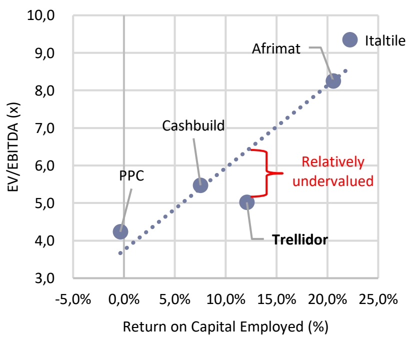
Sources: Profile Media & Blue Gem Research

Trellidor – Group Revenue



Sources: Trellidor & Blue Gem Research

Home Improvement & Build Materials Stocks: EV/EBITDA (x) versus ROCE (%) Relationship



Sources: Various Company Reports, Profile Media, Iress & Blue Gem Research workings & assumptions

Key Forecast (Rm)	FY 19A	*YoY %*	FY 20A	*YoY %*	H1:21A	FY 21E	*YoY %*	FY 22E	*YoY %*	FY 23E	*YoY %*
Revenue	515	*-4%*	422	*-18%*	282	523	*24%*	543	*4%*	559	*3%*
EBITDA	81	*106%*	12	*-85%*	58	99	*723%*	107	*8%*	111	*4%*
HEPS (cps)	**40,1cps**	***-26%***	**13,8cps**	***-66%***	**30,6cps**	**50,2cps**	***>100%***	**61,3cps**	***22%***	**65,5cps**	***7%***
Return on Equity (%)	*19,4%*	-	*-17,6%*	-	*16,4%*	*27,5%*	-	*28,7%*	-	*26,7%*	-
Price Earnings Ratio (x)	8,6x	-	25,0x	-	18,4x	6,9x	-	5,6x	-	5,3x	-
DPS (cps)	20,2cps	*-26%*	8,0cps	*-60%*	10,0cps	25,1cps	*>100%*	30,6cps	*22%*	32,7cps	*7%*
Dividend Yield (%)	*5,9%*	-	*2,3%*	-	*5,8%*	*7,3%*	-	*8,9%*	-	*9,5%*	-

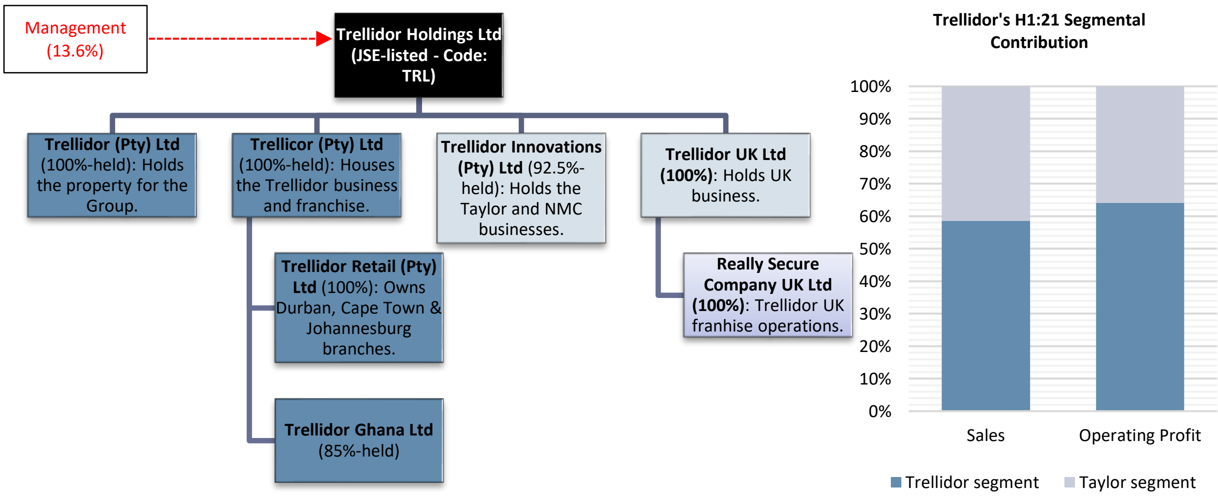
Sources: Trellidor Holdings, Iress, Profile Media, Bloomberg, and various Blue Gem Research assumptions & workings

Key Forecast (Rm)	FY 19A	YoY %	FY 20A	YoY %	H1:21A	FY 21E	YoY %	FY 22E	YoY %	FY 23E	YoY %
Revenue	**515**	***-4,5%***	**422**	***-18,1%***	**282**	**523**	***24,0%***	**543**	***3,8%***	**559**	***2,9%***
Trellidor	323	*-2,7%*	257	*-20,4%*	165	331	*28,8%*	343	*3,6%*	350	*2,2%*
Taylor	191	*-8,5%*	165	*-13,6%*	117	192	*16,4%*	200	*4,2%*	209	*4,2%*
Gross Profit	**232**	*-5,7%*	**176**	*-24,3%*	**126**	**236**	*34,3%*	**245**	*3,8%*	**252**	*2,8%*
Gross Profit Margin (%)	*45,0%*	-	*41,6%*	-	*44,6%*	*45,1%*	-	*45,1%*	-	*45,0%*	-
Operating expenses	-171	*6,0%*	-194	*13,4%*	-82	-162	*-16,7%*	-164	*1,4%*	-167	*1,9%*
EBITDA	**81**	*106%*	**12**	*-85%*	**58**	**99**	***723%***	**107**	*8%*	**111**	*4%*
EBITDA Margin (%)	*15,7%*	-	*2,8%*	-	*20,6%*	*18,9%*	-	*19,6%*	-	*19,9%*	-
Net Profit (Parents)	**43**	***-28%***	**-28**	***-165%***	**30**	**50**	***>100%***	**59**	***20%***	**63**	***6%***
*Issued Shares (millions)**	*105,8*	*-2,4%*	*100,2*	*-5,3%*	*98,0*	*97,0*	*-3%*	*96,1*	*-1,0%*	*95,1*	*-1,0%*
*Weighted Ave. Number of Shares (millions)**	*107,2*	*-0,7%*	*102,4*	*-4,5%*	*99,3*	*98,6*	*-4%*	*96,5*	*-2,1%*	*95,6*	*-1,0%*
EPS (cps)	**40,0cps**	*-28%*	**-27,2cps**	*-168%*	**30,6cps**	**50,2cps**	*>100%*	**61,3cps**	*22%*	**65,5cps**	*7%*
HEPS (cps)	**40,1cps**	*-26%*	**13,8cps**	*-66%*	**30,6cps**	**50,2cps**	*>100%*	**61,3cps**	*22%*	**65,5cps**	*7%*
Price Earnings Ratio (x)	*8,6x*	-	*25,0x*	-	*18,4x*	*6,9x*	-	*5,6x*	-	*5,3x*	-
Dividend Per Share (cps)	**20,2cps**	*-26%*	**8,0cps**	*-60%*	**10,0cps**	**25,1cps**	*>100%*	**30,6cps**	*22%*	**32,7cps**	*7%*
Dividend Yield (%)	*5,9%*	-	*2,3%*	-	*5,8%*	*7,3%*	-	*8,9%*	-	*9,5%*	-
Dividend Cover (x)	*2,0x*	-	*1,7x*	-	*3,1x*	*2,0x*	-	*2,0x*	-	*2,0x*	-
Property, Plant & Equipment	65	*6%*	57	*-12%*	58	59	*4%*	58	*-1%*	58	*0%*
Intangible Assets	113	*-3%*	83	*-27%*	90	41	*-51%*	38	*-8%*	33	*-13%*
Current Assets	182	*-8%*	177	*-3%*	189	211	*19%*	300	*42%*	282	*-6%*
Current Liabilities	106	*19%*	90	*-15%*	90	85	*-6%*	124	*81%*	69	*-44%*
Cash	13	*-54%*	23	*86%*	34	65	*180%*	70	*8%*	75	*7%*
Interest-bearing Liabilities	83	*-11%*	106	*29%*	108	89	*-16%*	89	*0%*	89	*0%*
Net Debt	70	*6%*	83	*18%*	74	24	*-72%*	-60	*-357%*	-37	*-38%*
Net Debt:Equity (%)	*32%*	-	*52%*	-	*40%*	*13%*	-	*-29%*	-	*-16%*	-
Net Debt: EBITDA (x)	*0,9x*	-	*6,9c*	-	*0,6c*	*0,2c*	-	*-0,6c*	-	*-0,3c*	-
Shareholder's Equity (Parent)	221	*4%*	159	*-28%*	185	180	*13%*	206	*15%*	234	*14%*
NAV per share (cps)	208,9	*6%*	158,4	*-24%*	189,2	185,3	*17%*	214,5	*16%*	246,1	*15%*
TNAV per share (cps)	101,6	*15%*	75,9	*-25%*	97,8	143,3	*89%*	175,4	*22%*	209,9	*20%*
Price-to-Book (x)	*1,7x*	-	*2,2x*	-	*1,8x*	*1,9x*	-	*1,6x*	-	*1,4x*	-
Price-to-Tangible-Book (x)	*3,4x*	-	*4,5x*	-	*3,5x*	*2,4x*	-	*2,0x*	-	*1,6x*	-
Free Cash Flow (post-capex)	30	*<100%*	-12	*<100%*	37	62	*>100%*	61	*-1%*	64	*5%*
Enterprise Free Cash Flow Yield (%)	***7,7%***	**-**	***-2,9%***	**-**	***18,4%***	***17,8%***	**-**	***23,2%***	**-**	***22,5%***	**-**
Cash Conversion Ratio (%)	*38%*	-	*-98%*	-	*63%*	*63%*	-	*57%*	-	*58%*	-
Return on Equity (%)	***19,4%***	**-**	***-17,6%***	**-**	***16,4%***	***27,5%***	**-**	***28,7%***	**-**	***26,7%***	**-**
Return on Capital Employed (%)	*26,9%*	-	*-3,4%*	-	*33,8%*	*29,9%*	-	*29,5%*	-	*28,1%*	-
Return on Assets (%)	*11,9%*	-	*-7,2%*	-	*17,1%*	*15,0%*	-	*14,3%*	-	*16,1%*	-

*Sources: Trellidor Holdings, Bloomberg, Iress, Profile Media, Blue Gem Research workings, assumptions, and forecasts; * We have assumed that 1% of the Group's issued share capital is bought back evenly throughout each of the forecast years.*

Group Overview

Figure 1: Summarised Group Structure & Segmental Contribution



Sources: Trellidor Holdings and Blue Gem Research workings

Trellidor Holdings Ltd's (code: TRL) group structure (Figure 1) is clean with the only material minority leakage in the Taylor and NMC businesses (7.5% minorities). Furthermore, sales synergies have and continue to flow across these two businesses and Trellidor's traditional business, as Taylor/NMC products start to gain traction in other provinces (it has always been strong in the Western Cape) and with Trellidor franchisees (Figure 5).

While the above Group structure shows the operating entities, it is important to appreciate that Trellidor also operates as a franchisor. Thus, in many instances, the final route-to-market involves a regional franchisee for both the sales and installation service. Indeed, the Group's manufacturing premises servicing the network does not carry finished good stock and only manufacturers the end-product upon receiving an order. This extensive franchise network and the Group's agile and flexible manufacturing operations are competitive advantages.

Recently, the Group has begun a strategy of buying-back franchises in major regions (outlying areas will not be acquired). This is not just accretive to margins but the Group is finding that they can also drive a higher sales run-rate with the reinvigorated and re-incentivized sales staff at these branches.

Table 1: Summarised Corporate Governance Checklist

Corporate Governance Aspect	In Place?	Comment
External auditors?	Yes	Trellidor's external auditor is Mazars. The latest audited results (FY 20) saw them publish an unqualified report. They have been the Group's auditors since it listed in 2015.
Internal audit function?	Yes, outsourced.	The Board considers it cost-effective to outsource the internal audit function to PKF Durban and PKF Cape Town. The Chairman has direct access to the internal auditors.
Appropriate management incentives?	Yes	Directors hold c.13.66m shares in Trellidor (c.13.6% of the share capital), thus strongly aligning them with shareholders. Executive directors earned R7.7m remuneration in FY 20 or c.2% of the Group's market capitalisation. Non-executives earned R0.9m or c.0.2% of the Group's market capitalization. Collectively, the Board earned c.2.6% of the Group's market capitalisation or c.2% of FY 20 revenues. Finally, management have long- and short-term incentives in place that—other than qualitative factors—revolve around achieving EBIT and ROIC (hurdle of 12%) targets. We would prefer a *per share* measure to be included but highlight the large shareholding held by executives as effectively achieving this. Thus, given the Group's lowly-valued share (i.e. inflating the remuneration as a % of market cap.) and the Board's large shareholding, we believe that management is appropriately remunerated and comfortably aligned with shareholders.
Independent non-executive Chairman?	Yes	Mark Cyril Olivier is the independent non-executive Chairman. He has been a non-executive director of Dynasty Group based in China and owned by Macquarie Bank and Blackstone Inc. He was Chairman of Rockcastle, a real estate company investing in Eastern Europe. He is a non-executive director of Greenbay Properties Limited, listed in both SA and Mauritius and is Chairman of African Rainbow Capital Investments, listed on the JSE.
Balance of non-executives on the Board?	Yes	There are three non-executive directors and two executives that compose the Board.

Sources: Company FY 20 AFS and Blue Gem Research

Overall, we are comfortable with the Group's governance, structure and underlying portfolio.

Trellidor Segment

With a well-established and trusted brand in the security gate industry (Figure 8), Trellidor runs a Durban-based flexible manufacturing operation that efficiently supplies orders-to-fit for its branch and franchise network. Its product range and business model have the following key fundamentals in place:

- **Security**: South Africa's crime rate remains high and creates a strong demand for residential security spending. An element of this spend is security doors, windows and other barriers but with these functional spaces retaining both their utility and their aesthetics.
- **Home improvement**: The same underlying demand drivers that see residential property owners investing in home improvement drives the demand for Trellidor's range. In many instances, these sales and home improvement decisions are made at or around the time that homeowners move *into* a newly acquired/built house. Therefore, a healthy underlying and liquid residential property market is a key demand driver of Trellidor's product range.
- **Steel price**: Steel (and, thus, iron ore) is a large raw material input into the production of most of Trellidor's product range (makes up c.29% of Cost of Sales). While it does not need to be sourced locally (the Group has import supply chains in place), either a large spot movement or a shortage of global supply may negatively impact these margins. That said, this business's Gross Profit Margin averages 48.6% since FY 13 and, thus, it has a lot of room to absorb such an increase *and* the product range has demonstrated sufficient pricing power to pass input-cost inflation onto customers.

The Group's traditional security gate products continue to sell well, though management has consciously fed new and innovative products into their route-to-market. Figure 2 clearly shows how successful the strategy to layer more *types* of products into the Group's franchise/branch network has been. We expect this conscious product range expansion to continue, adding incremental volumes, margin and diversification. Indeed, the acquisition of the Taylor and NMC businesses form part of this with their blinds, shutters, cornices and skirting product ranges slotting neatly into the existing route-to-market.

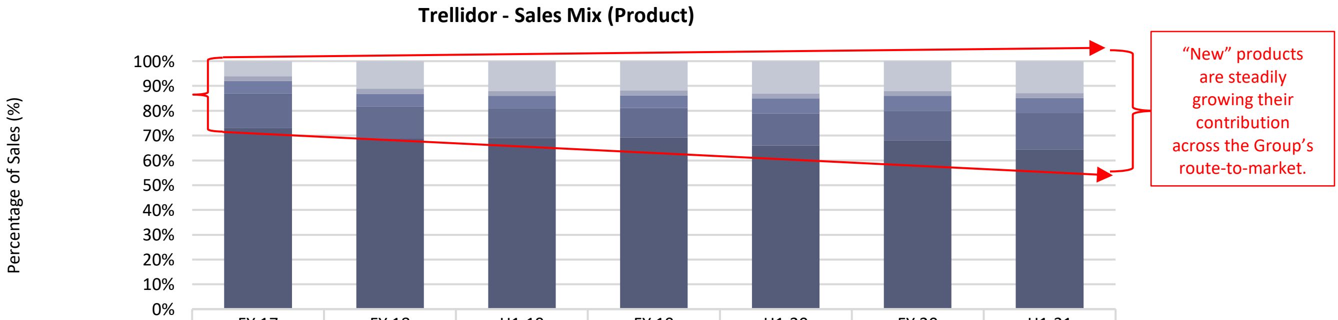
Figure 2: Snapshot of Some of Trellidor's Key Barrier Products, Sales Mix & Trends

Security Shutters

Rollerstyle Shutters

Clear Guard

Traditional Security Gates



	FY 17	FY 18	H1:19	FY 19	H1:20	FY 20	H1:21
Security Shutter	6%	11%	12%	12%	13%	12%	13%
Polycarbonate Bar	2%	2%	2%	2%	2%	2%	2%
Rollerstyle	5%	5%	5%	5%	6%	6%	6%
Clear Guard	14%	13%	12%	12%	13%	12%	15%
Traditional Trellidor	73%	68%	69%	70%	66%	68%	65%

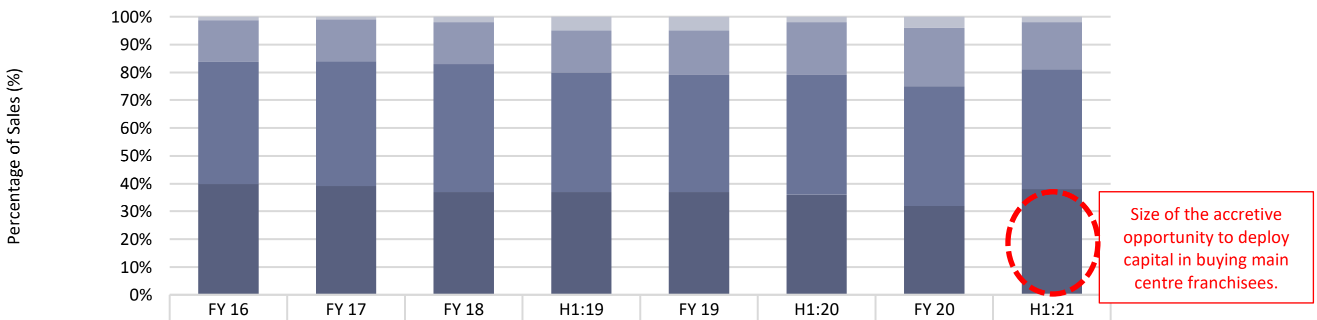
Source: Trellidor website, various Trellidor documents & Blue Gem workings & assumptions

During H1:21, management successfully concluded the acquisitions of franchisees in Durban, Johannesburg West and the United Kingdom. Interestingly, management has found that these acquisitions are not just accretive but that the operations can often be reinvigorated and see substantially sales growth (+27.5% y/y during H1:21) as operations are tidied, better incentives for sales staff are put in place and "lifestyle" businesses are professionalized.

Therefore, the Group is exploring buying-back more franchise operations in major regions (they will not pursue this strategy in outlying regions). This strategy will be opportunistic and where an existing franchisee either does not want to sell or is not struggling, the Group should keep the status *quo*.

We note this as a unique business driver but have not forecast any acquisitions in this space. If any were to occur, we would consider them highly likely to be accretive and create upside-risk to our forecasts. Given that Trellidor's main centres make up 38% of its revenue, this could generate material upside going forward.

Figure 3: Trellidor's Regional Sales Split



	FY 16	FY 17	FY 18	H1:19	FY 19	H1:20	FY 20	H1:21
UK & Israel	1%	1%	2%	5%	5%	2%	4%	2%
Africa	15%	15%	15%	15%	16%	19%	21%	17%
Outlying Regions	44%	45%	46%	43%	42%	43%	43%	43%
Main Centers	40%	39%	37%	37%	37%	36%	32%	38%

Sources: Trellidor and Blue Gem Research workings

In Table 2, we show our segmental forecast and, further, how it pushes down to a segmental-level Discounted Free Cash Flow (DCF) valuation. Other than discount rates and related assumptions (refer to the "Valuation" section for details on these), we have assumed the following in this segment:

- FY 21E catching up on the 10-weeks of lost sales in FY 20 with tailwinds into FY 23E,
- Medium-term sales growth of +1.8% y/y,
- Cost-savings in FY 20/H1:21 flow through to FY 21E and FY 22E while inflation runs at 3.2% y/y,
- A steady Gross Margin is held of 48.6% and the steel price remains flat for the forecast period, &
- Capex averages 2.5% of sales while net working capital averages 16.5%.

Table 2: Trellidor Segmental Forecast & Discounted Free Cash Flow (DCF) Model

(Rm)	FY 20	H1:21	FY 21E	H2:21E	FY 22E	FY 23E	FY 24E	FY 25E	FY 26E	FY 27E	FY 28E
Revenue	257	165	331	-	343	350	356	363	369	376	379
Revenue (%)	*-20,4%*	*3,5%*	*4,0%*	-	*3,6%*	*2,2%*	*1,8%*	*1,8%*	*1,8%*	*1,8%*	*0,9%*
Gross Profit	119	80	161	-	167	170	173	176	180	183	184
Gross Profit Margin (%)	*46,2%*	*48,5%*	*48,6%*	-	*48,6%*	*48,6%*	*48,6%*	*48,6%*	*48,6%*	*48,6%*	*48,6%*
Operating Profit	35	31	64	-	68	70	70	70	69	71	71
EBITDA	42	36	72	-	77	79	80	80	80	81	82
Tax	-10	-9	-17	-	-18	-19	-19	-19	-19	-19	-19
Working Capital	9	3	10	-	-2	-1	-1	-1	-1	-1	-1
Capex	-9	-5	-8	-	-9	-9	-9	-9	-9	-9	-9
Free Cash Flow (FCF)	32	25	57	32	48	51	51	51	51	51	52
Discount Rate	-	-	-	*0,95*	*0,85*	*0,76*	*0,68*	*0,61*	*0,54*	*0,49*	*0,43*
Discounted FCF	-	-	-	30	41	38	35	31	28	25	209
Enterprise Value (EV)											**R437m**
EV/EBITDA (x)											**6,1x**

Sources: Bloomberg, Blue Gem Research and Trellidor Holdings

Taylor Segment

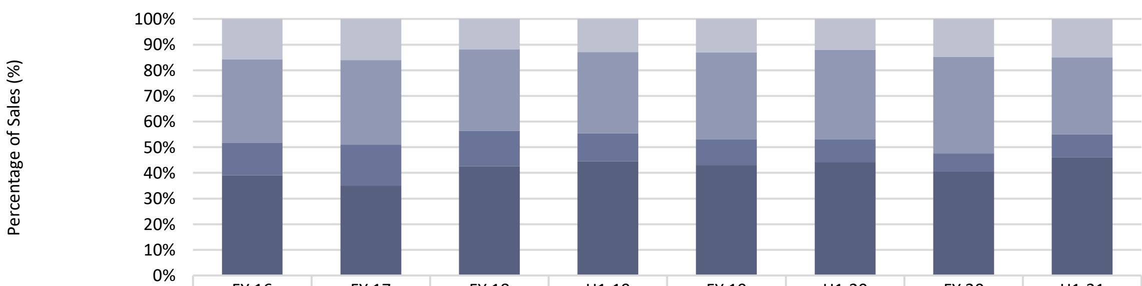
Similar to Trellidor, Taylor's range of blinds, shutters, cornices and skirtings (Figure 4) appeal to home improvement demand. While the security element noted in Trellidor's product is less central here, Taylor and NMC do see product demand driven by similar factors to Trellidor. Indeed, this was partly the rationale for acquiring the Taylor and NMC businesses (a 92.5%-stake in the business was acquired at a 5.7x Price Earnings for c.R148m during 2016) as their product range cross-sells into the existing Trellidor sales network. Taylor and NMC were both predominantly Western Cape businesses and, thus, benefited from access to an extensive national, African and, even, export sales network.

Figure 4: Snapshot of Some of Taylor/NMC's Key Products, Sales Mix & Trends

NMC (Cornices & Skirting)

Taylor (Aluminium Blinds & Shutters)

Taylor - Sales Mix (Product)

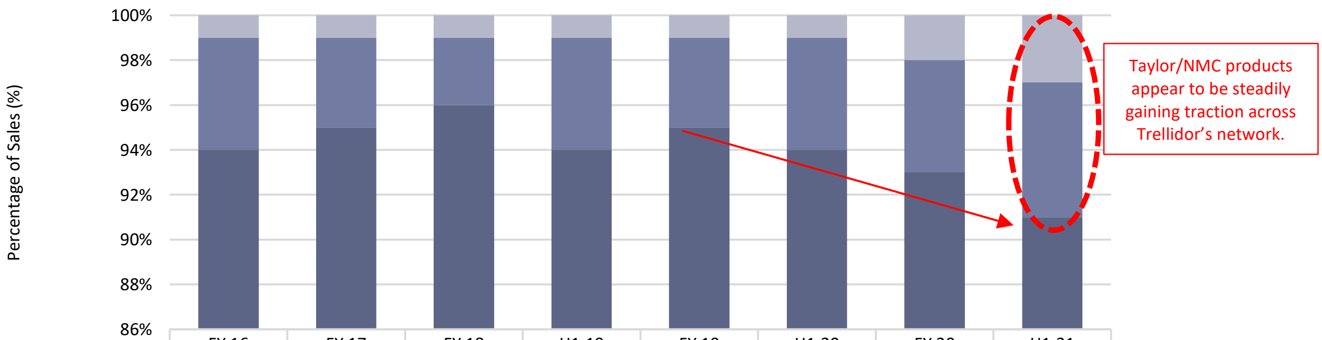


	FY 16	FY 17	FY 18	H1:19	FY 19	H1:20	FY 20	H1:21
NMC	16%	16%	12%	13%	13%	12%	15%	15%
Blinds	33%	33%	32%	32%	34%	35%	38%	30%
PVC Shutters	13%	16%	14%	11%	10%	9%	7%	9%
Aluminium Shutters	39%	35%	43%	45%	43%	44%	41%	46%

Source: Taylor & NMC websites, various Trellidor documents & Blue Gem workings & assumptions

As can be seen in Figure 5, Taylor's regional sales split is improving in non-Western Cape (i.e. Main Centres) regions as growing acceptance of its product range starts to permeate existing Trellidor routes-to-market.

Figure 5: Taylor's Regional Sales Split



	FY 16	FY 17	FY 18	H1:19	FY 19	H1:20	FY 20	H1:21
International	1%	1%	1%	1%	1%	1%	2%	3%
Outlying Regions	5%	4%	3%	5%	4%	5%	5%	6%
Main Centers	94%	95%	96%	94%	95%	94%	93%	91%

Sources: Trellidor and Blue Gem Research workings

In Table 3, we show our segmental forecast and, further, how it pushes down into a segmental-level Discounted Free Cash Flow (DCF) valuation. Other than discount rates and related assumptions (refer to the "Valuation" section for details on these), we have assumed the following in this segment:

- FY 21E catching up on the 10-weeks of lost sales in FY 20 with tailwinds into FY 23E,
- Cost-savings in FY 20/H1:21 flow through to FY 21E and FY 22E,
- Inflation of 3.2% y/y in the medium-term,
- A steady Gross Margin is held of 39.0% and the steel price remains flat for the forecast period, &
- Capex averages 2.0% of sales while net working capital averages 22.3%.

Table 3: Taylor Segmental Forecast & Discounted Free Cash Flow (DCF) Model

(Rm)	**FY 20**	**H1:21**	**FY 21E**	**H2:21E**	**FY 22E**	**FY 23E**	**FY 24E**	**FY 25E**	**FY 26E**	**FY 27E**	**FY 28E**
Revenue	165	117	192	-	200	209	217	226	236	246	248
Revenue (%)	*-13,6%*	*1,4%*	*16,4%*	-	*4,2%*	*4,2%*	*4,2%*	*4,2%*	*4,2%*	*4,2%*	*0,9%*
Gross Profit	60	45	75	-	78	81	85	88	92	96	97
Gross Profit Margin (%)	*36,5%*	*38,9%*	*39,0%*	-	*39,0%*	*39,0%*	*39,0%*	*39,0%*	*39,0%*	*39,0%*	*39,0%*
Operating Profit	-40	15	19	-	22	25	26	28	30	33	32
EBITDA	-26	22	29	-	32	35	36	38	40	42	41
Tax	-13	-3	-6	-	-4	-5	-5	-6	-6	-7	-7
Working Capital	2	-2	-1	-	-2	-2	-2	-2	-2	-2	-0
Capex	-3	-5	-8	-	-4	-4	-4	-5	-5	-5	-5
Free Cash Flow (FCF)	-40	11	14	2	22	24	25	26	27	28	29
Discount Rate	-	-	-	*0,95*	*0,85*	*0,76*	*0,68*	*0,61*	*0,54*	*0,49*	*0,43*
Discounted FCF	-	-	-	2	19	18	17	16	15	13	114
Enterprise Value (EV)											**R214m**
EV/EBITDA (x)											**5,0x**

Sources: Bloomberg, Blue Gem Research and Trellidor Holdings

Group Segment

Trellidor Holdings' Group segment includes HoldCo and listing costs, the management of the treasury function and it further receives management fee income.

In analysing this segment, we have attempted to build a net present value (NPV) based on historical representation. While this segment can make a profit, our NPV is negative, implying a discount should be taken out of the Group's sum-of-the-parts (SOTP) valuation.

We have assumed a standard 3.2% y/y inflation rate and allowed management fee income to track Group income upwards. We have pushed finance costs through this segment before consolidating it into the Group results.

Finally, as we have done with other groups that own underlying properties, we have not valued these separately and consider the yield it generates (or would generate, if externally tenanted) as being captured in the respective margins of each business and the broader Group.

Macro-economic Environment & Industry Snapshot

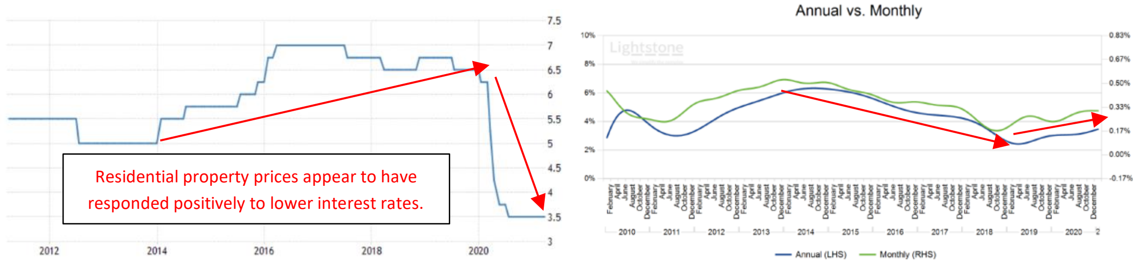
It should be well-known by the reader how the COVID-19 pandemic and related lockdowns have hampered both global and domestic economic growth. Therefore, we will not revisit this topic but attempt to look through the noise in understanding how the current macro-environment may be affecting the broader building materials/home improvement industry and, specifically, Trellidor.

A key sales-driver of home improvement sales and Trellidor's specific product range is a buoyant residential property market. New builds and move-ins in the residential property market can trigger homeowners to spend on blinds, shutters, security gates and related products from Trellidor's portfolio.

Following several years of high and rising (real) rates in South Africa, the response of the South African Reserve Bank's (SARB) to the pandemic was an aggressive cutting of its central repurchase (repo) rate. If one views this concurrently with the fact that residential property price growth was steadily slipping until this monetary response last year and that residential property price growth has now started to pick up, it is relatively clear that interest rates are an important driver of the residential property market.

Figure 6: Falling Repo Rate & Rising Private Property Market Appear Correlated (10-year views)

South African Reserve Bank's Repurchase Rate ("repo rate") **Lightstone Residential Property Price Index**



Sources: South African Reserve Bank, Lightstone Properties & Blue Gem Research workings

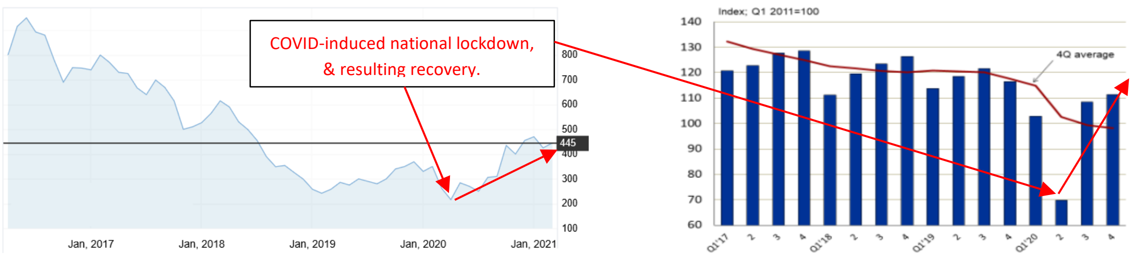
Since 2020, the SARB has kept the repo rate flat at 3.5% and, although its model guides to two 25bps hikes later this year, inflation remains persistently low and there is a good chance that these hikes get pushed out later into 2022/23.

All of this bodes well for residential property and, thus, implies positive demand-pull for Trellidor's products through its various sales channels and routes-to-market.

As a secondary check to the above narrative, in Figure 7, you can see the strong recovery in both Balwin Properties (as a proxy for the entry-level to mid-range residential property market) and Afrimat's Construction Index (a broader building materials, construction and fixed capital formation measure).

Figure 7: Anecdotal Indicators of Strong Private Property Recovery & Recovering Construction Markets

Balwin Properties Share Price Back at Pre-COVID Levels **Afrimat Construction Index Above Q1:20 Levels**



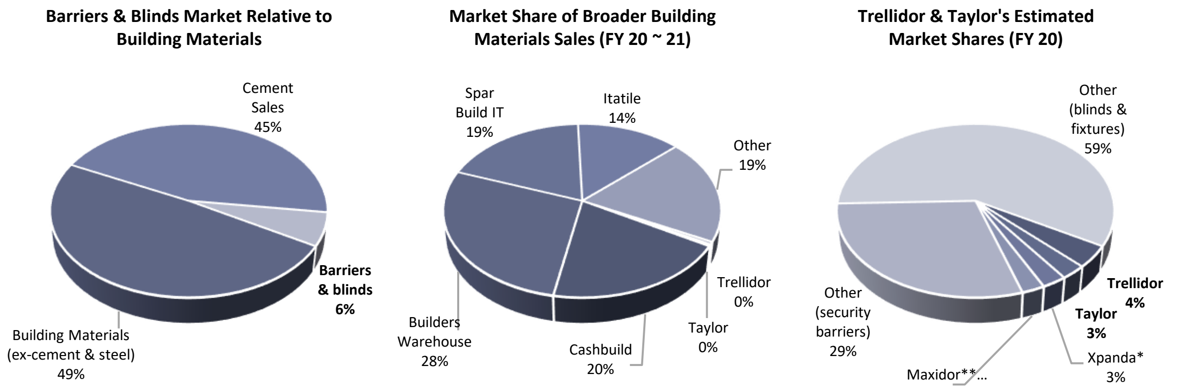
Sources: Afrimat Construction Index & Investing

Finally, we cast our eyes on the broader building materials market and, indeed, attempt to analyse the individual competitors (of which there are numerous private, unlisted ones) that compete with Trellidor on a *per-product* basis or compete for their share of homeowners' home improvement spending.

We estimate that the barriers and blinds market makes up only a mid-to-low single-digit percentage of the entire building materials market. Furthermore, Trellidor and Taylor's market share in the blinds and barriers market is likely to be a bit below a double-digit market share, leaving plenty of room for growth.

Thus, despite the above-noted recovery aspect of this market, Trellidor still has plenty of room to continue growing its existing products and/or expand into any related home improvement products (that would fit its Group and operations). In a way, this is the best of both worlds: The Group can grow through market share gains *and* grow through expanding its product range.

Figure 8: Estimated Market Shares of Building Materials, Home Improvement & Barriers/Blinds & Respective Participants



*Sources: Various company reports, Stats SA, and Blue Gem Research workings and assumptions; * Estimated based off Argent Industrial's segmental disclosure; ** Estimated relative to existing known operations*

In closing, South Africa and the world remain with a long list of known risks. But, in the absence of dramatic upsets, the above highlights how the currently accommodative monetary environment (probably helped by people being forced to spend lots of time at home!) has created tailwinds—and will hopefully sustain them--in the home improvement industry.

Trellidor should be a natural beneficiary of these tailwinds while its small market share of the much larger market offers many opportunities for expansion (e.g. product, geography & consolidation).

Valuation and 12m TP

Valuation Models

Refer to the Trellidor Segment and Taylor Segment for detailed assumptions that drive our segmental forecasts. We have selected a segmentally-drive Discounted Free Cash Flow (DCF) model and an implied relative Enterprise Value-to-EBITDA (EV/EBITDA) model to help guide our view of Trellidor Holdings' valuation.

Management has stated and is running a share buy-back programme and, thus, in the instance where this programme buys back shares at a price below our view of fair value, we would expect it to be value accretive.

That said, we cannot and have not taken this into account in our valuation models and use the currently issued share capital to arrive at *per share* valuations. In our Group-level forecasts, though, we do assume that management buy back 1% of the Group's issued share capital per year.

Discounted Free Cash Flow (DCF) Model

Besides the segmental-specific assumptions, we have made universal assumptions in building our DCF models:

- Cost of Equity (CoE) of 17.5% based on a "Rule of Thumb" beta of 1.5x and an Equity Risk Premium of 5.5%.
- Cost of Debt (CoD) of 7.4% (or 5.3% after tax).
- The Group's current gearing appears sustainable, thus we have used it to blend our CoE and CoD into a Weighted Average Cost of Capital (WACC) of 11.8%.
- We have applied this WACC at a segmental level to build DCF valuations before adding them together in a Sum-of-the-Parts (SOTP) model and then rolling this forward at our CoE to arrive at target prices.

Table 4: Sum-of-the-Parts (SOTP) of Segmental DCF Models – Trellidor Holdings

DCF SOTPs:	Fair Value	12m TP
Trellidor Segment	R436 707 780	R513 044 300
Taylor Segment	R213 993 036	R251 399 019
Less: Taylor Segment Minorities	-R16 049 478	-R18 854 926
Less: Net Debt	-R74 188 000	-R74 188 000
Less: Group Segment	-R127 302 879	-R149 555 422
Fair Value	**R433 160 459**	**R521 844 970**
Fair Value (cps)	**442cps**	**532cps**
EV/EBITDA (x)	*4,4x**	*4,9x***
Price Earnings (x)	*8,8x**	*8,7x***

*Sources: Trellidor Holdings, Bloomberg, Blue Gem Research workings and assumptions; * Based on FY 21E full-year expectations; ** Based on FY 22E full-year*

Our DCF SOTP implies a fair value of 442cps for Trellidor shares, putting it on a near-term Forward PE of 8.8x and EV/EBITDA of 4.4x. This implies that the current price of 335cps is 28% undervalued and generates a c.54% 12m return on a 12m TP of 532cps.

Refer to the EV/EBITDA model below for reference to why we believe that these multiples and the implied valuation appear reasonable in the current market.

Enterprise Value/EBITDA (EV/EBITDA) Model

Using some key relatives on the JSE to represent the home improvement, building materials and construction materials markets in South Africa—and then applying some conservative discounts against this basket—we have generated a relative valuation for Trellidor (Table 5):

Table 5: Enterprise Value-to-EBITDA (EV/EBITDA) Valuation Model

	Market Cap (Rbn)	Net Debt (Rbn)	Enterprise Value (Rbn)	12m EBITDA (Rbn)	EV/EBITDA (x)
Cashbuild	R7.5bn	R1.2bn	R6.3bn	R1.1bn	5,5x
Italtile	R22.3bn	R1.1bn	R21bn	R2.3bn	9,4x
PPC	R2.8bn	R4.5bn	R7.3bn	R1.7bn	4,2x
Afrimat	R6.8bn	R0.6bn	R6.8bn	R0.8bn	8,3x
Average					**6,8x**
Less: Discounts					-2,7x
- Small Cap Discount (20%)					*-1,4x*
- Illiquidity Discount (20%)					*-1,4x*
Trellidor's Implied EV/EBITDA (x)					4,1x
Trellidor's 12m EBITDA				R98,795,533	
Hence, Trellidor's EV			R404m		
Less: Net Debt		(R74m)			
Therefore, Trellidor's Fair Value	R330m				
Fair Value (cps)	**337cps**				

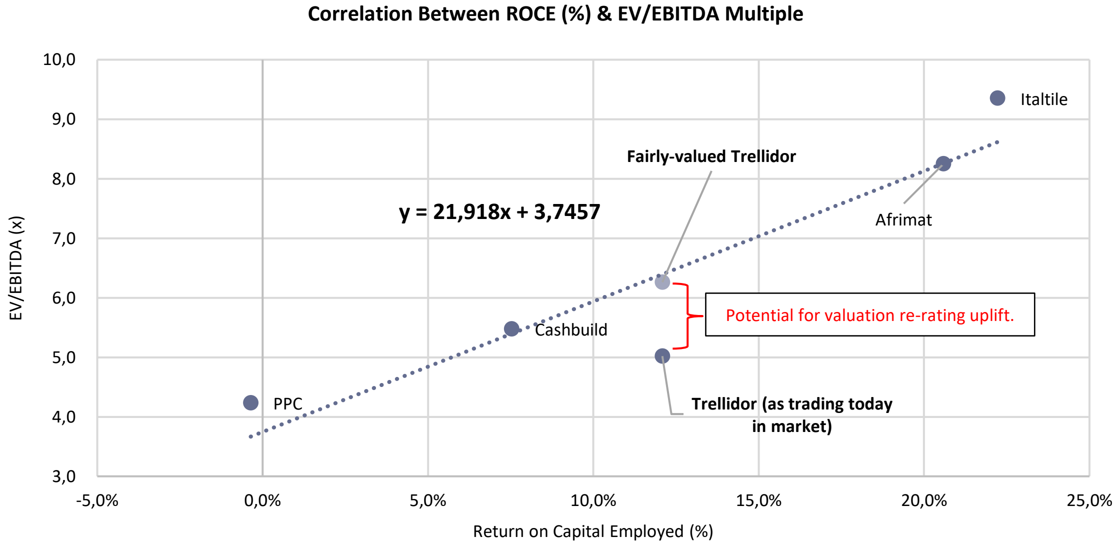
Sources: Iress, Profile Media, various company reports, and Blue Gem Research workings & assumptions

Unfortunately, given PPC Ltd's (PPC) and its current woes coupled with Trellidor's materially higher profitability than Cashbuild Ltd (CSB), we believe that the above model does *not* fairly reflect the Group's potential value.

In Figure 9, we have built a statistical correlation between profitability and market rating. Then, taking this a step further, in Table 6, we have applied this formula to Trellidor to arrive at a better market-based multiple.

We believe that this approach rewards Trellidor for its inherent profitability while still taking into account the existing market conditions and real-world relative valuations on the JSE.

Figure 9 & Table 6: Extrapolation of EV/EBITDA Multiple Relative to Profitability



Matrix of ROCE versus EV/EBITDA Multiples	ROCE (%)	EV/EBITDA
Cashbuild	7,5%	5,5x
Italtile	22,2%	9,4x
PPC	-0,4%	4,2x
Afrimat	20,6%	8,3x
Trellidor (Current Market Multiple)	12,1%**	5,0x
Trellidor (Fairly Valued – i.e. moved to the Best-Fit-Line)	12,1%**	6,3x*
Therefore, the implied fair value of Trellidor at a 6.3x EV/EBITDA		**555cps**

*Sources: Iress, Profile Media, various company reports, and Blue Gem Research workings & assumptions; * Based off the Line-of-Best-Fit's formula of Y = 21.918X + 3.7547 ~ EV/EBITDA = 21.918 x ROCE + 3.7547; ** Based off 12m trailing ROCE, including the poor H2:20 period. Therefore, we believe forward ROCE should be higher and, thus, Trellidor's potential for a positive re-rating of its valuation upwards remains possible.*

Thus, based on Trellidor's inherent profitability and using an EV/EBITDA model, the share appears arguably worth c.555cps.

Valuation, 12m TP and Implied Return

We believe that the market may be pricing Trellidor shares based solely on market averages (Table 5). This approach is arguably flawed due to some major underperforming peers and does not take into account Trellidor's high returns.

Therefore, using a SOTP approach with segmental-driven DCF models, we view Trellidor's fair value as 442cps. A linear regression on relative EV/EBITDA multiples tracking ROCE (%) provides further comfort as to the validity of this valuation and, indeed, points to upside risk in this fair value.

Using the SOTP DCF model as our primary valuation methodology, Trellidor appears worth 442cps or a c.8.8x PE and 4.4x EV/EBITDA against our expected FY 21E earnings. This valuation appear quite undemanding of a Group with a 5-year average ROE of >20% and a current Free Cash Flow/EV Yield just shy of 18%.

Rolling 442cps forward at CoE we arrive at a 12m TP of 532cps (ignoring dividends, which will come out of this), implying a total return of c.54%.

Key risks to our valuation

The key risks to our above valuation methodologies are:

- **Downside Risks**:
  - The usual basket of South African and global macro-risks, from geopolitics to interest rates to future developments in the COVID-19 pandemic.

  - Our expectations regarding the segments' various sales growth rates and their ability to maintain margins.
  - Any major collapse in the domestic residential property market.
- **Upside Risks**:
  - The Group's strategy to acquire main centre franchise operations may see sales and margin growth beyond what we have forecast.
  - Any other material, accretive acquisitions could add further upside to our forecasts and valuation.
  - A steadily rising steel price should lift Trellidor's traditional product price that—coupled with its high Gross Margin implying pricing power—could see revenues and related nominal Gross Profits coming in higher than we have forecast.
  - Finally, the Group's share buy-back programme remains a large variable in terms of quantum and price.

Disclaimer

Confused by this report? View our methodology, FAQ and this disclaimer.

** Peer group relatives are based on market prices in this report predominantly set to closing prices reported on 26 March 2021. Trellidor's share price is taken as of Closing Price on 9 April 2021.*

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