Press release

ARB celebrates 40th anniversary – reports cash resources of R152m and HEPS up 3% at year-end despite effects of COVID-19

Highlights

- 40th anniversary of group's establishment in 1980
- Revenue down 13.1% to R2 353 million (2019: R2 706 million)
- Despite the devastation of COVID-19:
    - Operating profit only down 6.1% to R145.9 million (2019: R155.4 million)
    - Headline earnings per share (HEPS) up 3.0% to 59.96 cents (2019: 58.20 cents)
    - Cash resources of R151.9 million (2019: R180.9 million)
- No dividend declared

21 August 2020 – JSE-listed investment and property holding company ARB Holdings Limited, which owns investments in related trading and distribution businesses, including 74% of ARB Electrical Wholesalers, a level 2 BEE company operating 21 electrical wholesale branches (2019: 22) throughout South Africa, and 60% of Eurolux, which imports and distributes light fittings, lamps and related accessories, today released results for the financial year ending 30 June 2020. This marks the group's 40th year in business.

According to group CEO, Billy Neasham, this financial year will be well remembered, albeit for the wrong reasons. "In the nine months up to March 2020 the South African economy, on which the group is largely dependent, failed to show any growth and continued to be hamstrung by the collapse of business confidence and the construction industry, the lack of any meaningful infrastructure development by government, Eskom or the private sector, and exacerbated by the damaging effects of Eskom's load shedding."

He added that these challenges subsequently became a secondary concern with the imposition of the COVID-19 national lockdown on 27 March 2020. "We took immediate action to protect our employees, preserve cash, defend our balance sheet and mitigate operating costs. This included allowing our people to work from home where possible, placing those who were unable to work from home on paid leave and allowing them to take up to 10 days of negative leave to soften the impact, and creating shifts for staff returning to work. All directors and managers who continued to work took a mandatory salary reduction of at least 25% for two months.''

Neasham said that economic measures included curtailing capital and operating expenditure, limiting stock purchases and embarking on a review of all operations in order to reorganise the business in anticipation of the "next normal".

He added that the group was proud to have been able to honour all supplier payments on time during this period. "Although this did initially negatively impact our cash available by approximately R100 million, as customers delayed their payments to us, our efforts in quickly collecting the amounts due recovered the initial cash outflow."

ARB's trading activities were severely impacted in April 2020 as the group was only permitted to trade for the supply of emergency spares for essential services and at best achieved 10% of budgeted turnover for that month.

"The amendments to the regulations from May 2020 enabled all our businesses to operate under strict health and safety protocols, which enabled us to achieve revenue of 60% and 70% of budget in May and June respectively. The fourth quarter has understandably been significantly lower than prior periods, but our mitigation strategies have ensured that we suffered minimal losses and have retained a strong balance sheet, which is substantially unencumbered."

Financial review

Revenue declined 13.1%, mainly as a result of the revenue lost in the fourth quarter with the lockdown of the economy. The decline is notwithstanding that Radiant revenue is included for a full year, as compared to only six months in the previous financial year.

Gross margins improved from 24.0% to 25.0% attributable mainly to the change in product sales mix, with the introduction of Radiant for 12 months, with higher margin lighting sales now a bigger proportion of the group's revenue.

"Likewise, while the cable and overhead line product margins remain under pressure, as they are predominantly project-related, the shift in the product mix to higher margin low voltage products has helped to maintain margins in this division."

Overheads declined by 9.0% during the year, even though the costs for Radiant for the full 12 months were included. These were affected by:

- the introduction of IFRS 16 lease capitalisation where lease finance charges of R8.9 million are now included in interest paid;
- the non-recurrence of certain rationalisation costs in the prior year from the inclusion of certain rationalisation costs incurred with the integration of Radiant and Eurolux, despite additional costs being incurred in the last six months with the consolidation of the Johannesburg facilities in the Lighting division; and
- the staff cost savings implemented during the lockdown, including a minimum salary reduction of 25% for all executives and senior management during the months of May and June.

Operating profit decreased 6.1% to R145.9 million (2019: R155.4 million), while operating margin improved to 6.2% (2019: 5.7%). This improvement is largely as a result of the focus on controlling cost increases in all divisions during the lockdown and more particularly by the efforts of ARB Electrical Wholesalers' management team to right size their business.

"Taking cognisance of the views expressed by economists, it is the view of the board is that it will take at least two to three years to get back to the level of activity prior to the lockdown necessitated by the COVID-19 pandemic. On this basis, evaluation of the future cash flows necessitated a write down of the Eurolux trademark and CraigCor goodwill, and an impairment in the value of certain properties. This negatively impacted the earnings of the group," said Neasham.

Headline earnings per share increased by 3.0% to 59.96 cents per share, compared to 58.20 cents in the prior period.

"Given the economic uncertainties which continue to prevail, the board is of the view that we must continue to preserve cash in the short term and took the decision to waive the declaration of a dividend at this time."

Electrical division (revenue down 16.7% and operating profit down 14.3%)
This division comprises ARB Electrical Wholesalers, GMC Powerlines, ARB Global, CraigCor and CED. Revenue continues to be hampered by the lack of any real economic growth or infrastructure expenditure in South Africa. The effects of the lockdown negatively impacted revenue generation in the fourth quarter of the financial year. Steps were taken to reduce overhead costs with "no work no pay" being applied across all levels of staff and securing some rental relief from external landlords.

Revenue decline during the year has been attributable to:

- The loss of significant trading opportunities during the initial lockdown period.
- The declining cable sales in a fragmented market as a result of the lack of any significant infrastructure projects in the declining South African economy, even before COVID-19.
- The limited spend by Eskom and municipalities on electrification projects.

Gross margin improved 0.2% as a result of the change in product mix, with the lower volume of cable sales and increase in proportionate revenue of the higher margin low voltage products.

"Prior to the pandemic hitting our shores, this division started a review of its operating structure, which was noticeable in the December 2019 interim results. Although these efforts were continued in the last six months, the savings during COVID-19 were insufficient and this division made losses during April 2020."

Despite significant reduction in revenue, the savings made in operating costs ensured that the operating margin improved marginally to 4.2%. This division is currently in the process of further staff rationalisation to restructure the business in anticipation of reduced demand in an ailing South African economy.

"The division's management of working capital is commendable enabling it to remain cash generative."

Lighting division (revenue up 4.0% and operating profit down 19.4%)
This division comprises Eurolux, Radiant and Cathay Lighting. Revenue was higher because of the inclusion of Radiant's turnover for the full 12-month period as compared to only six months to June 2019.

"The disappointing revenue is predominantly attributable to the delivery challenges experienced by the division during the third quarter as the consolidation of the Johannesburg warehouses resulted in unnecessary congestion in the operations, which impacted service delivery. After these were resolved, the lockdown resulted in a loss of approximately six full weeks of trading. Once the lockdown was reduced to level 4, the cost and effect of operating protocols implemented to ensure health and safety compliance to mitigate the contamination risks of COVID-19, continued to constrain operations in the fourth quarter."

Neasham said further that the division was overstocked at December 2019, which enabled customer requirements to be fulfilled when the supply chain from China was severely interrupted. "As previously reported, revenue from lamps has been negatively affected by the changes in technology, with the newer LED products being more durable and less expensive. The lack of minimum technical specifications has resulted in an unregulated market, allowing lower quality lamps to compete in the consumer market where price is the major purchasing consideration."

Operating overheads increased by 8.9% from last year due to the inclusion of a full 12 months of Radiant's trading, and the COVID-19 induced inability to extract operational cost savings of the consolidation move from Linbro Park to Wynberg.

"The restructuring of the division is now largely finalised, and the rightsizing of the business for the anticipated next normal should result in a significant reduction in the cost base. The decline in revenue and the inability to complete the facilities rationalisation process until June 2020 resulted in a further reduction in operating margin to 4.2% (2019: 5.5%) of turnover."

Neasham added that that the division remains overstocked and management's focus for the next six months is to complete the rightsizing of the operation while actively focusing on cash generation by reducing stock levels.

Corporate division (Revenue up 10.9 %, operating profit up 20.4 %)

This division comprises the property portfolio and the Xact ERP Solutions business. The increase in operating profit resulted mainly from the additional rental in respect of the Lords View development, which commenced in January 2019. Given the fixed nature of the property rental income, Neasham said the results are in line with expectations and that the inclusion of the rental for Lords View for a complete year is the main reason for the increase in revenue and operating profit.

"Xact ERP Solutions is actively involved in the implementation of the warehouse management system by the Electrical division but is developing a stand-alone identity relevant to its target market."

Neasham addeded that the division as a whole continued to show customer gains but remains a small revenue and profit generator for the overall group.

Outlook

"The pandemic has exacerbated the pre-existing weakness in Eskom, as well as in the building and construction sectors. Business and consumer confidence is also at historically low levels, and it appears unlikely that pre-pandemic levels of confidence, economic growth in our business sector, and normality in markets and many aspects of daily life will return before the end of 2020."

Neasham said that while it is difficult to forecast the group's performance with the current state of the lockdown, it is anticipated that ARB's trading is likely to remain constrained in the coming months while lockdown restrictions are maintained or slowly lifted. This has unfortunately necessitated both trading divisions to give effect to retrenchments under retrenchments under S189A of the Labour Relations Act.

"We also foresee difficulty in obtaining credit insurance for our customers in future, which will increase the risk of credit loss to the group and could hamper revenue generation as we limit our credit risk exposure. However, we remain committed to ensuring that we maintain sustainable operations capable of taking advantage of any short- or medium-term improvements in the South African economy," he continued, adding that this being said, notwithstanding the expected muted trading conditions, the group has significant financial resources, geographical footprint, distribution capability and a well-established solid management team that can manage the effects of COVID-19 on the business and lead it out of the recession profitably.

"While acquisitions remain an integral part of our growth and expansion strategy and the board is cognisant of the opportunities that are currently presenting themselves, the immediate focus is to ensure that the full benefits are finally realised from the integrated Eurolux and Radiant operation, and to manage the warehouse management system project implementation at the Lords View distribution centre to monetise the opportunities that this facility presents to the Electrical division."

-ENDS-

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