

Date 20 February 2023



RESULTS COMMENTARY

The ongoing overreaching effects of the operating challenges faced on a local level have proved too overwhelming for Bowler Metcalf Limited, whose interim results illustrate the extent of the depressed trading conditions in the country of operation.

- Revenue from continued operations realised a 13% increase to R358.3m from R316.6m in December 2021.
- The Plastic Packaging segment, the largest segment of the Group, saw EBIT decrease by 41% filtering through to a 25% decrease in overall EBIT to R38.5m from R51.2m in H1FY22.
- HEPS declined by 18% to 48.39cps during the period from 59.37cps achieved in H1FY22.
- An interim dividend amount of 15.8cps was declared for the period, a decrease of 18.6% from 19.4cps printed in H1FY22.

OUTLOOK FOR NEXT REPORTING PERIOD

With more than 200 days of loadshedding experienced in 2022, plastic packaging company BCF has felt the brunt of this disaster having seen its salient features knocked down in a period of anticipated recovery from the recent blow on businesses caused by the Covid-19 pandemic.

Despite major headwinds like high interest rates, increased input costs, high inflation, supply chain issues, and global uncertainties stemmed by the Russia-Ukraine conflict, Eskom's energy crisis has been the biggest blow on the Group which emphasises the direct necessity for a stable and continuous electricity supply for their plastics business.

BCF's response to the challenges have varied but management's view is that a multitude of solutions is required to tackle the problem. Maximising the available hours of energy supply by matching work hours to Eskom loadshedding schedules to keep supply chains operational has been a solution in the short term. This approach however is not sustainable with employees forced to work irregular hours to service their customers. Investment in intelligent energy management solutions remains the medium to long-term solution with a view of having a mix of energy supply, from the traditional Eskom power producer solution to solar, alternative energy and sophisticated energy storage solutions. With record high diesel prices, the cost to run generators during loadshedding hours is too great and poses a threat to the profitability of the Group.

A major concern of the Group is the anticompetitive environment brewing as a result of some manufacturers not being exposed to Eskom's loadshedding. Largely being on the receiving end, BCF extrapolates that this undue pressure will adversely affect the industry so long as the crisis persists with an expected shift in the plastics manufacturing market expected with several business shutdowns and job losses.

Continuing on their share repurchase programme, the Group repurchased 1 139 085 (2021: 272 805) shares during the period for a total consideration of R11.4m at an average cost of R10.01 (2021: R11.33) per share, positively influencing HEPS despite an overall decline in HEPS during the reporting period. The current share price of the company is trading at around R9.20 per share. The repurchases were made through a wholly owned subsidiary with no acquired shares cancelled subsequent to period end.

A significant 39% decrease in right of use assets has been realised from R4.4m to R2.7m in the reporting period as a result of current third-party property leases nearing their termination date, hence a 36% reduction in total lease liabilities from R4.5m to R2.9m. Cash and cash equivalents saw a 14% decline to R155.3m from R180.9m in H1FY22 following extensive investment in plant and equipment and a substantial share repurchase on the back of a low cash flow amount from weak trading activities in the pervious period.

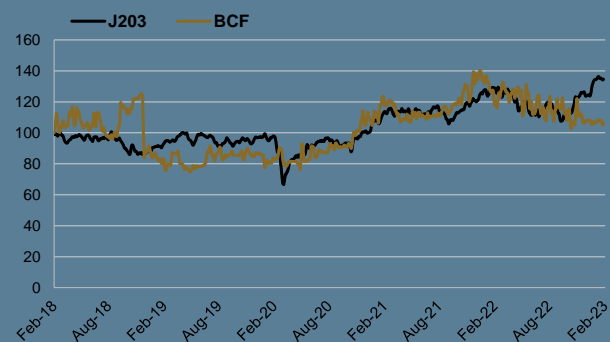
BCF – Bowler Metcalf Limited Interim Results Equity Update

Valuation: **Overvalued**

BCF released interim results on 7 February 2023 for the period ended 31 December 2022

Price (R)			9.20
PE Fair Value (R)			6.57
DCF Value (R)			7.32
Upside (Downside) to DCF (%)			-20.5%
DY%			4.7%
Price Performance		Absolute	Relative to JALSH
1 month		0.0%	0.3%
3 month		-12.4%	-21.6%
YTD		-1.1%	-4.9%
12 month (SA Rands)		High 11.99	Low 8.00
No. of shares (m)	76	Price (R)	9.20
NAV per share	9.30	Mkt cap (Rm)	700
EV (Rm)	495	Price/Book (x)	0.99

Financial Year	2021	2022	2023F	2024F
Turnover (Rm)	636	673	653	692
EBITDA	133	119	105	139
EBIT	111	100	82	100
PAT	91	83	77	87
HEPS (cents)	127.3	116.3	107.7	122.2
P/E ratio	9.1	7.9	8.5	7.5
EV/EBITDA	4.4	4.0	4.1	3.0
EBITDA margin (%)	21.0%	17.6%	16.1%	20.1%
ROCE (%)	15.3%	13.4%	10.8%	12.3%
ROE (%)	12.9%	11.5%	10.5%	11.2%



With several settlements of large capital expenditure related to creditors that occurred at the previous year end, trade and other payables realised a 40% decline to R42.8m from R71.8m as a result.

The Group believes that they have the adequate financial and human resources to stay afloat the sweeping waves posed by the many challenges in the South African trading environment, however, they have stated that the FY23 results are unlikely to show improvements from those printed in FY22, although they look forward to cost alleviations and a positive adjustment in market demand.

Overall, we forecast a 2.9% decrease in revenue on account of continued operational challenges in a period of multiple trading difficulties. This will take the revenue amount to R653.3m followed by a 6% uptake as market demand is corrected and operational challenges are alleviated. However, the cost of loadshedding is still expected to be a thorn in the profitability of the Group, leading us to conclude that FY23 will see an 18.1% decline in EBIT to R82m followed by a 21.4% uptake to R99.5m in FY24 for which we expect improvement in the electricity crisis and strict cost controls across the whole value chain of the business.

SEGMENTAL PERFORMANCE

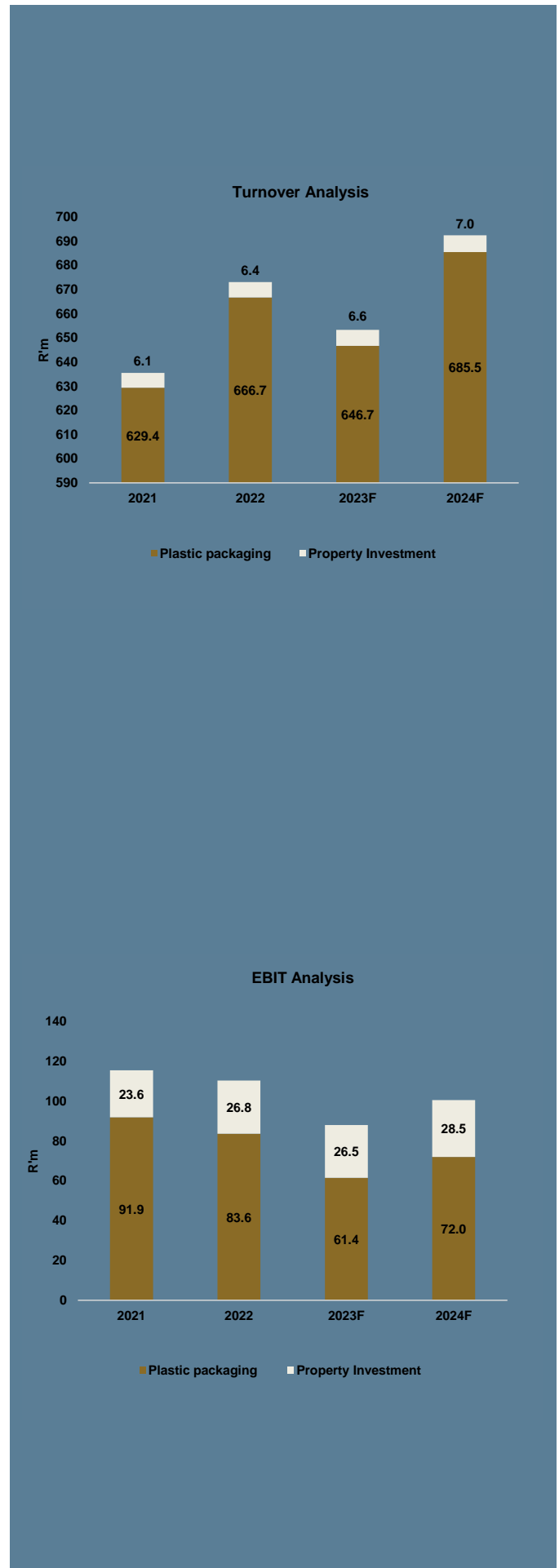
The Group has two reportable segments, namely **Plastic Packaging** and **Property Investment**.

The **Plastic Packaging** segment saw revenue for H1FY23 increase by 13% to R354.9m from R313.4m achieved in H1FY22. Traditional volumes remained relatively flat with the new Skye Plastics acquisition contributing largely to the revenue growth in additional sales contribution. However, management believes the results printed by Skye Plastics have been subdued by the bitter trading conditions in the country. An operating profit of R27.3m was realised, a sharp 41% decline from R46.2m printed in H1FY22. The decrease is largely attributed to increased input costs in an inflationary environment coupled with large increases in transport and energy costs. This had a detrimental effect on EBIT margins almost halving from 14.7% achieved in December 2021 coming in at 7.7%, the lowest margin recorded in recent times.

Plastic converting inherently requires a large amount of stable electricity supply and with the recent bout of unprecedented loadshedding, the segment has been largely muted in growing their revenue stream while incurring large operating costs. In the reporting period, BCF's production plants experienced various stages of loadshedding for 70% of the available production days, putting undue pressure on the Group's ability to deliver to customers. Stock-outs have occurred during the period, hindering the Group from revenue sales, leaving the segment helpless on account of a failing power utility. The inability of Eskom to keep the lights on underscores the harsh reality of doing business in South Africa as many businesses report filched revenues.

Project launch delays, product spoilage and unfair trading competition are factors raised by management on the overreaching effects of the energy crisis. With a huge reliance on electricity from the national grid, BCF has resolved to diversify their power supply but emphasise that they are way behind their competitors. A focus on smart power consumption, labour flexibility and increasing operating hours to squeeze out all potential from the segment will be placed going forward while strict management of costs and productivity will also become a great focus to keep the segment afloat.

Following a tough six months ended 31 December 2022, ailed with increased costs due to a multitude of reasons with the electricity crisis at the forefront, we forecast sustained pressure on profits with no loadshedding end in sight. As such, we anticipate revenue for the segment to decrease by 3% to R646.7m as the Group continues to struggle with stockouts and pressures on operations and demand. FY24 will see the revenue amount increase by 6% to R685.5m with the hope of a more stable electricity grid in the country together with an improved mixture of electricity supply. CAPEX expenditure during the period into new product lines will also improve volumes for the segment. FY23 will persist with elevated costs which lead us to forecast a decrease in margins from 12.5% to 9.5% resulting in an EBIT amount of R61.4m for FY23, down 26.5% from R83.6 printed in FY22. Margins are then expected to realise an increase to 10.5% in FY24, giving rise to an EBIT amount of R72m as costs are consolidated and energy availability is secured.



The **Property Investment** segment revenue increased by a moderate 6.3% to R3.4m during the reporting period, coming from R3.2m in H1FY22 as higher interest rates on account of increasing inflation bodes well for the segment. Operating profit increased slightly to R13.5m from R13.4m in the previous comparative period. It is important to note that intersegmental operations amounted to R13.5m during the reporting period. Of the R18.4m overall capital expenditure, R16.8m has been used in the property segment, largely pertaining to the completion of the Phillippi Warehouse. Strict management of cash utilisation has been in place as the Group suffers through a difficult trading environment, but the new warehouse can be expected to improve efficiencies for the Plastic Packaging segment which uses the facility for its operations. Boasting a solar system, the warehouse will decrease the reliance on Eskom for a stable power supply.

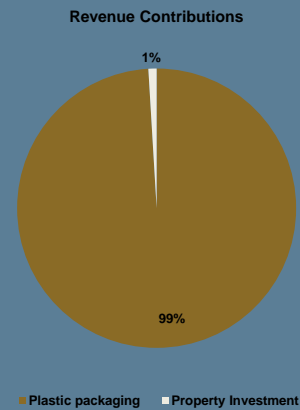
Given the high interest rate environment, we anticipate the segment to see a 3% increase in revenue to R6.6m followed by a 5% uptake in FY24 to R7m as CAPEX initiatives prove fruitful in the medium term. EBIT is expected to see a 1% decline to R26.5m to which FY24 will see a 7.6% uptake to R28.5m.

COMPANY RISK

- Continued high levels of loadshedding.
- Loss of market share due to lowered demand and anticompetitive environment on account of electricity supply.
- High input costs.
- Subdued trading environment.
- Project launch delays.

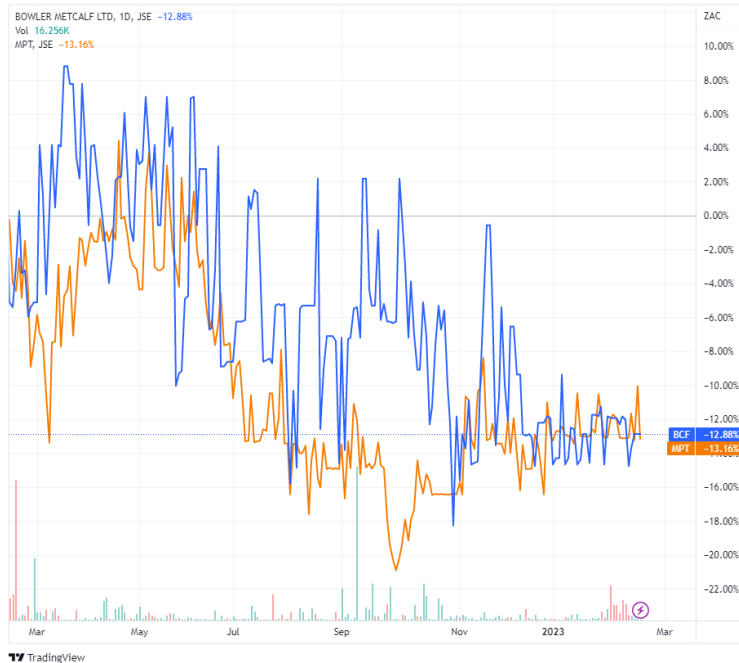
TECHNICAL ANALYSIS

On a technical analysis basis, BCF is currently in a wedge pattern with upper resistance around R9.80 per share and lower support at R8.80 per share. A breakout above the downward slopping line at around R9.80 could see some upward price potential. A fall below the lower line could potentially see the share price lower to more past support levels around R8 per share. We have used a lookback period of one year on a daily timeframe.



COMPANY COMPARISON

When comparing Bowler Metcalf to Mpact, the share price can be seen as moving closely together in price with the share price of BCF moving more volatile. The volatile price movement can be expected as BCF's share price is less liquid and has a wider bid-ask spread. Both share prices have decreased in value by more than 10%. We have used a lookback period of one year on a daily timeframe.



VALUATION

Inherently, most of what is consumed is packaged, cementing the longevity of the packaging industry and with developments in making such products more environmentally friendly and less energy dependent, packaging will remain essential as we transition into a more environmentally aware society. However, without the ability to service customers, the promise of sustained demand is redundant. Given the challenges posed on the industry, BCF has been dealt with significant blows to profitability but remain in prime location to take advantage of any uptick in the trading environment in the country. Strict controls on costs and growth are also likely to improve the upcoming results but with loadshedding forecast to become a norm in the short to medium term, dark days seem plenty for the packaging company.

Based on our DCF and relative P/E valuation, the share is currently **Overvalued**.

With reference to the DCF table, we have considered a discounted cash flow analysis with cash flows forecast to FY25, utilising a terminal growth rate of 4.5% to yield the sensitivity table to the right, for which we used a discount rate of 20.2%¹, yielding a value of **R7.32** per share.

With reference to the relative P/E table on the right, we have compared Bowler Metcalf to other small-cap packaging companies, which gives a better indication of value relative to other companies within the industry. The implied P/E valuation of 6.24x places Bowler at a price of **R6.57**.

¹ The discount rate is based on the average implied discount rate obtained from cash flow forecasts for companies with market capitalisations between R700m and R1bn in our research universe.

P/E Calculation			
PEERS	Price	Market Cap (R'm)	P/E ratio
Transpaco Limited	31.24	984	6.57
Mpact Limited	29.10	4231	7.72
Nampak Limited	0.96	609	2.67
Median			6.57
Bowler Metcalf Limited	9.20	700	8.73
Discounts			
Company specific discount			5.0%
Size discount			0.0%
Discount applied to weighted P/E			5.0%
Adjusted P/E			6.24
Total Valuation for Bowler Metcalf Limited			
Adjusted P/E multiple			6.24
Sustainable Forward earnings per share			1.05
P/E Value per share			6.57
<i>Implied current gain/(loss)</i>			-28.58%

DCF Sensitivity Analysis					
Discount rate					
Growth rate	19.2%	19.7%	20.2%	20.7%	21.2%
0.0%	6.33	6.16	6.00	5.84	5.69
2.5%	7.07	6.85	6.65	6.45	6.27
3.5%	7.43	7.19	6.96	6.75	6.54
4.5%	7.84	7.57	7.32	7.08	6.85
5.5%	8.31	8.01	7.72	7.45	7.20
6.5%	8.86	8.51	8.18	7.88	7.60
7.5%	9.50	9.09	8.72	8.37	8.06

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