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Research Update:

Operating Leasing Company enX Leasing Assigned 'zaA-' South Africa National Scale Rating

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Overview

- enX Leasing is an operating leasing business that offers full-service leases primarily on forklifts, as well as fleet leasing and logistics services for passenger and commercial vehicles.
- South Africa is the company's primary market of operation, where it generates most of its earnings, with smaller contributions from the U.K. and the rest of Africa.
- Our analysis of enX Leasing's credit quality incorporates local market and competitive position dynamics alongside the company's material leverage, elevated refinancing risk, and adequate liquidity, relative to global industry peers.
- We are assigning our 'zaA-' long-term South Africa national scale rating to enX Leasing.
- We expect the company's credit metrics to remain stable, as new business growth offsets increasing capital expenditures.

Rating Action

On Sept. 20, 2018, S&P Global Ratings assigned its 'zaA-' long-term South Africa national scale rating to South Africa-based operating leasing company enX Leasing Investments (Pty) Ltd.

Rationale

Our 'zaA-' rating reflects our expectation that enX Leasing's industrial equipment and fleet management operating segments, which are 85% exposed to South Africa, will maintain credit metrics at current levels under a range of foreseeable economic scenarios, provided that liquidity and funding availability remain adequate.

enX Leasing comprises two main operating segments, namely Industrial Equipment (EIE) and Fleet Management and Logistics (FML). Both segments generate revenues mainly by providing operating lease contracts (typically three to five years) to corporate customers. The sale of equipment and vehicles at the end of the initial lease term also generates a material and sustainable component of the company's revenues.

EIE, primarily comprising forklift leasing and materials handling equipment distribution activities, operates in South Africa (38% of the market) and the U.K. (5%). In our view, this segment will continue to benefit from its solid market position and customer diversification in South Africa, exclusive distribution rights on goods, and medium-term lease contracts that protect against the effects of an industry downturn.

FML leases passenger and commercial vehicles to corporations, and it operates in a highly competitive market segment with product substitution available to other

operating lease providers or from financial institutions (which typically provide financial leases). FML's lease book reflects an uneven run-down in capital and residual values over the next one to two years, so new business and increased capital expenditures (capex) are required to maintain and grow the book.

In our assessment of enX Leasing's business risk profile, we consider its significant country risk exposure to South Africa, its operations in the U.K. (around 10%), and distribution to the rest of Africa (5%). We consider the industry risk of the operating leasing sector to be moderate.

EIE's and FML's lease books have a medium-term contract life, with a relatively higher portion of assets' economic lives covered by the initial lease term in FML than in EIE. Both components of the company's leasing businesses offer extensive value-added services (including maintenance, insurance, and, where relevant, fleet management services) through a branch network, complemented by service partners in key business nodes in its areas of operation. Value-added services contribute around 30% of total revenues.

EIE has exclusive original equipment manufacturer (OEM) distribution contracts in place and supplies forklifts and other materials handling equipment under mostly exclusive distribution arrangements. Its exclusive forklift distribution agreement with Toyota in South Africa--which has been in place for more than 32 years--supports its leading market share. There are no material customer concentrations in this business. EIE has had adequate access to funding for growth in recent years.

FML does not benefit from OEM exclusivity, but purchases significant quantities from dealerships with extensive in-country presence, thus securing good rebates. Furthermore, FML has a good market position and competes mostly with South Africa's largest banks. There are no material customer concentrations in FML's book, with the exception of one key contract comprising 20% of its fleet book (and a lower proportion of its revenues), which has been in place for many years. The FML book has declined in recent years (prior to the acquisition of Eqstra Holdings), due to the capital required by its sister rental equipment company, and substantial new business and capital investments need to be written or undertaken to grow the book.

Barriers to entry for enX Leasing's particular business mix are high, given that leasing contracts are sensitive to the cost of capital, and the low likelihood that new entrants would have a lower cost of capital than existing players in the market. Furthermore, EIE's OEM exclusivity and service network cement its position. For FML, South Africa's heavy reliance on road transport and significant distances between the key business and population nodes increase the value of a dispersed distribution and servicing infrastructure, and reduces the ease with which customers can change their fleet management or logistics partners. Operating efficiency indicators, such as asset utilization, stock levels, and credit underwriting, are all well managed, in our opinion, and regular end-of-lease assets sales typically realize positive margins (averaging 5%-10% across the combined leased asset base).

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enX Leasing's S&P Global Ratings-adjusted EBIT margins average around 14% over our assessment period, which is below the average margins for the operating leasing businesses we rate, with some past volatility linked to economic cycles and capital availability. Furthermore, enX Leasing's debt-funded model also differs from that of several operating lease peers we rate (which frequently purchase assets through finance leases), resulting in an element of funding inefficiency.

enX Leasing's adjusted EBIT interest coverage stands near 2.1x and adjusted funds from operations (FFO) to debt is around 33%, based on a forward-looking weighted-average. In particular, we forecast higher capex levels for the fiscal years 2018-2020 (ending Aug. 31), as the company aims to rebuild its fleet asset base and expand its industrial equipment market share. enX Leasing is also considering acquisitions of additional branches in its U.K. EIE businesses, but these are likely to be of modest size and funded from local operating cash flows. enX Leasing's earnings and cash flows are exposed to economic fundamentals and, to a limited extent, foreign exchange movements (although asset import costs are hedged and costs can generally be passed on to customers).

In our base case for enX Leasing, we assume:

- Real GDP growth in South Africa of 2.1% in 2019 and 2.3% in 2020, with consumer price index (CPI) inflation at 5.3% and 5.4%, respectively.
- Real GDP growth in the U.K. of 1.4% in 2019 and 1.6% in 2020, with CPI inflation growth of 1.9% and 1.8%, respectively. We project a South African rand (ZAR)/British pound sterling exchange rate of 18.96 in 2019 and 19.93 in 2020.
- Revenue growth of about 8%-9% in fiscal years 2019 and 2020, owing to market share expansion in the forklift segment and new business growth in the fleet segment.
- Capex of around ZAR2.3 billion in fiscal 2019 and 2020, largely driven by expansionary capex investment in its fleet segment, on the back of new business growth.
- Working capital inflows of around ZAR300 million in fiscal years 2019 and 2020, primarily driven by sale of assets classified as inventory at the end of their lease periods.
- Dividends issued, to minority shareholders only, of ZAR20 million from 2019.

Based on these assumptions, we arrive at the following S&P Global Ratings-adjusted credit measures:

- Adjusted EBIT margin of 14%-15% in fiscal 2019-2020.
- Adjusted EBIT interest coverage of about 2.2x in fiscal 2019-2020.
- Adjusted debt to total capital of about 66% in fiscal 2019-2020.
- Adjusted FFO to debt of around 32%-34% in fiscal 2019-2020.

Other rating considerations

enX Leasing is reliant upon issuing unsecured (non-asset backed) capital market instruments to ensure sufficient funding to grow its leasing book, which is not a typical practice for operating lessors among rated peers, which tend to use asset-backed funding models, where asset or portfolio run-offs and liability amortizations are better matched. The company's chosen funding strategy exposes it to larger

single-debt maturities, so there is a greater mismatch between asset run-offs and debt maturities than usual for industry peers. While we note that enX Leasing has available liquidity facilities with its bankers to manage this to a certain extent, it does result in higher refinancing risk. Furthermore, the company is required to raise large amounts of funding up front, in order to secure liquidity for the period ahead, with excess cash reducing funding-structure efficiency.

Liquidity

We assess enX Leasing's liquidity as adequate. We expect the company's sources of liquidity will exceed uses of liquidity for the upcoming 12 months by at least 1.2x as of June 1, 2018. We note that enX Leasing has flexibility to cut capex in a downturn, as it has done in the past. We expect the group will continue to rely on projected cash generation and access to adequate funding sources for its requirements. enX Leasing's successful bond issuances in April and September 2018 indicate there is appetite from debt capital markets.

For the 12 months started June 1, 2018, we calculate that enX Leasing has the following principal liquidity sources:

- Cash and cash equivalents of ZAR115 million.
- Assumed committed undrawn credit lines of ZAR1.05 billion maturing beyond 12 months.
- Forecast cash FFO of about ZAR1.5 billion.
- Working capital inflows of ZAR350 million.

For the same period, we calculate the following principal liquidity uses:

- Debt maturities, including short-term uncommitted facilities, of around ZAR500 million.
- Capex of ZAR1.8 billion-ZAR2.2 billion.
- Dividends to minority shareholders of ZAR20 million.

The financial covenants on external bank borrowings relate to a net debt-to-EBITDA ratio, EBIT-to-net interest coverage, and other capital structure related covenants. We forecast that the group will maintain sufficient headroom (greater than 15%) under these covenants.

We do not anticipate changes to enX Leasing's stand-alone credit quality, based on our view that the company's adjusted EBIT interest coverage will remain above 1.3x (compared with 1.7x in fiscal 2017), which is commensurate with the current national scale rating.

However, we could lower the rating on enX Leasing if the company's operating performance deteriorates, owing to a weaker macroeconomic environment, material negative changes to distribution contracts or operational issues, or if the company is unable to secure external sources of capital to support its drive for new business growth and capex, primarily in its fleet segment. Rating pressure could also emerge if liquidity levels reduce, with sources covering uses by less than 1.2x.

We could raise the rating if enX Leasing's performance exceeds our expectations, such that adjusted EBIT interest coverage rises above 2.4x, and we assess that the company's access to capital, funding structure, and liquidity remain sustainable. A change in the capital structure to better reflect global industry norms and improve asset-liability matching would also be credit positive. Alternatively, a track record of resilient performance, adequate liquidity, and improved profitability across the business could also support our raising the rating.

Ratings Score Snapshot

National Scale Rating	zaA-/--/--
Business Risk	Weak
Country Risk	Moderately High Risk
Industry Risk	Intermediate Risk
Competitive Position	Weak
Financial Risk	Significant
Cash Flow/Leverage	Significant
Modifiers	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and Governance	Fair (no impact)
Comparable rating analysis	Negative (-1 notch)

Related Criteria And Research

Related Criteria

- General Criteria: Methodology For National And Regional Scale Credit Ratings - June 25, 2018
- Criteria - Corporates - Industrials: Key Credit Factors For The Operating Leasing Industry - December 14, 2016
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- General Criteria: Group Rating Methodology - November 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- Criteria - Corporates - General: Corporate Methodology - November 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments - November 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

Ratings List

enX Leasing Investments (Pty) Ltd.

Corporate Credit Rating

South Africa National Scale

zaA-/--/--

Regulatory Disclosures

- Primary Credit Analyst: Rishav Singh, Associate
- Rating Committee Chairperson: G.Andrew Stillman
- Date initial rating assigned: Sept. 20, 2018
- Date of previous review: N/A

Disclaimers

This rating has been determined by a rating committee based solely on the committee's independent evaluation of the credit risks and merits of the issuer or issue being rated in accordance with S&P Global Ratings published criteria and no part of this rating was influenced by any other business activities of S&P Global Ratings.

This credit rating is solicited. The rated entity did participate in the credit rating process. S&P Global Ratings did have access to the accounts, financial records and other relevant internal, non-public documents of the rated entity or a related third party. S&P Global Ratings has used information from sources believed to be reliable but does not guarantee the accuracy, adequacy, or completeness of any information used.

Materials Used in The Credit Rating Process

Sufficient information in general consists of both (i) financial statements that describe the Issuer's financial condition, results of operations and cash flows, and (ii) a description of the activities and obligations of the entity including of its governance and legal structure.

This credit rating was disclosed to the rated entity or related third party before being issued.

Glossary

- Anchor: The starting point for assigning an issuer a long-term rating, based on its business risk profile assessment and its financial risk profile assessment.
- Acceleration event: The means the right--as set out in the documentation--by which bank lenders or bondholders could demand early prepayment of loans or bonds, respectively.
- Business risk profile: This measure comprises the risk and return potential for a company in the market in which it participates (its industry risk), the country risks within those markets, the competitive climate, the company's competitive advantages and disadvantages (its competitive position).
- Capital: The sum of equity and debt.

- **Comparable rating analysis:** This involves taking a holistic review of a company's stand-alone credit risk profile (SACP), because each of the subfactors that ultimately generate the SACP can be at the upper or lower end, or at the mid-point, of such a range. It may also touch upon the overall comparative assessment of an issuer in relation to its peers across industry and jurisdiction and may capture some factors not (fully) covered, such as a short operating track record, entities in transition, unusual structures, or contingent risk exposures.
- **Competitive advantage:** The strategic positioning and attractiveness to customers of the company's products or services, and the fragility or sustainability of its business model.
- **Competitive position:** Our assessment of a company's: competitive advantage; operating efficiency; scale, scope, and diversity; and profitability.
- **Corporate Industry and Country Risk Assessment (CICRA):** Derived by combining an issuer's country risk assessment and industry risk assessment.
- **Country risk:** This measures a country's influence on the overall credit risks for a rated company with regards to a country's economic, institutional and governance effectiveness, financial system, and payment culture/rule of law risks.
- **CreditWatch:** This highlights the potential direction of a short- or long-term rating over the short term, typically less than three months. Ratings may be placed on CreditWatch where, in our view, an event or a deviation from an expected trend has occurred or is expected and additional information is necessary to determine the rating impact.
- **Creditworthiness:** Ability and willingness of a company to meet its debt and debt-like obligations; measured by assessing the level current and future resources relative to the size and timing of its commitments.
- **Diversification/portfolio effect:** Applicable to conglomerates. An assessment of the extent to which an entity's multiple core business lines are correlated and whether each contributes a material source of earnings and cash flow.
- **Earnings:** Proxy for profit or surplus yielded by an entity after production and overhead costs have been accounted for in a given period.
- **EBITDA margin:** This is EBITDA as a fraction of revenues.
- **EBITDA:** This is earnings before interest, tax, depreciation, and amortization.
- **Economies of scale:** This is the cost advantage that arises with increased size or output of a product.
- **Efficiency gains:** Cost improvements.
- **Financial headroom:** Measure of deviation tolerated in financial metrics without moving outside or above a predesignated band or limit typically found in loan covenants (as in a debt-to-EBITDA multiple that places a constraint on leverage) or set for the respective rating level. Significant headroom would allow for larger deviations.
- **Financial risk profile:** This measure comprises our assessment of a company's cash flow/leverage analysis. It also takes into account the relationship of the cash flows the organization can achieve given its business risk profile. The measure is before assessing other financial drivers such as capital structure, financial policy, or liquidity.
- **Financial sponsor:** An entity that follows an aggressive financial strategy in using debt and debt-like instruments to maximize shareholder returns. Typically, these sponsors dispose of assets within a short-to-intermediate time frame.
- **Free operating cash flow:** Cash flow from operations minus capital expenditure.
- **Funds from operations:** EBITDA minus interest expense minus current tax.
- **Government-related entity:** An entity that could, under stress, benefit from

extraordinary government support in order to meet its financial obligations; or conversely an entity controlled by a government that could be subject to negative extraordinary government intervention if the government is under stress.

- Group rating methodology: The assessment of the likelihood of extraordinary group support (or conversely, negative group intervention) that is factored into the rating on an entity that is a member of a group.
- Industry risk: This addresses the major factors that affect the risks that companies face in their respective industries.
- Issue credit rating: This is a forward-looking opinion about the creditworthiness of an obligor with respect to a specific class of financial obligations or a specific financial program.
- Issued share capital: The value of a company's shares that are held by shareholders.
- Issuer credit rating: This is a forward-looking opinion of an obligor's overall creditworthiness.
- Leverage: The level of a company's debt in relation to its earnings before interest, tax, depreciation, and amortization.
- Liquidity: This is the assessment of a company's monetary flows, assessed over a 12 to 24 month period. It also assesses the risk and potential consequences of a company's breach of covenant test, typically tied to declines in EBITDA.
- Management and governance: This addresses how management's strategic competence, organizational effectiveness, risk management, and governance practices shape the issuer's competitiveness in the marketplace, the strength of its financial risk management, and the robustness of its governance.
- Operating efficiency: The quality and flexibility of the company's asset base and its cost management and structure.
- Outlook: This is the assessment of the potential direction of a long-term issuer rating over the short to intermediate term (typically six months to two years).
- Profitability ratio: Commonly measured using return on capital and EBITDA margins, but can be measured using sector-specific ratios.
- Rating above the sovereign assessment: Our assessment of whether an entity can be rated above the sovereign rating on a jurisdiction it has a material exposure to.
- Scale, scope, and diversity: The concentration or diversification of business activities.
- Stand-alone credit profile (SACP): S&P Global Ratings' opinion of an issue's or issuer's creditworthiness, in the absence of extraordinary intervention or support from its parent, affiliate, or related government or from a third-party entity such as an insurer.
- Transfer and convertibility assessment: S&P Global Ratings' view of the likelihood of a sovereign restricting nonsovereign access to foreign exchange needed to satisfy the nonsovereign's debt service obligations.

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