

3Q23 Trading Update – broadly in line

- The update is broadly in line with our expectations; however, sales growth remains challenging, particularly cash sales. UFO remains under pressure with sales down 9.7% in the nine months ended December 2022. Traditional brands grew sales by 3.7%, supported by credit sales which are up 16.8% to 58.3% of total sales. Sales in comparable stores was up 0.4% for the nine month period. The operating environment is difficult made worse by loadshedding.
- Black Friday sales were strong resulting in growth for November (despite a high base), followed by further growth for December. January has been an acceptable trading month. We forecast 5% sales growth for Traditional and -10% for UFO for FY23E, equating to sales growth of 3% compared to the 2% achieved in the nine months ended December 2022.
- The Pepkor Holdings trading update for the three months ended December 2022 showed -0.5% growth for JD Group, -2.7% on a like for like basis. Its group credit sales growth was 21%. In comparison Lewis's Traditional business achieved 3Q sales in line with the prior year with 17.3% growth in credit sales.
- Growth in other revenue is improving given higher credit sales (positively impacting insurance and ancillary revenue) and finance income is achieving higher yields given higher interest rates. Finance income has lagged the rates hike cycle but will continue to benefit as the book reprices. Other revenue was up 4.2% for the nine month period and 5.3% for 3Q. We forecast 5.5% for FY23E.
- Ancillary income includes extended warranty insurance that only kicks in after 12 months after the sale – growth momentum will therefore rise. Insurance income is more reflective of credit sales growth but also requires upfront policy charges and therefore growth will lag the strong credit sales growth.
- The quality of the debtors book continues to improve, with a 0.2% rise in debtor costs for the nine months. We forecast the charge to rise by 3% in FY23E. Despite a challenging operating environment and robust growth in credit sales, loss ratios are well managed. The benefit of a growing percentage of debit order collections (42% at 1H23) continues to have a positive impact. Collection rates improved to 82% for the nine months from 79.1% and are running at 82.7% in 3Q. Credit granting criteria has remained consistent.
- GP margins have remained relatively stable and within the guidance provided by management, namely 40-42%. We forecast 40.5%, in line with the prior year. Some relief is coming through from lower shipping rates, although this will only be felt in FY24E. This will be positive for UFO and its pricing. Inventory levels will decline now that logistical constraints are easing. We make little change to our operating cost growth outlook, remaining at the upper end of management guidance of 4-8%.
- Our HEPS outlook remains broadly unchanged – 852c (+1%) in FY23E and 1053c (+23%) in FY24E. FY24E should benefit from improved UFO results and rising debtors book yields. The buyback programme will continue and a further 10% of shares are expected to be cancelled in FY23E and FY24E. We anticipate a dividend payout ratio of 53%, equating to a 424c DPS, a forward dividend yield of 9.2%.
- Lewis is trading on an attractive forward 12m P/E of 4.7x and an EV/EBITDA of 2.9x. We have ROE's rising from 11.7% to 13% in FY25E – management is targeting 15% in 5 years which would be positive for the stocks rating. In our DFCF valuation we calculate a fair value range of R65.42-R77.72, a mid-point of R71.

Date: 30 January 2023

Analyst

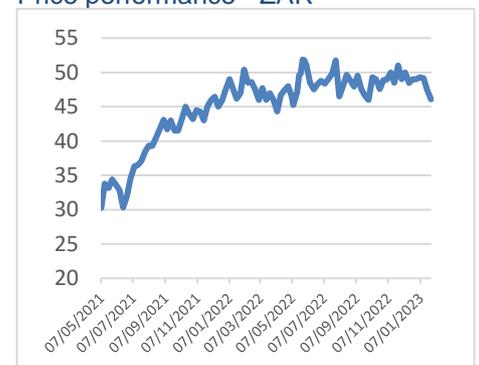
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Price (30/01/2023):	R46.00
Market cap	R2709mn
Shares in issue	58.8mn

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Price performance - ZAR



Source: FactSet

Figure 1 Financial summary

Year Ending	FY2019A	FY2020 A	FY2021 A	FY2022 A	FY2023 F	FY2024 F	FY2025 F
Income Statement							
Merchandise Sales	3,520	3,686	3,931	4,383	4,516	4,858	5,236
<i>Sales growth (%)</i>	22.9%	4.7%	6.7%	11.5%	3.1%	7.6%	7.8%
Gross profit	1,451	1,512	1,642	1,775	1,820	1,967	2,147
<i>growth %</i>	22.2%	4.2%	8.6%	8.1%	2.5%	8.1%	9.1%
Finance income	1,248	1,312	1,271	1,280	1,319	1,404	1,506
<i>growth %</i>	-8.4%	5.1%	-3.1%	0.7%	3.1%	6.4%	7.3%
Insurance income	647	666	707	776	857	898	953
<i>growth %</i>	-3.5%	2.9%	6.2%	9.7%	10.4%	4.8%	6.1%
Ancillary income	722	790	817	818	857	884	936
<i>growth %</i>	9.6%	9.3%	3.4%	0.2%	4.8%	3.2%	5.8%
EBITDA	522	629	1,039	1,095	1,047	1,177	1,277
<i>EBITDA Margin (%)</i>	14.8%	17.1%	26.4%	25.0%	23.2%	24.2%	24.4%
EBIT	443	254	696	668	665	820	909
<i>EBIT Margin (%)</i>	12.6%	6.9%	17.7%	15.2%	14.7%	16.9%	17.4%
Profit before tax	464	273	604	674	650	768	846
Net profit	310	182	433	483	474	557	613
Net profit post minorities	310	182	433	483	474	557	613
Headline Earnings	308	205	463	561	505	557	613
Basic EPS (ZAc)	377	232	576	731	800	1,053	1,291
Headline EPS (ZAc)	376	260	617	849	852	1,053	1,291
<i>% growth</i>	24.3%	-30.8%	137.0%	37.7%	0.4%	23.5%	22.7%
DPS (ZAc)	234	185	328	413	424	579	710
<i>Payout ratio (%)</i>	61.1%	78.9%	56.9%	56.5%	53.0%	55.0%	55.0%
Balance Sheet							
Cash and Cash equivalents	205	1,193	447	308	183	220	180
Current asset (ex – cash)	4,425	4,368	4,588	4,739	5,034	5,083	5,321
Net Fixed assets	299	1,018	1,021	396	439	507	579
Intangible assets	310	308	297	258	243	228	213
Investments	276	228	254	266	258	273	290
Other assets	274	273	218	940	954	1,002	1,042
Total assets	5,789	7,388	6,823	6,907	7,111	7,314	7,624
Debt	0	922	0	81	200	300	400
Current liabilities	783	1,052	1,295	1,305	1,477	1,521	1,563
Other liabilities	130	705	656	805	828	858	887
Total liabilities	913	2,679	1,951	2,190	2,505	2,679	2,850
Shareholders' equity	4,876	4,710	4,873	4,717	4,546	4,633	4,779
Minorities	0	0	0	0	0	0	0
Total shareholders' equity	4,876	4,710	4,873	4,717	4,546	4,633	4,779
<i>BVPS (ZAR)</i>	6,080	6,124	6,812	7,523	8,146	9,265	10,620
<i>ROE (%)</i>	6.0%	4.3%	9.7%	11.7%	10.9%	12.1%	13.0%

Year Ending	FY2019A	FY2020 A	FY2021 A	FY2022 A	FY2023 F	FY2024 F	FY2025 F
Cash Flow							
Reported net profit	310	182	433	483	474	557	613
Change in net working capital	151	-256	-139	-156	-130	-13	-203
Dividends paid	-168	-196	-147	-254	-244	-268	-317
Other adjustments	235	920	661	618	694	677	796
Cash flow from operations	528	650	808	691	794	953	889
Net Capex	-79	-104	-119	-67	-108	-136	-141
<i>Capex/sales (%)</i>	<i>2.2%</i>	<i>2.8%</i>	<i>3.0%</i>	<i>1.5%</i>	<i>2.4%</i>	<i>2.8%</i>	<i>2.7%</i>
Other investing cash flows	-48	96	23	102	5	-2	-2
Cash flow from investing	-127	-8	-96	34	-103	-138	-144
Equity raised/(bought back)	-105	-123	-136	-408	-391	-300	-250
Net inc/(dec) in borrowings	0	0	0	0	119	100	100
Other financing cash flows	-671	469	-1,323	-551	-545	-579	-638
Cash flow from financing	-776	347	-1,459	-959	-816	-777	-785
Net cash flow	-375	989	-747	-234	-125	37	-40
Free cash flow	439	179	610	680	632	816	699
Repayment of lease liabilities			-254	-297	-300	-309	-318
Net free cash flow	439	179	355	384	332	507	381
Valuation Summary							
Valuation Metrics							
Share Price (ZAc)	3,110	1,782	3,050	4,600	4,600	4,600	4,600
P/E (Underlying) (x)	8.3	6.8	4.9	5.4	5.4	4.4	3.6
P/BV (x)	0.5	0.3	0.4	0.6	0.6	0.5	0.4
EV/Sales (x)	0.9	0.9	0.8	0.7	0.7	0.7	0.6
EV/EBITDA (x)	6.1	5.0	3.0	2.9	3.0	2.7	2.5
EV/EBIT (x)	7.1	12.5	4.5	4.7	4.8	3.9	3.5
FCF Yield (%)	16.2	6.6	13.1	14.2	12.3	18.8	14.1
Dividend Yield (%)	7.5	10.4	10.8	9.0	9.2	12.6	15.4
Net debt	-205	567	359	723	996	1088	1258
Gearing ratio	-4%	12%	7%	15%	22%	23%	26%
Net debt (excluding lease liabilities)	-205	-271	-447	-227	17	80	220
Gearing ratio (excluding lease liabilities)	-4%	-6%	-9%	-5%	0%	2%	5%

Source: Company data, FactSet, ABS estimates

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