

Price (BWP): 14.00
 EPS TTM (BWP): 0.68
 PER TTM (x): 20.71
 PBV (x): 2.65
 Earnings Yield (%): 5.07
 Dividend Yield (%): 2.14
 Recommendation: FOLLOW RIGHTS

Sefalana launches Rights Offer.....

On 2 November 2016, Sefalana released a circular in relation to its previously announced renounceable Rights Issue wherein it is looking to issue 27,858,523 ordinary offer shares at BWP 12.60 each, on the basis of 1 offer share for every 8 shares held. The offer opened on 2 November 2016 and will close on 9 December 2016.

The company is seeking to raise net proceeds of approximately BWP 351.0m from the offer to fund the following:

- **The Lesotho Acquisition Transaction**
 - Sefalana, through its 95% owned Lesotho subsidiary, Sefalana Trading Lesotho (Pty) Ltd has entered into an agreement to purchase the Lesotho TFS Cash and Carry Business.
 - TFS operates in Maseru, Lesotho, selling a wide range of fast moving consumer goods.
 - The entire legal entity of TFS will not be acquired, but only specified assets, namely certain fixed assets, contractual rights, trade debtors, stock (inventory), trade name, intellectual property and goodwill.
 - The business operates from a single location and employs approximately 95 people.
 - The consideration for the purchase of the Lesotho business is ZAR 80.0m; comprising of the net asset value of specified assets (ZAR 23.0m), the value of inventory (ZAR 30.0m), and the value of intangible assets (ZAR 27.0m).
 - Sefalana group turnover is expected to grow by over BWP 300.0m in the year following the acquisition.
 - This is expected to translate into additional profit after tax of approximately BWP 7.0m in the first year after the acquisition.

- **The South Africa Investment Transaction**
 - Sefalana has entered into an agreement to participate in a Consortium which owns an existing retail and wholesale FMCG store network operating throughout South Africa.
 - Investment in the South Africa Consortium will be for a 25% interest in the share capital of the business.
 - Consideration for the transaction is ZAR 200.0m.
 - The business operates from multiple locations and currently employs approximately 450 people.
 - The Consortium is to acquire a number of target stores (approximately 30) commencing in January 2017.
 - This investment is expected to translate into an additional profit after tax of approximately BWP 19.0m in the first year.

Financial Summary

| Income Statement (BWP'm) | FY 16 | FY 15 | %ch |
|-----------------------------|----------|----------|--------|
| Revenue | 3,825.37 | 3,463.96 | 10.43% |
| Gross profit | 310.15 | 282.65 | 9.73% |
| EBIT | 206.80 | 185.30 | 11.61% |
| PBT | 207.14 | 191.15 | 8.37% |
| Net profit | 157.59 | 152.47 | 3.36% |
| EPS (thebe) | 67.60 | 65.39 | 3.38% |
| DPS (thebe) | 30.00 | 30.00 | 0.00% |
| NAV/share(thebe) | 527.38 | 492.90 | 7.00% |
| Balance Sheet (BWP'm) | | | |
| Non current assets | 907.66 | 776.72 | 16.86% |
| Current assets | 964.12 | 935.48 | 3.06% |
| Total assets | 1,879.79 | 1,719.36 | 9.33% |
| Non current liabilities | 174.40 | 139.39 | 25.12% |
| Current liabilities | 530.02 | 481.45 | 10.09% |
| Equity | 1,175.36 | 1,098.52 | 7.00% |
| Ratios and Margins | | | |
| Gross profit Margin (%) | 8.11% | 8.16% | |
| Operating profit margin (%) | 5.41% | 5.35% | |
| PBT margin (%) | 5.41% | 5.52% | |
| Net profit margin (%) | 4.12% | 4.40% | |
| Inventory Turnover (x) | 9.23 | 9.99 | |
| LT Debt / Equity (%) | 6.62% | 5.29% | |
| Current ratio (x) | 1.82 | 1.94 | |
| RoAE (%) | 13.86% | 16.75% | |
| RoA (%) | 8.76% | 10.50% | |
| Dividend cover (x) | 2.25 | 2.18 | |

Source: Sefalana Financial Statements

Along with the reasons stated above, some of the proceeds will be used to fund property acquisitions relating to the aforementioned transactions and other future transactions in the short to medium term that will aid the group's regional expansion plans.

Summary use of proceeds

| Use of proceeds | Amount (BWP' m) | % |
|--|--------------------|--------|
| Lesotho TFS acquisition | 63.0 | 17.95% |
| Investment in the South African Consortium | 156.0 | 44.44% |
| Further store openings in Lesotho | 40.0 | 11.40% |
| Purchase of related property | 80.0 | 22.79% |
| Other working capital requirements | 12.0 | 3.42% |
| TOTAL | 351.0 | |

Source: Sefalana Rights Circular

While Botswana's retail sector is nearing saturation, we believe that Sefalana will continue to register growth anchored by the group's diversified revenue streams (geographically and product offering). The company continues to be proactive with regard to expanding operations outside Botswana (currently has 14 stores in Namibia - which contribute 29% to group revenue and 10% to PBT, with a medium target of 20 stores). The expected profit impact of both the aforementioned transactions is accretive from year one, with EPS forecast to increase to 70.67t (FY 16: 67.60t) post acquisitions.

Although the Lesotho acquisition is pricier than the South Africa investment with its one year forward PER of 9.00x vs. 8.32x for South Africa, both transactions are at a discount to the peer average of 22.62x. Sefalana's strategy to invest into a consortium that invests in an existing network of retail and wholesale outlets, shields it from some execution and penetration risks normally associated with market entry, by virtue of the entities already having an established customer base and market share; and local knowledge of the market.

The offer price of BWP 12.60 puts the offer shares at a PER of 18.64x and P/Sales of 0.73x - Sefalana's outstanding shares trade at a PER of 20.71x and P/Sales of 0.82x while its peer, Choppies, is trading at multiples of 37.55x and 0.53x, respectively. The offer at BWP 12.60 is at an 8.99% and a 10% discount to the theoretical ex-rights offer price (TERP) of BWP 13.84 and share price of BWP 14.00, respectively, we therefore recommend holders **FOLLOW** their rights.

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