



# FINANCIAL CAPITAL

TURNOVER

**R26 809m**

2016: R24 171m  
2015: R22 070m

HEADLINE EARNINGS

**R1 269m**

2016: R1 099m  
2015: R960m

GROSS PROFIT  
MARGIN

**21.0%**

2016: 20.7%  
2015: 20.5%

OPERATING PROFIT  
MARGIN

**6.8%**

2016: 6.5%  
2015: 6.3%

COMPARABLE STORES TURNOVER GROWTH

**8.0%**

2016: 9.8%  
2015: 7.5%



# FINANCIAL CAPITAL

**The increase in turnover of 10.9% and 15.4% increase in operating profit underscores the overall economic health of the group. Our operating margin increased to 6.8%, benefiting from stronger retail growth.**

## CREATING VALUE THROUGH GOOD GOVERNANCE

### Corporate governance philosophy

Our robust governance and compliance framework is grounded in the principles of accountability, transparency, ethical management and fairness, and we live by the philosophy of sound governance.

### Role of the board

The directors are accountable for the sustainability of the business and they are responsible to the stakeholders of the company who elect them. The role of the board includes the accountability, responsibility and assigning of performance through:

- approving strategic plans;
- monitoring operational performance;
- ensuring effective risk management and internal controls; and
- monitoring legislative, regulatory and governance compliance.

The board must also approve significant accounting policies and the annual financial statements, monitor transformation and empowerment, manage director selection and appointment, and ensure the group has effective remuneration policies and practices. Certain of these functions are delegated to board committees. The board charter details the authority, responsibility, composition and functioning of the board.

### Independence of directors

All six non-executive directors are classified as being independent in terms of King III. This was confirmed in the 2017 internal evaluation of the status of the non-executive directors, which included an assessment of the chairman, David Nurek, who has served as a non-executive director for 21 years.

There are no shareholder interests represented on the board, further confirming its independence.

### Board diversity

Our directors reflect a diversity of gender, race and professional backgrounds, encouraging rigorous debate and ensuring that the board considers a plethora of stakeholder interests. With the board of directors consisting of 44% black directors for racial diversity and 44% female directors for gender diversity.

### Director election

Regular election of directors gives effect to the right of shareholders to appoint directors they believe will add value to the company. One-third of the non-executive directors are required to retire at the AGM each year. Executive directors retire on the third-year anniversary of their appointment or most recent re-election to the board.

### Annual performance evaluation

Each year the performance of the board, the chairman, the chief executive officer, individual directors and all board committees is evaluated by the directors to maintain the highest standards of good governance.

In the 2017 evaluation the board and its committees were found to have discharged their responsibilities adequately. The directors believe the board contributes to value creation in the company, is well balanced and has the relevant knowledge to make a meaningful contribution to the group's affairs.

Any of the non-executive directors has access to external legal consultants when necessary.

### Board and executive relationship

The roles of the chairman and chief executive are separate and clearly defined, ensuring that no director has unrestricted decision-making powers. The chairman, David Nurek, leads the board and the chief executive, David Kneale, is responsible for the executive management of the group.

The board and executive management work closely together to chart the strategic objectives of the group. Authority has been delegated by the board to the chief executive and the group executive committee for the execution of the strategy and management of the business.



### Board oversight

Specialised governance functions are delegated to three committees to help the board meet its oversight responsibilities. All board committees are chaired by independent non-executive directors and the composition of the committees conforms to the requirements of King III. With the introduction of King IV the composition of the social and ethics committee has been amended to meet the requirements of the code.



These committees are as follows:

- audit and risk committee;
- remuneration and nominations committee; and
- social and ethics committee.

Detailed disclosure on the roles and functioning of the committees is included in the corporate governance report on the website.

### King III and King IV application

The group has applied King III during 2017. King IV is effective for the 2018 financial year. Certain elements of King IV have already been adopted by the group and reporting for the 2017 financial year is in accordance with King IV.

### Ethics and values

At Clicks, we hold ourselves to the highest ethical standards of business practice. Our staff are expected to show integrity, mutual respect and openness and we have a set of values and a behavioural code of conduct to make this clear. What's more, our staff have the right and obligation to challenge anyone not keeping to these values. All employees must follow ethical business practices in their relationships with colleagues, suppliers, intermediaries, shareholders and investors. We have also set stringent standards on accepting gifts from third parties and declarations of potential conflicts of interest.

All new employees sign the code of conduct of the group and an overview of the code forms part of their introduction to the company. The Gift Declaration Policy is available on the internal intranet for employees to remind themselves of its contents at any stage.

Clicks does not tolerate fraud and our policy is to prosecute offenders. The internal forensic unit evaluates and manages the legal processes to ensure the highest

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possible level of recovery for the group arising from any fraudulent behaviour, which is then discussed in the audit and risk committee.

We care about the communities we serve and we've adopted the principles of the UN Global Compact and follow the guidance by the International Labour Organisation and the Organisation for Economic Co-operation and Development (OECD), which promote policies in support of the economic and social well-being of people around the world.

The group reviews these principles in the social and ethics committee, as can be viewed on the website.

### Legislative and regulatory compliance

Legislative and regulatory compliance is monitored by the head: group legal and the compliance officer.

To stay abreast of developments an analysis of current and pending legislation and regulation is presented at each meeting of the board, the audit and risk committee, and the social and ethics committee. Further information is provided in the corporate governance report on the website.

### Privacy and data security

We respect the privacy of our stakeholders, customers and employees, and always obtain the consent of anyone providing personal information to the business. The form to be completed when providing such information gives the option to be excluded from marketing from the group, providing information to third parties, indicates the reason if third parties will have access to individual data and gives contact details for individuals to update this information.

Access to personal information is limited to the employees of companies that undergo regular compliance auditing to make sure they stay within the boundaries set by Clicks. No personal information is sold or provided to any external party, except when the data is analysed for the group. All individuals have the authority to delete their data from the system and personal information is deleted automatically after a period of inactivity by the individual.



### Tip-offs Anonymous

We give employees the tools to report suspected fraudulent or unethical behaviour without fear of retribution via a toll-free telephone service managed by an external service provider. All reported incidents are investigated. We keep our staff aware of this facility through presentations, a quarterly newsletter and competitions, and by encouraging employees to report incidents before there are significant losses.

	2017	2016	2015
Tip-Offs reported	<b>263</b>	186	136
Direct reports received	<b>120</b>	160	175
Resultant dismissals/resignations	<b>191</b>	207	140
Employees counselled	<b>31</b>	39	14
Other disciplinary action	<b>83</b>	107	80

### Political party donations

While the group supports freedom of association in South Africa, our Code of Conduct does not endorse donations to individual political parties.

### Anti-competitive conduct

Our customers come first and that means we don't do anything that limits competition or that could adversely affect our customers.

All group executives and employees are expected to understand the requirements of competition law and regulations, and our directors are committed to making sure they do. We have robust risk management and supervisory oversight processes to ensure adherence to these laws and regulations. A Competition Act compliance process is carried out every year.

The group occupies a market-leading position in healthcare retailing and supply in South Africa and guards the confidentiality of intellectual property, customer and supplier data, business processes and methodologies.

Effective governance processes have ensured that the group has not been sanctioned for anti-competitive practices or non-compliance with the Competition Act during the year.

### Trade union

Collective salary increases are negotiated with the representative trade union for the Clicks bargaining unit. The negotiation team is headed by the Clicks head of human resources, who reports to the chief operating officer – a member of the executive committee. Trade union membership stands at 18.1% of the total group employees (2016: 17.9%)



## 16 PEACE, JUSTICE AND STRONG INSTITUTIONS



### SUSTAINABLE DEVELOPMENT GOAL

The Clicks Group supports the goals set in the UN's 16th SDG, namely peace, justice and strong institutions, through the above-mentioned governance practices. These are woven into the operations of the business at all levels. The group has a governance report available for further reference, if needed.



## STAKEHOLDER ENGAGEMENT

Clicks Group's stakeholder engagement process focuses mainly on the five primary stakeholders that management believes are the most likely to influence the ability to create sustainable shareholder value. Proactive and transparent relationships with these stakeholders enable the group to identify and address issues, opportunities and risks. Performance indicators have been developed for each primary stakeholder group to determine the quality of the engagement and relationship.

Rationale for engaging	Engagement issues	Outcome of engagement
<b>Customers</b>		
<ul style="list-style-type: none"> <li>■ Meet customer needs by providing products and services</li> <li>■ Create trust in products and pharmacy practices</li> <li>■ Customer loyalty and retention</li> <li>■ Grow market share</li> </ul>	<ul style="list-style-type: none"> <li>■ Product range in store and online</li> <li>■ Service levels</li> <li>■ Price competitiveness</li> <li>■ Pharmacy and clinic services</li> <li>■ ClubCard benefits</li> </ul>	<p>Clicks:</p> <ul style="list-style-type: none"> <li>■ 622 stores</li> <li>■ 473 pharmacies</li> <li>■ 45% of households live within 5 km of a Clicks store</li> <li>■ ClubCard active membership increased to 7.0 million (2016: 6.2 million) and accounts for over 77% of sales (2016: 77%)</li> <li>■ Clicks app launched in 2017</li> <li>■ Online shopping available in South Africa</li> <li>■ Market share gains in all categories</li> <li>■ Clicks independently rated by customers as first for price and value in health and beauty retailing</li> </ul> <p>UPD:</p> <ul style="list-style-type: none"> <li>■ Five distribution centres in South Africa and one in Botswana</li> <li>■ Servicing over 2 000 corporate and independent pharmacies</li> <li>■ 96.1% order fulfilment to customers (2016: 96.0%)</li> </ul>
<b>Shareholders and lending institutions</b>		
<ul style="list-style-type: none"> <li>■ Facilitate access to capital by attracting investors</li> <li>■ Facilitate attractive debt funding facilities from financial institutions</li> <li>■ Better informed investor community</li> <li>■ Balanced analysis of company</li> <li>■ Fair market rating relative to peers</li> </ul>	<ul style="list-style-type: none"> <li>■ Group strategy</li> <li>■ Current trading environment</li> <li>■ Trading and financial performance</li> <li>■ Store and pharmacy expansion plans</li> <li>■ Regulatory environment</li> <li>■ Capital management</li> <li>■ Prospects</li> </ul>	<ul style="list-style-type: none"> <li>■ Return on equity 44.1%</li> <li>■ Total shareholder return 25.2%</li> <li>■ Engagement issues addressed in annual and interim results presentations and webcasts, local and international investor roadshows, Integrated Report and annual financial statements.</li> <li>■ Met with 222 local and international funds and brokerages (2016: 219)</li> <li>■ Research coverage by 12 brokerages (2016: 11)</li> <li>■ 82.9% of shares traded (2016: 90.3%)</li> <li>■ International share ownership 66.1% (2016: 68.6%)</li> <li>■ Access to adequate group funding and trade finance facilities</li> </ul>



Rationale for engaging	Engagement issues	Outcome of engagement
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<b>Employees</b>		
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<ul style="list-style-type: none"> <li>■ Attract, motivate and retain talent</li> <li>■ Increase productivity</li> <li>■ Engender loyalty</li> <li>■ Accelerate transformation</li> </ul>	<ul style="list-style-type: none"> <li>■ Remuneration and benefits</li> <li>■ Performance management</li> <li>■ Personal development</li> <li>■ Career path planning</li> <li>■ Training and skills development</li> <li>■ Employee share ownership plan (ESOP)</li> </ul>	<ul style="list-style-type: none"> <li>■ Full-time staff turnover 15.9% (2016: 17.0%)</li> <li>■ Employment equity                             <ul style="list-style-type: none"> <li>– Black staff 91% of total staff (2016: 91%)</li> <li>– Female staff 63% of total staff (2016: 62%)</li> </ul> </li> <li>■ Training and skills development spend R125.8 million (2016: R95.7 million)</li> <li>■ 539 learners through Pharmacy Healthcare Academy (2016: 423)</li> <li>■ 64 pharmacy interns engaged (2016: 83)</li> <li>■ Fair and responsible remuneration for role performed based on external benchmarks</li> <li>■ 5 882 employees are shareholders through the broad-based ESOP</li> </ul>
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<b>Government and industry regulators</b>		
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<ul style="list-style-type: none"> <li>■ Legislative and regulatory compliance</li> <li>■ Lobby for regulatory reform and fair legislation which will improve access to affordable medicines</li> <li>■ Best-practice governance standards</li> </ul>	<ul style="list-style-type: none"> <li>■ Pharmacy licences</li> <li>■ Registration of medicines</li> <li>■ Complementary and alternative medicines</li> </ul>	<ul style="list-style-type: none"> <li>■ Ongoing engagement with regulators</li> <li>■ Insight into regulatory framework</li> <li>■ Formal submissions made in response to draft regulations</li> </ul>
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<b>Suppliers</b>		
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<ul style="list-style-type: none"> <li>■ Ensure stable supply of merchandise</li> <li>■ Quality standards maintained</li> <li>■ Understand market movement and new product launches that may change buying patterns</li> <li>■ Brand exclusivity</li> </ul>	<ul style="list-style-type: none"> <li>■ Quality and safety standards</li> <li>■ Product availability and exclusivity</li> <li>■ Product innovation, strength of brands</li> <li>■ Private label products</li> <li>■ Transformation and BBBEE scorecards</li> <li>■ Legislative compliance</li> </ul>	<ul style="list-style-type: none"> <li>■ Supplier infill levels                             <ul style="list-style-type: none"> <li>– Clicks 85.2% (2016: 83.8%)</li> <li>– UPD 96.1% (2016: 96.0%)</li> </ul> </li> <li>■ 72.8% (2016: 75.8%) spend on BBBEE empowered suppliers</li> <li>■ Consistent supply and maintenance of franchise agreements with The Body Shop International, GNC and Claire's</li> </ul>
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# 1 TRADING ENVIRONMENT

### WHY MATERIAL?

Economic conditions, political uncertainty, sovereign credit rating downgrades and the resultant negative consumer sentiment are impacting South Africa's already constrained retail trading environment. Consumer disposable income is being further eroded by higher health insurance costs, increased tax rates, rising energy and general living costs.

### RISKS

- Further deterioration in the economic environment will depress consumer spending which is already under severe pressure.
- Criminal activity, including syndicated crime, escalates during times of economic hardship.

### OPPORTUNITIES

- Clicks will continue to pursue a strategy to improve price competitiveness, grow sales volumes and entrench Clicks as a value retailer.
- Focus on differentiators, including extensive and convenient store and pharmacy network; private label and exclusive ranges; Clicks ClubCard loyalty and consistently high levels of customer care.

# 2 COMPETITION

### WHY MATERIAL?

Clicks faces competition on several fronts, including national food retailers and general merchandise chains, and other pharmacy businesses.

### RISKS

- Expansion by corporate pharmacy and retail chains impacting on market share growth in Clicks.
- Increasing price competitiveness of retailers could negatively affect sales and profitability in Clicks.

### OPPORTUNITIES

- Clicks has an extensive store network and plans to open 25 to 30 new stores each year, expanding to 900 stores in the long term.
- Continued expansion of the pharmacy network with the long-term plan to open pharmacies in all Clicks stores in South Africa.
- Continued recruitment of new members to the Clicks ClubCard.
- Ongoing improvements in pricing, product offer and customer service.

“The needs, expectations and concerns of stakeholders that influence our ability to create sustainable value are central to identifying the material issues.”

# 3 REGULATION

## WHY MATERIAL?

Healthcare markets are highly regulated across the world and approximately 50% of the group's turnover is in regulated pharmaceutical products. The group supports regulation that advances the government's healthcare agenda of making medicines more affordable and more accessible but opposes regulation which inhibits access to affordable healthcare and limits customer choice.

## RISKS

- Legislative and regulatory changes introduced by the Department of Health (DoH), SA Pharmacy Council (SAPC) and SA Health Products Regulatory Agency (SAHPRA, formerly the Medicines Control Council) could impact on Clicks' and UPD's turnover and margins.
- Impacts include the ability to obtain pharmacy licences and to launch private label and exclusive scheduled and complementary medicines.

## OPPORTUNITIES

- Ensure Clicks and UPD are operating efficiently to maintain margins and profitability.
- Continue management engagement with the DoH, SAPC and SAHPRA on legislation and regulation.
- Formal written and oral submissions to DoH, SAPC and SAHPRA in response to draft legislation or regulations.
- As the market leaders in retail pharmacy and pharmaceutical wholesaling, position Clicks and UPD to benefit from market consolidation arising from changes in legislation and regulation.

# 4 INFORMATION TECHNOLOGY

## WHY MATERIAL?

Real-time, uninterrupted IT systems are essential in today's technology-driven business environment while robust IT security and governance processes are required to limit breaches of customer privacy and loss of data to avoid legal liability and reputational damage.

## RISKS

- Confidential customer or sensitive internal data could be compromised as a result of an undetected data security breach or cyberattack.
- IT systems and architecture no longer appropriate in an environment of ever-increasing scale and requirement for real-time IT systems.
- Inability to restore business operations and IT systems in the event of a disaster.

## OPPORTUNITIES

- Improved information security practices and compliance as a result of increased online presence.
- Planned implementation of a new IT platform roadmap with improved system efficiencies and cost savings that supports the organic growth strategy.

# 5 PEOPLE

## WHY MATERIAL?

Retail and healthcare skills are scarce and in high demand locally and internationally. Attracting and retaining talent is therefore critical to the group's continued success. As the largest employer of pharmacy staff in the private sector in South Africa the group is actively building capacity to address the critical shortage of pharmacists which is a challenge the world over.

## RISK

- Inability to recruit, attract and retain talent for core business needs, including merchandise and planning, store management and pharmacy.

## OPPORTUNITIES

- Salaries and incentives externally benchmarked to ensure the group remains competitive.
- Group resourcing function established, including specialist pharmacy team.
- Bursary and internship programmes to attract pharmacy graduates.
- Retail graduate programme offered.
- Accredited training programmes for store management, key store roles, and merchandise and planning being developed.
- Senior leadership development programme strengthens pool of management talent and provides succession plan.