

EQUITY INSIGHTS

Clicks Group: Defensive Long-Term Growth Prospects

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ESTABLISHMENT OF A RETAIL POWERHOUSE

Clicks was conceived as a drugstore in 1968 and began operating as a corporate pharmacy when regulation allowed in 2003. Today, Clicks is a co-leader in dispensary with 23% market share from 510 pharmacies within 640 Clicks stores. Their designated service provider status with private Medical Aid schemes enables Clicks to dispense medicines at lower fees than independents, driving footfall into the 'front shop' which drives a value for money proposition and contributes 70% of retail revenues.

Clicks is innovative and increasingly sells a combination of exclusive brands and private label products. In the front shop, Clicks is the market leader in Personal Care & Beauty as well as Baby Care. Promotions now cover 35% of products and the 7.8 million member rewards program provides an edge in understanding customers, targeted promotions and communicating cash savings. Over the decade, trading area has grown 50% to 300,000sqm and trading density expanded to the present R90,000 per sqm.

A unique source of competitive advantage for Clicks is its vertical integration. Subsidiary UPD, is the leader in wholesale and pre-distribution of pharmaceuticals with a 26% market share. UPD supplies Clicks stores, 1,200 independent pharmacies and fulfils bulk distribution for manufacturers. The group also owns a generic pharmaceutical product marketer called Unicorn, which distributes generic drugs produced by third party manufacturers. Private label medicine now constitutes 5% of the generics dispensed by Clicks.

EXEMPLARY MANAGEMENT STEWARDSHIP

Management have consistently met or exceeded targets on store, space, revenue and profitability growth. The ESG impact is favourable, and a strong incentive structure is in place. Of 16,000 employees, 5,800 participate in the broad-based share ownership plan. Capital Allocation has been excellent over the past decade, with stock repurchases and dividends averaging 100% of earnings and dividends per share growing over 500%.

CEO Vikesh Ramsunder took the reigns in January 2019 from David Kneale who had led the business since 2006. Vikesh has 25 years of experience in Clicks including as MD of UPD, head of the Clicks chain and Group COO. He along with CFO Michael Fleming have strong reputations and are continuing the execution of the business strategy.

TWO CLEAR WINNERS IN PHARMA RETAIL

The pharma retail industry is highly attractive from the perspective of Clicks and Dis-Chem, and much more challenging for independent pharmacies, front shop suppliers and competing retailers. Over the last 5 years, Clicks and Dis-Chem combined have gained more than 9% market share in each of the following segments; Dispensary, Healthcare & Nutrition, Baby Care and Personal Care & Beauty.

BEST IN CLASS BUSINESS WITH SUSTAINABLE GROWTH DRIVERS

Clicks has one of the best operating cash flow margins of Drugstore chains anywhere in the world, recently surpassing industry giant Walgreens Boots Alliance. Cash generation is reliably 130% of earnings enabling high dividend pay-outs whilst funding organic growth. Returns on net tangible assets of 18% are superior to global listed peers.

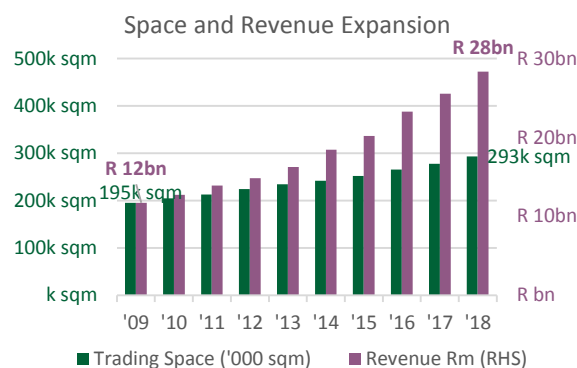
Clicks leads the market in low dispensing fees, loyalty members, private label and promotional items. Clicks' growth drivers include the above average GDP growth of the sector, consolidation of the independents, continued market share gains across front shop categories and continued growth in wholesale and pre-distribution. Clicks has identified locations to expand their footprint to 900 in the coming years. Unicorn may provide a key long-term advantage to Clicks in expanding margins as customers continue to migrate from original to generic drugs. As Clicks continues to gain scale and share, we expect benefits to flow to the business in the form of improved working capital, rebates, fees, and supplier-funded promotions.

CONCLUSION

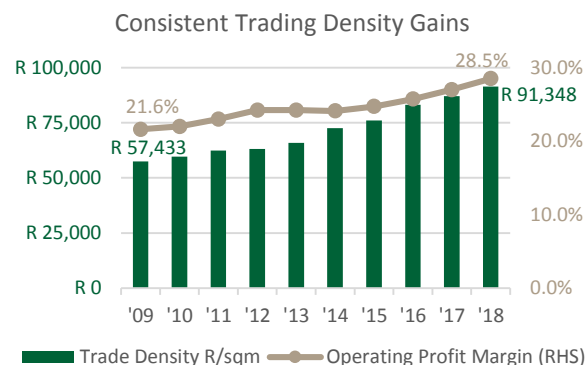
At present, we assess the market price to be a fair reflection of value for this first class asset, which we expect to grow shareholder value substantially over the long term.

| | Clicks Group Limited |
|----------------------------|----------------------|
| Market Cap | R 49bn |
| Current Share Price | R 191.80 |
| 5 Year Total Return in ZAR | 225.9% |
| Forward Price to Cash Flow | 21.6x |
| Forward Dividend Yield | 2.5% |

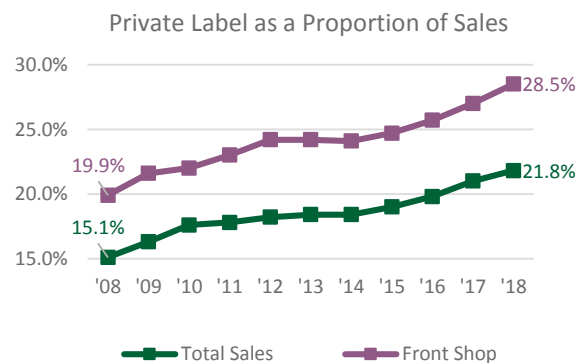
Sources: FactSet, August 2019



Sources: Company Filings, August 2019



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