Chairman's Report

Gary Morolo, Chairman

The chairman's report in the last annual report alludes to the evolving nature of Datacentrix' product offerings and business proposition from a basic infrastructure integrator and services provider to a full solutions supplier. As it was put to the market last year, Datacentrix' product and service mix has been slowly evolving from small transactional deals to bigger, more complex solutions as the company increasingly sells into the data centre as opposed to primarily the desktop environment.

The intended effect has been to make Datacentrix a more strategic long-term partner to clients as opposed to merely a purveyor of infrastructure hardware and services, away from commoditised offerings. Added to this mix has been the planned growth of our selective outsource business, not only in IT infrastructure and services, but also in print output market and resource provisioning. This has meant that Datacentrix' deal cycles have become longer, with each deal having proportionately more potential impact on the bottom line than has been the case in the past. Deal slippage has consequently become an issue with potential significant impact on the bottom line in any reporting period. Datacentrix embarked on this strategy by investing significantly in resources and competencies that we could otherwise only have got on board through acquisitions, thus further impacting the bottom line.

The strategy shift has yielded very pleasing results in many of our operating business units, growing the overall business in the private sector and repositioning the company favourably in the market. While in the last annual financial year we expressed positive views about government's anticipated IT spend and fairly bearish views about IT spend in the private sector, ironically Datacentrix delivered traditionally pleasing results that the market has come to expect of Datacentrix in all business units with a private sector exposure. The strategy evolution referred to above has delivered the desired results that also went a substantial way towards compensating for the lack of performance in the public sector. All these businesses with a private sector bias, such as outsourcing, managed print services, resourcing, technology solutions, enterprise content management, and of course the traditional commercial (private sector) infrastructure division, have showed excellent growth. We continue to build on these areas and anticipate extracting the desired performance from them.

On the other hand the developments in the public sector outpaced the company and a combination of factors contributed to a very poor performance in this sector. It has become apparent over the last few years that Datacentrix' market positioning was coming under threat principally because of increasing commoditisation of infrastructure hardware and the concomitant increased ability of SMMEs to play in this space.

Additionally, in the public sector some of the departments and government entities, especially SOEs, prefer or are obliged to implement parallel BEE evaluation criteria, which invariably require black equity ownership of at least 25%. Datacentrix has fully vested and unencumbered black ownership of just over 10%.

This requirement is putting Datacentrix under increasing competitive pressure, especially from the aforementioned well established SMMEs. Datacentrix anticipated that its business model would come under pressure and that it needed to move up the value chain. The move up the value chain has been organic, measured, and gradual, to build a strong and sustainable competency.

In our half yearly results, we flagged the poor performance of the divisions, which serve the government. For the reasons alluded to above, and further elucidated upon below, Datacentrix has a good understanding and even some measure of anticipation of this poor performance. The company had reasonable expectation that it would overcome the poor performance of the first half but this did not materialise.

While measures were put in place to address this issue or even substitute this business, the results have taken longer than anticipated, hence the failure to match, much less improve, on last year's performance. Firstly, government's policy to favour SMMEs where appropriate has been implemented more aggressively, leading to an intensely competitive environment.

Datacentrix can no longer compete effectively in the commoditised space because some of the SMMEs have graduated in the scale of their offerings to occupy the space that Datacentrix has occupied for many years during its own early growth phase. Some of the other reasons we outlined at our half yearly results. These included delays in tender awards occasioned by the anticipation of elections and the hiatus created by change in decision-making office bearers and officials.

Associated with this was a freeze on all major spending, and a re-direction of funding to re-prioritised areas. Also, as we have moved up the value chain in government, the deal cycle has become much longer and the adjudication process often aborted or subjected to a lot of pressure and unanticipated delays. A substantial portion of the business we anticipated from government remains unawarded, some of it for periods exceeding the last twelve months under review.

Governance

In line with implementing the pertinent aspects of King III, the roles of some directors have changed. Joan Joffe has assumed the role of Lead Independent Director because the Chairman is not an independent non-executive director in line with King III.

Risk management has been separated from the Audit Committee and a new Risk Committee of the board has been set up under the chairmanship of Thenjiwe Chikane. Alwyn Martin continues with his role as Chairman of the Audit Committee. Dudu Nyamane assumed the chairmanship of the Remuneration and Human Resources Committee.

A full review of King III and the new Companies Act is underway to ensure full compliance with the pertinent aspects at the earliest opportunity.

Black Economic Empowerment

Datacentrix has recently been awarded Level 3 Contributor status (EmpowerDex "AA" Rating) based on the DTI Codes of Good Governance. Ordinarily this would be regarded as excellent, sufficient to satisfy BEE requirements. As mentioned above, this is not necessarily the case, with some state-owned entities requiring at least 25% black-owned equity. Discussions on the promulgation of the ICT Charter especially on equity ownership have also resurfaced. The board has tasked the Lead Director, Joan Joffe, to have proposals developed on how best to address this imminent equity ownership requirement.

It also remains a concern of the board that the current management and other key members of staff are not invested in the business and this presents a risk to the company in terms of senior executive retention.

Prospects

Management has been driving a strategy to reposition Datacentrix to operate higher up the value chain. This has borne fruit so far and indications are that it will set Datacentrix up for its next growth phase. While our optimism in government related business was misplaced, a significant portion of the business that Datacentrix was in line for is yet to be awarded and we continue to have faith in our tender submissions.

Recent wins in the outsourcing businesses have substantially augmented the base for annuity income going forward. While Datacentrix has a bias towards organic growth, management and the board are actively considering bolt-on acquisitions to kick-start a strategic revitalisation of specific aspects of the Business Solutions division.

I thank the board for its wise counsel and its support to management, and to management and staff for effecting significant strategic shifts while growing most parts of the business and setting the stage for further growth.

Gary Morolo
Chairman

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