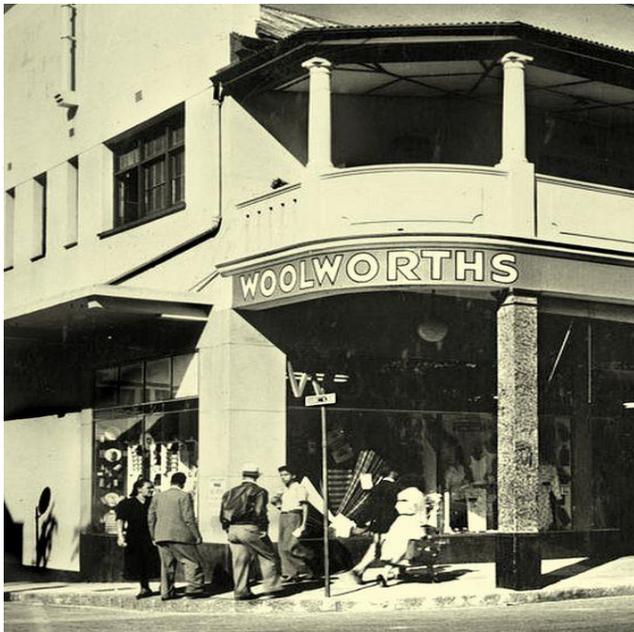


This Quarter, we will look back on the company South Africans fondly refer to as Woolies, specifically the food division.

Where it all began

In 1931, in the midst of one of the world's worst financial crises, Woolworths's founder Max Sonnenberg opened the first store in Plein Street Cape Town, in the dining room of the recently closed down Royal Hotel. Three years later, a second branch opened in Durban, with another two in Port Elizabeth and Johannesburg a year later.

Figure 1: Woolworth Plein Street Cape Town



The first Woolworths store sold a wide range of products such as haberdashery, jewellery and tools. Customers couldn't walk around the shop and browse but were rather assisted from behind the counters. Sonnenberg believed that success lay in providing a quality product at reasonable prices, this initial strategy has led Woolworths to be the company it is today.

Figure 2: Woolworth Plein Street Cape Town



Woolworths Holdings Limited listed on the JSE in 1997 and is now one of the top 40 JSE-listed companies.

Today, the Woolworths Group has 3 main divisions: Woolworths SA, David Jones and Country Road. The South African Woolworths business consists of full-line fashion, home and beauty stores, many of which also incorporate a premium food retail offering. Stand-alone food stores and "Food Stops" attached to Engen petrol stations are also located in urban areas.

Woolworths operates 218 full line stores and 430 stand-alone food stores in South Africa, with an additional 64 stores throughout the rest of Africa.

Food Business – A cut above the rest

Differentiators such as health, wellbeing, innovation, and sustainable sourcing make Woolworths's food products superior to that of other food retailers. Their ability to ensure the freshness and quality of their products through excellent supply chain management is a clear and sustainable competitive advantage.

Innovation started early, in 1974 Woolworths became the first South African retailer to introduce “sell by” dates on food packaging. They were also the first retailer to offer pre-washed lettuce and machine washable wool. If you took a visit to their head office in Cape Town, you would find their innovation kitchen where chefs explore different recipes and come up with new ideas whilst at the same time making sure the quality of the food is at the highest standard. Innovation is on a different level to its competitors, inspiring to be a supermarket with the soul of a deli.

THE DIFFERENCE THAT **INSPIRES** **AND CARES**

Another one of Woolies key values is to be ‘customer obsessed’ and this shows in their customer service and the meticulous detail given to each store layout. The stores are designed with the purpose of giving the customer a truly first-rate shopping experience.

Woolworths then took convenience to a new level, being the first major South African retailer to make its products available in the 24-hour convenience retail market. By 2009, there were over 40 Woolworths Food Stops in Engen garages around the country.

Leading the way in the ESG

With a vision to be one of the worlds most responsible retailers, Woolworths launched the Good Business Journey in 2007. A sustainability roadmap without equal. It consists of eight focus areas: people and transformation, social development, health and wellness, ethical sourcing, sustainable farming, waste, water, as well as energy and climate change. These are all key drivers in value creation.

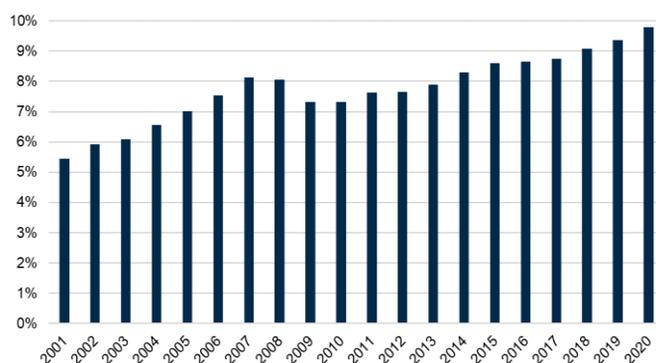


Some health and wellness initiatives that really stand out is that they were one of the first retailers to remove artificial additives and preservatives as far as possible from their food. Tartrazine and MSG are no longer used in Woolies branded food products and in 2009 Woolworths became the first South African retailer to remove artificial sweeteners such as aspartame. Ayrshire dairy products is guaranteed free of added rBST growth hormones. In 2008 Woolworths became the first South African retailer to sign the Southern African Sustainable Seafood Initiative’s Retail Charter.

The Groups Cash Cow

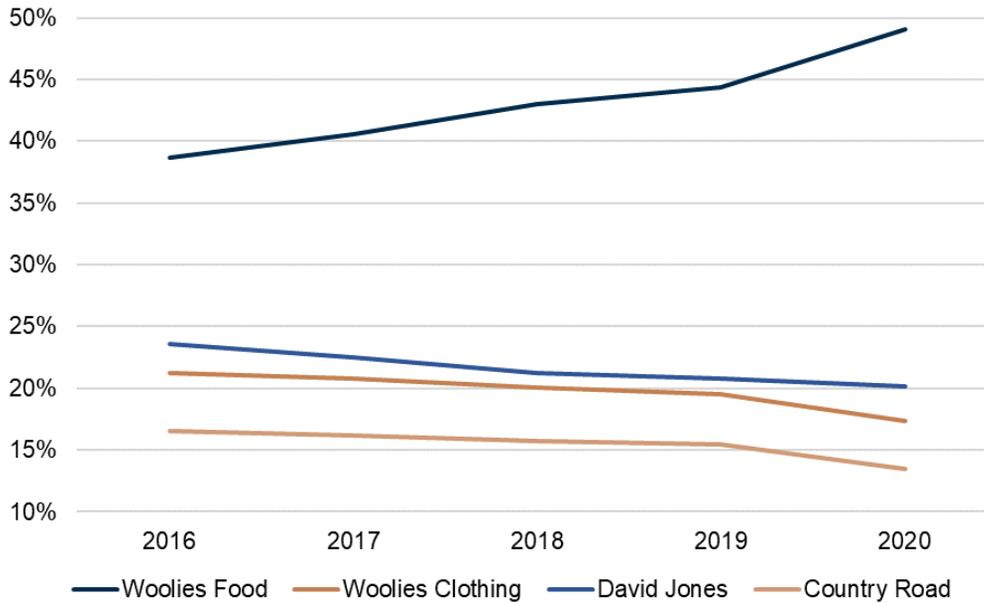
A decision in 2014 to purchase businesses in Australia, predominately David Jones has disrupted the investment case. The Woolworths food division has held the fort while resources have been bleeding into David Jones. The South Africa business far exceeds its cost of capital and the food division continues to gain market share.

Figure 3: Woolies Food Sales by market share



Source: Morgan Stanley

Figure 4: Group Revenue Contribution



Source: Morgan Stanley

Competitors, such as Checkers are starting to dip their toes into the premium food retail space, however Woolies competitive advantage will be very tough to replicate.

It is back to the races for Woolworths Holdings Limited. Management is actively correcting past weaknesses. The Australia investment was as disaster and there are now strong indicators that the problem is being addressed. The group has elected a new CEO, Roy Bagattini, who is taking action by essentially ring fencing the Australia businesses. With more focus on fixing the Australian component, we expect Group returns will improve meaningfully.