



Black knight Gijima comes to rescue

Published: October 2005

A new sense of optimism now prevails in the corridors of what used to be AST, since its rescue from what was technically an insolvent position by black IT company Gijima. Management hopes that new blood, a stronger balance sheet, and empowerment credentials will finally lay to rest the negativity and scepticism of the past.

"Regard your good name as the richest jewel you can possibly be possessed of," wrote Socrates in antiquity, "for credit is like fire; when once you have kindled it you may easily preserve it, but if you once extinguish it, you will find it an arduous task to rekindle it again."

The directors of GijimaAST, newly formed from the merger between black-owned company Gijima and the much larger – by revenue – AST Group, would nod at this quotation, before launching into the reasons why things are better now.

But as poet, cleric and wit, Joseph Hall, wrote some four centuries ago: "A reputation once broken may possibly be repaired, but the world will always keep their eyes on the spot where the crack was."

Heeding wisdom of luminaries

By the wisdom of luminaries, then, John Miller and Robert Gumede, CEO and deputy chairman respectively of the company, have their work cut out for them.

The "old AST", as it is now known, has suffered for several years under a historically weak balance sheet, a customer base that is reliant on a handful of crucial customers, allegations of mismanagement – if not outright fraud – against some former directors, and a series of share-diluting and confidence-sapping rights issues.

It came as a surprise, then, when the company's annual results and its most recent R160-million rights issue raised the interest of both existing shareholders and several new institutional investors.

Among the high-profile institutions that underwrote the issue or bought shares on the open market are Rand Merchant Bank and Allan Gray, both of which are perceived to be good company for GijimaAST, if reputation is what it is after

However, it is not so much what GijimaAST did report at its annual results in August, than what it didn't report, that continues to prompt mixed signals from analysts and market watchers.

Core problems at heart of it all

According to the company's CEO, John Miller, there had been four core problems before this set of results was announced.

The first was a potentially expensive dispute with the South African Revenue Services over a trademark deduction. Though not unique to the former AST Group, it ominously sat on the books as a contingent liability of half a billion rand. This dispute has now been resolved, though still at a hefty settlement expense of R83.1-million.

The second was the company's weak balance sheet. The company – as a result of rapid expansion under previous CEO Gerrie de Klerk – was deeply indebted, without the means to pay for it. Several rights issues later, the pressure has been somewhat relieved, and although last year's R88-million rights issue "was never going to be enough", according to Miller, he claims that this year's R160-million puts the new

merged company on a sound financial footing. The balance sheet still carries substantial debt, however, and while non-current liabilities and interest-bearing debt have been reduced sharply, current liabilities remain high.

The third was insufficient capital and reserves – not only to service debt, but according to Miller this also made the pursuit of new business opportunities difficult. The much-strengthened position in this year's results will give some breathing room while the company whittles away at its remaining debts.

Finally, the company did not have a meaningful empowerment profile, which substantially hampered its ability to win new business, both in the public and private sector, and attract competent staff.

Says Miller: "Gijima assisted on all four points – including with SARS – in a way I can't disclose. This supported our [most recent] rights issue."

Confidence restored

He makes a careful distinction, therefore: "Confidence has been restored not in AST, but in GijimaAST. AST might have been big, but Gijima was successful. The merger has taken a lot of the risk – both financial and client risk – out of GijimaAST. Before the merger, losing one account would have been terminal. Now, it would hurt badly, but we could survive it."

Although AST's reputation is a mixed bag, it claims customer loyalty as a sign that its reach and ability to service its customers was never in question.

Says Carlos Ferreira, the company's newly-appointed financial director: "The core of AST, operationally, was sound. It took on debt it couldn't swallow, and that put the financial position at risk. But operationally it remained capable."

Gumede agrees: "None of the old AST's clients jumped ship. They're not spaza shops, so why did they stay? One thing only: capability, delivery, skills. The pressures were real, but the vote of confidence came from clients."

Loyalty or vested interests?

Sceptics – both analysts and competitors – claim that this is largely related to the vested interests some of its bigger customers have in AST's success. These interests include, for example, a large (but dwindling) shareholding in the company by Kumba Resources.

One competitor, who for obvious reasons prefers not to be named, claims – though this could not be independently confirmed – that the company charges some of its customers well above market rates. He believes that once Gijima exercises its option to buy the remaining 4.5 percent stake held by Kumba (as Gumede says Gijima intends to do by January 2006), "I bet we'll take Kumba's business away from them."

This view is relevant in the light of the fact that the company's revenue has declined by a fifth in the last two years, coming in at only R1.6-billion for the year ended 30 June 2005.

Failure to win new business

It has also not reported any major new customer wins – although Miller points out that having 90 percent of the top 100 companies in its portfolio means new business wins often have to come from existing clients. He names some smaller new clients, such as Harvey World Travel, Parmalat, Nuclinks, Namclear, Grinaker LTA and Shoprite Checkers, but also points to new business with big customer names such as ABSA. Giving some credence to the claim about competitive pricing, he adds, "We won ABSA's operating system migration on open tender, without the lowest price."

Although Miller admits to still being very dependent on Kumba Resources, he adds that Gijima's clients – such as the State Information Technology Agency (SITA) – now contribute too.

"We've been successful in government with transversal business," explains Gumede. "We're the only listed IT company that supplies seat management to all government departments. That's where we see huge growth."

Ferreira points out that GijimaAST's top 10 clients now represent less than 40 percent of the business, and product sales accounts for 22 percent of revenue.

Miller emphasises that the company's failure to win much new business to date was both as a result of the debt spiral in which it found itself, as well as the fact that services lag the resurgent market for IT products. Underscoring that risk remains high, however, is the decline in revenue, which was attributed largely to the substantial underperformance of the solutions division, which in turn faltered with the loss of only a few big contracts.

The real deal

Still, the biggest upside for the new company derives from the fact that Gijima brings to the company fully-vested black ownership of over 30 percent. "No special-purpose vehicles, no preference shares; they own the shares outright," explains Miller.

"Why," asks Gumede pointedly, "should I compete with someone who does a deal just before a big contract like Hanis, and is either part of a failed BEE deal or one stuck in a debt trap because of the structure? Our deal is different. It's a business deal that just happens to include empowerment."

"Gijima took on real risk," comments Ferreira. Adds Miller: "With others, if the shares are underwater, they walk away. Gijima can't do this."

Bridging the divide

"If this doesn't work, I can't walk away and do a deal with someone else. Both of us," Gumede says, referring to himself and Miller, "will be out of jobs. The beauty of the ICT Charter is that it gets rid of pure investment players. I'm putting in the hours as an employee."

Despite the implicit criticism of many empowerment deals, Gumede does list several examples – listed and unlisted – he considers successful. "Datacentrix is another example of a really successful empowerment deal, Torque IT – which is celebrating its 10th anniversary – Cornastone, Arivia.kom, the Mopatlane brothers – they've really bridged the divide."

The active interest and involvement from Gijima's shareholders and directors, its foothold in public sector business, and the support the deal won for raising yet more capital from shareholders, means the merger can only be described as a rescue. "White empowerment", if you like: A leg-up for a struggling white-owned company from a profitable black-owned firm. Uncharacteristically for BEE deals, it even retains a white chairman.

"It works for us," says Gumede. "But we also needed to appoint black directors who could add value and weren't subject to the criticism of being overstretched. The directors we've appointed add value and they've integrated very well with existing board members."

Miller confirms the revitalised nature of the company's management structure, saying that, excluding him, the average age is probably below 40, and only two people retain the same jobs they held six months ago.

"The beauty for us," says Gumede, "is that we came into a company where people welcomed change because of past torrid times. We're in the same office." Expressing what is probably his key view on the merger, he adds: "The deal was not an empowerment deal – it was a business deal that made sense anyhow."

Good intentions

For Gijima's business, it's just as big a win as for AST's embattled shareholders, however.

"Show me any 100 percent black company with 90 percent government clients that can get 90 percent private sector clients," says Gumedé. "AST had a happy client base, and that is what we needed."

"Our intention is to push government business to 50 percent from the current 28 percent," says Miller, "so that's some 20 percent on current revenue." This would at least, recover much of the revenue lost in the last few years, and may warrant Miller's perception of GijimaAST's competitive position. "The things we've invested in – retail, mining software, Microsoft certification and training – they're starting to pay off. We're building our networking business, and we're third or fourth alongside Business Connexion, behind Telkom at number one and Dimension Data at number two. In infrastructure and desktop outsourcing, BMI already rated us at number one, prior to the merger."

Despite signs of a turnaround, in terms of both balance sheet health and profitability, the company's directors – and the shareholders that have shown renewed faith in them – will have to be patient while the merged entity turns good intentions into new business and consistent profits.

As modern-era industrialist Henry Ford observed, "You can't build a reputation on what you are going to do."