Woolworths in R7bn David Jones setback

By Nick Hedley

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Woolworths said on Wednesday it had impaired the value of Australian department store chain David Jones by nearly R7bn, or about a 10th of the South African retailer's total market capitalisation.

Image credit: ABC News

Woolworths announced a noncash impairment charge for David Jones of A712.5m (R6.9bn) after the JSE's close, which reflected "the cyclical downturn and structural changes" affecting Australia's retail sector.

The group also conceded to "poor or delayed execution" on some key initiatives and said it would continue to invest in the business, which it bought for R23.3bn in 2014.

Analysts said that having written down nearly a third of that amount, Woolworths clearly overpaid for the business. Just One Lap founder Simon Brown - a now "grumpy" Woolworths shareholder - said the impairment was "terrifying but not a surprise".

"They had warned of a writedown but that write-down looks quite chunky to me. I hadn't expected quite so much." Accounting for it as a noncash entry "is true but misses the point because of course it's cash when they bought it".

Brown said that while David Jones had initially appeared to be "a fairly good deal" for Woolworths, he was starting to loathe large mergers and acquisitions. "I'm also a Famous Brands shareholder and I'm just getting tired of all these big deals unravelling."

Famous Brands said in late 2017 that its Gourmet Burger Kitchen acquisition - the biggest deal under former CEO Kevin Hedderwick - had soured.

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South African companies had been too aggressive in their offshore strategies, having overpaid for assets, particularly listed targets. "Department stores in Australia have been struggling," Damon Buss, equity analyst at Electus Fund Managers, said.

"Myer, David Jones's competitor in the Aussie department store market, continues to battle, they're not having any success with their turnaround."

Except in the UK, department stores around the world were struggling because of competition from online retailers, such as Amazon, and the fact that consumers no longer had time to browse through multistorey stores, Buss said.

"You had Amazon entering Australia at the end of 2017, so it's still relatively new there and I think that will put a lot of pressure on."

But Buss said department stores in the UK had adapted by establishing strong online sales platforms and there was still potential for a turnaround at David Jones.

"David Jones was in quite a mess when Woolies bought it. They didn't have operating systems, stock planning systems, they didn't know what was being sold or what they had in their warehouses or stores," he said.

Now that David Jones was implementing systems like Woolworths's in SA, "I think they can improve the business significantly, but it is going to take quite a long time."

Momentum analyst Nesi Chetty said that Australian department stores had been struggling and retail sales in general had been hampered by tepid wage growth.

However, grocery sales remained resilient and "typically companies that have a higher food offering do much better than clothing, footwear and textiles".

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Chetty expects a strategy shift at David Jones, whereby the company would incorporate more grocery products in its stores, similar to the Woolworths model.

"I think the Australian market will remain very competitive, what you're finding is that discount retail tends to work quite well there, players like Aldi. Everyone is looking for relative value and discounting is quite large, and David Jones hasn't played in that space," Chetty said.

Woolworths said its headline earnings per share for the 26 weeks to 24 December were expected to drop between 12.5% and 17.5%. Its share price closed 2% down at R65.67.

Source: Business Day