

**CREDIT RATING ANNOUNCEMENT****GCR upgrades KAP Industrial Holdings Limited's rating to A<sub>(ZA)</sub>; Outlook Stable.**

Johannesburg, 30 Nov 2015 -- Global Credit Ratings has today upgraded the national scale ratings assigned to KAP Industrial Holdings Limited to A<sub>(ZA)</sub> and A1<sub>(ZA)</sub> in the long and short term respectively; with the outlook accorded as Stable.

**SUMMARY RATING RATIONALE**

Global Credit Ratings has accorded the above credit rating(s) to KAP Industrial Holdings Limited ("KAP") based on the following key criteria:

KAP continues to build on the base of the former Steinhoff International Holdings Limited ("Steinhoff") businesses acquired in April 2012. Post the disposal of marginal assets and extensive streamlining, the group now consists of two clusters (Diversified Logistics and Diversified Industrial), and according to management, is effectively positioned for sustainable growth. KAP still has access to Steinhoff's robust, well-established treasury, legal, tax and other structures, and has retained the executives and other skilled staff from the businesses it acquired from its former parent.

Revenue rose by 8% to R15.7bn in F15, with an even contribution from both clusters. Logistics revenue growth slowed to 2%, constrained by the termination of sub-optimal contracts and reduced fuel prices, while Industrials reported a 10% organic uptick, and a further 3% from acquisitions. Both units achieved double digit EBIT growth (10% and 16% respectively), which saw KAP's EBIT margin tick up to 10.3% (F14: 9.5%), and operating profit to R1.6bn (F14: R1.4bn). The group is underpinned by mostly defensive businesses, whose strong market share derives from their contractual nature and integration into customers' operations. Together with efficiencies from the consistent investment in fixed capital, as well as strict cost controls, this should sustain margins despite waning local demand.

KAP has reconfigured its funding profile in recent years, having raised R5.4bn in bank facilities and R1bn from medium term notes. In addition to refinancing the Steinhoff loans, it had also progressively reduced its total debt to a low of R3.5bn by FYE15 (FYE14: R4bn). As such, credit protection metrics outperformed expectations, with net gearing and net debt to EBITDA improving to 33% and 88% respectively (FYE14: 48%; 127%). With group capex continuing to be funded from internally generated cash flows, the conservative metrics are expected to be sustained in the medium term. Cash generation remains robust, as evidenced by the improved cash conversion ratio of 137% in F15 (F14: 129%), which underpinned a 25% increase in operating cash flows to R1.8bn. Debt serviceability has improved further, with net interest cover having risen to 5.6x in F15 (F14: 4.2x), and discretionary cash flows equating to 53% of debt (F14: 29%). Cash closed F15 at a stable R1.4bn, while R2.4bn of the bank facilities remained unutilised. Note is also taken of the improved debt maturity profile, with no lumpy maturities in the short term.

Overall growth will continue to be restrained by the weak domestic economy, with operations facing pressure from waning local demand and high utility expenses (*inter alia*). However, comfort is taken from KAP's balanced exposure to both cyclical and defensive sectors, as well as burgeoning regional footprint.

Looking ahead, upward rating pressure could come from the ability to expand on the strong market position held by the core brands, coupled with a stronger regional presence, which should ensure sound cash generation despite the difficult operating environment. However, a material deterioration in gearing due to the underperformance of any of the key subsidiaries, or acquisitions that place undue pressure on the balance sheet, could warrant ratings a downgrade.

**NATIONAL SCALE RATINGS HISTORY**

Initial rating (April 2014)

Long term: A<sub>(ZA)</sub>; Short term: A2<sub>(ZA)</sub>

Outlook: Stable

Last rating (May 2015)

Long term: A<sub>(ZA)</sub>; Short term: A1<sub>(ZA)</sub>

Outlook: Stable

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## APPLICABLE METHODOLOGIES AND RELATED RESEARCH

Criteria for rating corporate entities, updated February 2015  
KAP Industrial Holdings Limited Rating Reports, 2014 - May 2015

### GLOSSARY OF TERMS/ACRONYMS USED IN THIS DOCUMENT AS PER GCR'S CORPORATE GLOSSARY

Balance Sheet	A statement of a company's assets and liabilities provided for the benefit of shareholders and regulators. It gives a snapshot at a specific point in time of the assets the company holds and how they have been financed.
Budget	Financial plan that serves as an estimate of future cost, revenues or both.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Corporate Governance	Corporate governance broadly refers to the mechanisms, processes and relations by which corporations are controlled and directed, and is used to ensure the effectiveness, accountability and transparency of an entity to its stakeholders.
Credit Rating	An opinion regarding the creditworthiness of an entity, a security or financial instrument, or an issuer of securities or financial instruments, using an established and defined ranking system of rating categories.
Credit Risk	The possibility that a bond issuer or any other borrowers (including debtors/creditors) will default and fail to pay the principal and interest when due.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Default	Failure to meet the payment obligation of either interest or principal on a debt or bond. Technically, a borrower does not default, the initiative comes from the lender who declares that the borrower is in default.
Downgrade	The assignment of a lower credit rating to a corporate or sovereign borrower's debt by a credit rating agency. Opposite of upgrade.
EBITDA	EBITDA is useful for comparing the income of companies with different asset structures. EBITDA is usually closely aligned to cash generated by operations.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For a company, its exposure may relate to a particular product class or customer grouping. Exposure may also arise from an overreliance on one source of funding.
Fixed Capital	Fixed capital is the part of a company's total capital that is invested in fixed assets such as land, buildings and equipment that remains on the balance sheet, usually for years, but for at least one accounting period.
Gearing	With regard to corporate analysis, gearing (or leverage) refers to the extent to which a company is funded by debt and can be calculated by dividing its debt by shareholders' funds or by EBITDA.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Interest Cover	Interest cover is a measure of a company's interest payments relative to its profits. It is calculated by dividing a company's operating profit by its interest payments for a given period.
Interest Rate	The charge or the return on an asset or debt expressed as a percentage of the price or size of the asset or debt. It is usually expressed on an annual basis.
Margin	A term whose meaning depends on the context. In the widest sense, it means the difference between two values.
Maturity	The length of time between the issue of a bond or other security and the date on which it becomes payable in full.
National Scale Rating	The national scale provides a relative measure of creditworthiness for rated entities only within the country concerned. Under this rating scale, a 'AAA' long term national scale rating will typically be assigned to the lowest relative risk within that country, which in most cases will be the sovereign state.



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Operating Cash Flow	A company's net cash position over a given period, i.e. money received from customers minus payments to suppliers and staff, administration expenses, interest payments and taxes.
Operating Profit	Profits from a company's ordinary revenue-producing activities, calculated before taxes and interest costs.
Refinancing	The issue of new debt to replace maturing debt. New debt may be provided by existing or new lenders, with a new set of terms in place.
REPO	In a REPO one party sells assets or securities to another and agrees to repurchase them later at a set price on a specified date.
Risk	The possibility that an investment or venture will make a loss or not make the returns expected. There are many different types of risk including basis risk, country risk, credit risk, currency risk, economic risk, inflation risk, liquidity risk, market or systemic risk, political risk, settlement risk and translation risk.
Shareholder	An individual, entity or financial institution that holds shares or stock in an organisation or company.

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GCR affirms that a.) no part of the rating was influenced by any other business activities of the credit rating agency; b.) the rating was based solely on the merits of the rated entity, security or financial instrument being rated; c.) such rating was an independent evaluation of the risks and merits of the rated entity, security or financial instrument; and d.) the validity of the rating is for a maximum of 12 months, or earlier as indicated by the applicable credit rating document.

KAP Industrial Holdings Limited participated in the rating process via face-to-face management meetings, teleconferences and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible.

The credit rating/s has been disclosed to KAP Industrial Holdings Limited with no contestation of the rating.

Information received from KAP Industrial Holdings Limited and other reliable third parties to accord the credit rating(s) included;

- 2015 audited annual financial statements (plus four years of comparative numbers);
- revised group budgets/financial forecasts for the years 2016 to 2018;
- corporate governance and enterprise risk framework;
- industry comparative data and regulatory framework;
- information relating to affiliated listed entities and
- a breakdown of facilities available and related counterparties.

The ratings above were solicited by, or on behalf of, the rated client, and therefore, GCR has been compensated for the provision of the ratings.

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