iM guest column

ANTHONY
CLARK

Down but not out of contention

There is potential on these two shares – for those who can make the right judgment calls

I was asked by the editor for updates on two stocks that have been beaten up by the market in 2018.

One is consumer electrical and satellite services provider Ellies Holdings, a micro-cap with a market value of R118m and trading at 20c at time of writing, down 48% year to date. The other is agricultural investment fund Zeder Investments, now on a 20% discount and a share price of 470c. It has suffered via its large holding in Pioneer Foods, and Zeder has fallen 31% in 2018.

Ellies Holdings' fall has been epic. Listed on the JSE's Alt-X market in 2007 at 200c a share, Ellies ran to 990c by 2013. But in 2013 it was becoming clear the wheels were falling off.

What caused the calamity was the realisation that a large Eskom contract would not be renewed; and signs of early cracks at the R180m infrastructure 2008 acquisition of Megatron.

Piles of debt, bloodcurdling losses from Megatron and a weak consumer environment nearly sunk Ellies between 2014 and 2017. A reprieve by its bankers and the appointment of turnaround specialist Adrian Bock as FD in 2016 (and later CEO, though he announced in June that he was leaving at end-2018) helped Ellies stabilise, cut costs and realign its strategy. It moved back into two periods of earnings and profits in 2018.

Ellies reported HEPS of 8.07c a share for April 2018, placing the stock on an earnings multiple of 2.5 times with good prospects in place for financial 2019.

A new CEO was appointed in August 2018. Shaun Prithivirajh will look to align the consumer business with the needs of modern consumers. That could allow Ellies to offer far more services to its consumers in the internet and fibre sector rather than just extension leads, remote blasters and DStv installations.

This is a bold move for Ellies. With a market value of R118m, this realigned strategy is the "last roll of the dice". There is some financial flexibility (with debt reduced), which could open the way for small bolt-on deals.

On such a modest earnings multiple, Ellies is a steal. I can't see the earnings multiple falling below two times in financial 2019, especially given discussions I've had with the company. But it is a highly risky play. Institutional investors will stay clear – but this may give private clients a chance to latch onto the continuing recovery.

Zeder Investments, part of the PSG Group, is the flagship agricultural investment fund in SA with an asset value of R9.9bn. In its 12-year listed life Zeder has occasionally traded at a premium to its assets, and at its worst traded at a 40% discount. Now, at 470c, it trades at a 20% discount to the sum of its parts.

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Much of the recent weakness in the Zeder share price has been derived from two key issues.

Zeder has a large stake in JSE-listed Pioneer Foods which accounts for 43% of Zeder's sum of the parts value or 60% of its current market capitalisation.

Pioneer Foods has been its stumbling block for the past three years. Pioneer's results have disappointed, with weak earnings and profit warnings. This has resulted in it being down 60% from R210 in 2015 to a current R80 a share.

That has had its effect on Zeder's asset base, given the disproportionate weighting of Pioneer Foods to Zeder's fund.

Second, the 2016-2017 drought cast a pall over many of Zeder's agricultural interests such as Capespan and Kaap Agri.

But the drought now appears to be over. A recovery in the agricultural sector is forecast in 2019, which will benefit many of Zeder's interests.

What remains uncertain is Pioneer, where a weak and highly competitive consumer environment hampers earnings. Without a Pioneer Foods share price recovery, I cannot see Zeder materially recovering. However, the stock bounced recently when fruit and logistics business Capespan sold its 9.23% stake in a Chinese fruit enterprise, gaining a hefty R1.2bn for the minority stake. ●