INNSCOR 9 MONTHS ENDED 30 JUNE 2016 REPORT

PLATINUM INVESTMENT MANAGERS PVT LTD
influence the future

Market Data			
Current Share Price(Usc)			**23**
Shares in Issue			**541,593,440.00**
Market cap(US$)			**124,566,491.20**
YOY high(Usc)			**62**
YOY Low(Usc)			**17**
YTD			**-33.90%**
YOY			**-66.40%**
EPS			**3.20**
P/E			**7.19**
Income Statement	**FY2016**	**FY 2015**	**% Change**
Revenue	586,910,708.00	554,288,478.00	**5.9%**
EBITDA	55,026,751.00	43,550,254.00	**26.4%**
Profit After tax	30,477,416.00	23,140,039.00	**31.7%**
Operating margin	9.4%	7.9%	**19.3%**
Net Profit margin	5.2%	4.2%	**24.4%**
Financial Position			
Total Assets	453,060,615.00	576,099,406.00	**-21.4%**
Total Liabilites	188,778,586.00	244,161,269.00	**-22.7%**
Attributable Equity	171,351,687.00	216,437,154.00	**-20.8%**
Cashflows and Ratios			
Cashflows from Operations	35,390,082.00	46,885,003.00	**-24.5%**
Cashflows from Investing	(30,794,938.00)	(40,480,637.00)	**-23.9%**
Cashflows from Financing	(10,368,426.00)	(9,675,519.00)	**7.2%**
ROE	10.55%	11.60%	**-9.1%**
Current Assets to CLs	1.30	1.41	**-7.6%**
Total asset turnover	1.30	0.96	**34.6%**
Gearing ratio	11.48%	9.93%	**15.6%**
PAT/CFO	0.86	0.49	**74.5%**

Innscor Revenues Up 6%, PAT Up 32%

The restructuring activities of the Group appear to be visibly bearing fruits according to the impressive set of results of the Group's continuing operations which are now mainly comprised of light manufacturing. Revenue was up 6% supported by an improvement in volumes sold across all of its operations that is National Foods, Baking Operations, Irvine's, Colcom, Profeeds and Natpak. Operating profits recorded an even better performance of 26% growth due to improved efficiencies that led to major cost cutting despite a reduction in prices meant to drive volumes. PAT grew by an even higher 32% and were bolstered by higher profits from associate companies that is Profeeds and Pure Oil industries. Below is the performance of the various segments that now make up Innscor Africa Limited;

BAKERY OPERATIONS

- 30% growth in bread volumes driven by management structure realignment, improved product quality and market coverage.
- 265% growth in operating profit.
- Old vehicle fleet replaced completely by a new fleet.

NATIONAL FOODS

- 13% growth in total volumes with strong performance from Maize and Flour division.
- Volume growth achieved through low prices and improved national coverage.
- 5% growth in Revenues and 12% growth in Operating profit due to procurement and production efficiencies.

COLCOM

- 14% growth in pork volumes. It has become self-reliant in its pig supplies.
- Revenues down 7% due to a change in the sales mix whilst favorable maize positions and an excellent cost containment programme resulted in a similar level of operating profit being achieved.

IRVINES

- 6% growth in revenues.
- Operating profit down 22% due to lower prices induced by high competition.

CAPRI

- Volumes down 7% whilst revenues were down 17% due to low demand and influx of grey imports.
- 67% drop in operating profit.

NATPAK

- 57% growth in volumes driven by a new packaging line.
- 46% increase in revenues and 235% increase in operating profit.

PROFEEDS

- 10% growth in volumes but lower prices resulted in same revenue as previous year.
- High operating costs resulted in 9% decline in operating profit.
- Acquired non-controlling stake in Probands
- UHT plant to be commissioned in November 2016.

Overally, operating and net profit margins were much stronger recording growths of 19% and 24% respectively. Total asset turnover also indicated much improvement of 35% together with quality of earnings which although remains below one, recorded an impressive growth of 75% to 0.86. Basic EPS for continuing operations stood at 3.2cents and was up 101% from the previous year. A final dividend of 0.6cents was declared giving a payout ratio to 19%.

DISCONTINUED OPERATIONS

Discontinued operations are made up of the unbundled Quick Service Restaurants which relisted as Simbisa and Specialty Retail and Distribution which relisted as Axia. Interests in Spar Retail and Shearwater were sold. Spar Distribution Centre was closed and negotiations to dispose of interests in Zambia and The River Club are underway. Overally these discontinued operations recorded a 5% decline in revenues with worst performance coming from the businesses which were either disposed of, closed or are in the process of being disposed. Operating profit was down 46% also due to poor performance from the other businesses which had once off charges of $10 million. Below is the performance of the various discontinued operations;

TV SALES AND HOME

- Reporting was done for a period of 9 months from unbundling.
- Revenue down 17%, volumes down 15% and prices down 3%.
- 5 additional stores were added.

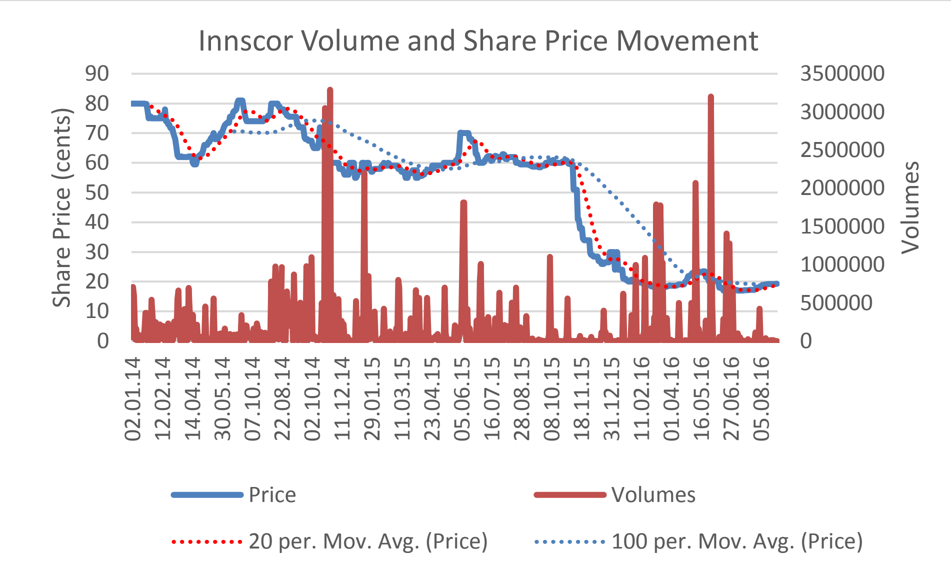
TRANSERVE

- 10% drop in revenue.
- Improved buying efficiencies ensured a drop in operating profits was limited to 2%.
- 4 fitment centres opened.

DGA

- 28% growth in volumes, 14% revenue growth and 30% growth in operating profit.
- Creation of Vital logistics resulted in administrative, warehousing and distribution cost efficiencies.

Technical Analysis



The sharp decline in the Innscor share price in November 2015 was due the market price correction after the unbundling of the Quick Service Restaurants. There was another price adjustment after the unbundling of Axia but this one is not quite visible in the price trend as it was only a small price change. Although trading volumes have remained resilient, there is visible evidence of thinning in 2016 due to lower investor participation on the ZSE. Towards the end of August, the short term average line appears to be on the verge on cutting the long term average from below, a sign of an emerging uptrend. Given the strong performance from the released results we believe that despite the low trading interest on the local exchange, the emerging uptrend can persist resulting in an improvement in the Innscor share price.

Investment case

- The group's unbundling activities have led to a substantial improvement in efficiencies of all continuing operations.
- Cost management initiatives and higher volume movements have contributed to stronger margins in a declining margin environment.
- The Group has laid strong foundations for sustainable earnings through rightsizing its stuff, closing or disposing of non-performing units that were weakening the performance of the conglomerate and making acquisitions that are meant to further strengthen in-house synergies.
- Innscor's management has shown high levels of competence so far in its current and even previous restructuring activities that were meant to enhance shareholder value. A much improved performance has been observed after the latest restructuring and even previous similar exercises like the unbundling of Padenga continue to enhance shareholder value as has been observed from the strong performance of the company.
- Going forward the Group will continue to have a strong focus on cost containment activities and so far some important ground work has been laid such as the complete replacement of the old fleet belonging to Baking operations, complete self-reliance in its pig supply and strategic synergies.
- Innscor stands as one of the key beneficiaries of the introduction of Statutory Instrument 64 which is meant to protect local manufacturers.
- Although the Group also experiences a delay in its foreign payments for raw materials, it is in the high category list in the RBZ foreign payments system and as such it is in a better position in its raw materials acquisition.
- An even better performance is expected in the coming period as the disposal and closure of the non performing entities which were pulling down Group performance would have been completed.

Investment concerns

- The continued deterioration of the operating environment poses a significant threat to the impetus of the business. Of high importance is is the shortage of physical notes which is reducing consumer expenditures, low inflation levels, high competition and the rising levels of unemployment.
- The impending introduction of bond notes has already created a high level of risk aversion especially among foreign traders on the local exchange. This has affected trading volumes of previously actively traded stocks like Innscor. If these bond notes are over printed as is the general fear then this will certainly affect the performance of Innscor in a number of critical ways such as the importation of key raw materials.

Valuation and Recommendation

Going forward, we expect revenue growth to be supported by a continued positive momentum in volumes across all the segments as the Group has laid the necessary foundations to support production. Further price cuts will be instituted so as to maintain and where possible grow market share. To further support volumes will be the Statutory Instrument 64 which seeks to promote local manufactures like Innscor. We expect Innscor to reap some benefits from this policy instrument albeit with the porous border posts. Growth in 2016 came from a low base particularly in segments such as Bakery operations, Natpaks and Natfoods as these did not perform very well in 2015. As such we expect revenue growth to taper off to 4% in 2017 in consideration also of the difficult operating environment. Margins are however expected to improve slightly given the continued intensive drive to reduce costs and also the absence of some nonrecurring expenses such as the $1.4 million impairment expenses charged for the old bakery fleet that was replaced during 2016. We also expect equity accounted earnings to also improve supported by SI 64 which is anticipated to bolster volumes of Pure Oil where Natfoods has 40% interest. EBIT margin is therefore expected to improve by 0.6% to 7.3%. The complex restructuring of Innscor makes the use of various valuation models complex and as such in our valuation we considered the Maintainable Earnings Approach and the Net Asset valuation of the company. The former method gives us a fair value of 27c per share whilst the NAV of the counter stands at 31.7c. A combination of both valuations gives us a forecasted fairvalue of 29.3c per share which gives an upside potential of 28% from the current price of 23c. We therefore give a **BUY** recommendation.