

Australian Pharmaceutical Industries Limited
2012 Annual General Meeting
Tuesday, 22 January 2013

Address by Stephen Roche, CEO & Managing Director

Good afternoon ladies and gentlemen – I hope you enjoyed the short video.

I'd like to highlight some of the operational achievements of the 2012 financial year and then touch on some of the key environmental factors that are with us now and will impact us for the foreseeable future.

From there, I'll recap our strategic priorities and detail some of the activity we are planning to deliver.

As the Chairman has noted, we:

- Grew Soul Pattinson, Pharmacist Advice and Club Premium membership to 690 stores
- Maintained leadership in retail pharmacy distribution
- Took action to mitigate the impact of continued PBS Reform
- Continued strong progress in New Zealand, aided by Blackmores and the Cancer Society of New Zealand
- Recommissioned our Queensland distribution centre following the disastrous floods

Priceline continued to outperform the sector, and with the launch of our online business and a return to significant growth in our bricks and mortar store network, it is clear that Priceline Pharmacy is the future growth engine of our business.

Of course, given that Priceline Pharmacy is a franchise business, it is crucial that we deliver for our franchisees, our pharmacists. So significantly outperforming the norm in the Australian franchise sector was an important achievement. As was the continued expansion of our Sister Club program which delivers our pharmacists an unrivalled loyalty program.

I think it is worthwhile recapping why we've pinned our future on the health and beauty market and, in particular, our focus on women.

This Australian Bureau of Statistics data shows very clearly that pharmaceutical, cosmetics and toiletries have far outperformed other retail sectors over the last five years. And, as you'll note, even though we're no longer seeing the double digit growth we enjoyed before the impact of the GFC, we're nonetheless experiencing growth that remains healthier than other retail sectors.

The key demographic trends also remain in our favour, with our older consumers, having more disposable income than those from previous generations and their life expectancy is also greater.

Hence their increasing spend on health-related products, particularly on prescription medicines, where we see 70 per cent of scripts are for our population over 60 years of age. And not only do women care more about how they look, they're typically much more careful than men about their physical health, so they live longer.

Our ageing population has resulted in approximately \$10 billion being spent by those over the age of 65, even though they account for only 13 per cent of the population. This graph is a very good illustration of the seismic shift in the demographics of our country. If you look at the early 1970s, we were experiencing growth of around ten or twenty thousand in the number of people over the age of 65. Since 2010 we've seen annual increases in that age group of over 100,000 per annum and we'll see increases of circa 120,000 every year between now and 2030.

API has evolved its business to take advantage of these economic and social trends. Priceline Pharmacy's strategy is unashamedly geared to women and we have a significant focus on health, recognising the demands of the older members of our country and local communities.

But we are not blind to the impact of PBS reform on health spending. Our front-of-shop offering has strengthened considerably in the last five years and we offer one of the best ranges of quality, value for money beauty products of any retailer in Australia. Having that strong front-of-shop offering is one of the primary reasons we've seen such a strong resurgence of interest from independent pharmacists looking to become Priceline franchisees.

So I hope that background helps explain our strategic priorities, which are:

- become the dominant mass market health and beauty retailer in Australia;
- extend our leadership in pharmacy distribution; and,
- ensure we're doing the necessary internal work and influencing our external environment to facilitate our growth plans.

And a little later in this presentation I'll explain why our strategic imperatives have major synergistic benefits.

I'll now detail the key activity that underpins these three strategic pillars.

Last financial year we reported we'd grown our Priceline Pharmacy network by 20 stores. Our franchisee pharmacists support our strategy. They recognise it as a real solution to cope with the negative impacts of PBS reform. And they recognise that our focus on making the pharmacist the champion while expanding our strength in beauty is a winning combination.

Underpinning that focus has been our commitment to deliver what Australian women want and they reap the rewards accordingly. We now have 3.9 million members in the Priceline Sister Club program whose average spend is 50 per cent higher than non-Sister Club customers.

Our Priceline Sisterhood community program has increased our bond with our Sister Club members. We've raised over a half million dollars in the last 18 months to support the charities that matter most to women, Alzheimer's Australia, PANDA (Post Ante Natal Depression Association), the Cervical Cancer Institute, Victor Chang Heart Research Foundation, Look Good...Feel Better and Moira Kelly's Children First charity.

And we've increased our marketing penetration via social media which has resulted in greater consumer engagement.

In the year ahead we will deliver further growth in our Priceline Pharmacy store numbers, at least on a par with last year. We'll focus our Sister Club activity on increasing the activity of our 3.9 million members because we know that's the most cost-effective way to grow sales. We're learning quickly from our online shopping offering and, in my view, will continue to learn and adapt for some time.

And we're Going Pink in 2013. You'll see our strength in beauty increasingly matched by our health offering. You'll see it through our partnership with Ita Buttrose who has a clear commitment to improving women's health.

We'll have a challenge to maintain the exceptional scores we achieved last year in our franchisee satisfaction survey. We're investing in best practice research to help improve our franchisee pharmacists' bottom line.

So that's the plan going forward, our strength in beauty increasingly matched by the marketing of our health offering. Priceline Pharmacy's unique national offering of health **and** beauty will be clear to both franchisees and customers.

Our second strategic pillar, where we are the leader in retail pharmacy distribution, saw us strengthen that position in 2012. We continue to take a leadership role in managing PBS reform and have completed our investment in Supply Chain, having now recommissioned our Queensland Distribution Centre at Bundamba following its damage in the Queensland floods. We will also leverage our expertise from our New Zealand business in the manufacture of our proprietary range of over the counter cough colds, analgesics and body washes by integrating them in our Australian offers.

In the coming year, we must protect our margins following the continuous nature of PBS Reform. We have previously and will continue to work with our customers to ameliorate the impact – but there are only two levers to pull; reduce our operational costs or reduce discounts. We have been consistent in stating that we would review the impact annually and as a consequence will do so again in April this year.

We will also build on our strategic partnership agreement with Alphapharm which I'm delighted to say we've extended for another three years.

And we'll continue to develop our relationship with pharmacists with a view to increasing the flexibility and range of choice we offer both our Soul Pattison and Pharmacist Advice banner customers and independent pharmacists through our Club Premium offering.

To ensure our enablers for future growth are in place, we have in our Sister Club program a key marketing advantage over all our direct competitors. No-one in our sector has a program that is remotely comparable. But we've only beginning to realise its true potential. We can increase the activity of our existing members and mine the wealth of information we've garnered through our data collection and add to that the insights that we're deriving from our online store experience.

This combination will help us keep pace with the changing demands of our customers and we'll continue to drive productivity through our distribution network.

I am determined that wholesalers will be more involved in the development of the 2015 Community Pharmacy Agreement and the funding arrangements to allow us to deliver on the Government's Community Service Obligations. To that end we'll be engaged very closely with both Government and the Pharmacy Guild so that all stakeholders' positions are taken into account in framing the next agreement.

And just to re-emphasise, our strategic imperatives have major synergistic benefits. Extending our lead in pharmacy distribution, helps build relationships with potential Priceline Pharmacy franchisees which leads to profit growth; which in turn leads to further brand investment and buying power; which means we can offer better programs to our wholesale customers and so the circle goes on.

That is our strategy. We have established a first-mover advantage that will be extremely difficult to overtake and our key financial indicators are continuing to improve.

Priceline Pharmacy's major business model is highly scalable and we're not going to lose our dual focus on the pharmacist as the centre of our offering, while maintaining the loyalty of our female shoppers.

So, looking to the year ahead. We fully expect further growth in our Priceline Pharmacy network. This growth, allied to our investment in ecommerce, should help us maintain retail sales growth of circa 3 per cent.

And as I have said, we'll leverage our investment in the Sister Club program; maximise our health credentials; continue to work to mitigate the ongoing impact of PBS reform and maintain our leadership in pharmacy distribution through offering our customers best in market service offers, whether branded or independent.

That is why, absent of any major external environmental or economic impacts, we anticipate a continued lift in underlying earnings this financial year.

In closing, I would like to add my thanks to the API staff and my management team for all their hard work during the year; to my fellow board members for their support; and to you, the shareholders.

Thank you.