INTUITION
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Mr Price: value for money

Mr Price ("MRP") has been a household name over the years for many mothers with teenagers and with the apparel retailer's new funky baby section, this brand will now be embedded from an early age. We all know that the recent macro headwinds have caused havoc on our pockets. Interest rates are being hiked to suppress inflationary pressures and our discretionary income is just shrinking. Most households will look to down trade and with MRP still providing fashionable clothes at reasonable prices, having MRP in your portfolio has proven to be a safe choice, especially given that it has consistently delivered on dividends, bar Covid. In this article we will look at the why the fundamentals of this company make it a good share that can weather this tumultuous storm.

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Mr Price has been operating for more than 35 years and is the second-largest apparel retailer in SA (after Pepkor) when ranked by market capitalization. Their vision is "to become the most valuable retailer in Africa". Although the Group does have stores in the rest of Africa, expansion there has been measured. Consequently, SA still accounts for the lion's share of sales at 93%.

So, what makes this Group so attractive? For starters, MRP has ensured that they have strong representation across all market segments. This has been done through organic growth but also through new acquisitions. Let's look at MRP's three different divisions to see how the Group is cementing its future.

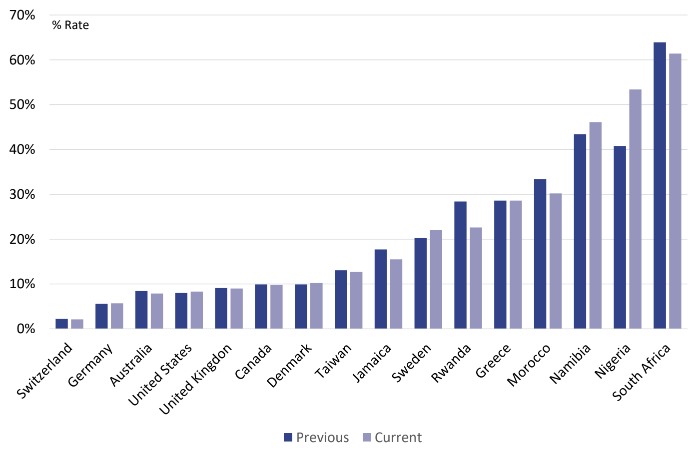
1. The Apparel segment consists of Mr Price Apparel, Mr Price Sport, Miladys and the newly acquired Power Fashion that came into effect on 1 April 2021. Mr Price targets consumers that lie in the 4 – 10 LSM categories, between the ages of 16 - 24. Of South Africa's 60.6 million inhabitants, 16% of the population fall into this bracket. Based on official statistics, SA has one of the highest rates of youth unemployment in the world, which might suggest that MRP is poorly positioned. But as we have articulated in prior issues, the township economy is far more vibrant than expected. Supported by social grants, the youth have more spending power than the official statistics would suggest, and MRP offers them value-orientated fashion. Mr Price Apparel was already a big role player in this segment, but the Group has expanded its reach with the purchase of Power Fashion, which allows them to compete against the likes of Pep.

MRP has also recently acquired a 70% stake in the Studio 88 Group, a niche apparel retailer of branded athleisure and lifestyle urban wear – a market to which MRP has historically not been exposed. Studio 88 represents brands such as Adidas, Converse, Levi's and VANs. This category has shown remarkable growth in recent years and was further fueled by the Pandemic as consumers opted for casual clothes over workwear. For the year ended September 2021, Studio 88 posted revenues of R5.6 billion across 711 stores. We expect this acquisition to be immediately earnings accretive for MRP shareholders.

SPEED READ

- **Previous issues have focused on companies that exemplify our investment philosophy – namely those with good track records of delivering steady growth and consistent dividends.**
- **MRP fits this mould, having delivered a compound annual rate of growth in dividends of 7.5% over the past ten years.**
- **With three strategic acquisitions over the past eighteen months, the Group has entrenched its position in the value retail segment and grown in the aspirational value category.**
- **MRP offers both organic growth and growth via acquisitions, which provides the base for profit and dividend growth without compromising on its balance sheet. What more can you ask for?**

YOUTH UNEMPLOYMENT RATE



South Africa has one of the highest rates of youth unemployment in the world. Nonetheless, it is encouraging to note that the rate has improved. It is now 5.1% lower than its all-time high reached in Q3 2021.

An example of organic growth underway is "Mr Price Baby". Traditionally this formed part of a normal Mr Price Apparel store, but now the Group has opened standalone stores across 6 different malls around South Africa. Provided it is a success, this concept will be rolled out countrywide.

2 The Home segment includes Mr Price Home, Sheet Street and another new acquisition, Yuppiechef, that was effective from August 2021. With this acquisition the Group was able to enter the aspirational value segment for the Homeware category and one of the key growth drivers was the omni-channel expansion (the combination of both online sales and brick & mortar stores.) Investors will be interested to know that when Mr Price presented their 2022 annual results in May this year, their fashion app was ranked number one in SA and second overall in terms of market share of traffic. Unsurprisingly, Takealot took the number one spot.

3. The Financial & Telecoms segment, which contributes 6.7% of the Group's revenue, exceeded the R1 billion turnover mark for the first time last year. It comprises of Mr Price Money and Mr Price Cellular. These services are available in 374 stores and Mr Price Cellular has now opened its first standalone store.

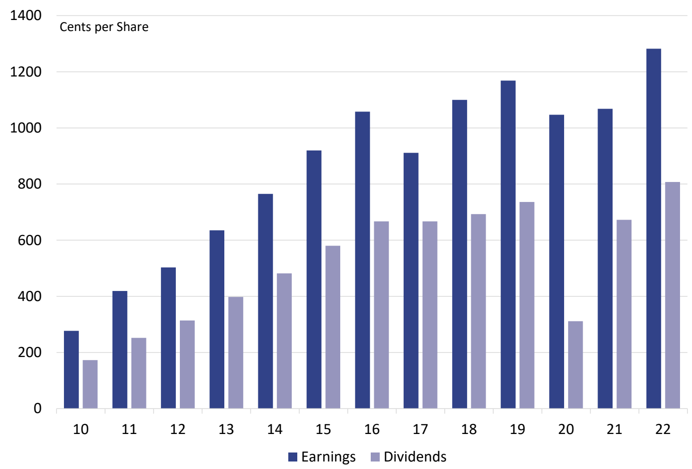
> "Amidst the civil unrest in July 2021, 31% of Mr Price's total stores were temporarily closed and 111 stores (9.5% of the total) were closed due to severe damage."

For years the Mr Price Group had very little inorganic growth (i.e. acquisitions). In fact, the Group's last acquisition was 25 years ago with Sheet Street. Consequently, the company was able to build up a good cash reserve. Over the past five years, MRP has come under increasing criticism from shareholders for having a "lazy" balance sheet. Cash balances exceeded R8 billion and shareholders were pressuring management to pay a special dividend. Management resisted and that prudence has been handsomely rewarded. With ample firepower, MRP was able to pounce on suitable targets as conditions became more challenging. Furthermore, all the recent acquisitions were cash purchases (no new shares were issued) and MRP's balance sheet is still debt-free! That is comforting given steadily rising interest rates. Now the Group boasts a total of 1,721 stores. Over the next year MRP is planning to spend R900 million to expand, which includes opening 180 – 200 new stores. Taken together, MRP has a strong growth profile that should stand shareholders in good stead, regardless of the rate of broader economic growth.

Amidst the civil unrest in July 2021, 31% of their total stores were temporarily closed and 111 stores (9.5% of the total) were closed due to severe damage. Despite half of their stores being affected, Power Fashion was still able to reach over 90% of their turnover target for the 2nd half of the 2022 financial year. Furthermore, the MRP Group was able to post improved turnover growth of 28.5% for the period, far outstripping growth of 14.2% reported by their peer group. This allowed them to achieve another significant milestone – operating profit surpassed R4 billion for the first time.

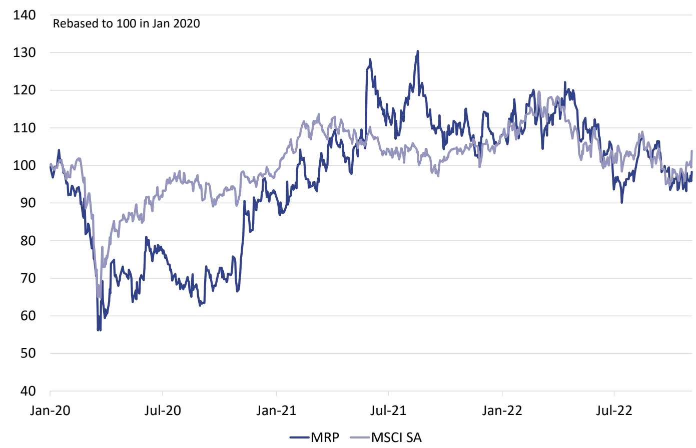
COVID restrictions emphasized the need to localise manufacturing as supply chain disruptions meant that by the time stock arrived it would have already been "out of fashion". Currency volatility has further supported this trend. Mr Price identified this risk as early as 2014. The Group started sourcing garments from Southern Africa, in particular Mauritius. For the 2022 financial year the Group sourced 78.6 million units (R4.3 billion worth of stock) from local South African suppliers, which represents 38% of its procurement costs. Not only does this improve efficiencies and lead times, which means better working capital management and improved gross profit margins, but it also benefits local employment, underpinning the ability of consumers to spend in its stores.

EARNINGS AND DIVIDEND TRACK RECORD



Despite the challenges facing SA, Mr Price has built a track record of consistent growth.”

SHARE PRICE



The price plummeted when we entered the hard lockdown, but has since steadily recovered.

Retailers were hard-hit during the Pandemic, with many opting to forgo dividends for twelve months (or more). Due to its strong balance sheet and financial prudence, Mr Price Group only had one six-month period when it did not pay a dividend. Despite all the headwinds mentioned, MRP was able to declare both record earnings and dividends, reflecting growth of 20% from last year and a payout ratio of 63%. We take comfort from the fact that MRP generates more than sufficient cash flow to ensure steady dividends to shareholders, underpinned by its debt-free status. Apart from the Covid wobble, the Group has grown its dividend every year for the past 12 years – no mean feat given the challenges in SA.

In our opinion, the recent share price performance does not reflect its exemplary track record and low-risk characteristics. The share price is barely changed from where is traded prior to the Pandemic, and it has largely tracked the performance of the broader SA market. Like so many other examples that we have highlighted, we believe that its only a matter of time before MRP’s resilience and superior growth is reflected. In the meantime, shareholders will continue to reap the benefit of the Group’s prudent financial management through steadily rising dividends.

Children growing up in the late 80’s and early 90’s were not as fashion conscious as children are today!
MRP certainly caters for the more distinct fashionista.

The world and financial markets have lurched from one crisis to the next over the past few years.

Will 2023 be any different?

Join us as we look ahead to what the new year may hold.

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Topic: **The World in 2023**

Natal Midlands	
Date:	24th of November 2022
Venue:	Oasis Conference Centre, 72 Main Road, Howick
Morning Time:	10am for 10.30am
Evening Time:	5.30pm for 6pm

Johannesburg	
Date:	6th of December 2022
Venue:	Rosebank Union Church, Cnr William Nichol and St Andrews Road, Hurlingham
Time:	7am for 7.30am

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