

RUSSELSMITH NIGERIA LIMITED

Final 2024 Corporate Rating Report



RUSSELSMITH NIGERIA LIMITED

Issuer Rating:

Bbb

A company with satisfactory financial condition and adequate capacity to meet its obligations as and when they fall due relative to all other issuers in the same country.

Outlook: Stable

Issue Date: 30 December 2024

Expiry Date: 30 June 2025

Previous Rating: N/A

Industry: Oil and Gas Servicing

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RATING RATIONALE

Agusto & Co. hereby assigns a “Bbb” rating to RusselSmith Nigeria Limited (“RusselSmith,” “RNL” or “the Company”). The assigned rating reflects the Company’s healthy earnings and cash flows driven by its expanding portfolio of oil and gas services contracts with International Oil Companies (IOCs) and the operational efficiency from the use of in-house expertise (as against expatriates), which has effectively reduced operating costs. The rating also considers RusselSmith’s diversified business structure and its predominantly dollar-denominated revenue streams, which provide resilience against currency devaluations. The rating is however constrained by RNL’s high leverage, its weak equity buffer, particularly considering the limited contribution of core equity (retained earnings and paid-up capital) to its shareholder funds, and the need for improvement in its corporate governance framework.

RusselSmith Nigeria Limited was incorporated on 26 July 2001 and commenced operations in July 2005. The Company is an integrated energy solutions provider with a core focus on asset integrity management within Nigeria’s Oil and Gas (Upstream) Industry. Its services cover topside and subsea assets integrity management, aerial inspection services and operations and production support. Since its inception, RNL has completed over 800 projects and currently has three active contracts with Mobil Producing Nigeria Unlimited (MPN), Nigeria Liquefied Natural Gas Limited (NLNG) and Shell Nigeria Exploration and Production Company Limited (SNEPCo). The Company owns a fleet of seven remotely operated vehicles (ROVs), which are capable of reaching depths of up to 2,000 meters, and two unmanned aerial vehicles (UAVs) for specialized inspections. In 2023, RusselSmith launched its additive manufacturing division, thus representing a strategic expansion beyond the traditional oil and gas services. However, the scalability of this new business segment remains to be seen considering uncertainties in both raw material supply chain and product demand. Therefore, we expect contributions from its oil & gas services to continue to drive the Company’s revenue in the near to medium term.

In the 2023 financial year, RusselSmith significantly expanded the scope of work under its contract with MPN. Consequently, the Company’s revenue in the financial year ended 31 December 2023 (FYE 2023) grew by 93% to ₦5.2 billion. The Company’s top-line was further bolstered by translation gains given that about 60% of the contract pricing is dollar-denominated. During the year, RNL strategically reduced its reliance on expatriates for contract execution, thereby optimizing costs. This resulted in a decline in direct cost-to-sales ratio to 51.4% in 2023 (2022: 62.5%). However, operating cost-to-sales ratio increased to 23.2% in FYE 2023 (2022: 17.4%), driven primarily by a 350% surge in depreciation expenses following the revaluation of

some items of property, plant, and equipment (PPE). Notwithstanding, the Company posted a higher operating profit margin of 25.4% in FYE 2023 (2022: 20.1%). However, RusselSmith's profit before tax (PBT) margin declined to 13.3% in 2023 (2022: 18.4%) due to increased finance costs driven by the prevailing high interest rates. Nonetheless, the Company posted an improved pre-tax pre-interest return on assets (ROA) of 15% in FYE 2023 (2022: 9%) and a pre-tax return on equity (ROE) of 23% (2022: 19%), both within our acceptable band.

In October 2023, RNL secured a five-year contract with SNEPCo to deliver maintenance, engineering, and project support services for the BONGA floating production, storage and offloading (FPSO) vessel, with contract execution commencing in 2024. To initiate this new contract, RusselSmith employed the services of expatriates, with a phased plan to integrate more local staff as the contract execution progresses. Based on unaudited accounts for the ten months ended 31 October 2024, RusselSmith's revenue increased to ₦7.8 billion, surpassing its full-year 2023 performance, driven by the commencement of work under this contract. However, direct cost-to-sales ratio increased to 59.6%, reflecting the increased reliance on expatriates for the contract execution. In contrast, the operating cost-to-sales ratio improved to 15.5%, driven largely by economies of scale. RusselSmith posted an operating profit margin of 24.9% and a PBT margin of 11.2% in the period, which we consider good. This translated to an annualized ROA of 35%, surpassing our benchmark and ROE of 27% which was within our expectation. In the near term, we expect the Company's revenue to continue to grow, supported by its new contracts with NLNG secured in March 2024 and the ongoing execution of the SNEPCo contract.

In FYE 2023, RusselSmith's operating cash flow (OCF) surged by 96% to ₦1.8 billion driven by higher profits and increase in trade and other payables, notably withholding tax payable. The Company's OCF in 2023 represented 34% of revenue and was sufficient to cover returns to providers of finance (RTPOF), solely interest payments, 3.7x, which we consider good. In the near term, we expect the Company to continue generating positive OCF, supported by good profitability and favorable trade terms with its customers and suppliers.

As at FYE 2023, RusselSmith's spontaneous financing increased by 58% to ₦3.6 billion due to its expanded scope of work. RNL's spontaneous financing outstripped its working assets, leaving a short-term financing surplus of ₦206 million. As at the same date, the Company's long-term funds of ₦4.4 billion comprising equity (66%) and long-term loans (34%), were sufficient to cover its long-term assets, leaving a working capital of ₦492 million. overall, RNL closed the year with a working capital surplus of ₦698 million. As at 31 October 2024, RusselSmith's spontaneous financing was insufficient to cover its working assets due to a sharp decline in trade payables following the recent clearance of payable backlogs. This resulted in an overall working capital deficiency of ₦927 million. In our opinion, RNL's working capital requires improvement.

As at FYE 2023, RusselSmith's interest-bearing liability (IBL) comprised solely the outstanding balance from the dollar-denominated Bank of Industry loan secured in 2018, which was fully liquidated by October 2024. The Company's finance cost to sales ratio increased to 9.3% in 2023 (2022: 6.3%) due to higher interest rates, exceeding our 5% maximum threshold. Furthermore, RusselSmith's IBL (net of cash) to equity ratio (net of revaluation surplus) and net debt to total assets ratios were elevated at 352% and 166% respectively. In our opinion, RNL's leverage is high.

In the medium term, we expect demand for asset integrity management services to remain high given the state of Nigeria's upstream assets, and the dearth of fresh investment into the sector. RusselSmith, is therefore positioned to drive revenue growth via the acquisition of new contracts and the expansion of existing ones. Furthermore, the Company is actively diversifying into the additive manufacturing sector. Management has disclosed the successful completion of its proof-of-concept phase, with the pilot stage scheduled to commence in Q1 2025. This expansion is expected to further contribute to topline growth, while the 100% dollar-denominated revenue from this division is anticipated to positively impact profit margins.

Based on the foregoing, we attach a **stable** outlook to RusselSmith Nigeria Limited.

Figure 1: Company's Strengths, Weaknesses, Opportunities and Challenges

Strengths
<ul style="list-style-type: none"> • Natural hedge against currency risk given its dollar-denominated revenue • Good profitability • Good operating cash flow • Potential for increased earnings from additive manufacturing
Weaknesses
<ul style="list-style-type: none"> • High leverage • Weak equity cushion • Corporate governance that requires improvement
Opportunities
<ul style="list-style-type: none"> • Nigeria's abundant hydrocarbon reserves • Expansion of marginal fields, opening up more opportunities for oil field servicing operators • Opportunities to expand across Africa leveraging the Africa Continental Free Trade Area Agreement • Local content development creating opportunities for indigenous service companies to thrive • Aging infrastructure driving demand for asset maintenance services • Government's renewed commitment towards revitalizing the oil and gas industry
Challenges
<ul style="list-style-type: none"> • Insecurity in the oil production areas discouraging investment in the Oil and Gas Industry • Infrastructure deficit • Volatility in oil prices • Climate change concerns creating more regulatory hurdles

OVERVIEW OF THE OIL AND GAS SERVICING INDUSTRY IN NIGERIA

The Oil and Gas Industry is strategic for Nigeria's economic sustainability, accounting for over 90% of total export earnings and contributing approximately 50% to government revenue. The Oil and Gas Industry is divided into three main segments: upstream, midstream and downstream, with oil servicing companies operating across all segments.

The Nigerian Oil and Gas Servicing Industry (the Industry) is integral to the oil and gas exploration and production process. It covers the manufacturing, maintenance and repair of equipment used in the extraction and transportation of oil and gas, as well as specialized services such as seismic testing, well construction and production support. Based on the nature of operations, the Industry is categorised into Drilling and Dredging; Engineering, Procurement, Construction and Commissioning (EPCC); Geophysics and Geological Services; Marine Logistics; and Manufacturing and Supply. Industry performance is closely tied to the activity levels of oil field operators, which are in turn influenced by current and future oil and gas price expectations.

The Nigerian Oil and Gas Industry continues to grapple with persistent challenges, including oil theft, vandalism, and broader security concerns that disrupt production operations. These issues have led international oil and gas companies to scale back investments in Nigeria, redirecting capital to other African markets. As a result, the country's oil production has experienced substantial declines, dropping from a daily average of 2.2 million barrels in 2014 to approximately 1.3 million barrels per day in 2024¹. Nigeria has therefore consistently fallen short of its Organization of the Petroleum Exporting Countries (OPEC) production quota currently set at 1.5 million barrels per day (mbpd) over the past three years and remains below its 2024 budgetary target of 1.7 mbpd. These developments have adversely impacted the Oil and Gas Servicing Industry, whose revenue streams are largely dependent on upstream activity levels.

The Industry is heavily regulated and faces increasing public scrutiny, especially in recent times, given growing concerns about environmental sustainability. In response, the Nigerian Upstream Petroleum Regulatory Commission (NUPRC) has introduced a regulatory framework for energy transition, decarbonization and carbon monetization within Nigeria's upstream sector, structured around seven core pillars – natural gas transition; zero routine flaring and methane reduction; carbon market development; technological advancement; operational efficiency; incentives; and collaborative risk management². The Gas Flaring, Venting and Methane Emissions (Prevention of Waste and Pollution) Regulations 2023 provides legislative support for these efforts, imposing a \$3.50 per thousand cubic feet (mscf) fine on unauthorized gas flaring, venting, or wastage, and a \$10,000 fine for non-compliance with gas data reporting or metering equipment installation requirements. This is expected to impact the operating modalities of the Industry, especially with respect to drilling and dredging services.

Though previously dominated by a few large foreign players, the Industry has transformed significantly in recent times, with local operators emerging as dominant players, largely attributable to the Nigerian Content Development Act. Notwithstanding, the Industry remains dependent on imports for most equipment and machinery, and in some cases, expatriates' workforce. This reliance poses considerable foreign exchange risk. However, with payments for contracts being largely dollar-denominated, the Industry is substantially hedged against currency risk. In addition, ongoing reforms aimed at boosting Nigeria's oil output to 2 mbpd present promising growth opportunities for the servicing sector. The resurgence of in-country refining has also broadened the scope of work for the Industry players.

Based on the above, we attach a **stable** outlook to the Oil and Gas Servicing Industry in Nigeria.

¹ OPEC

² <https://www.nuprc.gov.ng/cop28-nuprc-unveils-regulatory-framework-for-energy-transition/>

COMPANY PROFILE

RusselSmith Nigeria Limited (“RusselSmith”, “RNL” or “the Company”) was incorporated on 26 July 2001 and commenced operations in July 2005. RNL is an integrated energy solutions company with a core focus on asset integrity management within the Nigeria’s Oil and Gas Industry, covering both topside and subsea assets. The Company also offers aerial inspection services as well as operations and production support.

Since its inception, RusselSmith has completed over 800 projects and currently has three active contracts with Mobil Producing Nigeria Unlimited (MPN), Nigeria Liquefied Natural Gas Limited (NLNG) and Shell Nigeria Exploration and Production Company Limited (SNEPCo). The Company is a significant player in topside asset integrity management segment. However, RNL is yet to achieve considerable scale in subsea asset management. RusselSmith’s operational capacity is enhanced by its fleet of seven remotely operated vehicles (ROVs) capable of reaching depths of up to 2,000 meters, and two unmanned aerial vehicles (UAVs) for specialized inspections. Due to the intense competition for contracts in the Oil and Gas Services industry, most service companies, including RusselSmith, operate as price takers.

The Company’s services are primarily conducted within the volatile, oil-rich Niger Delta Region. To mitigate potential operational disruptions, the Company strategically prioritizes deep offshore projects, which are inherently less susceptible to security threats. However, for its onshore operations, RusselSmith has established a community liaison framework, anchored on community-relations agreements which are tailored to each project. This serves to foster positive community engagement and reduce security risks.

In 2023, RusselSmith established an additive manufacturing division, marking a strategic diversification beyond the traditional oil and gas services, and unlocking opportunities in adjacent industries. RusselSmith’s additive manufacturing division leverages strategic partnerships with key international players such as Speed3D which specializes in metal 3D printing for industrial and commercial applications; Additive Academy - focused on additive manufacturing training and education and Roboze - a provider of industrial 3D printing systems. Management has disclosed the successful completion of its proof-of-concept phase, and plans to commence the pilot phase of its additive manufacturing operations in Q1 2025. In October 2024, the company secured approval from the NUPRC to deploy metallic and non-metallic additive manufacturing solutions in the Oil and Gas Industry.

RusselSmith Nigeria Limited is certified by Lloyd’s Register for thickness measurement of hull structure and DNV for thickness measurement across all types and sizes of ships. The Company also has permits from NUPRC for offshore pipeline laying, non-destructive testing and corrosion prevention control services in the Oil and Gas Industry, as well as a certificate from the Standards Organization of Nigeria to offer integrated energy services including topside and subsea operation, production support and unmanned aerial vehicle inspection services. RusselSmith is a member of the Manufacturers Association of Nigeria (MAN) and the Industrial Rope Access Trade Association (IRATA). The Company is also a participating member of the Additive Manufacturing Green Trade Association (AMGTA).

OWNERSHIP, GOVERNANCE, MANAGEMENT AND STAFF

As at 31 December 2023, RusselSmith Nigeria Limited had an authorized share capital of ₦100 million composed of 100 million ordinary shares at ₦1 each. Of these, 90 million shares have been issued and fully paid up, with the remaining set to be issued within the next financial year. The Company's shares are equally held by Mr. Leslie Oghomienor (50%) and Mr. Oluwakayode Adeleke (50%).

RusselSmith has a four-member Board of Directors ("the Board"), comprising the Chairman and three executive directors. Mr. Leslie Oghomienor leads the Board as the Chairman while Mr. Oluwakayode Adeleke serves as the Managing Director. In our opinion, the Board would benefit from expanded membership, incorporating professionals with diverse expertise and industry experience. In addition, the inclusion of non-executive directors (NEDs) would enhance the Board's composition, driving independent oversight and fostering greater accountability in line with international best practices.

Table 2: RusselSmith Nigeria Limited's Board of Directors

Name	Role
Mr. Leslie Oghomienor	Chairman
Mr. Oluwakayode Adeleke	President/Chief Executive Officer
Ms. Chinedu Aiaegbu	Director, Corporate Services
Mr. Divakar Puri	Director, Finance and Corporate Division

Source: RusselSmith Nigeria Limited

The Managing Director is backed by a team of five senior management professionals, each responsible for key operational areas, including topside and subsea operations, unmanned aerial vehicle and digital solutions, supply chain management, integration of additive manufacturing technologies and advancing the Company's sustainability initiatives. Collectively, the senior management team brings an average of over 18 years of relevant industry experience. In our opinion, RusselSmith has a qualified and experienced management team.

Management Team

Mr. Oluwakayode Adeleke is the President/Chief Executive Officer of RusselSmith Nigeria Limited. He holds a Bachelor's degree in Computer Science from the University of Ibadan, Oyo State, as well as dual Masters Degrees in Business Administration and Information Systems from Southeastern University, Washington, D.C. He has over 23 years of experience, predominantly in the Oil and Gas Industry, where he has led and contributed to significant projects, including consulting engagements with the World Bank. Mr. Adeleke is a certified Internal Quality Auditor, a Fellow of the Institute of Management Consultants, a registered member of the Financial Reporting Council of Nigeria, and a member of the Institute of Directors. He is also an active member of the Sustainability Professionals Institute of Nigeria. Mr. Adeleke is the founding President of the RusselSmith Toastmasters Club.

Table 3: Other Members of RusselSmith Nigeria Limited's Management Team

Name	Position
Mr. Sooravan Tharmalingam	Senior Vice President/Divisional Chief Executive, Topside and Subsea Division
Mr. Effiong Okwong	Vice President/Divisional Executive, UAV and Digital Solutions
Mr. Mohammed Mazhar	Vice President/Executive Sub-divisional Head, Facilities, Services & Procurement Management
Mr. Mudiaga Agege	Vice President/Executive Divisional Head, Niger-Delta Regional Division
Mr. Livinus Ojefua	Head, Business Sustainability Division

Source: RusselSmith Nigeria Limited

As at 31 December 2023, RusselSmith had a staff strength of 157 personnel (2022: 151) comprising 35 full-time employees and 116 contract staff. The Company's average cost per employee increased to ₦6 million in FYE 2023 (2022: ₦4 million) due largely to upward salary reviews. During the same year, RusselSmith recorded an average operating profit per employee (adjusted for staff cost) of ₦14.7 million which was sufficient to cover the average cost per employee 2.3x, which we consider to be satisfactory.

FINANCIAL CONDITION

ANALYSTS' COMMENTS:

Agusto & Co has analysed the audited financial statements of RusselSmith Nigeria Limited for the three years ended 31 December 2023 and its management account for the ten months ended 31 October 2024.

PROFITABILITY

RusselSmith Nigeria Limited generates revenue by providing asset integrity management services to companies in the Oil and Gas Industry. Its scope of work covers topside and subsea asset integrity management, operations and production support as well as aerial inspection services. In 2023, the Company diversified into additive manufacturing. This operation is still in its nascent stage, contributing less than 1% to revenue so far in 2024.

In the financial year ended 31 December 2023 (FYE 2023), RusselSmith Nigeria Limited's revenue grew by 93% to ₦5.2 billion driven primarily by expansion of the scope of work under its existing contract with Mobil Producing Nigeria Unlimited. The Company's revenue was also impacted by favourable foreign exchange rates given that about 60% of its contract revenues are denominated in dollars. Topside asset integrity management accounted for 96% of the Company's revenue in FYE 2023, while subsea services and operations and production support contributed 3% and 1% respectively. In October 2023, RNL secured a five-year contract with Shell Nigeria Exploration and Production Company Limited (SNEPCo) to provide maintenance, engineering and project support services to its BONGA floating production, storage and offloading (FPSO) vessel, and another 5-year contract with Nigeria Liquefied Natural Gas Limited (NLNG) in Q2 2024, for the provision of marine facilities inspection and assurance services. Execution of the SNEPCo contract commenced in Q1 2024, while the NLNG contract implementation is expected to begin during Q1 2025. These new contracts are expected to drive revenue growth for the Company in the near to medium term.

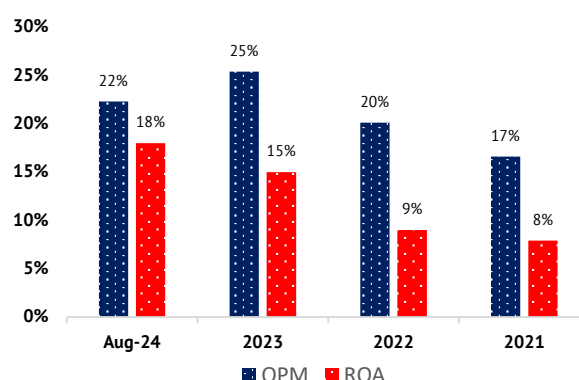
Being a service company, labour expenses are a major component of RusselSmith's direct costs, accounting for 74% in FYE 2023, with material and transportation costs contributing 16% and 9% respectively. In the year ended 31 December 2023, RusselSmith's direct cost-to-sales ratio declined to 51.4% (2022: 62.5%), reflecting a strategic shift towards greater reliance on in-house expertise for contract execution. While RNL possesses the requisite capabilities to handle most contracts, third-party services are engaged when specialized expertise is required or where the scope of work exceeds internal capacity within specified timelines. This often comes at a higher cost. In 2023, contractor and subcontractor costs accounted for 34% of the Company's total labor expense, a reduction from the 51% recorded in FYE 2022, contributing to an enhanced gross profit margin of 48.6% (2022: 37.5%). However, the operating cost-to-sales ratio increased to 23.2% in FYE 2023 (2022: 17.4%), driven primarily by a 350% surge in depreciation expenses following the revaluation of some items of property, plant, and equipment (PPE). Nonetheless, the Company posted an improved operating profit margin of 25.4% in FYE 2023 (2022: 20.1%), due majorly to better direct cost management.

In the financial year ended 31 December 2023 (FYE 2023), RusselSmith Nigeria Limited's interest expense increased by 182% to ₦479 million, due primarily to the adverse impact of naira devaluation on the Company's dollar-denominated loan from the Bank of Industry (BOI), and the high interest rate environment. Consequently, the Company's interest expense-to-sales ratio rose to 9.3% (2022: 6.3%), exceeding our benchmark of not more than 5%. The BOI loan was fully liquidated in October 2024.

RusselSmith posted a lower profit before tax (PBT) margin of 13.3% in FYE 2023 (2022: 18.4%) due to higher finance cost. However, pre-tax pre-interest return on assets (ROA) improved to 15% in FYE 2023 (2022: 9%) and pre-tax return on equity was better at 23% (2022: 19%), both remaining within our acceptable band for oil and gas servicing companies.

Based on unaudited accounts for the ten months ended 31 October 2024, RusselSmith earned a total revenue of ₦7.8 billion, surpassing its full-year 2023 performance. This growth was primarily driven by the commencement of work under the newly secured contract with SNEPCo. However, direct cost-to-sales ratio increased to 59.6% during the period, reflecting a reliance on expatriates to execute the SNEPCo contract. This metric is expected to moderate as more in-house staff are integrated into the contract's execution in the near term. Conversely, operating cost-to-sales ratio improved to 15.5% due majorly to economies of scale. RusselSmith posted an operating profit margin of 24.9% in the period and a PBT margin of 11.2% which are acceptable. This translated to an annualized ROA of 35%, surpassing our benchmark and ROE of 27% which was within our expectation.

Figure 2: OPM & ROA (2021 – Oct. 2024)



RusselSmith Nigeria Limited has benefitted from increased production efforts by upstream operators to bridge shortfalls in meeting OPEC's production quota. This production drive has resulted in higher demand for inspection, repair and maintenance services for aging upstream assets, leading to new contract acquisitions. RNL is poised for continued revenue growth in the near term, driven primarily by the newly acquired contracts with SNEPCo and NLNG. In addition, the planned launch of the pilot phase of its additive manufacturing operations in Q1 2025 is expected to further enhance revenue performance. However, we expect the Company's profitability to be moderately impacted by rising borrowing costs especially as it plans to secure new borrowings to fund working capital and ongoing business expansion.

In our opinion, RusselSmith Nigeria Limited's profitability is good.

CASH FLOW

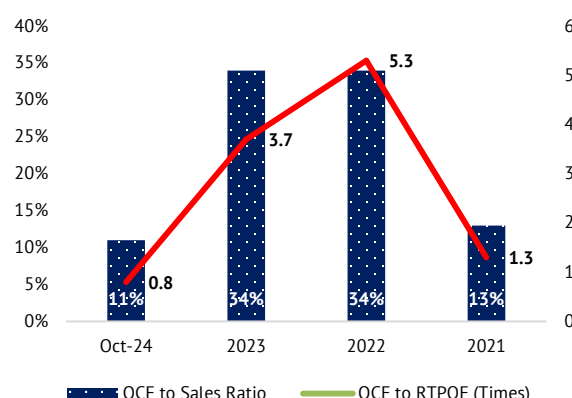
RusselSmith Nigeria Limited generates cash by providing topside and subsea asset integrity management services, operations and production support to IOCs, and more recently, from offering additive manufacturing solutions. The Company's services are rendered largely on credit, with payment expected between 45 and 50 days of invoicing. On the other hand, the Company enjoys up to 60 days of credit from its suppliers, reflecting favourable trade dynamics. As at 31 December 2023, the Company's receivable days stood at 54, which was slightly above the allowable credit term. However, over the last three years (2021 – 2023), the Company's receivable days averaged 122, reflecting delays often associated with preparing the requisite documentation for invoicing, particularly for complex projects. During the same period, the Company's payable days averaged 279, a significant stretch from the 60-day credit terms granted. This was primarily due to the spill over of vendor payments from 2020 owing to the COVID19 pandemic and the difficult years that followed. However, as at 31 October 2024, the Company had made substantial progress in addressing outstanding payables, reducing trade payable days to 40.

In the year ended 31 December 2023, RusselSmith's operating cash flow (OCF) grew by 96% to ₦1.8 billion, driven primarily by higher profits and increase in trade and other payables, notably withholding tax payable. The Company's OCF represented 34% of revenue, exceeding our expectation and was sufficient to cover returns to providers of finance (RTPOF), comprising solely interest payments, 3.7 times, which we consider good. Over the period between 2021 and 2023, RusselSmith has consistently generated sufficient OCF to cover RTPOF, resulting in a cumulative cover of 3.4x, underscoring its ability to meet its obligations.

In the ten months ended 31 October 2024, RusselSmith's OCF declined to ₦861 million, due to significant reductions in spontaneous financing as the Company settled its backlog of trade payables. The Company's OCF represented only 11% of revenue, and was insufficient to cover RTPOF. In the near term, we expect improvements in RusselSmith's cash flow position supported by better profitability and a realignment with established credit terms with suppliers following the recent clearance of backlogs.

In our view, RusselSmith's cash flow position is good.

Figure 3: OCF to Sales & OCF to RTPOF



LIQUIDITY PROFILE

As at 31 December 2023, RusselSmith's liquidity position comprised mainly free cash flow and unrestricted cash, totalling ₦2.4 billion. This was sufficient to cover the Company's maturing obligations 3x, which we consider good. In the near term, we expect the Company to continue to maintain adequate liquidity levels given its propensity to hold substantial cash reserves and its good cash generating capacity supported by favourable trade terms with suppliers and customers.

FINANCING STRUCTURE AND ADEQUACY OF WORKING CAPITAL

As at 31 December 2023, RusselSmith's working assets increased by 41% to ₦3.3 billion, due primarily to elevated levels of other receivables (majorly withholding tax credit notes).

As at FYE 2023, RusselSmith's spontaneous financing increased by 58% to ₦3.6 billion reflecting its expanded scope of work. The Company's spontaneous financing was sufficient to cover its working assets, leaving a short-term financing surplus of ₦206 million. This represents a shift from historical trends of posting working capital needs. However, we do not expect this trend to be sustained in the near term given recent clearance of trade payable backlogs, which has reduced the Company's spontaneous financing.

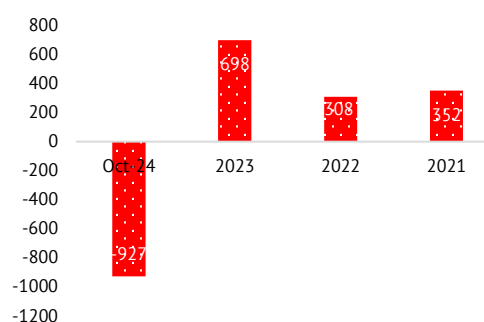
As at 31 December 2023, the Company's long-term assets declined by 12% to ₦3.9 billion due to depreciation. As at the same date, the Company's long-term funds of ₦4.4 billion, comprising equity (66%) and long-term loans (34%), were sufficient to cover its long-term assets, leaving a working capital of ₦492 million. On the whole, RusselSmith Nigeria Limited closed the year with an overall working capital surplus of ₦698 million.

We note however that during the 2022 financial year, the Company's long-term assets increased by 336% due primarily to the revaluation of its property plant and equipment (PPE). This raised the value of PPE from ₦872 million in 2021 to ₦3.8 billion in 2022. The revaluation was conducted by Osas and Oseji Estate Surveyors and Valuers, a company licensed by the Estate Surveyors and Valuers Registration Board³. As at FYE 2023, revaluation surplus accounted for 92% of the Company's equity

As at 31 October 2024, RusselSmith's spontaneous financing was insufficient to cover its working assets, resulting in a working capital need of ₦1.3 billion. However, as at the same date, the Company's long-term funds were sufficient to cover its long-term assets, resulting in a working capital of ₦395 million, which was inadequate to offset its working capital need. The Company therefore posted an overall working capital deficiency of ₦927 million as at 31 October 2024. We note that RusselSmith's spontaneous financing reduced by the recent clearance of trade payable backlogs. In the near term, we expect increase in the level of spontaneous financing, as the Company realigns with established credit terms. Furthermore, the planned injection of additional long-term debt will support the Company's overall working capital position, even though we note the high finance risk associated with increased debt funding.

In our opinion, RusselSmith Nigeria Limited's working capital requires improvement.

Figure 4: Overall Working Capital Position (₦Millions)



³ https://www.osasoseji.com/index.php/en/176/about_osas_oseji

LEVERAGE

As at 31 December 2023, RusselSmith Nigeria Limited's liabilities totalled ₦5 billion, comprising interest-bearing liabilities (IBL) - 30% and non-interest-bearing liabilities – 70%. The Company's non-interest-bearing liabilities comprised trade and other payables, deferred taxation and taxation payable. RusselSmith's IBL was solely the outstanding balance from the dollar-denominated Bank of Industry loan secured in 2018, which was sourced from the Nigerian Content Intervention Fund, and utilized for business expansion. This loan was restructured in 2020 and 2021 due to the impacts of the COVID-19 pandemic on the Company's operations. Consequently, the maturity date of the loan moved from June 2023 to December 2024. However, the loan was completely liquidated by October 2024 due to plans to secure a fresh facility.

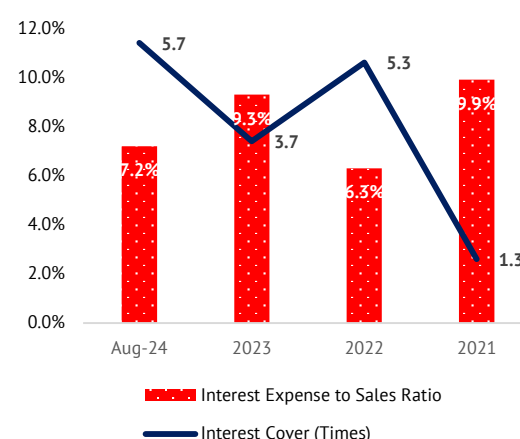
As at FYE 2023, the Company's operations were funded by interest-bearing-liability (19%), non-interest-bearing liability (44%) and equity (37%). We note however that 92% of equity comprised notional gains from the revaluation of some items of PPE. Without this notional gains, the Company's equity would have been less than 5% of its total assets. In the near term, we expect the Company's equity cushion to weaken further given plans to secure another BOI loan for business expansion, with no immediate plans for equity injection.

As at 31 December 2023, the Company's interest-bearing debt decreased by 36.5% to ₦1.5 billion due to repayments. However, RNL's interest expense in FYE 2023 increased by 181% to ₦479 million, owing primarily to the impact of naira devaluation on the servicing of its dollar-denominated debt. Consequently, the Company's finance cost to sales ratio increased to 9.3% (2022: 6.3%), exceeding our 5% threshold. Furthermore, The Company's interest-bearing debt net of cash as a percentage of equity (without revaluation surplus) and net debt to total assets ratios were elevated at 352% and 166% respectively.

In the ten months ended 31 October 2024 (unaudited), RusselSmith's finance cost to revenue ratio worsened to 13.7% due to a short-term borrowing of ₦1 billion obtained during the period to support working capital. Similarly, interest cover reduced to 0.8x, owing to significant declines in spontaneous financing following the settlement of trade payable backlogs. The Company's interest-bearing debt net of cash as a percentage of equity (without revaluation surplus) and net debt as a percentage of average total assets (excluding revaluation surplus and cash) were also elevated at 113% and 63% respectively. In the near term, RusselSmith plans to secure additional debt to fund its expansion into additive manufacturing. This is expected to further raise the Company's debt profile.

In our opinion, RusselSmith Nigeria Limited's leverage is high.

Figure 5: Interest Expense to Sales Ratio & Interest Cover



OUTLOOK

The Nigerian upstream sector has been experiencing a dearth of investments due primarily to the prevalence of security challenges in the oil and gas production areas, and increasing incidences of crude oil theft. Consequently, the country's ongoing campaign to ramp up production to bridge budgetary gaps and meet its OPEC quota has been largely reliant on aging assets. This has driven demand for asset integrity management services by upstream companies. RusselSmith Nigeria Limited, has benefitted from this dynamic. In 2023, the scope of the Company's contract with Mobil Producing Nigeria Unlimited, which has been ongoing since 2008, was expanded considerably. Furthermore, the Company secured new five-year contracts with Shell Nigeria Exploration and Production Company (SNEPCo) and the Nigeria Liquefied Natural Gas Limited (NLNG), with execution of the SNEPCo contract already commenced.

RusselSmith Nigeria Limited is also diversifying into additive manufacturing to address a critical gap in the broader economy. According to management, the Company has completed its proof-of-concept phase and is now transitioning to the pilot stage of its additive manufacturing operations. This phase will be anchored by its 3D Manufacturing and Innovation Centre, a much bigger facility expected to commence operations by Q1 2025. We expect that revenue from the additive manufacturing operations, along with increased earnings from the new jobs under the contracts with Mobil, SNEPCo and NLNG, will drive revenue growth for the Company in the near to medium term. Furthermore, revenue from the additive manufacturing operation, which will be 100% dollar-denominated is expected to drive margins. This is will be further enhanced by the anticipated integration of more in-house personnel into the execution of the SNEPCo contract for cost optimization.

We anticipate that the Company's operating cash flow will remain good in the near to medium term, supported by expected improvements in margins and favourable trade terms with customers and suppliers. Given plans to inject long-term debt to drive ongoing expansion activities, we expect the Company's debt profile to increase considerably and equity cushion to further weaken. However, this planned debt injection will support adequate working capital levels in the near to medium term.

Based on the above, we attach a **stable** outlook to RusselSmith Nigeria Limited.

FINANCIAL SUMMARY

STATEMENT OF COMPREHENSIVE INCOME	31-Dec-21		31-Dec-22		31-Dec-23		31-Oct-24 (Unaudited)	
	₦'million		₦'million		₦'million		₦'million	
REVENUE	1,852	-100%	2,686	100%	5,171	100%	7,841	100%
GROSS PROFIT	1,196	65%	1,006	37%	2,512	49%	3,168	40%
OPERATING PROFIT	307	17%	539	20%	1,312	25%	1,949	25%
INTEREST EXPENSE	(183)	-10%	(170)	-6%	(479)	-9%	(1,073)	-14%
PROFIT BEFORE TAXATION	138	7%	495	18%	685	13%	876	11%
TAX (EXPENSE) BENEFIT	(32)	-2%	(136)	-5%	(316)	-6%	(289)	-4%
PROFIT AFTER TAXATION	106	6%	358	13%	369	7%	587	7%
DIVIDEND	-	0%	-	0%	-	0%	-	0%
PROFIT RETAINED FOR THE YEAR	106	6%	358	13%	369	7%	587	7%
OTHER APPROPRIATIONS/ ADJUSTMENTS	2		-		-		-	
PROFIT RETAINED B/FWD	(387)		(596)		237		132	
PROFIT RETAINED C/FWD	(279)		(237)		132		719	

STATEMENT OF FINANCIAL POSITION	31-Dec-21		31-Dec-22		31-Dec-23		31-Oct-24 (Unaudited)	
	₦'million		₦'million		₦'million		₦'million	
ASSETS								
CASH & EQUIVALENTS	352	9%	309	4%	698	9%	73	1%
TOTAL TRADING ASSETS	2,563	63%	2,376	33%	3,348	42%	3,104	47%
TOTAL LONG-TERM ASSETS	1,133	28%	4,497	63%	3,946	49%	3,457	52%
TOTAL ASSETS	4,049	100%	7,182	100%	7,992	100%	6,634	100%
<i>Growth</i>	11.2%		77.4%		11%		-17%	
LIABILITIES & EQUITY								
TOTAL INTEREST-BEARING LIABILITIES	2,330	58%	2,378	33%	1,510	19%	1,000	15%
TOTAL NON-INTEREST-BEARING LIABILITIES	1,900	47%	2,246	31%	3,554	44%	1,782	42%
TOTAL LIABILITIES	4,229	104%	4,624	64%	5,065	63%	2,782	42%
SHAREHOLDERS' EQUITY	(180)	-4%	2,558	36%	2,927	37%	3,852	58%
TOTAL LIABILITIES & EQUITY	4,049	100%	7,182	100%	7,992	100%	6,634	100%

CASH FLOW STATEMENT	31-Dec-21		31-Dec-22		31-Dec-23		31-Oct-24 (Unaudited)	
	₦'million		₦'million		₦'million		₦'million	
OPERATING ACTIVITIES								
POTENTIAL OPERATING CASH FLOW	432		575		1,435		2,389	
WORKING CAPITAL CHANGES:								
CASH FROM (USED BY) SPONTANEOUS FINANCING	303		346		1,309		(1,772)	
CASH FROM (USED BY) TRADING ASSETS	(498)		(17)		(972)		244	
CASH FROM (USED IN) OPERATING ACTIVITIES	237		904		1,772		861	
RETURNS TO PROVIDERS OF FINANCING (RTPOF)								
INTEREST PAID	(183)		(170)		(479)		(1,073)	
DIVIDEND PAID	-		-		-		-	
OPERATING CASH FLOW AFTER RTPOF	54		734		1,292		(212)	
CASH FROM (USED IN) INVESTING ACTIVITIES	277		(826)		(36)		642	
CASH FROM (USED IN) FINANCING ACTIVITIES	(3)		48		(868)		(510)	
CHANGE IN CASH INC/(DEC)	39		(44)		389		(625)	
OPENING CASH & MARKETABLE SECURITIES	312		352		309		698	
CLOSING CASH & MARKETABLE SECURITIES	352		308		698		73	

KEY RATIOS	31-Dec-21	31-Dec-22	31-Dec-23	31-Oct-24 (Unaudited)
PROFITABILITY				
SALES GROWTH	38%	45%	93%	82%
OPERATING PROFIT MARGIN	17%	20%	25%	25%
RETURN ON ASSETS (PRE-INTEREST PRE-TAX)	8%	9%	15%	65%
RETURN ON EQUITY (PRE-TAX)	-77%	19%	23%	129%
CASH FLOW				
OCF AS % OF RETURNS TO PROVIDER OF FINANCING	130%	531%	370%	80%
OCF AS % OF SALES	13%	34%	34%	11%
WORKING CAPITAL				
WORKING CAPITAL NEED (DAYS)	0	0	0	0
OVERALL WORKING CAPITAL DEFICIENCY (DAYS)	0	0	0	0
LEVERAGE				
NET DEBT AS % OF AVERAGE TOTAL ASSETS	150%	135%	166%	63%
TOTAL LIABILITIES TO EQUITY	-2348%	-3349%	2191%	340%
OTHER ADDITIONAL INFORMATION				
STAFF COSTS (₦' MILLION)	357	642	1,008	1,008
AVERAGE NUMBER OF STAFF		53	53	53
STAFF COSTS PER EMPLOYEE (₦' MILLION)		12	19	19
CAPITAL EXPENDITURE (₦' MILLION)	0	481	587	0
DEPRECIATION AND AMORTISATION (₦' MILLION)	125	130	587	391
EBITDA (₦' MILLION)	446	795	1,752	2,340
AUDITORS	Lawal Olofin & Co.	Lawal Olofin & Co.	Paul Fadairo & Co.	Unaudited
OPINION	CLEAN	CLEAN	CLEAN	N/A

RATING DEFINITIONS

Aaa	A company with the best financial condition and strongest capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
Aa	A company with very good financial condition and a strong capacity to meet its obligations as and when they fall due relative to all other issuers in the same country.
A	A company with good financial condition and a strong capacity to meet its obligations relative to all other issuers in the same country.
Bbb	A company with satisfactory financial condition and adequate capacity to meet its obligations as and when they fall due relative to all other issuers in the same country.
Bb	A company with satisfactory financial condition but limited capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
B	A company with weak financial condition and weak capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
C	A company with very weak financial condition and very weak capacity to meet obligations as and when they fall due are relative to all other issuers in the same country.
D	In default.

Rating Category Modifiers

A "+" (plus) or "-" (minus) sign may be assigned to ratings from 'Aa' to 'C' to reflect comparative position within the rating category. Therefore, a rating with + (plus) attached to it is a notch higher than a rating without the + (plus) sign and two notches higher than a rating with the - (minus) sign.

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