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TFG stars as wizard of Oz

Unlike Woolies, Pick n Pay and almost every other SA company, the early signs are that TFG is thriving Down Under

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It's not often that an SA retailer's venture into Australia pays off, but for apparel group TFG its expansion Down Under has worked out rather nicely.

Though the likes of Woolworths and Pick n Pay have famously lost their way in Australia, TFG's purchase in the past financial year of the Retail Apparel Group (RAG) for R2.94bn, and of Phase Eight, Whistles and Hobbs in the UK for an undisclosed sum, is paying off handsomely.

RAG now falls under TFG Australia, and it increased sales 170% to A$239m for the six months to September. In rand terms, pretax profit jumped from R33.5m to R179.2m.

This was a big boost for the group as a whole. Overall, revenue rose 28.6% to R15.9bn, its gross margin expanded from 51% to 53.6% and profit jumped from R1bn to R1.15bn.

It's a thumping vindication of its Australia foray, which raises the question of what TFG has done differently to others.

In SA the consumer is very constrained given low wage growth and increased costs like VAT and fuel

Bjorn Samuels

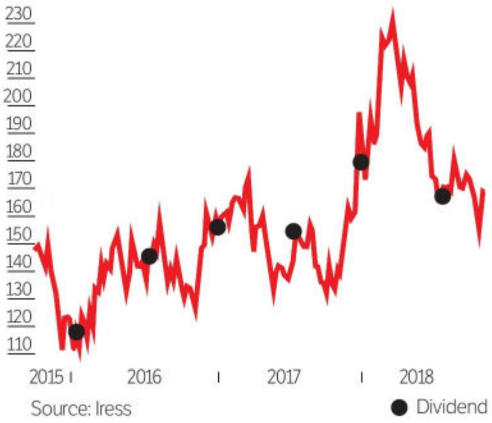
"[Its] offshore strategy has been well executed relative to listed peers," says Argon Asset Management equity analyst Bjorn Samuels.

Anthony Thunström, TFG's new CEO who has been in the job only a few months, says the company went into the UK and Australia with the mindset that it couldn't simply imitate what it was doing in SA. "Every single country has its nuances," he told the FM this week.

TFG resisted the urge to "parachute in" an SA management team to lead these acquisitions, but relied instead on local managers who already knew the lie of the land.

DIVERSIFICATION PAYS OFF

TFG share price (R) – weekly



Thunström says TFG, as a niche retailer and not a department store, had an advantage over other SA companies that have gone to Australia. Department stores around the world are struggling to adapt to changing consumer preferences and meet the challenge of e-tailers.

Investors are happy. Over the past three years TFG has been the best-performing clothing retailer, with its share price up 17%, ahead of Mr Price (up 7.7%) and streets ahead of Truworths (down 15.5%) and Woolworths (down 44%). And on a p:e of 15, it's still trading at a reasonable price.

Samuels likes what he sees. "They have acquired businesses abroad that have a similar operating model to TFG, and have largely kept the original management in place to ensure business continuity," he says.

Those purchases also offered some insulation from the move to e-commerce. "[TFG] operates in segments that are less disrupted by some of the structural headwinds driven by online disruption," says Samuels.

This robustness can be seen in TFG London: its online revenue grew 15% in a market where trade was moving rapidly from high street to online retail.

On the surface, TFG London's 50.7% rise in revenue to £200.4m looked good, but it was no way as impressive as the Australian operation, as revenue was up only 2.3% when measured on a like-for-like basis.

The Australian acquisition might be going swimmingly, but it wasn't the only part of the business that performed. TFG Africa produced impressive numbers despite SA, its biggest component, being in a technical recession. Sales rose 8.4% to R10.45bn and pretax profits grew from R972m to R1.01bn.

Samuels reckons TFG is helped by its diverse spread of products that target customers across various income segments. "We believe that TFG is able to retain a downtrading customer via another brand in the portfolio," he says.

Besides clothing brands Foschini and Markham, the group also owns jewellery brands like American Swiss, décor chain @home, and low-cost brands like exact! and fashionexpress.

Though the numbers look decent, Thunström is cautious. "We expect trading conditions to remain challenging in all three of our major territories, as consumer spending and business confidence remain under pressure."

Samuels agrees. "In SA the consumer is very constrained given low wage growth and increased costs like VAT, fuel and general household expenses."

These are issues that threaten the Australian business too. Says Samuels: "In Australia, we are seeing more reports of an overindebted consumer, while consumer sentiment and the general retail environment in the UK remain negative."

Australia also seems to be at risk of a bubble in its property market. Even so, with GDP growth of 3.4%, it looks to be the strongest of all TFG's territories.

TFG
BUY
Target price: **R196.19**
Potential upside: **21.8%**
* Based on analysts' consensus forecast

Thunström says the UK remains TFG's toughest market because of the uncertainty surrounding Brexit and the fact that British department stores are struggling to keep customers. "It's a lot like how SA was in November last year," he says.

He's right to be cautious, given that shoppers are under stress and that 45% of TFG's customers buy on credit. While the signs are certainly good, it would be premature to declare victory just yet. x

Anthony Thunström: The company went into the UK and Australia with the mindset that it couldn't simply imitate what it was doing in SA