**Results Note**
**15 September 2021**

# Trellidor Holdings Ltd
## Secured a Good Result

**Share Code: TRL – Market Cap: R323m – PE: 8.3x – DY: 6.2%**

| | |
|---|---|
| **12m Target Price** | **656cps** |
| **Share Price** | **340cps** |
| **Implied Return** | **93%** |

**Industrials | South Africa**

### FY 21 Results: Sterling results, strong cash flows & good dividend

- Trellidor released strong results, reflecting the Group's healthy recovery with revenue rising +23% y/y, cost-savings, efficiencies & lower finance costs lifting headline earnings by +181% y/y and HEPS doubling (+195% y/y) to 40.8cps (FY 20 – 13.8cps).
- Underpinning the results was strong cash generation; management declared a full-year dividend of 21cps (FY 20 – 8cps) putting the share on a juicy 6.2% Dividend Yield.
- Management continued to grow the Group's product range (four new products were successfully launched & a commercial product range expansion is planned in the coming year) while bringing underperforming Main Centre franchisees in-house to great effect (acquired franchises grew revenue +46% like-for-like!), yet the Group also managed to control its overheads and saw a mere +4.3% y/y rise in operating expenses.

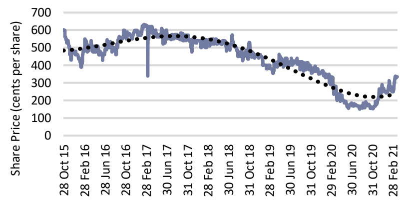
### Our Thoughts: Bottom-line momentum likely to continue

- Given the Group's tight cost control, the price increases that it will leak into the market and franchisee consolidation & growth uplift that we expect, Trellidor's EBITDA, operating profits and, ultimate, bottom-line momentum appears likely to continue for FY 22E.
- We have raised our expectations of share buy-backs from 1.0% pa to 1.5% pa, especially if the share price remains languishing at its current market price.
- All these initiatives imply attractive upside to forward HEPS.

### Forecast, Valuation and Implied Return: Undervalued & Yielding

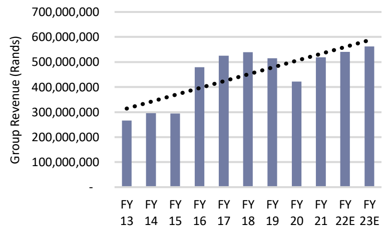
- Our DCF Models imply that Trellidor is worth c.548cps (previously: 442cps) on a c.13.5x PE and c.7.1x EV/EBITDA.
- Rolling this fair value forward at our CoE, we arrive at a 12m TP of 656cps (previously: 532cps) implying a large 93% return from the current share price (including dividends).
- Speaking of dividends, irrespective of fair values, Trellidor shares still trade on an attractive 6.2% Dividend Yield (& Forward DY of > 7%) that looks to be comfortably sustainable.

**Trellidor – Share Price Since Listing**



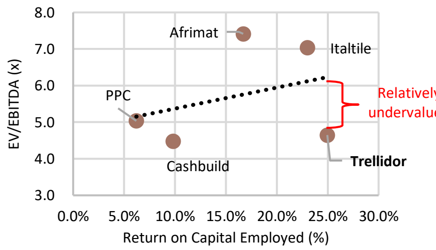

*Sources: Profile Media & Blue Gem Research*

**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 %*** | **FY 21A** | ***YoY %*** | **FY 22E** | ***YoY %*** | **FY 23E** | ***YoY %*** |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenue | 515 | *-4%* | 422 | *-18%* | 518 | 23% | 585 | *13%* | 609 | *4%* |
| EBITDA | 81 | *106%* | 12 | *-85%* | 85 | 610% | 89 | *4%* | 107 | *20%* |
| **HEPS (cps)** | **40.1cps** | ***-26%*** | **13.8cps** | ***-66%*** | **40.7cps** | **>100%** | **49.7cps** | ***22%*** | **61.5cps** | ***24%*** |
| *Return on Equity (%)* | *19.4%* | - | *-17.6%* | - | *22.6%* | - | *27.2%* | - | *29.3%* | - |
| *Price Earnings Ratio (x)* | *8.5x* | - | *24.6x* | - | *8.4x* | - | *6.8x* | - | *5.5x* | - |
| DPS (cps) | 20.2cps | *-26%* | 8.0cps | *-60%* | 21.0cps | >100% | 24.8cps | *18%* | 30.8cps | *24%* |
| *Dividend Yield (%)* | *5.9%* | - | *2.4%* | - | *6.2%* | - | *7.3%* | - | *9.0%* | - |

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

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BLUE GEM RESEARCH

| **Table 1: Key Forecast (Rm)** | **FY 19A** | ***YoY %*** | **FY 20A** | ***YoY %*** | **FY 21A** | ***YoY %*** | **FY 22E** | ***YoY %*** | **FY 23E** | ***YoY %*** |
|---|---|---|---|---|---|---|---|---|---|---|
| **Revenue** | **515** | ***-4.5%*** | **422** | ***-18.1%*** | **518** | ***23.0%*** | **585** | ***12.9%*** | **609** | ***4.0%*** |
| Trellidor | 323 | *-2.7%* | 257 | *-20.4%* | 315 | *22.8%* | 365 | *15.7%* | 380 | *4.1%* |
| Taylor | 191 | *-8.5%* | 165 | *-13.6%* | 204 | *23.8%* | 220 | *7.9%* | 229 | *4.0%* |
| **Gross Profit** | **232** | *-5.7%* | **176** | *-24.3%* | **219** | *25.0%* | **244** | *11.0%* | **263** | *8.1%* |
| *Gross Profit Margin (%)* | *45.0%* | - | *41.6%* | - | *42.3%* | - | *41.6%* | - | *43.2%* | - |
| Operating expenses | -171 | *6.0%* | -194 | *13.4%* | -163 | *-15.8%* | -180 | *10.1%* | -183 | *1.8%* |
| **EBITDA** | **81** | *106%* | **12** | *-85%* | **85** | **610%** | **89** | *4%* | **107** | *20%* |
| *EBITDA Margin (%)* | *15.7%* | - | *2.8%* | - | *16.4%* | - | *15.2%* | - | *17.5%* | - |
| **Net Profit (Parents)** | **43** | ***-28%*** | **-28** | ***-165%*** | **40** | ***>100%*** | **47** | ***18%*** | **57** | ***22%*** |
| *Issued Shares (millions)** | *105.8* | *-2.4%* | *100.2* | *-5.3%* | *95.2* | *-5%* | *93.8* | *-1.5%** | *92.4* | *-1.5%** |
| *Weighted Ave. # of Shares (millions)** | *107.2* | *-0.7%* | *102.4* | *-4.5%* | *97.7* | *-5%* | *94.5* | *-3.3%** | *93.1* | *-1.5%** |
| **EPS (cps)** | **40.0** | *-28%* | **-27.2** | *-168%* | **40.7** | *>100%* | **49.7** | *22%* | **61.5** | *24%* |
| **HEPS (cps)** | **40.1** | *-26%* | **13.8** | *-66%* | **40.7** | *>100%* | **49.7** | *22%* | **61.5** | *24%* |
| *Price Earnings Ratio (x)* | *8.5x* | - | *24.6x* | - | *8.4x* | - | *6.8x* | - | *5.5x* | - |
| **Dividend Per Share (cps)** | **20.2** | *-26%* | **8.0** | *-60%* | **21.0** | *>100%* | **24.8** | *18%* | **30.8** | *24%* |
| *Dividend Yield (%)* | *5.9%* | - | *2.4%* | - | *6.2%* | - | *7.3%* | - | *9.0%* | - |
| *Dividend Cover (x)* | *2.0x* | - | *1.7x* | - | *1.9x* | - | *2.0x* | - | *2.0x* | - |
| Property, Plant & Equipment | 65 | *6%* | 57 | *-12%* | 58 | *1%* | 61 | *6%* | 65 | *5%* |
| Intangible Assets | 113 | *-3%* | 83 | *-27%* | 88 | *7%* | 83 | *-6%* | 78 | *-6%* |
| Current Assets | 182 | *-8%* | 177 | *-3%* | 192 | *9%* | 187 | *-3%* | 234 | *26%* |
| Current Liabilities | 106 | *19%* | 90 | *-15%* | 116 | *29%* | 108 | *-6%* | 131 | *21%* |
| Cash | 13 | *-54%* | 23 | *86%* | 18 | *-24%* | -19 | *-205%* | 16 | *-184%* |
| Interest-bearing Liabilities | 83 | *-11%* | 106 | *29%* | 99 | *-7%* | 86 | *-13%* | 86 | *0%* |
| Net Debt | 70 | *6%* | 83 | *18%* | 81 | *-2%* | 105 | *29%* | 71 | *-33%* |
| *Net Debt:Equity (%)* | *32%* | - | *52%* | - | *46%* | - | *61%* | - | *36%* | - |
| *Net Debt: EBITDA (x)* | *0.9x* | - | *6.9x* | - | *1.0x* | - | *1.2x* | - | *0.7x* | - |
| Shareholder's Equity (Parent) | 221 | *4%* | 159 | *-28%* | 176 | *11%* | 173 | *-2%* | 195 | *13%* |
| NAV per share (cps) | 208.9 | *6%* | 158.4 | *-24%* | 185.0 | *17%* | 184.3 | *0%* | 211.3 | *15%* |
| TNAV per share (cps) | 101.6 | *15%* | 75.9 | *-25%* | 92.1 | *21%* | 95.5 | *4%* | 126.9 | *33%* |
| Price-to-Book (x) | 1.6x | - | 2.1x | - | 1.8x | - | 1.8x | - | 1.6x | - |
| Price-to-Tangible-Book (x) | 3.3x | - | 4.5x | - | 3.7x | - | 3.6x | - | 2.7x | - |
| Free Cash Flow (post-capex) | 31 | *-529%* | -11 | *-135%* | 56 | *-607%* | 27 | *-52%* | 68 | *154%* |
| ***Enterprise Free Cash Flow Yield (%)*** | ***8.1%*** | - | ***-2.8%*** | - | ***14.2%*** | - | ***6.4%*** | - | ***17.6%*** | - |
| *Cash Conversion Ratio (%)* | *39%* | - | *-92%* | - | *66%* | - | *30%*** | - | *64%* | - |
| ***Return on Equity (%)*** | ***19.4%*** | - | ***-17.6%*** | - | ***22.6%*** | - | ***27.2%*** | - | ***29.3%*** | - |
| ***Return on Capital Employed (%)*** | ***26.9%*** | - | ***-3.4%*** | - | ***25.0%*** | - | ***28.5%*** | - | ***32.3%*** | - |
| ***Return on Assets (%)*** | ***11.9%*** | - | ***-7.2%*** | - | ***11.0%*** | - | ***13.4%*** | - | ***14.5%*** | - |

*Sources: Trellidor Holdings, Bloomberg, Iress, Profile Media, Blue Gem Research workings, assumptions, and forecasts; * We have assumed that 1.5% (previously: 1%) of the Group's issued share capital is bought back evenly throughout each of the forecast years. ** Artificially low as investment in working capital creates short-term drag on the cash flows across the Group.*

## FY 21 Results Summary

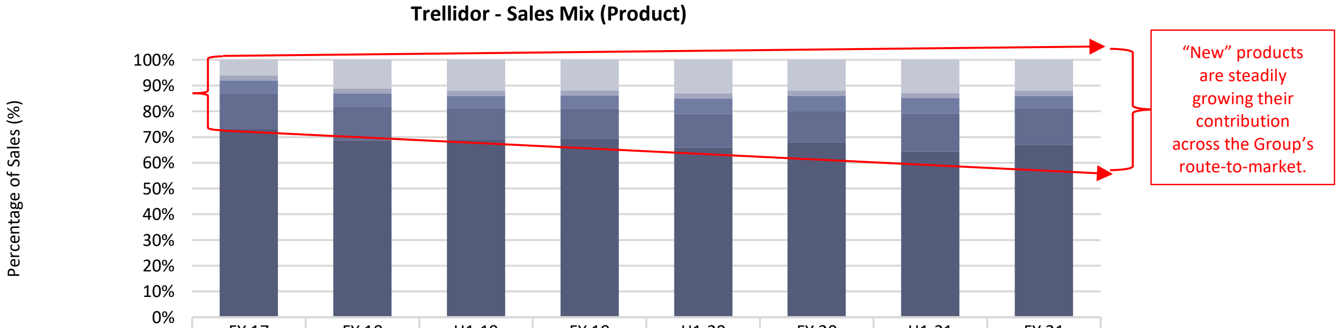
- Trellidor (code: TRL) released strong FY 21 results. While these results are admittedly off FY 20's low base, they also do reflect the Group's healthy recovery and continued strategy of driving route-to-market, product mix expansion & returns while controlling costs:
  - Revenue rose +23% y/y to R518m (FY 20 – R422m), though some timing issues & soft pan-African sales saw this slightly below our forecast revenue of R523m (the timing issues should see this revenue shift into FY 22E),
  - Cost-savings, efficiencies and lower finance costs saw headline earnings rise by +181% y/y (i.e. more than revenues) to R39.8m (FY 20 – R14.2m) and HEPS leap +195% y/y to 40.8cps (FY 20 – 13.8cps). HEPS grew more than Headline Earnings due to the below noted share buy-back.
  - The Group has continued its share buy-back programme during the period (deploying a further R12m capital to this initiative for c.5.1% of issued share capital). We have lifted our rate of share buy-backs from 1% of share capital a year to 1.5% per year, particularly if the share price stays languishing at its current levels.
  - Finally, underpinning the results were strong cash generation, and management has declared a full-year dividend of 21cps (FY 20 – 8cps) putting the share on a 6.2% Dividend Yield.
- Qualitatively, the Group continued to grow its route-to-market & product range while bringing underperforming Main Centre franchisees in-house to great effect:
  - Four new products were launched during H2:21 (they were well received by the market), and a further extension to the Group's commercial product in South Africa offering is planned for FY 22E (taking some lessons from products in the UK).
  - Durban and Johannesburg West branches were fully integrated during the period and saw a +46% like-for-like sales growth following this.
  - The Trellidor UK business acquisition has been completed and bedded down with exciting prospects appearing on its horizon in FY 22E as the UK bounces back.
  - Despite the above, the Group managed to control its overheads and saw a mere +4.3% y/y rise in operating expenses.
- After year-end, Trellidor's KwaZulu-Natal-based manufacturing operations and sales channels were affected by the recent domestic riots.
  - Management estimate that they have lost seven days of production in H1:22E.
  - It remains to be seen if they win any subsequent uplift in demand for their security-related products from either a post-riot rebuild or heightened residential demand.
  - See Figure 6 for some real-time data points for this period in KwaZulu-Natal.

### Trellidor Segment

- The core Trellidor business performed well:
  - Revenue grew +23% y/y, though missed our estimates by c.5% as the pan-African sales underperformed. Management have increased marketing and management support in these markets and expects a near-term rebound here.
  - Q4:21 margins saw some pressure as the rising input costs of steel (and freight) were absorbed, though management has already put a price increase into the market and expects to put a couple more hikes to (somewhat) protect Gross Profit (GP) margins here.

- Management believes the business is well-position to absorb rising material prices as the value-add to the raw materials through the Group's manufacturing is significant (raw material costs in Trellidor were only c.30.8% of the end sale price).
- Supply chain disruptions and shipping challenges are trickier to deal with, thus the Group has decided to strategically invest in higher stock levels (see our DCF commentary later).
- It is also worth noting that management's focus in the coming year is to protect *operating* margins. Thus, only some of the above GP margin pressure will be passed into the market while the rest will be made up by central efficiencies & operating leverage.

**Figure 1: Sales Mix & Trends**

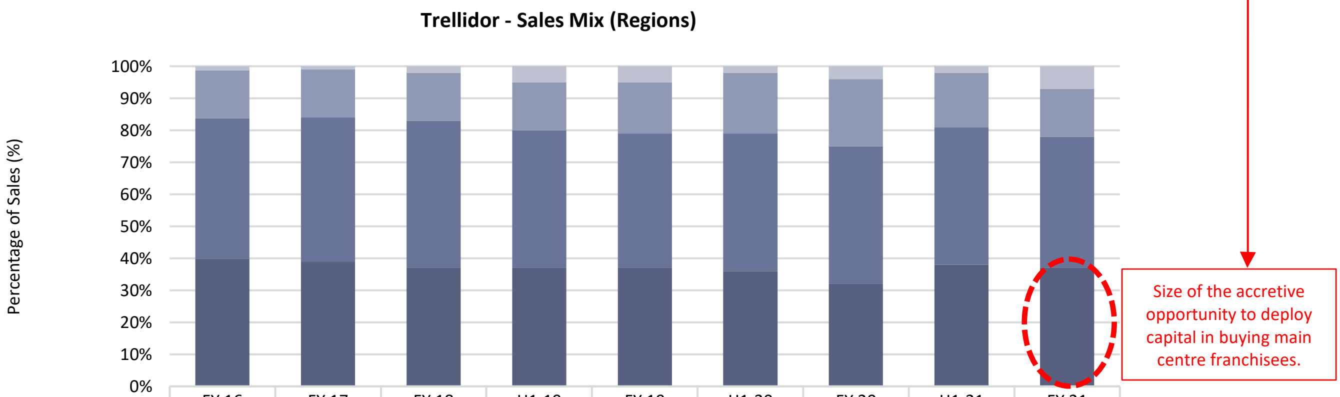



| | FY 17 | FY 18 | H1:19 | FY 19 | H1:20 | FY 20 | H1:21 | FY 21 |
|---|---|---|---|---|---|---|---|---|
| Security Shutter | 6% | 11% | 12% | 12% | 13% | 12% | 13% | 12% |
| Polycarbonate Bar | 2% | 2% | 2% | 2% | 2% | 2% | 2% | 2% |
| Rollerstyle | 5% | 5% | 5% | 5% | 6% | 6% | 6% | 5% |
| Clear Guard | 14% | 13% | 12% | 12% | 13% | 12% | 15% | 14% |
| Traditional Trellidor | 73% | 68% | 69% | 70% | 66% | 68% | 65% | 67% |

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

- Geographically, the contribution from the Main Centres was material & helped by the +46% like-for-like sales growth in the newly acquired franchises. The success of these acquired franchisees has reinforced management's view that they will keep opportunistically acquiring Main Centre franchise operations where they are underperforming and become available. See opportunity size below.
- The Group's International sales more than doubled as the UK franchise acquisition was bedded down (prospects here are looking particularly exciting). We have consolidated this in for a full FY 22E period.

**Figure 2: Trellidor's Regional Sales Split**




| | FY 16 | FY 17 | FY 18 | H1:19 | FY 19 | H1:20 | FY 20 | H1:21 | FY 21 |
|---|---|---|---|---|---|---|---|---|---|
| UK & Israel | 1% | 1% | 2% | 5% | 5% | 2% | 4% | 2% | 7% |
| Africa | 15% | 15% | 15% | 15% | 16% | 19% | 21% | 17% | 15% |
| Outlying Regions | 44% | 45% | 46% | 43% | 42% | 43% | 43% | 43% | 41% |
| Main Centers | 40% | 39% | 37% | 37% | 37% | 36% | 32% | 38% | 37% |

*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:

- We see the 7 days of lost production in H1:22E as being made-up throughout the year & we expect price increases to be fully absorbed by customers; the UK acquisition contributes a further R25m in revenues for FY 22E (and operating expenses) while GBP/ZAR exchange rate remains flat,
- Cost-savings & efficiencies in FY 22E and FY 23E keep inflation <2% but thereafter it runs at 3.2% y/y,
- Medium-term sales growth of +3.9% y/y,
- Some short-term GP margin pressure sees margins decrease by a couple hundred basis points into FY 22E and FY 23E before normalizing thereafter to historical averages (48.6%), &
- Capex averages 4.0% of sales while net working capital averages 16.7% (though we have hiked inventory days in FY 22E and FY 23E somewhat to control for higher "safety" stock levels).

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

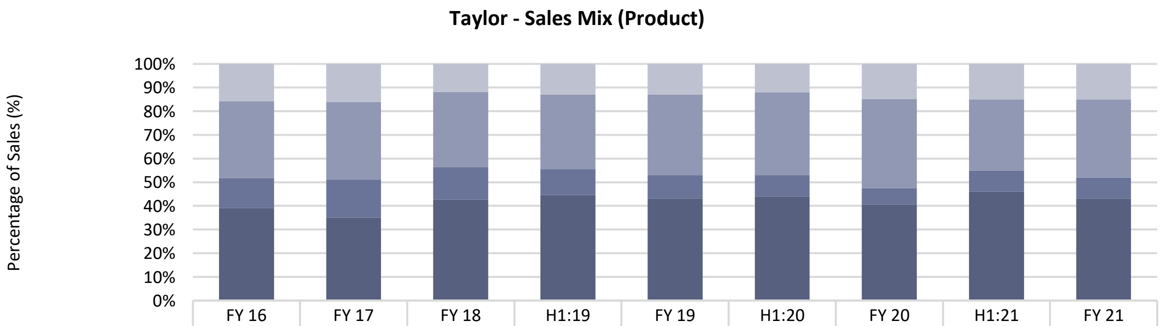
| (Rm) | FY 20 | FY 21 | FY 22E | FY 23E | FY 24E | FY 25E | FY 26E | FY 27E | FY 28E |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | 257 | 315 | 365 | 380 | 394 | 410 | 426 | 442 | 451 |
| *Revenue (%)* | *-20.4%* | *22.8%* | *15.7%* | *4.1%* | *3.9%* | *3.9%* | *3.9%* | *3.9%* | *1.9%* |
| Gross Profit | 119 | 145 | 164 | 178 | 192 | 199 | 207 | 215 | 219 |
| *Gross Profit Margin (%)* | *46.2%* | *46.0%* | *45.0%* | *47.0%* | *48.6%* | *48.6%* | *48.6%* | *48.6%* | *48.6%* |
| Operating Profit | 35 | 50 | 49 | 61 | 71 | 74 | 78 | 82 | 84 |
| EBITDA | 42 | 60 | 60 | 73 | 84 | 88 | 93 | 98 | 100 |
| Tax | -10 | -13 | -12 | -16 | -18 | -19 | -20 | -21 | -22 |
| Working Capital | 9 | 5 | -21 | 8 | 6 | -3 | -3 | -3 | -1 |
| Capex | -9 | -14 | -15 | -15 | -16 | -16 | -17 | -18 | -18 |
| **Free Cash Flow (FCF)** | **32** | **38** | **12** | **50** | **56** | **50** | **53** | **56** | **59** |
| *Discount Rate* | - | - | *0.89* | *0.80* | *0.71* | *0.64* | *0.57* | *0.51* | *0.46* |
| Discounted FCF | - | - | 11 | 40 | 40 | 32 | 30 | 29 | 273 |
| **Enterprise Value (EV)** | | | | | | | | | **R455m** |
| **EV/EBITDA (x)** | | | | | | | | | **7.6x** |

*Sources: Bloomberg, Blue Gem Research and Trellidor Holdings*

## Taylor Segment

- Taylor's revenue grew by +24% y/y to R204m (FY 20 – R165m) beating our forecasts of R192m by a wide gap as the business was buoyed by the strong domestic DIY demand.
- Given the current supply chain challenges, higher freight rates and general input cost pressure, Taylor's margins contracted somewhat over this period and, despite the revenue beat, the segment missed our bottom-line expectations.
- NMC's contribution has been maintained following a strong performance in F21, and the Thermowood Shutter range has grown as the Group expands the product mix.

**Figure 3: Snapshot of Some of Taylor/NMC's Key Products, Sales Mix & Trends**

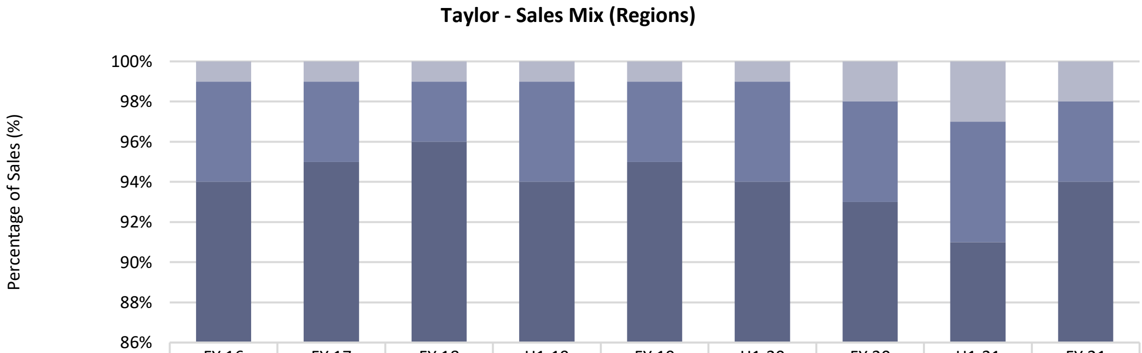



| | FY 16 | FY 17 | FY 18 | H1:19 | FY 19 | H1:20 | FY 20 | H1:21 | FY 21 |
|---|---|---|---|---|---|---|---|---|---|
| NMC | 16% | 16% | 12% | 13% | 13% | 12% | 15% | 15% | 15% |
| Blinds | 33% | 33% | 32% | 32% | 34% | 35% | 38% | 30% | 33% |
| PVC Shutters | 13% | 16% | 14% | 11% | 10% | 9% | 7% |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

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

- This segment's sales continue to be concentrated to the Western Cape (where the original business was founded) and Gauteng (due to its sheer market size) but its products are increasingly gaining distribution through the existing Trellidor franchise network.
- Specifically looking at the sales of Taylor product's through Trellidor's franchises sees that this revenue stream grew by +50% y/y. We see no reason that this positive trend should not continue.

**Figure 4: Taylor's Regional Sales Split**




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

*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:

- Continued DIY spend for the product driving volume recoveries, though tapered somewhat by supply chain disruptions and stocking challenges. These opposing vectors should drive a c.4.0% y/y sales growth, particularly as the segment continues to gain high double-digit growth through the existing Trellidor franchise network.
- Overhead cost-savings achieved in FY 21 flowing through in FY 22E (overheads rising only 0.5% y/y) and into FY 23E (+1.6% y/y) before stabilising at a more normal long-term inflation of 3.2% y/y thereafter,
- Much like the Trellidor segment, we see GP margin pressure in the short-term and shaved off about 50bps GP in FY 22E into FY 23E before normalizing at a more historically steady GP margin of 38.8% thereafter, &
- Capex averages 4.0% of sales while net working capital averages 21.8%.

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

| **(Rm)** | **FY 20** | **FY 21** | **FY 22E** | **FY 23E** | **FY 24E** | **FY 25E** | **FY 26E** | **FY 27E** | **FY 28E** |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | 165 | 204 | 220 | 229 | 238 | 248 | 257 | 268 | 273 |
| *Revenue (%)* | *-13.6%* | *23.8%* | *7.9%* | *4.0%* | *4.0%* | *4.0%* | *4.0%* | *4.0%* | *1.9%* |
| Gross Profit | 60 | 75 | 79 | 85 | 92 | 96 | 100 | 104 | 106 |
| *Gross Profit Margin (%)* | *36.5%* | *36.5%* | *36.0%* | *37.0%* | *38.8%* | *38.8%* | *38.8%* | *38.8%* | *38.8%* |
| Operating Profit | -40 | 13 | 17 | 22 | 27 | 29 | 30 | 37 | 37 |
| EBITDA | -26 | 26 | 31 | 36 | 42 | 44 | 46 | 48 | 48 |
| Tax | -13 | -5 | -3 | -4 | -6 | -6 | -7 | -9 | -9 |
| Working Capital | 2 | 3 | -2 | -2 | -8 | -2 | -2 | -2 | -1 |
| Capex | -3 | -5 | -9 | -9 | -10 | -10 | -10 | -11 | -11 |
| Free Cash Flow (FCF) | -40 | 18 | 16 | 20 | 18 | 25 | 27 | 27 | 28 |
| **Discount Rate** | - | - | **0.89** | **0.80** | **0.71** | **0.64** | **0.57** | **0.51** | **0.46** |
| *Discounted FCF* | - | - | *15* | *16* | *13* | *16* | *15* | *14* | *129* |
| **Enterprise Value (EV)** | | | | | | | | | **R217m** |
| **EV/EBITDA (x)** | | | | | | | | | **8.4x** |

*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. Consistent with our Initiation of Coverage, we have built a net present value (NPV) for this segment. While this segment can make a profit, our NPV is negative, implying a small 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 (consistent with our above communicated inflation rates & other evidence) and allowed management fee income to track Group income upwards. We have pushed (most) finance costs through this segment before consolidating it into the Group results.

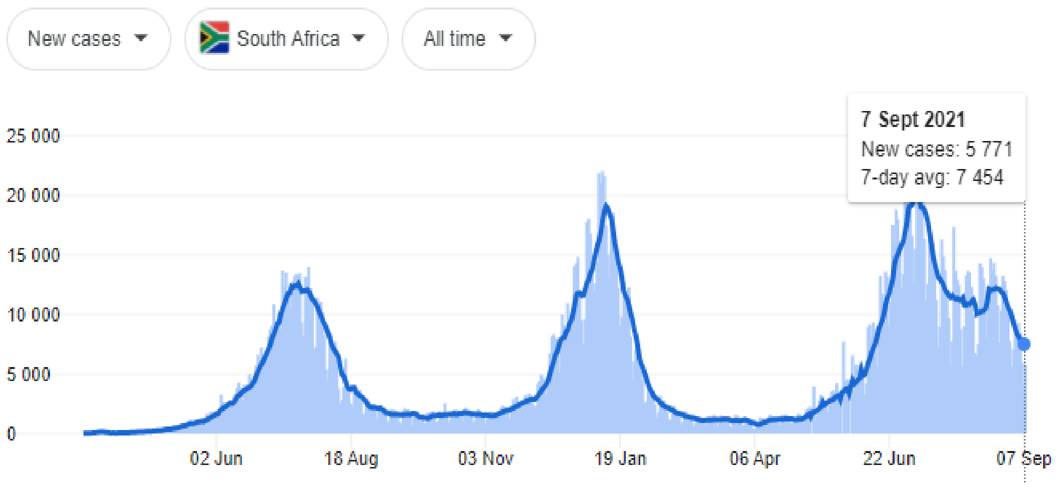
Finally, as we have done with other groups that own underlying properties, we have *not* valued these separately and consider the yield it generates (or would generate, if externally tenanted) as being captured in the respective operating margins of each business and the broader Group (via rental savings).

## Macro-economic Environment & Industry Snapshot

The macro-environment is currently being dominated by three major and inter-related variables:

- **Domestic riots**: The violent and destructive riots that broke out in KwaZulu-Natal (and, to a lesser extent, in Gauteng) from late June into July 2021 were both destructive to property and businesses *and* hugely disruptive to supply chains. Luckily, Trellidor escaped unscathed, albeit disrupted (the Group estimates that it lost one full week of production). This should negatively affect H1:22E results, though the rebuilding of properties and refitting thereof may see a *boost* to demand in H2:22E, such that the final effects are impossible to forecast. Also, there remains a risk that these riots flare up again, though the current political will of the Government is strongly opposed to this, and any resurfacing should (hopefully) see a much swifter and harsher response.
- **COVID-19**: Figure 5 shows that the world entering the 3rd-wave while South Africa has (so far) successfully passed this wave's peak. While vaccines appear to have dulled the mortality effects of COVID, the disruptive effects—both to supply chains and overall demand and economic activity—remain hard to quantify (but certainly not positive). Likewise, any future waves, mutations, & vaccines benefits are near impossible to quantify or forecast at this point.
- **Lockdown-induced recession(s)**: Related to the above note on COVID, a key variable is how global *Governments* respond to future waves. Harder lockdowns will see deep drawdowns in economic activity and more severe disruptions to supply chains. Likewise, the opposite remains true.

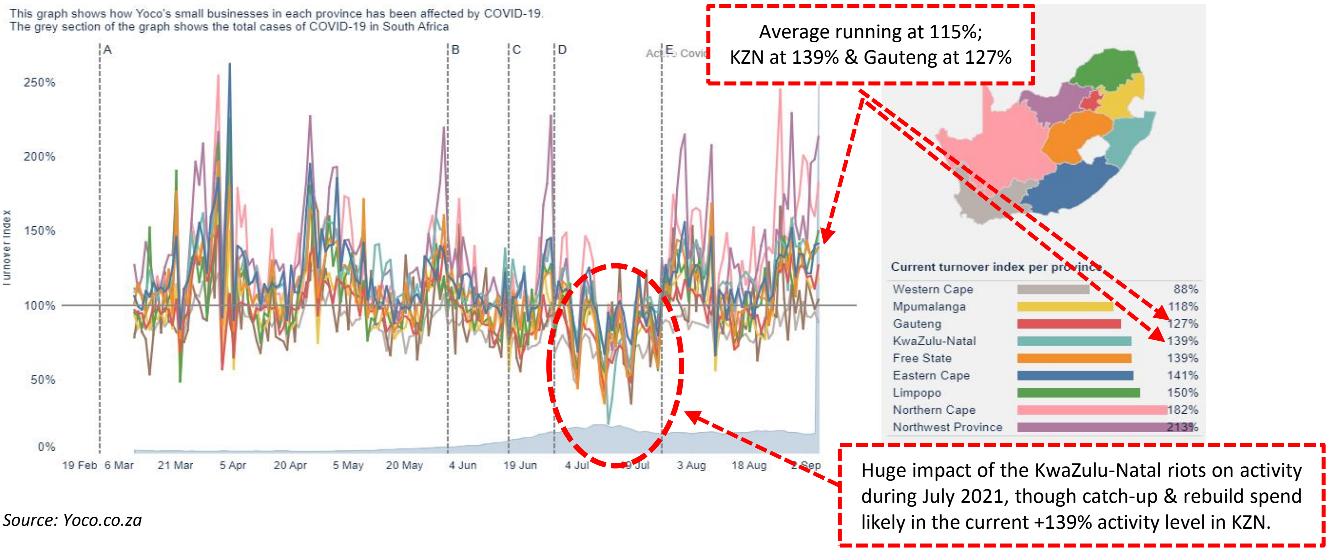
**Figure 5: COVID-19 Daily Cases**




Source: Google (August & September 2021 latest global statistics)

- The Yoco payment monitor is a useful (though somewhat bias) real-time ground-level data source, and highlights how the local economy may be doing *right now*:
    - Yoco has installed Point-of-Sales devices across South Africa in a wide swathe of SME's and merchants. The business aggregates and displays this data on their website: LINK.
    - This data is skewed towards card transactions (not cash) and towards SME's domestically. Despite this bias, the SME sector is also arguably both a leading indicator of the downside and a lagging indicator of recovery (given that most domestic SME's are more fragile than larger corporates and the public sector).
    - Therefore, this data paints the "worst-case" picture of the most fragile part of the domestic economy and, thus, can be used to extrapolate how the real-time recovery is performing.
    - I.e. When SME's have recovered fully in South Africa, we can assume the same is probably true of most other parts of the economy.
- Refer to the full data in Figure 6 on the next page.
- What we can extrapolate from this data that is relevant for Trellidor Holdings is:
    - Overall activity has recovered its current c.115% range as the economic recovery (even post-riots) seems to continue.
    - This is more weighted towards Gauteng (at c.127% of its activity level) and KwaZulu-Natal is *higher* (c.139% its activity level).
    - This latter point is important for Trellidor as the Group's business is traditionally weighted more towards KwaZulu-Natal having been founded there, though Gauteng is a major market and the recent franchise acquisitions included one in this geographic zone.
    - If we specifically zoom into KwaZulu-Natal, the large impact of the riots on this province's activity level can be seen as Yoco payments dropped to a trough of nearly zero during July 2021.
    - Post-riots, though, this activity has recovered strongly (c.139% of activity level) as it probably plays catch-up with delayed demand and/or some rebuild/restocking spending is starting to appear in this data.
    - While more anecdotal that persuasive, the Yoco data adds somewhat to our confidence that the domestic recovery continues—irrespective of the riots—and Trellidor is likely well-positioned to benefit from this.

**Figure 6: Yoco Payments Monitor (as of 8 September 2021)**

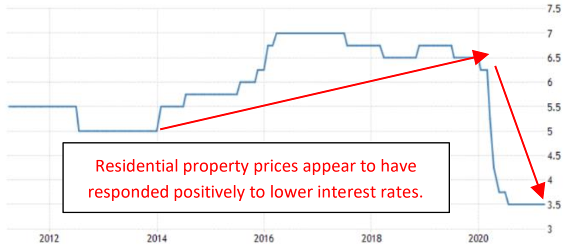



*Source: Yoco.co.za*

- Given Trellidor's close alignment to the domestic residential property market, Figure 7 reveals that this property market continues to recover on the back of all-time low interest rates.
- A recent speech by the South African Reserve Bank Government (read the full speech here) indicates a view towards lower rates for longer as the SARB's inflation targeting framework is shifted towards lower levels of overall inflation (i.e. positive for residential property and, thus, positive for Trellidor).

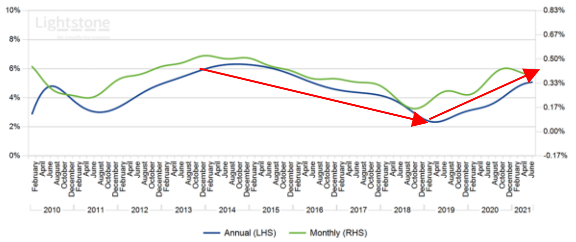
**Figure 7: Falling Repo Rate & Rising Private Property Market Appear Correlated (10-year views)**

**South African Reserve Bank's Repurchase Rate ("repo rate")**




**Lightstone Residential Property Price Index**

Annual vs Monthly

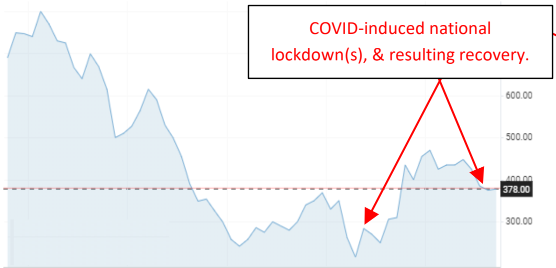



*Sources: South African Reserve Bank, Lightstone Properties & Blue Gem Research workings*

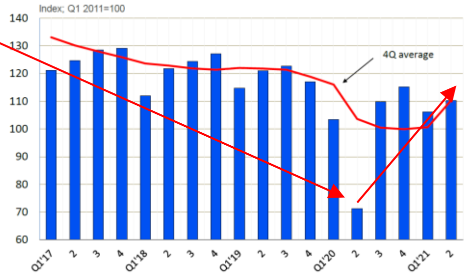
- As a secondary check to the above narrative (Figure 8) you can see the strong recovery in both Balwin Properties (as a proxy for the entry-level to mid-range residential property market) & the Afrimat's Construction Index (a broader building material & construction index).
- These both lend more weight to our view of a continuing domestic recovery and, thus, underpins our underlying growth assumptions that Trellidor should be a beneficiary of these macro tailwinds.

**Figure 8: 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: JSE, Afrimat Construction Index, & Investing*

## Valuation and 12m TP

### Valuation Models

Refer to the Trellidor and Taylor Segments 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 a *per share* valuation. In our Group-level *forecasts*, though, we do assume that management buys back 1.5% pa of the Group's issued shares (previously we assumed 1% pa, but also note that 5.1% of issued shares was *actually* bought-back in FY 21!).

#### Discounted Free Cash Flow (DCF) Model

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

- Cost of Equity (CoE) of 17.1% (previously 17.5%) based on a "Rule of Thumb" beta of 1.5x and an Equity Risk Premium of 5.5% (unchanged),
- Cost of Debt (CoD) of 8.7% (or 6.2% 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 11.9% (previously 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**

| | Fair Value | 12m TP |
|---|---|---|
| Trellidor Segment | R454,874,797 | R532,612,900 |
| Taylor Segment | R217,254,773 | R254,383,614 |
| Less: Taylor Segment Minorities | -R16,294,108 | -R19,078,771 |
| Less: Net Debt | -R81,098,000 | -R81,098,000 |
| Less: Group Segment | -R52,917,036 | -R61,960,558 |
| **Fair Value** | **R521,820,426** | **R624,859,185** |
| **Fair Value (cps)** | **548cps** | **656cps** |
| ***EV/EBITDA (x)*** | ***7.1x*** | ***8.0x*** |
| ***Price Earnings (x)*** | ***13.5x*** | ***13.2x*** |

*Sources: Trellidor Holdings, Bloomberg, Blue Gem Research workings and assumptions*

Our DCF SOTP implies a fair value of 548cps (previously 442cps) for Trellidor shares, putting it on a Price Earnings (PE) of 13.5x and EV/EBITDA of 7.1x. This implies that the current price of 340cps is 61% undervalued and generates a c.93% 12m return on a 12m TP of 656cps.

Refer to the EV/EBITDA model below for our sense checking of this fair value against peers and implied profitability-driven multiples.

#### 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 (R's) | Net Debt (R's) | Enterprise Value (R's) | 12m EBITDA (R's) | EV/EBITDA (x) |
|---|---|---|---|---|---|
| Cashbuild | 6,963,410,835 | -1,215,000,000 | 5,748,410,835 | 1,402,863,000 | 4.1x |
| Italtile | 22,322,738,560 | -1,100,000,000 | 21,222,738,560 | 2,940,000,000 | 7.2x |
| PPC | 5,591,831,197 | 2,231,000,000 | 7,822,831,197 | 1,598,000,000 | 4.9x |
| Afrimat | 8,159,984,922 | 85,492,000 | 8,245,476,922 | 1,095,667,000 | 7.5x |
| Average | | | | | **5.9x** |
| Less: Discounts | | | | | -2.4x |
| *- Small Cap Discount (20%)* | | | | | *-1.2x* |
| *- Illiquidity Discount (20%)* | | | | | *-1.2x* |
| Trellidor's Implied EV/EBITDA (x) | | | | | 3.6x |
| Trellidor's 12m EBITDA | | | | R85,257,000 | |
| Hence, Trellidor's EV | | | R303,563,950 | | |
| Less: Net Debt | | R81,098,000 | | | |
| Therefore, Trellidor's Fair Value | R222,465,950 | | | | |
| **Fair Value (cps)** | **227cps** | | | | |

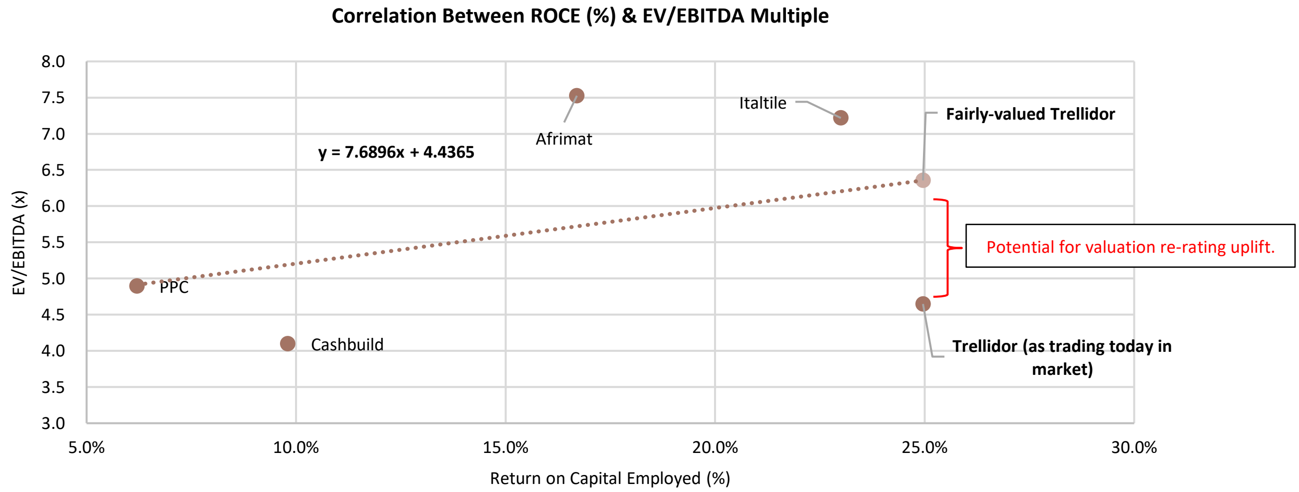
*Sources: Iress, Profile Media, various company reports, and Blue Gem Research workings & assumptions*

As noted in our Initiation of Coverage & still our opinion, PPC Ltd's (PPC) current woes coupled with Trellidor's materially higher profitability than all these peers make this comparison flawed.

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 | 9.8% | 4.1x |
| Italtile | 23.0% | 7.2x |
| PPC | 6.2% | 4.9x |
| Afrimat | 16.7% | 7.5x |
| Trellidor (Current Market Multiple) | 25.0% | 4.6x |
| Trellidor (Fairly Valued) | 25.0% | 6.4x* |
| **Implied Fair Value for Trellidor shares** | | **470cps** |

*Sources: Iress, Profile Media, various company reports, and Blue Gem Research workings & assumptions; * Based off the Line-of-Best-Fit's formula of Y = 7.6896x + 4.4365 ~ EV/EBITDA = 7.6896 x ROCE + 4.4365 = 6.4x implied EV/EBITDA for Trellidor*

Thus, based on Trellidor's inherent profitability and using an EV/EBITDA model, the share appears worth c.470cps.

While this number does not entirely agree with our DCF SOTP fair value, both models indicate a fair value well in *excess* of the current 340cps share price.

## Valuation, 12m TP and Implied Return

Using a SOTP approach with segmental-driven DCF models as our primary valuation tool, we view Trellidor's fair value as 548cps (previously 442cps). Checking this DCF-driven fair value against a linear regression based on EV/EBITDA and ROCE metrics of peers provides some comfort that the current 340cps share price does *not* accurate reflect Trellidor's likely fair value.

Rolling this DCF SOTP fair value forward at CoE we arrive at a 12m TP of 656cps (previously 532cps) implying a total return of c.93%.

## 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 to any potential future riots.
  - Our expectations regarding the segments' various sales growth rates and their ability to maintain margins (and, indeed, their ability to successfully pass on price increases to customers).
  - 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.
  - Given the growing importance of the UK to the Group, any Pound exchange rate strength (i.e. Rand weakness) could boost consolidated profits out of this region.
  - Finally, the Group's share buy-back programme remains a large variable in terms of quantum and price.

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** Peer group relatives are based on market prices in this report predominantly set to closing prices reported on 7 & 8 September 2021. Trellidor's share price is taken during 8 September 2021.*

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