EDCON’s GROSS PROFIT MARGIN IMPROVES DESPITE CONSTRAINED MARKET

Key features

Pertaining to the third quarter 2018 compared to the third quarter 2017:

- The Edcon Group’s retail sales decreased by 9.4% to R7,646 million from R8,441 million impacted by the sale of the Legit business, the exit of non-profitable international brands and the closure of unprofitable stores
  - Like-for-like retail sales decreased by 4.9%
- Excluding Legit, Edgars Shoe Gallery, international brands being exited and the alignment\(^1\) of the trading period, retail sales decreased by 3.8% to R7,710 million
- Gross profit margin up 190bps from 36.1% to 38.0%
- Excluding the impact of Legit, Edgars Shoe Gallery, brands being exited and the alignment\(^1\) of the third quarter 2018 trading period to the third quarter 2017, gross profit increased by 2.3% to R2,952 million
  - The gross profit margin increased 230bps from 36.0% to 38.3%
- Pro-forma Adjusted EBITDA decreased by 31.4% to R619 million
- Operating cash before changes in working capital increased by R397 million in third quarter 2018 compared to an increase of R449 million in the third quarter 2017
- Ladieswear continues to trade up in both Edgars and Jet
- The super senior liquidity facility was extended to 30 September 2018 and Edcon is in discussions with stakeholders on options to refinance the Edcon Group’s indebtedness

\(^1\) includes 24 December 2017 and excludes 24 September 2017 (the “alignment of the third quarter 2018 trading period”).

Johannesburg, 7 March 2018: The Edcon Group’s gross profit margin for the third quarter 2018 (ended 23 December 2017) was 38.0%, up 190bps from 36.1% in the third quarter 2017.

Grant Pattison, Edcon CEO, commented, “The pleasing increase in the gross profit margin was achieved through improved input costs, negotiated supplier rebates and settlement discounts as well as a reduction in clearance and promotional markdowns”.

Pro-forma adjusted EBITDA decreased by R283 million, or 31.4%, from R902 million in the third quarter 2017, to R619 million in the third quarter 2018. After the alignment of the third quarter 2018, pro-forma adjusted EBITDA increased by R43 million to R662 million in third quarter 2018, a decrease of 26.6% from R902 million in the third quarter 2017. Pro forma adjusted EBITDA was impacted by weak trading performance and additional operating costs in the credit and financial services division of R153 million, of which R23 million relates to additional costs of administering Edcon’s own funded trade receivables book and R130 million relates to net bad debts and an increase in the trade receivable provisions.
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Total Group revenues decreased by R712 million, or 8.0%, from R8,899 million to R8,187 million due to a decrease in retail sales of R795 million compared to the prior period, whilst like-for-like retail sales decreased by 4.9%. Retail sales decreased primarily as a result of a reduction in promotion activity compared to the third quarter 2017, following the introduction of better entry price points in fiscal 2017.

The overall gross profit decreased by R139 million to R2,907 million in the third quarter 2017. Excluding the impact of Legit, Edgars Shoe Gallery, brands being exited and aligning the third quarter 2018 trading period, gross profit increased by R66 million, or 2.3%, from R2,886 million in the third quarter 2017 to R2,952 million in the third quarter 2018. The gross profit margin increased 230bps from 36.0% in the third quarter 2017 to 38.3% for the third quarter 2018.

Generally, consumer confidence has remained low, and economic factors continue to impact consumers, while the Group is experiencing increased competition from established market participants as well as new market entrants.

Sales volumes remained under pressure, with retail sales excluding the impact of the Legit sale, Edgars Shoe Gallery, brands being exited and aligning the third quarter 2018 trading period, decreasing by R308 million, or 3.8%, to R7,710 million from R8,018 million. Grant Pattison added, “While retail sales were affected by weak consumer demand and fierce price competition through ongoing promotions and clearance activity by competitors, it is pleasing that both Edgars and Jet continued to trade positively in ladieswear and footwear in Edgars”.

Credit sales decreased by 11.2% (9.2% excluding Legit and Edgars Shoe Gallery) compared to a decrease of 8.7% in the third quarter 2017 as the Group tightened its credit scorecards during the quarter. Edcon’s in-house trade receivables book as at 23 December 2017 was R790 million, up R460 million from R330 million as at 24 December 2016 and has increased by R372 million compared to R418 million as at 25 March 2017. Credit sales contributed 34.6% of total retail sales for the third quarter 2018, a decrease of 0.7%, from 35.3% in the third quarter 2017. The Group has made good progress in respect of finding a securitisation solution for the Group’s own book.

Cash sales including the Legit business, Edgars Shoe Gallery and the exit of unprofitable international brands decreased by 8.4% (3.5% excluding Legit and Edgars Shoe Gallery cash sales) mainly because of low consumer demand in the third quarter 2018.

Operating cash before changes in working capital decreased by R52 million from a cash inflow of R449 million to a cash inflow of R397 million in the third quarter 2018. The decrease was a result of subdued trading performance and was impacted further by the fact that 24 December 2017 was excluded from the third quarter 2018 (whereas in fiscal 2017, 24 December 2016 fell in the third quarter 2017).

Working capital generated a R988 million cash inflow in the third quarter 2018 compared to a R1,341 million inflow in the third quarter 2017 impacted by higher inventory levels following weaker than expected peak trade retail sales and a reduction in trade accounts payable.
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Total store costs were well controlled, and increased by R36 million, or 2.0%, from R1,813 million to R1,849 million. Higher rental costs in both Edgars and Jet contributed to the increase in store costs as well as higher asset write-offs as non-performing stores were closed during the period.

Capital expenditure decreased to R118 million. In the third quarter 2018, Edcon opened 34 new stores which, combined with store refurbishments, resulted in investments in stores of R105 million (excluding Zimbabwe), compared to the third quarter 2017 during which 17 new stores were opened, resulting in an investment in stores of R64 million (excluding Zimbabwe). Edcon invested R43 million in information systems infrastructure in the third quarter 2018 compared to R153 million in the third quarter 2017. The Group is in the process of revisiting the IT simplification and upgrade strategy. The Group has planned total capital expenditure of approximately R500 million to R600 million for fiscal year 2018.

The total net third party debt decreased by R20,537 million or 83.1% from R24,703 million as at 24 December 2016 to R4,166 million as at 23 December 2017, which is as a result of the Agreement with Creditors and the Restructuring effective 1 February 2017. Net financing costs decreased by R555 million, or 59.9%, from R926 million in the third quarter 2017 to R371 million in the third quarter 2018.

The Group extended the super senior liquidity facility during the third quarter 2018 and is currently in discussions with its stakeholders with respect to options to refinance the Group’s financial indebtedness.

Edgars

Retail sales decreased by R262 million, or 6.9%, from R3,787 million in the third quarter 2017 to R3,525 million in the third quarter 2018. Retail sales for the October and November months combined, decreased by 2.9%, whilst December decreased by 11.4% when compared to the same periods of the third quarter 2017. Aligning the third quarter 2018 trading period, retail sales decreased by 6.3%. Edgars achieved positive retail sales growth in ladieswear and footwear for the third consecutive quarter realising benefits from the new strategies introduced in these categories. Cosmetics, menswear, childrenswear, homeware, cellular and active clothing retail sales decreased when compared to the third quarter 2017. Edgars cash sales decreased by 4.8% compared to the third quarter 2017, and credit sales decreased by 9.5% over the same period as a result of tightened credit scorecards introduced during the quarter. Same store sales decreased by 6.7% compared to the third quarter 2017. The gross margin improved by 100bps from 40.0% to 41.0% (41.1% aligning the third quarter 2018 trading period), which is due to better input costs, increased supplier discounts and a marginal reduction in markdown activity in the third quarter 2018, compared to the third quarter 2017.

Jet

Retail sales decreased by R90 million, or 2.7%, from R3,383 million to R3,293 million. Aligning the third quarter 2018 trading period, retail sales decreased by 1.3%. Credit sales decreased by 9.5% as
cred
score
cards were
tightened
during the quarter whilst, cash sales increased slightly by 0.1%.
Ladieswear performed positively compared to the third quarter 2017 following strategic initiatives introduced, whilst the remaining categories including menswear, childrenswear, footwear, homeware and hardlines continued to underperform in a competitive market. Same store sales decreased by 3.9% compared to the third quarter 2017. The gross profit margin increased 200bps to 35.0% (35.1% after aligning the third quarter 2018 period) from 33.0%, due to improved input costs, higher supplier rebates received and a reduction in markdown activity.

Specialty

Specialty includes CNA and the mono-branded stores, while the third quarter 2017 figures include the Legit business, the majority of which was sold in January 2017 and the sale of the remaining business in Botswana was sold effective 30 April 2017, as well as the Edgars Shoe Gallery stores which were closed during fiscal 2017. Total retail sales for the third quarter 2018 was R600 million, a decrease of R483 million, or 44.6%, compared to retail sales of R1,083 million in the third quarter 2017. Excluding Legit, Edgars Shoe Gallery and unprofitable brands being exited such as Lucky Brand, Tom Tailor, River Island, One Green Elephant, Geox, Express and others, retail sales for the third quarter 2018 was R587 million, a decrease of R73 million, or 11.1% (10.2% after aligning the third quarter 2018 trading period). Retail sales in CNA decreased by 9.8% whilst the mono-branded stores retail sales decreased by 37.0% (15.0% excluding the exiting of non-profitable brands). Supplier discounts and increased rebates contributed to an increase in gross margin of 2.6% from 31.2% to 33.8% (34.9% after aligning the third quarter 2018 period).

Africa

Sales from countries other than South Africa decreased by 3.7% (10.3% excluding Zimbabwe) and contributed 11.3% (8.5% excluding Zimbabwe) of retail sales. All territories except Zimbabwe and Ghana reported a decrease in retail sales with the biggest decline experienced in Namibia. Retail sales in Swaziland, Lesotho, Namibia, Zambia and Botswana were impacted by the sale of the Legit business. Zimbabwe, Ghana and Zambia reported an increase in local currency sales.

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About Edcon

Edcon is southern Africa's largest non-food retailer. We have been in operation for more than 80 years and have expanded our footprint to 1,292 stores as at 23 December 2017, including 186 stores in eight countries outside of South Africa. We operate our business under three principal operating divisions comprising eight key store chains as well as mono-branded stores throughout southern Africa:

- Our Edgars Division, is targeted at middle-to-upper-income customers and includes the Edgars store chains. We have 286 stores in our Edgars Division and an average retail space of 740 thousand square meters.
- Our Jet Division, which consists of discount stores selling value merchandise targeted at lower- to middle-income customers, includes store chains Jet and Jet. We have 737 stores in this division and an average retail space of 648 thousand square meters.
- Our Specialty division, which consist of stores selling value merchandise targeted at middle to upper-income customers, includes store chains CNA, as well as our mono-branded stores. We have 218 stores in this division and an average space of 88 thousand square meters.

We offer credit and insurance products to the Edcon's customers via our strategic partnerships. Edcon owns a controlling stake in Celrose Proprietary Limited which controls Eddels Proprietary Limited, which are both South African manufacturing businesses. Celrose manufactures apparel whilst Eddels manufactures footwear.

Our Thank U rewards program, which was introduced in 2012, allows customers to earn Thank U points for their purchases in most of our stores which can be redeemed on future purchases.

Our primary operations are in South Africa where Edcon generated 89% of our retail sales in financial year 2017. The rest of our operations are in neighbouring Namibia, Botswana, Lesotho, Swaziland, Mozambique, Ghana, Zimbabwe and Zambia, where we operate 186 retail outlets. Edgars Zimbabwe is managed independently and disclosed as a separate division.

For more information, please visit the Edcon website: www.edcon.co.za