

## Shoprite Holdings: throwing the playbook at their competitors.

*The one good thing that came out of Covid lockdown was the acceleration of home deliveries. I am a happy Checkers shopper and have even joined the new Xtra-savings subscription. Before I leave work, I put in my Checkers Sixty60 order and by the time I get home, my delivery has already arrived. I can do a full article just on my personal online delivery stats alone, and this highlights one of the advantages that the Shoprite Group has - data sourcing. Knowing your customer and enticing them to return with specials tailored to their needs. If you haven't made the conclusion yet, I am a biased investor, but what is not to love? Let us delve into a few key trends that have made Shoprite Holdings such a fierce competitor.*



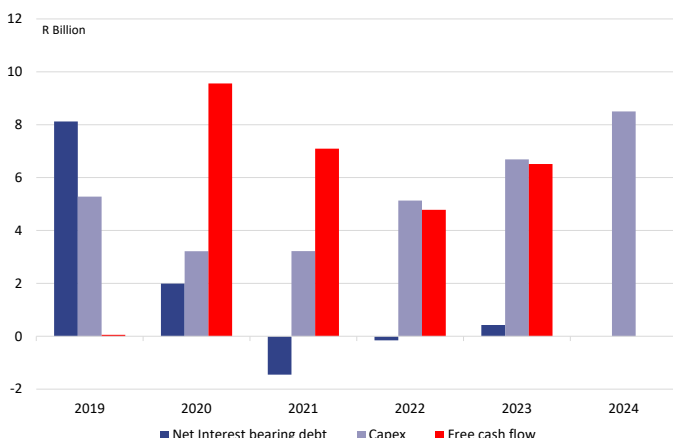
**Jana  
van Rooyen**

Returning, newly appointed CEO of Pick n Pay, Sean Summers, said that Pick n Pay wrote the playbook years ago on how to be a successful food retailer. However, now their competitor at Brackenfell (where Shoprite Holdings has its headquarters) is throwing the book back at them. Let us look at some of the key trends that have set Shoprite Holdings apart.

### Management strategic ability

Since his appointment in 2017, CEO Pieter Engelbrecht has

### CASH AND BALANCE SHEET CAPACITY



*Until recently, Shoprite had a large debt balance spread across Africa that limited its ability to invest for growth. The Group was intentional about repaying that debt, which has freed up cash for investment. Its capex has risen significantly, yet that expansion and investment has not caused any balance sheet stress.*

### SPEED READ

- Since his appointment in 2017, Shoprite CEO Pieter Engelbrecht has had a clear strategy with brand focus.
- Shoprite has been investing through the cycle for future growth and has the balance sheet capacity to make these significant investments.
- The company has gained market share amongst SA food retailers for fifty-five consecutive months. For the 2023 financial year the Group's sales growth was an impressive 16.8%.
- All these trends have resulted in good profit growth and hence good shareholder returns. But the valuation is pricing in much good news. Shareholders should be patient for a better entry point.

had a clear strategy centered on brand focus. In 2018 the SAP IT platform was implemented, allowing for future-fit IT and digital innovation. This paved the way for further market leading investment with the launch of Checkers Sixty60 in 2019, their online grocery app, and the Group's digital innovation hub and rewards program, Shoprite X, which was a clear advantage. Shoprite's Xtra Savings reward members have now reached the 27.8 million mark. 2021 saw the launch of complementary brands such as Little Me (baby shop) and Petshop Science, a gap in the market that Woolworths is only now entering with the acquisition of Absolute Pets. Since then, more stand-alone stores have been opened such as Checkers Outdoor and UNIQ clothing stores (which offers Country Road quality clothes at more reasonable prices).

## Strong Balance sheet to support growth

Shoprite has been investing through the cycle for future growth and has the balance sheet capacity to make these significant investments. The Group has spent R23.5 billion on capital expenditure (capex) over the past five years, R6.7 billion of which was over the past 12 months alone. Despite the significant amount, this level of spending represents just 3.1% of its annual sales, highlighting how scale opens opportunities that in turn result in more scale. For the 2024 financial year, capex is guided to rise further still to R8.5 billion, as shown in the graph below. Interesting, this equates to 67% of Pick and Pay's current market capitalization, compared to just 5.7% of that for Shoprite Group.

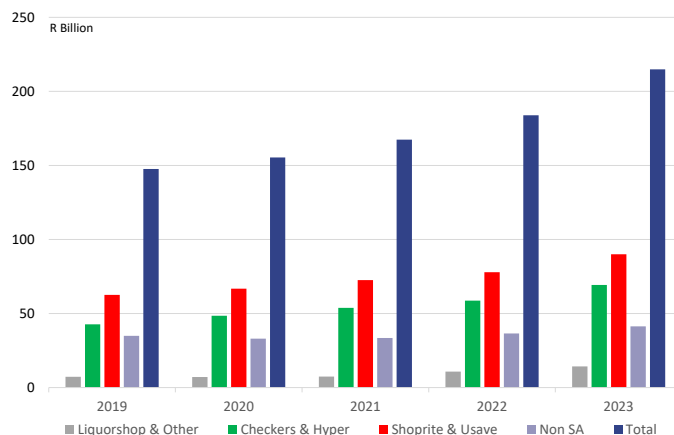
## Consistent sales growth and market share gains

The key to Shoprite's recent success has been its focus on precision retailing whereas most competitors have been guilty of reactive retailing. For the 2023 financial year the Group's sales growth was an impressive 16.8%. Consequently, Shoprite now claims that it has grown market share across food retail in South Africa for 55 consecutive months. This is based on data submitted by all retailers to the Retail Liaison Committee, which collates industry-wide statistics. Encouragingly, it looks like that trend has persevered as Shoprite has indicated that it has continued to gain market share (another 124 basis points) over the past 4 months since its June year end. There is no doubt that Shoprite's peers in the higher LSM categories are complaining about losing out to the Shoprite juggernaut.

Some of Shoprite's success can be attributed to their ability to penetrate and grow across all income groups in the country. As a brand, Shoprite may be known for targeting middle to lower LSMs, but they have successfully grown into the higher LSMs through their various Checkers formats, and into lower LSMs through USave and others. Like Spar, they have aggressively grown their liquor and pharmacy presence, and are now expanding into other formats, as mentioned earlier. Crucially, their Private Label (no name brands) portfolio had aggressive on-shelf pricing and has achieved the highest household penetration among SA retailers. While consumers are feeling the pinch, Shoprite's Private Labels provide consumers with an opportunity to down trade, ensuring that the Group does not lose any footfall but simultaneously is able to capture a higher share of spending. Private labels offer food retailers

**"The cost of diesel to run generators for Shoprite Group was an extraordinary R1.3 billion for the last financial year."**

## REVENUE GROWTH BY SEGMENT



*Shoprite's investment into their business has paid off handsomely. Their market-leading innovation is clearly visible in their superior revenue growth - a 5-year CAGR of 7.8% for the Group. The Checkers and Checkers Hyper segment, which has gained market share amongst higher LSMs, has had a 5-year revenue CAGR of 10.2%.*

good margins which, together with more promotional activity on other products, allowed Shoprite to offer substantial value to shoppers across a range of products and yet still maintain their gross profit margin at 25% - no mean feat given the challenging conditions facing consumers.

## Market leading profit growth

Most companies in South Africa have been remarkably resilient through loadshedding, but it does come at a cost, notably in much lower operating margins. The cost of diesel to run generators was an extraordinary R1.3 billion for the last financial year. Excluding this cost, the operating profit

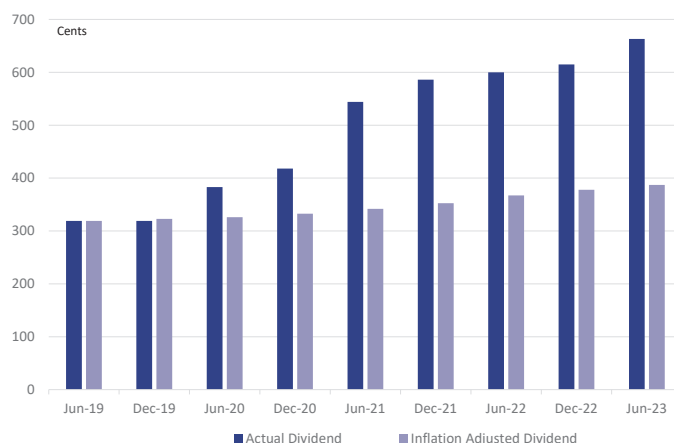
margin would have been 6.1%, but it fell to 5.5% because of loadshedding pressures. The highest margin that Shoprite has achieved over the past six years was in June 2021, when it achieved a margin of 6.1%. So, this result should be seen in that context – near record margins despite the numerous challenges. We remain of the opinion that 2023 will be the

year of peak loadshedding in this country, with the cost of loadshedding mitigation measures falling steadily over the next two years. That implies further margin improvement in the years to come, which is good news for the economy as a whole. Shoprite will certainly benefit too, given its efficient operations. Solid margins allowed Shoprite to declare profits of almost R12 billion, which in turn has given them

scope to reward shareholders through consistent, and rising, dividends.

Unfortunately, life is full of compromises, and investing is no different. Unlike most companies in South Africa that are currently trading at or near historically low valuations, Shoprite is at the other end of the scale. It is trading at a significant premium to both the market and its own history given its strong share price performance in recent years. Nonetheless, Shoprite has developed a distinct competitive advantage, and they have the ability and financial strength to continue reinvesting in that competitive advantage, which offers an exciting, compounding growth trajectory. For that reason, the Group remains firmly on our radar. But as the old saying goes, “Price is what you pay, value is what you get.” The valuation leaves little room for error. We believe investors should be patient and wait for a better entry point.

#### ACTUAL DIVI' VS INFLATION-ADJUSTED DIVI'



*Shoprite's robust performance has allowed it to reward its shareholders with consistent and growing dividends, well in excess of the rate of inflation.*

#### FREE MARKETING

## WHO WORE IT BEST?



*Much to the horror of die-hard Springbok fans, their alternative kit's colour during the recent Rugby World Cup was very similar to that of Checkers! Who could have asked for better advertising?*





Our next Insight seminar will take place in December in Cape Town, Johannesburg and Howick. After an eventful 2023 which has delivered its fair share of surprises, our next seminar will take stock of the year and focus on the outlook for 2024.



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**Topic:** **Outlook for 2024**

### **Natal Midlands**

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

### **Cape Town**

Date:	4th of December
Venue:	ABRU Motor Studio, Lourensford Wine Estate, Somerset West
Time:	5.30pm for 6pm

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Performance figures quoted for the portfolio is from Morningstar, as at the date of this document for a lump sum investment, using NAV-NAV with income reinvested and do not take any upfront manager's charge into account. Income distributions are declared on the ex-dividend date. Actual investment performance will differ based on the initial fees charge applicable, the actual investment date, the date of reinvestment and dividend withholding tax. Performance fees do not apply to any funds managed by Harvard House. The manager does not provide any guarantee either with respect to the capital or return of the portfolio. A schedule of fees, charges, and maximum commissions are available on request from the manager.

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