CEO's report

This past year will be remembered as a period that irrevocably changed the way we live, work and trade. Shopping behaviours have been altered, and emerging trends are changing the retail landscape.

Ivan Saltzman

New stores opened	Online revenue growth of	Baby City contributed to revenue for two months	Continued to enhance
25	over 260%	R128m	ROIC

These changes and adjustments have become critical for Dis-Chem, not only to ensure continued relevance, but to lessen the impact on the health and wellness of millions of people in South Africa. We have enhanced our focus on aligning management and all operations to a future that takes cognisance of the devastation that the pandemic has brought.

Driven by our values of excellence, customer service, doing the right thing and leveraging our entrepreneurial spirit, the Dis-Chem team responded with urgency and has shown tremendous agility in combating the pandemic and its devastating effects. This has been additionally impressive considering the exceptionally tough current economic environment.

It has necessitated changes in our operating environment which we enthusiastically embraced and used to position the Group for continued success. The Dis-Chem team adapted superbly well and rose to the challenge, ultimately delivering an encouraging set of results.

Financial overview

Despite restricted trading conditions over the past year, we have remained committed to organic and acquisitive growth. We largely maintained our capital investment programme and opened 25 new retail stores in the period. This included 22 new stores and three Mediclinic stores, and we acquired two new pharmacies during the year. The Dis-Chem property footprint now sits at 194 stores. The Group's total capex, incorporating expansion and maintenance expenditures, rose 10.4% to R401 million – which equates to 16 500m^2 of new Dis-Chem floor space – as we strive to maintain the momentum of being the destination of choice for health, beauty and other personal needs.

COVID-19 has, naturally, thrown additional challenges at Dis-Chem.

It is also fortunate that our online strategy was ideally positioned prior to the onset of COVID-19. The investment in online over the past five years has supported increased volumes, resulting in a step change in our online revenue, the growth of which exceeded 260%. This was achieved largely as a result of our key digital platforms being ready and well-suited to serve the stay-at-home and out-of-office trend that has rapidly emerged.

Overall Group revenue was 9.6% up at R26.3 billion, while operating profit rose 1.4% to R1.3 billion. The new stores contributed R491 million to revenue, while Baby City contributed R128 million to revenues in January and February 2021.

CEO's report (continued)

Dis-Chem's retail unit's revenue was 7.6% higher, with its operating profit down on last year at R1.2 billion, which is commendable considering the environment. The wholesale segment's performance continued to improve, reporting a revenue increase of 16.4% to R19.3 billion and an operating profit of R65 million following a loss declared last year. Wholesale revenue to our own retail stores remains the largest contributor to this segments' sales, while external revenue to independent pharmacies and The Local Choice (TLC) franchises grew by 27.7% and 37.1%, respectively, over the corresponding period.

Group expenses were fairly well maintained at R6.6 billion. Our determination to ensure continued employee health, protection and wellness resulted in COVD-19 related costs of R56.7 million, spent largely on vouchers and donations to assist employees, as well as on PPE, screening and testing.

Earnings per share (EPS) and headline earnings per share (HEPS) both increased by 11.8% at 77.8 cents.

Operating environment

With trading restrictions imposed during the different levels of lockdown, the Group was not able to maintain its usual operating hours and selling across all categories. During level 5 of the lockdown period the Group was unable to sell 20% of its products, including higher-margin products from its beauty category.

With the customer being at the centre of everything we do we continued our focus on the Pharmacy First Approach, coupled with consumers' "single shop" patterns in key categories, and we enhanced our strategic intent toward online sales. Consequently, our dispensary market share continued its strong position, despite fewer cold and flu cases than in previous years, and there were market-share gains in most other categories. Trading restrictions did have an impact on the dispensary category, specifically on over-the-counter sales. However, strong chronic drug adherence due to health education, awareness and higher patient risk partially offset the impact across the winter months.

The strength of the Group's financial position has been critically important throughout this time. Various measures taken have ensured that the balance sheet and cash flows of the Group have remained solid, and we have maintained our financial liquidity position. While this has been helped by the lowering of interest rates, our improving efficiencies, focused cost, inventory and working capital management, as well as closer scrutiny of the allocation of capital, have all supported our ability to maintain our strong position. Cash generated from operating activities amounted to R1.1 billion, while cash and cash equivalents were R136 million, compared to R300 million last year.

With trade restrictions top of mind, Dis-Chem's management did not waiver in terms of the Group's continued ambition of enhancing our return on invested capital, which we believe will position us well given today's fast-changing trading patterns. This has meant, for example, understanding consumers' demands for a changing product portfolio and assessing the transaction mix to maintain margin, which included growing private-label products. Higher trade terms from suppliers were encouraged and resulted in a deeper penetration into the supplier base together with higher fees for rebates. Importantly, the rationalisation of stock and improving buying efficiencies became critical and were successfully optimised through the use of demand forecasting and inventory management.

Innovation, technology and digital improvements were essential in this regard and it is comforting that these systems have been enhanced to a degree where this will remain beneficial to the Group in the years to come. We intend to capitalise on these and other essential working capital components for future growth.

The growth in our clinics, together with our telemedicine offering, will play an important role in our delivery and growth. We now have nearly 11 million customer profiles on our loyalty programme, of which some six million are benefit members who contribute around 70% of "front shop" revenue. This is a remarkable achievement and has been accomplished in a relatively short space of time using technology-driven platforms such as a recently introduced app.

We firmly believe that the urgent restoration of economic activity will only materialise when the vaccination has been safely and successfully implemented across the entire population in South Africa. Dis-Chem is therefore working closely with all industry and business stakeholders to do whatever we can, and offering the use of our facilities as vaccination sites and all other relevant resources, to ensure this objective is achieved. Our commitment to partnering with government and the industry to fight the COVID-19 pandemic will remain steadfast.

CEO's report (continued)

Strategic growth by acquisition

Our strong organic growth is being complemented by key strategic acquisitions, in which we have invested R1 billion over the last year. Whenever we assess an acquisition we ensure that there is an ability to integrate it vertically, ultimately to the benefit of customers and financial returns.

Baby City: We acquired 100% of Baby City, the specialist destination baby retailer, on 1 January 2021 for R422 million. The transition into the Dis-Chem Group has been smooth and we are starting to see the intended benefits and synergies emerging. All Baby City stores have completed the migration onto the Group's common technology platform.

Healthforce: On 1 March 2021 we acquired Healthforce, which has been introduced to the Group's 336 clinic rooms. Healthforce is now our single technology platform that we use to facilitate all nurse-led consultations. Over the three months since migration we have facilitated 180 000 nurse-led consultations within Dis-Chem's clinics. Healthforce offers clinic management software that, amongst other system capabilities, sets up clinic nurses as the low-cost entry point into the healthcare system. The technology includes a telemedicine platform that provides real-time video connections between patients and nurses and an on-demand remote doctor network. Dis-Chem intends to be at the forefront of innovation in the delivery of care, and we see this investment as an important step through which we can advance this ambition.

Medicare: The purchase consideration of R282 million for 100% of Medicare is still subject to competition authority approval. Medicare is a healthcare and pharmacy group operating 50 pharmacies across four provinces. Many of the stores in the Medicare portfolio are located in convenience centres, in geographies where Dis-Chem is currently under-represented, giving the Group access to new markets. For the year ended 28 February 2021, Medicare generated revenue of R1.1 billion, with dispensaries contributing approximately two-thirds.

Kaelo: We have entered into agreements to acquire 25% of the equity of Kaelo for a purchase consideration of up to R195 million, subject to company performance hurdles. Kaelo houses a complementary portfolio of health assets, including benefit-rich gap and primary health insurance products, occupational health clinics, and the AskNelson psychological well-being platform. The transaction was recently filed with the Competition Authorities.

Dividend reinstated

With indications of normalised trading patterns, it is pleasing that we have been able to reinstate dividends, subsequent to year-end, a dividend of 31.1 cents per share was declared on 20 May 2021 and paid on 14 June 2021.

Outlook and appreciation

While there are early indications of a return to acceptable trading activity and improved transactional gross margins as consumer shopping patterns normalise, we fully expect that the third, and any subsequent, waves of COVID-19 infections will continue to put pressure on the economy and consumers. This makes the forecasting of financial and operating results difficult, and we are continuing to monitor this carefully.

We will not reduce our commitment to ensuring the health and wellness of our nearly 19 000 Dis-Chem team members. We are being vigilant in the fight against the pandemic, and we are acutely aware that our employees are at the front line of this battle.

The Group has secured 17 additional Dis-Chem stores, and four new Baby City stores, scheduled to be opened in 2021, which will contribute to revenue and profitability within the retail segment. Wholesale profitability will continue to be driven by operational efficiencies and increased support from TLC franchises and independent pharmacies.

This past year has tested our strategic resolve and operating model. It is very encouraging that the end result has proven that our strategy is intact, that it remains solid and has the agility to adapt to changing market circumstances. This has given us the confidence to continue along the strategic trajectory that we established over recent years, and in some areas to accelerate where we can extract enhancements to our overall offering. The ability to stay the course and deliver a good end result would not have been possible without the core team of people that make up the Dis-Chem Group.

I remain extremely grateful to all our people for their unrelenting support, contribution and efforts to ensuring that our Group remains relevant to our vast, and growing, stakeholder base. We could not have done this without you.

My appreciation must also be directed toward my fellow Board members, from whom I have received tremendous guidance and support. Rest assured, we remain well positioned to see through this period, and emerge stronger and better.

Ivan Saltzman