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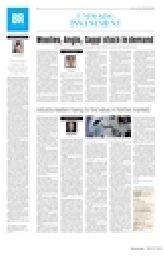

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AMELIA MORGENROOD

The Foschini Group is the notable exception in South Africa

THE FUTURE and prospects of the retail sector remain very much debated and unsure. Not only is it the health of the South African consumer that is a concern, but international trends like internet shopping also plays a role.

Last week the Investment Analyst Society presented an Analysts Masterclass with the emphasis on the retail and consumer goods sector of the JSE. Much insight was provided by veteran analysts Syd Vianello and Chris Gilmour, featured on the panel discussion. They unpacked several topics like the size and diversity of the sector, the impact of foreign players, consumer behaviour, and retail companies venturing offshore, and notably into Australia, often terminating these ventures in the graveyard.

Early 2018 retail stocks had a rally on the JSE, and share prices rose substantially thanks to the momentum created by Cyril Ramaphosa's ascent to the presidency. The gains started in November 2017, when the market began to price in the expected positive political changes. Ever since it lost steam and investor demand faded away. Traditionally offshore investors favoured retail stocks, but statistics show foreign investors remaining net seller of the JSE to the value of R37 billion. The South African economy is experiencing the most prolonged downturn since 1945, and for the retail sector, this is the worst situation ever. They are stuck in a low growth environment, and there are few exceptions, so far the only one unscathed is The Foschini Group (TFG).

It does not seem like the retail environment will get much easier soon, with households under immense pressure from higher taxes, higher petrol price, unemployment, high debt levels and low confidence levels. Everybody expected a consistent improvement after the election, but this did not materialise. In a low inflation environment, the food retailers margins come under pressure, and their opportunity for high stock profits disappear.

Online shopping threatens the traditional retailers in the developed markets, but it doesn't seem to be a real threat in South Africa and the rest of Africa yet. It varies from country to country; in South Africa, it is still a low 2 to 3 percent of retail sales while it is for example, much higher in the UK closer to 30 percent. In Africa, there are delivery issues, and the traditional shopping centre is not as much under threat as in the developed world. Even when Stuttafords blew up, it didn't take long for all the space to be filled up by smaller retailers and pop-up shops. In the UK, USA and Europe it is different; shopping will decrease dramatically in the future, and there is a vast oversupply of retail space.

The South African landscape changed in the last couple of years and quite a few of the global brands have already left. Some came in on a franchise basis, but they didn't make it. The franchise mark-up, import duties and margin for the retailer made the clothes too expensive. There is just too much competition in South Africa.

For many years retailers were boosted by the up and coming middle class and ever-increasing social grants, but the growth in both are questionable for the foreseeable future.

Foreign investors used to love SA retailers because we have world-class management and high profit margins, not necessarily found in other emerging markets, but are management still considered to be good?

The question is probably yes to retailers like Mr Price, PicknPay, and TFG.

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