CHAIR & CHIEF EXECUTIVE UPDATES

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Joan Withers
Chair, The Warehouse Group


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CEO, The Warehouse Group

CHAIR'S REPORT

Staying on course

In a year buffeted by the disruption of a global pandemic and the rollout of a national vaccination programme, The Warehouse Group has stayed on course.

We have remained true to our strategy and lived our values by putting customers first, doing good for our people and planet, and delivering on what we said we would do.

During the 2021 financial year (FY21), we have made material progress while also embracing the disciplines required to become an agile business and operate effectively within a changing environment.

The Warehouse Group is the first major retailer to adopt and implement the agile framework to improve performance. By steadily enhancing the ways we conduct our business we have been able to act for the good of our customers, communities, people and investors in an era of uncertainty, upheaval and isolation.

Our culture and mindset and our teams' expertise have enabled the business to open and shut stores and move to Click & Collect almost overnight during the first wave of COVID-19 alert level changes. And now again, subsequent to year end we have had to adapt as the country reverted to Level 4 lockdown.

Agile is not an easy journey – and I want to give full credit to all our people for having the bravery and stamina to meet the challenge of such fundamental change.

The execution of the strategy has gone to plan and it is heartening to now see the benefits of the decision we took in 2017 to transform our business by striving to build New Zealand's most sustainable, convenient and customer-first company.

Four years ago, we would not have anticipated the record results we have achieved in FY21. There is no doubt that the Group has benefitted from the changes to the way New Zealanders now live, work and shop. Some of that change was driven by COVID-19 but there has undoubtedly been a shift in behaviours that will be significant and enduring.

COVID-19 was a causative component of our results for the last financial year and we were able to capitalise on the tailwinds arising from border closures and restricted international travel to the fullest extent because of the transformation journey we have been on.

However that is not the whole story of FY21 and the fundamental changes we have made in the business are undoubtedly providing significant benefit. Our increasing competency in data utilisation, and ability to understand and meet customers' product and service needs much better than we did in the past have contributed to margin improvement. Alongside this, our focus on defining the future customer experience, the continued execution of Every Day Low Pricing in The Warehouse and reduced discounting across other brands positioned us to catch the rising wave of in-store and online retail demand amplified by the impacts of COVID-19.

People are now much more used to shopping remotely. The significant investment in our digital future and a quality customer experience has delivered material returns as people embraced services such as Click & Collect, which grew 21.1% year-on-year.

Financial performance across the Group was strong, and the sales growth at Torpedo7 in particular merits a call out – up 22.2% on last year, a testament to the execution of the growth strategies put in place by the team as well as the way Kiwis have pursued cycling, water sports and other outdoor activities locally instead of holidaying offshore.

Two years after the launch of TheMarket.com, our investment in this platform has been vindicated as more and more Kiwis shop from a screen. TheMarket.com's growth during FY21 includes almost 397,000 active customers and over 50,000 Market Club members.

We started our strategic and operational transformation back in 2017 and our FY21 results further strengthen our resolve and confidence in our course of travel.

The results

Our adjusted net profit after tax (NPAT) was $175.5m, up from $32.1m last year, with reported NPAT being $117.7m - a record for The Warehouse Group.

Strong operational performance, sustained sales momentum and a robust financial position enabled the Group to repay the Government COVID-19 wage subsidy of $67.6m for our 11,000 employees in December 2020.

We could not have delivered such a lift in profitability without the improvements our teams have made in our stores, distribution and fulfilment centres, our Store Support Office and to our digital platform.

The fact that we did this during a year which started with Auckland entering Level 3 lockdown for two weeks on 12 August is a testament to the resilience of our people and our business. As I write this, post financial year end, the country is once again in Level 4 lockdown and Nick Grayston, the executive leadership squad and our entire team are responding to the challenges and opportunities we again face.

On virtually all of our key measures, The Warehouse Group has made significant strides year-on-year. Total retail sales increased from $3.2b to $3.4b, and operating margin has risen from 1.6% to 7.0%.

Reported net profit attributable to shareholders for the year was $117.7m, compares to $44.5m last year.

Capital management

As I noted previously, reported work undertaken 18 months ago in terms of balance sheet management continues to assist us with our capital management.

We are comfortable with our capital structure and continue to focus on ensuring that we have the required liquidity for the Group and that we are able to reward our shareholders with a sustainable and coherent dividend policy.

In the current uncertain economic environment the Group considers it appropriate to maintain high levels of liquidity. Our undrawn bank debt facilities of $330m, together with cash on hand at year end provide a liquidity buffer of $490.5m.

"Our culture and mindset and our teams' expertise have enabled the business to open and shut stores and move to Click & Collect almost overnight during COVID-19 alert level changes."

Capital expenditure has risen on the prior year, with increased spend on customer-facing digital and core system initiatives including the Group eCommerce platform and enterprise resource planning systems for finance and inventory.

FY21 capex spend was $85m, lower than initially budgeted, but higher than the average last three years of $65m.

Dividend policy

The Board took a cautious approach to cash preservation in FY20 due to COVID-19 and the resultant operational uncertainty. We made the difficult decision to cancel the FY20 interim dividend and declared no FY20 final dividend.

However, following stronger than expected trading performance in November and December 2020, the Board declared a special dividend of five cents per share in February 2021.

The Board undertook a review of the Group dividend policy, comparing it to market practice and other listed retailers, and taking into account current and forecast Group operational cash flow, forecast capital expenditure and liquidity requirements.

Directors approved a new dividend policy in March 2021.

The new policy is to distribute at least 70% of the Group's full year adjusted net profit, at the discretion of the Board and subject to trading performance, market conditions and liquidity requirements.

This dividend policy provides the Group with flexibility to maintain a stable capital structure, allowing for capital expenditure to invest for future growth, and progressive and sustainable dividends.

In accordance with this new policy the Board declared a fully imputed FY21 interim dividend of 13.0 cents per ordinary share paid on 22 April 2021.

The Board is pleased to announce a fully imputed final dividend of 17.5 cents per share. The final dividend has been declared on the basis that New Zealand is predominantly at Alert Level 2 or below from the end of October 2021. The record date for the dividend will be 18 November 2021 and will be paid on 3 December 2021.

Sustainable and affordable

Our customers increasingly expect that businesses with which they interact have a transparent and measurable commitment to sustainability.

The Warehouse Group aspires to be New Zealand's most sustainable retailer and is implementing initiatives in three focus areas: people, products and planet.

Through efforts including ethical sourcing, reduction in packaging and plastics, and prioritising sustainable products and materials, our brands now offer over 11,500 products with sustainable attributes – up from 6,000 a year ago.

We are working with community organisations such as The Salvation Army, Plunket, and Women's Refuge and taking leadership positions on issues such as reducing family violence, period poverty, supporting diversity, and helping to equip hundreds of vulnerable Kiwi children with much needed back to school essentials.

During FY21 we established a board committee which oversees our governance of environmental, social and sustainability issues. The company achieved carbonzero status back in FY19, and right from the time our founder Sir Stephen Tindall opened the first The Warehouse store back in 1982, we have had a strong focus on sustainability. The Board is committed to understanding and implementing ways we can fulfil our obligations to stakeholders as greater expectations and a requirement for more transparency around Environmental and Social Governance (ESG) unfold.

I am incredibly proud of these and the many other initiatives detailed elsewhere in this report that demonstrate a commitment to sustainability and action.

Board activity

We have continued to refresh the Board, following the retirement of Sir Stephen Tindall and Keith Smith last year.

In February we appointed Rachel Taulelei as a non-executive director. Rachel has unique commercial experience as chief executive of large operational locally owned businesses, including co-founding business design and brand strategy firm, Oho and at Kono, a top 100 New Zealand food and beverage company. She was also founder of Yellow Brick Road which specialises in direct seafood supply into restaurants.

Rachel also has strong credentials leading business councils and in non-executive directorships with particular expertise in primary industries.

She currently chairs the APEC Business Advisory Council and was a member of the Prime Minister's Business Advisory Council.

Rachel's broad-ranging experience adds an important skillset to our Board and complements the skills of existing directors. (Please refer to the Board Skills Matrix available on page 88).

Future Director Renee Mateparae attended her final meeting in September. The Board has valued her contribution very highly and her expert knowledge of agile structures and processes gained through her leadership role at Spark. She has been highly committed to her Future Director role, and we have thoroughly enjoyed having Renee at the board table.

"The Group has traded well through the turbulence of FY21. However, the COVID–19 environment continues to evolve and it would be premature to anticipate a return to full normality in FY22."

Our new Future Director is Caroline Rainsford. Caroline is currently the Country Director for Google NZ, a role she has held since 2017. Prior to this, she was the Marketing and Product Director for Latitude NZ as well as the Brand Director for the Australian and New Zealand region, with her earlier career including roles with Philips Royal Electronics in the Middle East, Turkey and Africa.

I am delighted to welcome Caroline as our latest Future Director. The Warehouse Group remains committed to the scheme and we have derived enormous benefit from the various incumbents we have had sitting around the table for the past seven years.

I attended our Investor Day in May – the first since 2017 – and was heartened by the engagement of the attendees and their interest in the Group. It was a good opportunity to update investors on the progress achieved over the past four years and provide a deeper understanding of our strategy.

Following last year's Board performance review we have undertaken a couple of 'pulse checks' with our external provider to monitor progress on the areas we identified for improvement in the full performance assessment.

The Board will be asking shareholders at our upcoming Annual Meeting for an increase to Directors' Fees. The last increase was in 2013 and we have based our request on an independent report on comparator companies and after canvassing a number of key shareholders on their view of a proposed increment to the existing fees.

The year ahead
Uncertainty remains the dominant factor in assessing the year ahead.

The Group has traded well through the turbulence of FY21. However, the COVID–19 environment continues to evolve – and it would be premature to anticipate a return to full normality in FY22.

While New Zealand's economy strengthened post the initial COVID–19 lockdowns of 2020, the recent closure of the trans-Tasman bubble, the impact of the Delta variant on one of our most important trading partners and most latterly the incursion of the Delta variant to New Zealand shores are yet to play out in terms of repercussions on the retail and wider business sectors.

The sustainability of heightened consumer retail spending levels, the impacts of catastrophic climate-related events, constraints on global supply chains, and lack of clarity about the global roadmap out of COVID–19 restrictions are among the factors that will challenge The Warehouse Group in the year ahead.

We have demonstrated agility and courage in FY21 – and the record result is a tribute to Nick Grayston, his leadership team and all our team members. On behalf of the Board, I thank them most sincerely.

The Board has endeavoured to provide wisdom and steady governance oversight during the upheavals and opportunities and, most importantly, support the exemplary response our team has demonstrated during this global pandemic. Guiding the transformation of a retail business of the scale and reach of The Warehouse Group in a trading environment impacted by tight border controls, logistical disruptions and sudden lockdowns has placed additional demands on Directors. I thank them for their support, their energy and commitment throughout the year.

It is pleasing to be in a position to reward our shareholders for their forbearance last year, with a return to the payment of dividends this year. As always, the Board values your support and looks forward to meeting with you at our Annual Shareholders Meeting in November.

Joan Withers – Chair

CEO'S REPORT

More than a year after the onset of the global pandemic, The Warehouse Group has seen the investment in the move to agile working practices prove worthwhile by demonstrating that it can innovate, adapt and deliver the services Kiwis need in the context of massive disruption.

While New Zealand united around a strategy to keep COVID-19 out, our teams aligned around a business strategy to fulfil customers' demands for frictionless convenience.

Our strategic priorities - to build a customer ecosystem, define the future customer experience and excel in retail fundamentals – became magnified by the radically altered retail environment in which we now operate. Our combination of local assets, global partnerships, and a strong financial position meant we were able to grow our business and expand our capabilities to deliver solutions for customers in a year when they relied on us more than ever.

Changes made to the way we work and the investments in our future have been guided by a core imperative: knowing what our customers want and delivering it so that shopping with us is easier and more rewarding than shopping with anyone else.

Refining our ways of working
Following a record half-year profit the business maintained its momentum, achieving a 7.6% increase in sales revenue which contributed to gross profit increasing 20% to $1.2b compared to the prior year.

The 2021 financial year tested our ability to adapt and flex amid ongoing business interruption.

In August 2020, we formalised our move to becoming a business guided by agile principles within our Store Support Office, enabling us to further strengthen our focus on anticipating and meeting New Zealanders' needs, however and whenever they choose to shop with us.

As the first major retailer to go agile, there was no blueprint. We had to make some compromises and manage our way through a lot of unknowns. As a result, some pockets of historic inefficiencies and old ways of doing things remained. We are now addressing these by re-examining what constitutes 'must-do' and discretionary activities by a process of 'zero-basing' the work. This is ongoing work that will support our stated goal of becoming New Zealand's most sustainable, convenient and customer-first company.

In our stores, it was a year of implementing standardised processes and adjusting the deployment of team members. In The Warehouse, we changed the rostering and tasks of our teams so we had team members on the shop floor when customers needed them most: in the weekends and evenings.

In October 2020, after a period of consultation, about 750 roles became redundant following a Group restructure.

"The 2021 financial year tested our ability to adapt and flex amid ongoing business interruption."

That was tough for everyone – those who departed as well as those who remained.

Since then, however, we have seen the employee net promoter score (NPS) in our stores rise significantly, and it has been pleasing to see that customer NPS has also increased over that time.

Building our ecosystem
We have started to deliver an ambitious programme of infrastructural and technological innovation required to enable The Warehouse Group's ability to do good for all our stakeholders and excel for our customers.

We are building an ecosystem which allows customers to be recognised and rewarded however and whenever they choose to interact with us.

Part of our competitive moat is the physical locations that we have all around New Zealand with most Kiwis no more than 20 minutes from one of our stores.

As COVID-19 lockdowns restricted shopping behaviour, we ramped up one-day Click & Collect at The Warehouse and scaled one-hour Click & Collect at Noel Leeming.

Additionally, we accelerated our 'store-within-a-store' (SWAS) model, integrating a further eight The Warehouse and Warehouse Stationery stores. We will continue to co-locate our brands where it makes sense to do so, while also investing over the next two years in renovating approximately 40 stores in order to improve the omni-channel shopping experience.

While it is unlikely that our total footprint will grow, there will be targeted new store openings. During FY21, these included becoming part of the new Ormiston Town Centre in South Auckland, where we opened new The Warehouse, Warehouse Stationery and Noel Leeming stores.

Across our store brands, we recorded a 5.0% increase in online sales, making up 11.5% of total Group sales. We plan continued technology investment to support this ongoing change in customer behaviour.

We have delivered the re-platforming of The Warehouse website, nearly completed the re-platforming of the Noel Leeming site and are now looking at enhancements to our mobile apps.

Our new warehouse management system has gone live in our South Island Distribution Centre and will be activated in the North Island Distribution Centre after Christmas.

Over the next three years we will enhance our Master Data Management, build and deploy enterprise management systems which tie together a multitude of business processes and enable the flow of data between them. We will also optimise our supply chain systems and processes to include providing more options to flex between speed and cost of online fulfilment options for our customers.

We are broadening the scale and scope of programmes that deepen the connection between our brands and our customers.

In addition to growing our existing loyalty programmes - myNoelLeeming, Torpedo7 Club, TheMarket Club, and BizRewards – we have successfully launched an app-first loyalty programme trial in The Warehouse. We have now confirmed the rollout of a unified loyalty programme across the Group, to be named Market Club, which will include both a free and a subscription offer, with subscriptions offering unlimited free shipping on millions of items. This will evolve to integrate all existing programmes, giving even more benefit and utility to our customers, with the rollout starting this calendar year.

Our loyalty programmes are already benefitting New Zealanders by linking with offers from other major brands. In September 2020, TheMarket.com and Vodafone New Zealand entered an exclusive partnership which rewards all Vodafone customers with a free subscription to TheMarket's loyalty scheme and its membership benefits.

The shift to working from home forced people to grapple with technical and IT issues that were formerly the responsibility of workplace experts. Our services were in huge demand, resulting in Noel Leeming Tech Solutions revenue increasing by 42%. In addition to expanding the use of artificial intelligence, chat bots, and digital humans to help solve customer problems, we trained more people to be present on the shop floor and able to provide advice backed by deep knowledge of our products and customers, supported by technology.

Do Good – Kia Oha

One of our core values as a leading New Zealand-owned retailer is to do good, acting as one team that stands up for our people, our planet and our communities.

Sustainability has become increasingly important to our customers and shareholders.

This year we launched the Sustainable & Affordable campaign which highlights that customers can make more sustainable choices without products becoming prohibitively expensive.

We think about value as being the synthesis between price and quality, with today's customers rejecting the trade-off between affordability and sustainability - they are asking for both.

More than 11,500 of our products now carry sustainable attributes which include certified sustainable materials or plastic-free packaging. We are working with recognised programme providers such as the Better Cotton Initiative and Forestry Stewardship Council to ensure the products we purchase are better for our planet and our customers.

Sustainable packaging guidelines are being rolled out across all new products to reduce unnecessary plastic usage and improve packaging recyclability, reusability, or compostability. Our Soft Plastics Recycling Scheme in 29 of our stores allows our customers to drop their soft plastics into recycling bins, diverting them from landfill. We have also launched e-waste recycling capability in 16 of our Noel Leeming stores and will roll this out to more stores as soon as possible.

For the past 17 years, The Warehouse has had an ethical sourcing programme in place to protect the welfare of workers in its supply chain. (You can read more on this in our Ethical Sourcing report on our website).

With our vision to become New Zealand's most sustainable company, we know we have to measure up.

That's why each year we work alongside the Carbon Disclosure Project, a not-for-profit charity that runs the foremost global disclosure system for investors, companies, cities, states and regions to help them manage their environmental impacts. In December The Warehouse Group received a score of A- for 2020, increasing from a C in 2018 and 2019. With C being the current industry, regional and global average, receiving a rating of A- puts us in the highest category of "Leadership", acknowledging we are currently "implementing current best practices" in the fight against climate change.

"We think about value as being the synthesis between price and quality, with today's customers rejecting the trade-off between affordability and sustainability – they are asking for both."

To tackle family violence further, we have partnered with charities to address some of New Zealand's most pressing social issues. We have enhanced support for team members experiencing family violence by providing 15 days' paid leave and three nights' accommodation as well as an online support tool under our Family Violence is not OK platform.

As part of our effort to help remediate period inequity in New Zealand, The Warehouse offered $1 period products and gave one pack to charity for every 10 sold. We partnered with The Period Place to offer a new educational hub on thewarehouse.co.nz aimed at reducing the stigma associated with periods. The Warehouse was also successful in being appointed as an official supplier of period products to schools through the government programme.

During the year we supported our team members through a variety of efforts such as counselling, wellbeing initiatives and via The Warehouse Group Foundation we provided support for those facing financial hardship.

Further information about the many actions and commitments made by the Group, our brands and our teams within our evolving ESG model can be found on pages 46 to 48.

Performance

Each of our brands contributed to our record Group profit through sales growth, improved operating margins, rising online sales, and substantial Click & Collect fulfilment growth.

The Warehouse sales increased 5.8% to $1.8b as we continued to improve products and refine our offer to customers during FY21.

That's despite the Auckland region experiencing 18.5 days of COVID-19 lockdown in August 2020 when stores were unable to trade as normal, and heightened alert levels in March and June 2021. During the August 2020 lockdown The Warehouse sales declined 17.4% year-on-year.

Warehouse Stationery continued to build on its momentum from the prior year, benefitting from the store-within-a-store model and the emerging hybrid work practice of splitting days between the office and home. We delivered another record profit with sales of $274.6m, an increase of 2.2% on last year.

Noel Leeming had a stellar year with sales growth of 11.7% to $1.1b. The 9.3% growth in Click & Collect fulfilment with most customers choosing our one-hour service showed the extent to which people have gravitated to online purchases since the COVID-19 lockdowns.

Both Noel Leeming and Warehouse Stationery benefitted from our recent inclusion in the all of government procurement panel for office supplies and Information and Communication Technology (ICT) consumables.

Torpedo7 was our turn-around hero with total sales increasing 22.2% on the same period as last year to $158.7m. Simon West and the team have worked very hard to reverse profit losses and are now reaping the benefits of scale and improved merchandising and operations. We see additional growth opportunities as we continue to scale the business to achieve coverage and critical mass across New Zealand.

TheMarket.com is another growth story, now with 2.5 million available products and over 5,300 brands from more than 800 merchants. More than 18.6m online sessions were completed in FY21, up 138% compared to the same period last year. We are continuing to invest in this critical part of our ecosystem as we move towards scale.

Ready to meet challenges

The pace of modern life in the digital age means that the biggest risk to companies is becoming anachronistic and lacking the flexibility to respond to the ever-increasing pace of change.

COVID-19 was an accelerant for us, and made it all the more imperative to work our way through some difficult decisions.

Pressure creates diamonds but you must have the carbon to create them in the first place. During FY21 we saw the benefits from the plans that we laid prior to the pandemic, and the execution that we are now delivering.

Product improvements, building our own private label and sourcing capabilities, and price optimisation have all enabled us to extract more value as well as manage costs.

We are now being rewarded for many of the things we have been working on since we confirmed our strategy in 2017.

We acknowledge that a buoyant market contributed to our significant increase in profitability. COVID-19 lockdowns spurred people to focus on the quality of their home environments which has benefitted consumer electronics and homeware in particular.

A nearly 27% increase in New Zealand's minimum wage since 2017 means there is more disposable income flowing into the economy and some of that has benefitted retail.

When New Zealand reopens its borders there is the potential for growth rates to contract. However, we have made good use of these unusual times to get our house in order and have constrained costs where possible to be able to protect profits in that eventuality.

We have long anticipated that an online behemoth like Amazon would enter the local market. Although they do not have a distribution centre here yet, they have three in Australia and are building a fourth so it's only a matter of time. They have formally launched in New Zealand where they are already the third most trafficked website without a physical presence.

It is vital that we become a modern, vigorous and competitive option so that The Warehouse Group can retain our 11,000 people employed within New Zealand instead of losing those jobs overseas.

Further modernisation of our supply chain will be a major focus over the next few years. COVID-19 has created global supply challenges and we need to stay ahead of these.

Last Christmas we reduced our focus on seasonal product and put more effort into basic continuity product. That meant we left some business on the table but we also reduced risk through better inventory management. The worst case scenario is seasonal product arriving too late to sell.

A shortage of shipping containers in the right place at the right time to carry manufactured goods from source to destination is a symptom of the havoc the pandemic has wrought on international supply chains. As a result, freight costs are rising which will inevitably translate into higher prices for customers.

Issues like these will continue to challenge us. By staying true to our strategy, we will deal with them – and I am confident we have the leadership strength and commitment from our people to do so and prosper.

We farewelled three members of the leadership team over the course of the year.

In October 2020 Chief Operating Officer Pejman Okhovat resigned to take up a senior executive position with an overseas retailer. Pej joined The Warehouse Group in 2005 and played a key role in improving the performance of The Warehouse and Warehouse Stationery, and enabling The Group to trade through COVID-19 during the Level 4 and 3 lockdowns in 2020.

Chief Transformation Officer Scott Newton, who led our transformation over the past three years, also decided it was time to move on, having made a significant contribution to reducing complexity, driving performance improvements and strengthening The Warehouse Group's health and capabilities.

In September 2021 Chief Sales Officer Tim Edwards resigned. Tim has been with the Group since 2009 in the roles of CEO Noel Leeming and CEO Torpedo7 prior to taking on his current position. He played a key role in the Noel Leeming brand's significant growth, achieving over $1b in annual sales in FY20, as well as growing the Services and Commercial businesses.

We wish Pej, Scott and Tim all the best for the future.

Our executive leadership team has continued to become leaner and more agile. At the next leadership level we have grown our diversity considerably with women now holding 50% of these senior roles.

A successful retail business runs on the energy, commitment and skills of its people.

By living our values, everyone working at The Warehouse Group brings us closer to our vision of being New Zealand's most sustainable, convenient and customer-led company.

I want to thank all of our team members for their resilience, dedication and courage in embracing the changes we have made, and those we must continue to make.

Nick Grayston – CEO