CHAIRMAN’S REPORT

Weakening consumer economy
South Africa’s economic landscape continued to be impacted by instability in the labour market, high levels of unemployment and low productivity, a weakening and volatile currency and rising inflation, with the outlook for domestic economic growth deteriorating as the year progressed.

The growth in the gross domestic product (GDP) for 2014 has been revised downwards to 1.4%. GDP is anticipated to increase to 2.5% in 2015.

The depreciating currency has created inflationary pressures. Inflation, as measured by the increase in the consumer price index, increased to 6.4% in August and is expected to average 6.3% for 2014 before returning to the SA Reserve Bank’s (SARB) 3% – 6% target range in 2015.

After a stable interest rate environment with rates at their lowest levels in more than 40 years, the SARB increased its benchmark interest rate, the repurchase (repo) rate, during the year by a total of 75 basis points to 5.75%.

Increasing interest rates will place further pressure on consumers already facing higher utility, medical and education costs. Fortunately food and fuel price increases have moderated in recent months.

Against this background of a slowing economy, consumer sentiment understandably remained weak, although the Consumer Confidence Index of -1 for the third quarter of 2014 is higher than the same time last year. However, confidence levels are well below the long-term average of +5 for the past 20 years and are not supportive of strong growth in consumer spending.

With limited prospect of any significant improvement in domestic economic conditions to stimulate consumer disposable income, the retail trading environment is likely to remain constrained in the next 12 months.

Sustained financial returns
The focused delivery of the strategy of achieving pre-eminence in health and beauty retailing, and in healthcare supply management has ensured the group continued to generate strong returns to shareholders, with the return on equity at 57.0% remaining the highest in the retail sector.

The group’s diluted headline earnings per share (HEPS) for the period increased by 12.9% to 336.8 cents. The total dividend was increased by 13.1% to 190 cents per share, based on a dividend cover ratio of 1.8 times HEPS.

Diluted HEPS has shown a five-year compound annual growth rate of 15.2%, with dividends per share increasing at a compound rate of 17.7% over the same period.

The group continues to be highly cash-generative. Over the past five years the group generated over R4.3 billion in cash and through its proven capital management strategy has invested R1.3 billion in organic growth and returned R3.2 billion to shareholders in dividends and share buy-backs.

Considering the continued strong cash generation, the board has shown its confidence in the group’s prospects and has resolved to reduce the dividend cover from 1.8 to 1.7 times HEPS from the 2015 interim dividend, which will further enhance returns to our shareholders.

“The group continued to generate strong returns to shareholders, with the return on equity at 57% remaining the highest in the retail sector.”
The excellent all-round performance was recognised when Clicks Group was ranked third in the Financial Mail Top Companies 2014 survey and the highest rated retailer. The ranking is based on a combination of long-term financial performance, return on equity, as well as an assessment of the company’s corporate governance, commitment to empowerment, quality of management and prospects for the company and the sector.

The trading and financial performance for 2014 is covered in the Chief Executive’s Report and in the Chief Financial Officer’s Report.

Healthcare regulation
Healthcare markets are highly regulated across the world and it is critical that the South African regulatory regime advances the national healthcare agenda of making medicine more affordable and more accessible.

However, this is not always the case and management engages with the Department of Health on an ongoing basis to ensure satisfactory resolution of these regulatory issues. Further detail is provided by the chief executive on pages 16 and 17.

Board of directors
The group has a stable board that is well balanced in terms of skills and expertise, and is rich in diversity. Four of the ten directors (40%) are black and three (30%) are female. The independence of the non-executive directors is reviewed annually and all six non-executive directors, including the chairman, are classified as independent in terms of King III and the JSE Listings Requirements. The board elects the chairman after the annual general meeting (AGM) each year.

Keith Warburton, the chief operating officer of the Clicks chain, was appointed as an executive director in February 2014. He previously served as an executive director and chief financial officer of the group until 2011, and rejoined the group in 2013.

Executive remuneration
Long-term executive incentive schemes are aligned with shareholder interests by rewarding executives for the creation of shareholder value. These long-term incentive (LTI) schemes are regularly reviewed and enhanced, with performance hurdles being incorporated into the schemes last year.

Following further engagement with shareholders the LTI scheme for 2014 to 2017 has been revised to strengthen the alignment between executive and long-term investor interests by exposing executives to market volatility. Total shareholder return (TSR) over a three-year period has been introduced in addition to the earnings performance metric included in the other schemes.

The group’s remuneration policy and practices, including the details of incentive schemes, are covered in the Remuneration Report on pages 40 to 45.

In line with the recommendations of King III, the group’s remuneration policy is proposed to shareholders annually for a non-binding advisory vote. The policy was approved by 99.1% of the votes at the AGM in January 2014.

Acknowledgements
The group has delivered a pleasing performance in an increasingly competitive retail environment and on behalf of the board I thank David Kneale and his executive team for their outstanding leadership. My fellow non-executive directors provide valuable insight and guidance and I thank them for their ongoing support.

Thank you to our 8 600 employees across the country who have ensured that the group continues to strengthen its market position. Finally, to all our external stakeholders, including our customers, shareholders, suppliers, industry regulators and business partners, thank you for your continued support.

David Nurek
Independent Non-executive Chairman