APPENDIX 4E

Australian Pharmaceutical Industries Limited

ABN 57 000 004 320

Final report for the year ended 31 August 2018

The following information is presented in accordance with ASX listing rule 4.3A and should be read in conjunction with the attached Financial Report for the year ended 31 August 2018.

1. DETAILS OF THE REPORTING PERIOD AND THE PREVIOUS CORRESPONDING PERIOD

Current period	Year ended 31 August 2018
Previous corresponding period	Year ended 31 August 2017

2. RESULTS FOR ANNOUNCEMENT TO THE MARKET

For the year ended 31 August	2018 $'000	2017 $'000	Change $'000	Change %
Revenue from ordinary activities	**4,026,302**	4,061,200	(34,898)	(0.9%)
Net profit after tax for the year (NPAT)	**48,202**	52,371	(4,169)	(8.0%)
Earnings before interest, tax, depreciation and amortisation (EBITDA)	110,573	117,900	(7,327)	(6.2%)
Earnings before interest and tax (EBIT)	82,397	89,276	(6,879)	(7.7%)
Profit before tax	70,027	76,412	(6,385)	(8.4%)
Net profit after tax for the year, attributable to members of the Company	**48,056**	52,371	(4,315)	(8.2%)
Underlying net profit after tax for the year, attributable to members of the Company (i)	**54,669**	54,215	454	0.8%
Earnings per share (in cents)				
Basic earnings per share	**9.8**	10.7	(0.9)	8.4%
Diluted earnings per share	**9.7**	10.6	(0.9)	8.5%
Underlying basic earnings per share (i)	**11.1**	11.1	-	0.0%

(i) Refer to Attachment 1 for reconciliation of reported net profit and basic earnings per share to underlying net profit and basic earnings per share

Commentary on the results for the period

For an explanation of the results, refer to the Results Announcement and Results Presentation issued 18 October 2018.

3. DIVIDEND INFORMATION

	Amount per share (cents)	Franking percentage	Total Amount A$	Date of payment
Year ended 31 August 2018				
Final ordinary dividend - declared Record date: 9 November 2018	**4.0**	**100%**	**19,697,141**	**7 December 2018**
Interim ordinary dividend - paid	3.50	100%	17,235,010	1 June 2018
Year ended 31 August 2017				
Final ordinary dividend - paid	3.50	100%	17,229,050	8 December 2017
Interim ordinary dividend - paid	3.50	100%	17,143,023	2 June 2017

There are no dividend reinvestment plans currently in operation.

4. NET TANGIBLE ASSET BACKING (CENTS PER SHARE)

As at 31 August 2018	2018	2017
Net tangible asset backing - cents per share	**46.6**	73.6

Net tangible asset backing has reduced due to the acquisition of Clearskincare business as noted below.

5. SUBSIDIARIES AND GAIN OR LOSS OF CONTROL OVER ENTITIES DURING THE YEAR

On 31 July 2018, the Company acquired a 50.2% controlling interest in the Clearskincare Clinic business and 100% controlling interest in the Clearskincare Products business. The details of this acquisition, including contribution to the Group results by the acquired business, are set out in Note 20 of the attached Financial Report.

The Company has a New Zealand subsidiary which adopts the New Zealand equivalents of the International Financial Reporting Standards ('NZIFRS') which is consistent with the framework adopted by the Company.

6. FINANCIAL STATEMENTS

The following additional Appendix 4E disclosure requirements can be found in the attached Financial Report for the year ended 31 August 2018, which contains the Directors' Report (including the audited Remuneration Report), the Directors' Declaration and the 31 August 2018 consolidated financial statements and accompanying notes:

- Consolidated statement of profit or loss and other comprehensive income;
- Consolidated balance sheet;
- Consolidated statement of changes in equity;
- Consolidated statement of cash flows;
- Notes to the consolidated financial statements;
- Operating and financial review; and
- Returns to shareholders including distributions and earnings per share.

The consolidated financial statements have been audited and the auditor has provided an unmodified opinion.

7. SHAREHOLDER CALENDAR

Results announcement	18 October 2018
Record date	9 November 2018
Final dividend payment	7 December 2018
2018 Annual General Meeting	
Date	23 January 2019
Time	2:00 pm
Location	Rydges Parramatta, 116-118 James Rose Drive Rosehill NSW 2142
Approximate date that Annual Report will be available	7 December 2018

8. FURTHER INFORMATION

INVESTOR CONTACT
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MEDIA CONTACT
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Email: saylmer@respublica.com.au

APPENDIX 4E

Australian Pharmaceutical Industries Limited

ABN 57 000 004 320

Final report for the year ended 31 August 2018

ATTACHMENT 1 – RECONCILIATION OF REPORTED INFORMATION TO UNDERLYING INFORMATION

Reconciliation of reported NPAT to underlying NPAT	**Year ended 31 August**	
In thousands of AUD	**2018**	**2017**
Reported Net profit after tax	**48,202**	52,371
Add:		
Costs incurred in relation to business acquisitions	4,057	1,844
Costs incurred for business restructuring	2,556	-
Underlying NPAT	**54,815**	**54,215**
Less: Non-controlling interests	(146)	**-**
Underlying NPAT attributable to members	**54,669**	**54,215**
Underlying basic earnings per share (in cents)	**11.1**	**11.1**

Underlying NPAT and Earnings per share are non-statutory measures used by the Chief Operating Decision Maker to measure the financial performance of the Company.

AUSTRALIAN PHARMACEUTICAL INDUSTRIES LIMITED

ABN: 57 000 004 320

ASX Code: API

FINANCIAL REPORT FOR THE YEAR ENDED 31 AUGUST 2018

TABLE OF CONTENTS

Glossary

Below is a glossary of abbreviations used in the Financial Report including the Directors' Report and the Remuneration Report.

Abbreviation	Definition	Abbreviation	Definition
CAGR	Compound annual growth rate	STIP	Short term incentive plan
CEO	Chief Executive Officer	TRIFR	Total recordable injury frequency rate
CSC	Clearskincare business	TSR	Total shareholder return
EBITDA	Earnings before interest, tax, depreciation and amortisation	Underlying cost of doing business (CODB)	Total operating expenses, excluding cost of sales, depreciation, amortisation and excluding one-off charges, as a percentage of total revenues for the year.
EBIT	Earnings before interest and tax		
EPS	Earnings per share		
FY18	Financial year ended 31 August 2018		
KMP	Key management personnel		
LTIFR	Lost time injury frequency rate		
LTIP	Long term incentive plan		
MTIFR	Medical treatment injury frequency rate		
NPAT	Net profit after tax		
PBS	Pharmaceutical Benefits Scheme		
ROE	Return on equity		
ROIC	Return on invested capital		

All currencies are expressed in Australian Dollars, unless stated otherwise.

DIRECTORS' REPORT

BOARD OF DIRECTORS

The Directors present their report together with the financial report of Australian Pharmaceutical Industries Limited (the Company or API) and its controlled entities (the Group) for the financial year ended 31 August 2018 and the auditor's report.

DIRECTORS

The Directors of the Company during the financial year and up to the date of this report are:

Director	Appointment date and Committee memberships	Profile
Mr Mark Smith Dip Business (Marketing), FAICD, FIML, FAMI, CPM	Independent Non-executive Director appointed on 6 September 2017 Chairman of the Board appointed on 24 January 2018 Member (interim) Audit and Risk Committee from 6 September 2017 to 9 November 2017	Mr Smith was previously the Chair of Patties Foods Limited for three years and a Non-executive Director of Toll Holdings Limited for eight years. Mr Smith has extensive senior management experience in the fast moving consumer goods industry globally and was Managing Director of Cadbury Confectionery ANZ from 2001, Managing Director of Cadbury Schweppes Australia and New Zealand from 2003 to 2007, and a member of the Cadbury Schweppes Asia Pacific Regional Board. He also has a strong commitment to not-for-profit organisations as Chair of Enactus Australia and Chair of the Humour Foundation Ltd. <u>Other current listed company directorships:</u> • GUD Holdings Limited (Non-executive Chairman)
Mr Robert D. Millner FAICD	Non-executive Director appointed on 5 May 2000 Member – Remuneration Committee appointed on 2 October 2007 Member – Nomination Committee appointed on 15 August 2012	Mr Millner has extensive management and public company experience across a number of industries. <u>Other current listed company directorships:</u> • Brickworks Limited • BKI Investment Company Limited • Milton Corporation Limited • New Hope Corporation Limited • TPG Telecom Ltd • Washington H Soul Pattinson and Company Limited
Ms Lee Ausburn M.Pharm,B.Pharm, Dip.Hosp.Pharm, FAICD	Independent Non-executive Director appointed on 7 October 2008 Member – Audit and Risk Committee appointed on 7 October 2008 Chair – Nomination Committee appointed on 8 April 2015 and member since 15 August 2012	Ms Ausburn is a pharmacist with experience in retail and hospital pharmacy and in academia. She had a long career in the pharmaceutical industry with Merck Sharp and Dohme (Australia) Pty Ltd and was previously Vice President, Asia, for Merck and Co Inc with responsibility for the company's operations across Asia. Ms Ausburn was President, Pharmacy Faculty Foundation, University of Sydney until December 2017. <u>Other current listed company directorships:</u> • nib holdings limited • Somnomed Limited

DIRECTORS' REPORT

BOARD OF DIRECTORS *(Continued)*

Director	Appointment date and Committee memberships	Profile
Mr Gerard J. Masters	Independent Non-executive Director appointed on 7 September 2010 Member – Nomination Committee appointed on 15 August 2012 Chairman – Remuneration Committee appointed on 30 January 2014 Member (interim) – Audit and Risk Committee from 1 March 2017 to 6 September 2017	Mr Masters has extensive experience in retailing. Until his resignation in early 2006, he spent more than 33 years with the Coles Myer Group. This included a 10 year period as Managing Director of Bi Lo, Coles and then the total Supermarkets Group which was Coles Myer's largest and most profitable business. His most recent role, until his resignation in 2009, was as the Managing Director and Chief Executive Officer of The Reject Shop Limited.
Mr Kenneth W. Gunderson-Briggs B. Bus, FCA, MAICD, FIML	Senior Independent Non-executive Director appointed on 2 September 2015 and Director since 6 May 2014 Chairman – Audit and Risk Committee appointed on 25 January 2017 and member since 6 May 2014 Member – Remuneration Committee appointed on 8 April 2015	Mr Gunderson-Briggs is a chartered accountant, registered company auditor and public company Director, with broad experience in finance and the retail franchise sectors. Mr Gunderson-Briggs finished his tenure as Chairman of Glenaeon Rudolf Steiner School Limited in May 2018, having been a Director since 2009 and Chair since 2013. <u>Other current listed company directorships:</u> • Harvey Norman Holdings Limited
Ms Jennifer Macdonald B.Com, ACA, MEI, GAICD	Independent Non-executive Director appointed on 9 November 2017 Member – Audit and Risk Committee appointed on 9 November 2017	Ms Macdonald is a chartered accountant with a strong background in financial and general management roles across a range of industry sectors including fast moving consumer goods, travel and digital media. Ms Macdonald has previously held the roles of Chief Financial Officer and Interim Chief Executive Officer at Helloworld Travel and Chief Financial Officer and General Manager International at REA Group, as well as various company directorships. <u>Other current listed company directorships:</u> • Redbubble Limited • Redflow Limited • Bapcor Limited

DIRECTORS' REPORT

BOARD OF DIRECTORS *(Continued)*

Director	Appointment date and Committee memberships	Profile
Mr Richard C. Vincent B.Bus, (Accountancy), CPA	Executive Director Managing Director and Chief Executive Officer appointed on 15 February 2017	Mr Vincent started his professional career in finance with Bridgestone before moving to Britax Rainsfords where he was CFO. He joined FH Faulding & Co Limited in 1998 and remained with that company until 2005, during which time he held a number of senior leadership roles, including responsibility for the pharmacy distribution, retail merchandise and generic pharmaceutical development. Mr Vincent joined API in 2005 where he has held a number of General Management roles that have included pharmacy business development, strategy, supply chain, franchise recruitment, IT, manufacturing and mergers and acquisition. Mr Vincent is the Deputy Chairman of the National Pharmaceutical Services Association and was also a Director of CH2 Holdings Pty Ltd from 2006 to 2015.
Retired Directors		
Mr Peter R Robinson B.Com, FAICD	Non-executive Director appointed on 5 May 2000 Chairman of the Board appointed on 8 July 2003	Mr Robinson ceased to be a Director and Chairman on 24 January 2018.

COMPANY SECRETARY

Mr Peter Sanguinetti has been Company Secretary and General Counsel since November 2007. Mr Sanguinetti BJuris, LLB, GAICD has extensive experience and was previously Company Secretary and General Counsel of Kodak (Australasia) Pty Ltd for 9 years, responsible for legal and company secretarial activities for the Kodak group across Asia. Mr Sanguinetti was also a Non-executive Director of HPAL Limited (formerly listed on the ASX) from January 2005 to November 2007.

Ms Kylie Barrie is Deputy General Counsel and Joint Company Secretary. Ms Barrie, LLB (Hons), AAICD is a qualified lawyer and supports the Company Secretary.

DIRECTORS' MEETINGS

The number of Board and Board Committee meetings held and attended by each of the directors during the financial year are listed below.

Director	Board		Audit and Risk		Remuneration		Nomination	
	Held(i)	Attended	Held(i)	Attended	Held(i)	Attended	Held(i)	Attended
Mr Mark Smith(ii)	17	17	4	1 (iii)	-	-	-	-
Mr Robert D. Millner	17	15	-	-	3	3	1	1
Ms Lee Ausburn	17	16	4	4	-	-	1	1
Mr Gerard J. Masters	17	17	-	-	3	3	1	1
Mr Kenneth W Gunderson-Briggs	17	17	4	4	3	3	-	-
Ms Jennifer Macdonald	14	14	3	3	-	-	-	-
Mr Richard C. Vincent(ii)	17	17	-	-	-	-	-	-
Retired Directors								
Mr Peter R. Robinson(iv)	6	6	-	-	-	-	-	-

(i) Number of meetings held during the time the Director was a member of the Board or Committee. Directors who are not members of Board Committees are invited and attend Committee meetings from time to time. The above table shows meeting attendance of Directors who were members of the relevant Committee(s).

(ii) The Chairman and the Managing Director and CEO attended all Committee meetings by invitation.

(iii) Attended meeting as a member prior to being appointed as Chairman.

(iv) Ceased to be a Director and Chairman on 24 January 2018.

DIRECTORS' REPORT

OPERATING AND FINANCIAL REVIEW

As required by Section 299A(1) of the Corporations Act, and in accordance with ASIC Regulatory Guide 247 Effective Disclosure in an Operating and Financial Review (RG247) issued in March 2013, the Directors present the Operating and Financial Review (OFR) of the Company as follows.

PRINCIPAL ACTIVITIES

The principal activities of the Group were the wholesale distribution of pharmaceutical goods to pharmacies, and retail of health and beauty products to consumers through a network of Priceline and Priceline Pharmacy franchise stores and company owned Priceline stores in Australia. The Group also manufactures in New Zealand and distributes pharmaceutical and toiletry goods to the New Zealand, Australian and Asian markets. There have been no significant changes in the nature of the principal activities during the year, other than the acquisition of the Clearskincare businesses on 31 July 2018. The Clearskincare businesses operate predominately in the Australian market with some operations in New Zealand.

FINANCIAL PERFORMANCE

FINANCIAL HIGHLIGHTS VERSUS PRIOR YEAR

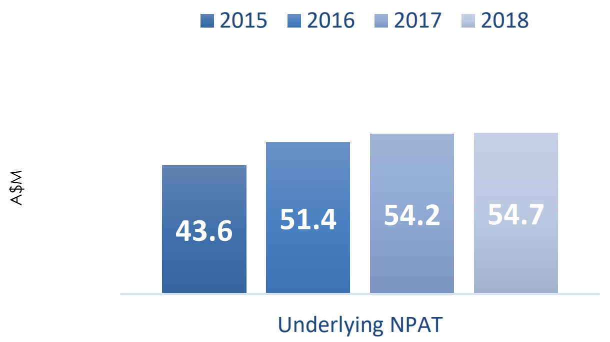
+0.8%	+3.3%	+4.5%	+10 bps	+11.9%
UNDERLYING NPAT TO $54.7 MILLION	REVENUE EXCLUDING HEPATITIS C MEDICINE	IMPROVED WORKING CAPITAL EFFICIENCY	IMPROVED UNDERLYING COST OF DOING BUSINESS DOWN TO 10.3%	IMPROVED REPORTED DIVIDEND PAYOUT RATIO TO 76.9%

COMPANY GROWTH

Clearskincare Clinics
SKIN, LASER + ACNE EXPERTS

ACQUISITION OF CLEARSKINCARE CLINICS AND PRODUCTS BUSINESS

API CONSECUTIVE UNDERLYING NPAT GROWTH



Underlying NPAT CAGR of 7.9% from FY15 to FY18

DIRECTORS' REPORT

OPERATING AND FINANCIAL REVIEW *(Continued)*

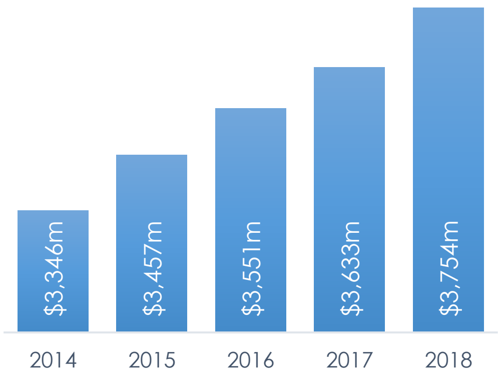
GROUP PERFORMANCE

Consolidated $'000	FY2018	FY2017	Change (%)
Revenue*	3,753,884	3,633,427	3.3%
Gross Profit*	495,482	492,279	0.6%
Operating Expenses	423,203	410,312	3.1%
Reported EBITDA	110,573	117,900	(6.2%)
Underlying EBITDA	118,878	120,534	(1.4%)
Reported NPAT	48,202	52,371	(8.0%)
Underlying NPAT (attributable to API)	54,669	54,215	0.8%
Underlying NPAT (excluding Clearskincare)	54,540	54,215	0.6%

*Revenue and Gross profit reported on an ex Hepatitis C Medicine basis

REVENUE GROWTH (A$M EXCLUDING HEPATITIS C MEDICINE)

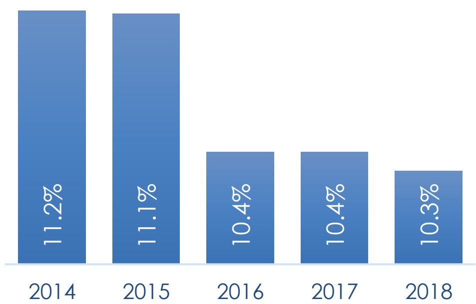
The Group's revenue excluding Hepatitis C Medicine[(i)] was $3.75 billion representing a 3.3% increase on prior year. Growth was primarily driven through continued development of the API's Pharmacy Distribution business. Pharmacy Distribution grew to $2.7 billion (excluding Hepatitis C Medicine) up 4.7% on the prior year. Priceline and Priceline Pharmacy recorded register sales (including dispensary) growth of 2.1% on prior year. Priceline and Priceline Pharmacy network grew to 475 stores, adding 13 new stores during the year.



(i) Hepatitis C medicine sales have varied materially between the 2017 and 2018 reporting periods due to the specific nature of the Government treatment program for patients which sees the disease successfully treated and demand decrease. Excluding the medicine class from reporting is relevant due to its very high cost and inconsequential profit contribution.

UNDERLYING COST OF DOING BUSINESS (EXCLUDING HEPATITIS C MEDICINE)[(ii)]

The Group's Underlying Cost of Doing Business (CODB) has consistently reduced throughout the past 4 years. In FY18 there was renewed focus in building a strong operating platform for future growth.



(ii)Depreciation excluded

DIRECTORS' REPORT

OPERATING AND FINANCIAL REVIEW *(Continued)*

PRICELINE AND PRICELINE PHARMACY

Priceline and Priceline Pharmacy recorded register sales (including dispensary) growth of 2.1% to $2.1 billion. With the challenging retail landscape experienced throughout the year this result was in line with expectations, and reflects our strong consumer offer and Priceline brand loyalty. It should be noted that 'register' sales made by franchisees do not form part of the financial results of the Group.

Strong brand proposition continues to create demand for new stores from potential pharmacist franchise partners driving new store openings and contributing to the register sales growth. The Priceline Pharmacy network finished at 475, up from 462 at 31 August 2017. Consumer engagement has always been a strong focus of the brand and remains a key driver of loyalty for the brand and continues to grow. The Sister Club loyalty program remains the leading Australian health and beauty membership programme.

PHARMACY DISTRIBUTION

Pharmacy Distribution sales were consistent with prior year at $2.9 billion. Excluding Hepatitis C Medicine, overall reported sales growth was 4.7%. Adding back Pharmaceutical Benefits Scheme (PBS) reforms, the underlying sales growth was 6.4%. The business grew independent accounts as well as a number of large pharmacy groups, demonstrating that pharmacists preference API due to the tailored programs to suit the individual business needs of the pharmacists.

NEW ZEALAND

The New Zealand manufacturing segment recorded an increase in profit to $2.8 million. Continued focus on profitable market segments, has resulted in the winning of new contracts to support the growth of the healthcare range in Australia and New Zealand as well as the Personal care product range in other export markets.

CLEARSKINCARE

API completed the first stage of the Clearskincare (CSC) acquisition in July 2018. API paid $61.6 million and received 50.2% of the Clearskincare Clinics and 100% of the Clearskincare Products business. The acquisition was funded through new medium term debt facilities of $65 million.

The Clearskincare acquisition positions API as a leading Health and Wellbeing company in Australia. Clearskincare as leading provider of non-invasive aesthetic services is differentiated by its focus on skincare treatments with all procedures reviewed by medical doctors. The beauty services industry remains largely fragmented with no brand having a decisive market share. With consumer adoption rates increasing, combined with API's proven network expansion capability, the Clearskincare acquisition provides a strong platform for growth.

FINANCIAL POSITION

The Company reported a net debt position of $55.9 million. After excluding net debt relating to the acquisition of CSC ($61.7m), API delivered a net cash surplus of $5.8 million. The Company is currently operating comfortably within the Group's facility limits and associated banking covenants.

The capital expenditure for the year was $25.7 million and cash generated from operations was $98.7 million.

In line with the solid operational performance the Company has declared a fully franked final dividend of 4.0 cents per share, bringing the full year dividend to 7.5 cents per share fully franked, an increase of 7.1% on the prior year dividend of 7.0 cents.

DIRECTORS' REPORT

OPERATING AND FINANCIAL REVIEW *(Continued)*

BUSINESS STRATEGIES AND PROSPECTS FOR FUTURE FINANCIAL YEARS

API remains focused on leveraging its organisational, strategic and physical assets across Australia and New Zealand to drive continued value accretion for its shareholders. To ensure that API's business strategies remain relevant and market leading, the Company's Board performs an annual review of the short and long term strategies to deal with the economic challenges faced by the Company. The Board reviews and approves the Company's strategic goals and supporting initiatives across all business units and functions.

The overall business strategies relevant to the Company's future financial position and performance are set out below.

By applying the strategic goals to the Company's business plans, there will be a continued emphasis on capitalising on the strengths of the Company in the health and beauty retail market and to optimise its strong national community pharmacy wholesale distribution business. This means the Company intends to:

- Consistently deliver a differentiated and personalised experience for our customers, and continue to promote the Priceline Pharmacy Franchise proposition to grow the store network;
- Priceline Pharmacy to continue to be a compelling proposition for pharmacists who wish to offset the impact of PBS reform, leverage pharmacy expertise, and drive further growth from integrated dispensary and retail programs;
- Build loyalty and increase engagement of the Priceline Sister Club loyalty program, and promote increased customer engagement through all channels including the Priceline website and social media;
- Optimise the size and value of the store network for all brands;
- Deliver superior value and service to independent pharmacy customers;
- Provide consistent, valued, and measurable service improvement to all customers and suppliers;
- Optimise the value of our business portfolio through investment, divestment, and acquisition;
- Be at the forefront of Health, Beauty and Wellbeing industry trends, insights and innovation, and use customer insight to drive connectivity of Beauty, Health, and the Dispensary;
- Enrich the community by active support of our Sisterhood Foundation;
- Enhance the employee value proposition, and to create an environment to generate, prioritise and execute innovation; and
- Increase lead indicator safety performance.

DIRECTORS' REPORT

OPERATING AND FINANCIAL REVIEW *(Continued)*

MATERIAL BUSINESS RISKS

The Group's activities expose it to a number of economic and business risks. The Group's risk management framework involves an annual review of the risk profile of the Group, by management and the Audit, Risk and Compliance team, along with a refresh at half year which includes assessing the effectiveness of current controls in place to manage the identified risks. The results of these reviews are provided to the Audit and Risk Committee for its consideration and recommendation to the Board. The most recent update in respect of risk profile and risk management plans was in July 2018. The risks are then reviewed throughout the year.

The risk management process is integrated with the strategic planning process and involves identifying the risk universe and documenting those factors that contribute to the inherent risk environment. Inherent risk is determined by combining likelihood and consequences assessments determined in the absence of any controls within the business.

The following is a summary of the most material and significant risks facing the Group, and how the Group addresses the risk factors.

Risk	How the risk is addressed by the Group
Structural reforms within the Australian Community Pharmacy sector This relates to the risk of continued Government PBS reforms, changes in Government initiatives, regulation and legislation.	The Group monitors the changes to PBS medicines and responds, where appropriate, with a combination of reduced discounts to Pharmacy customers and operational adjustments. The Group also closely monitors costs associated with the Community Service Obligation (CSO).
Continued competitor threats There is a risk that the Group is exposed to significant existing or new competitors in the Australian pharmacy, retail, healthy and beauty markets.	Continue to leverage the differentiated market leading Priceline offering including further personalisation of offers to Sister Club members as well as offering new and exclusive ranges. Continue to ensure we provide market leading service to our customers.
Execution of Retail Pharmacy strategy with associated growth of Priceline Pharmacy stores There is a risk that the expansion of the Priceline Pharmacy franchise network is unsuccessful or the growth in the next five years is slower than planned.	Existing key business processes and responses to mitigate this risk include the continuation of dedicated Retail Pharmacy Business Development teams, and the inclusion of landlords, banks and industry accountants in pharmacist familiarisation and recruitment forums. Tracking measures to monitor growth rates are reported to the Managing Director and the Board on a monthly basis.
Merger & Acquisition Execution There is a risk that integration of the Clearskincare Clinics and Products businesses into the group is not successful or the projected growth is not achieved.	Detailed plans have been established to address key risks identified during the acquisition due diligence phase. An integration team has been activated. A management structure has been developed to provide long-term guidance and stability for this positive addition to the API Group.
Cyber security and IT systems failure There is a risk that the Group's IT systems are breached by a cyber threat, including customer privacy breaches, or there are major IT system failures that adversely impact the business.	The Group performs regular reviews of all security configurations aligned with current industry standards. There is regular security testing across the entire IT landscape, and protocols in place for regular monitoring and reporting.
Financial Risk The Group has exposure to a number of financial risks including customer payment defaults, financial guarantees supporting Pharmacy customers, and general retail trading conditions.	The Group adopts a financial risk management program which seeks to minimise potential adverse impacts on the financial performance of the Group. The Group has undrawn funding lines throughout the year.

DIRECTORS' REPORT

SUSTAINABILITY REPORT

API is pleased to present the following report on Sustainability in its business. This report is to be read in conjunction with the previous section dealing with material business risks. API's commitment to Sustainability spans the entire business with a focus on:

- caring for its employees;
- serving its customers and community;
- partnering with those who share its values;
- providing quality products and services; and
- protecting its reputation,

all underpinned by the financial resilience of its business.

The following diagram illustrates API's sustainability model.

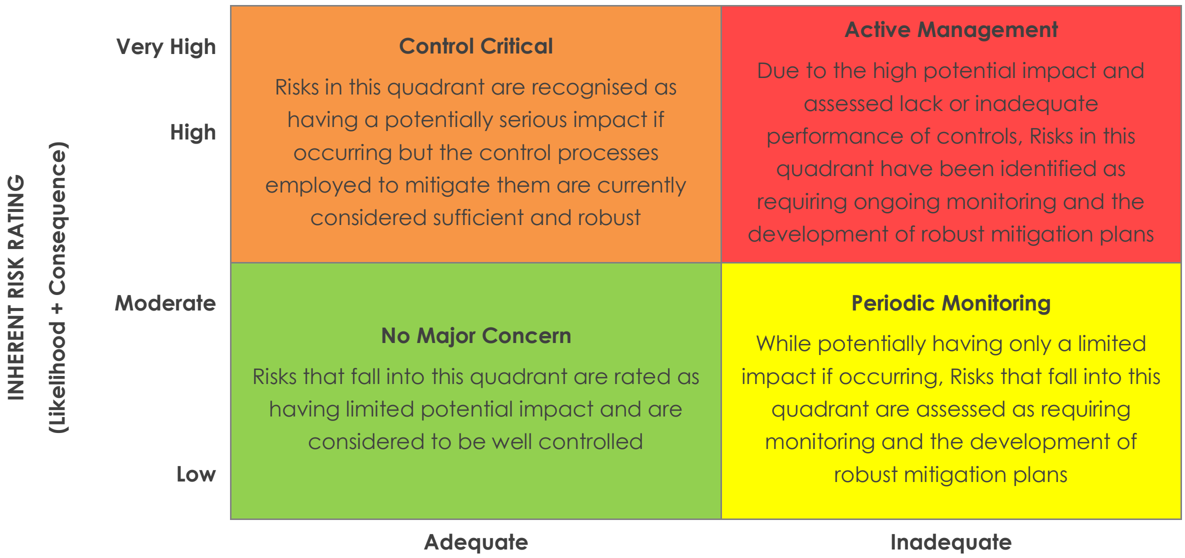
Confidence in our Products	Engaging and caring for our Employees	Serving and sharing with our Customers and Community	Selecting Partners that share our values	Protecting our Reputation
➢ Product quality ➢ Product compliance ➢ Product recalls ➢ Waste ➢ Supply Chain	➢ Safety/health/ wellbeing ➢ Capability ➢ Retention ➢ Diversity	➢ Engagement ➢ Loyalty ➢ Environment	➢ Franchisee suitability ➢ Franchisee engagement	➢ Fraud ➢ Cybersecurity
Financial sustainability ➢ Regulatory changes				

GOVERNANCE

Sustainability issues are managed by the Audit and Risk Committee of the API Board.

Each year, the API Audit and Risk Committee reviews the API Risk Assessment, which considers risks and controls in place in the API business. Key risks are subject to bi-annual Executive review. The Audit and Risk Committee receives regular "deep dives" and presentations by respective risk "owners" on Key Risks, including Sustainability risks.

The following 'Risk Map' illustrates API's approach to risk management, allocating to each material risk an Inherent Risk rating and a Control Effectiveness rating. From these ratings, appropriate risk mitigation plans are developed and implemented.



DIRECTORS' REPORT

SUSTAINABILITY REPORT *(Continued)*

When API acquires new businesses, such as the recent staged acquisition of Clearskincare Clinics and Products business, existing processes and procedures are overlayed into pre-acquisition due diligence and post-acquisition processes of that business, to ensure any new sustainability risks are identified and managed.

MATERIAL SUSTAINABILITY RISKS AND FOCUS

From the Risk Assessment, the material Sustainability risks impacting on API's business are identified. These risks can be summarised as:

- Financial sustainability and impacts of regulatory changes;
- Confidence in its products and services and its impact on the environment;
- Engaging and caring for its employees;
- Serving and sharing with its customers and community;
- Selecting partners that share its values; and
- Protecting its reputation including fraud and cybersecurity.

FINANCIAL SUSTAINABILITY

API's continuing strong financial performance allows the Company to reinvest in the business. API is focussed on financial resilience that can respond to a changing environment with issues such as Government policy and funding, and trends in shopper behaviour. Its strong balance sheet, derived from consistent cash generation, has provided confidence for investors in the long-term health of the Company.

API's strategic planning is focussed on pillars that combine to build financial strength in our core business operations. These pillars are:

- the way we work to deliver a high performance culture which is based in safety, being values driven and innovation;
- what we do in delivering a compelling customer offer and through a focus on execution excellence; and
- delighting customers with the product, services and experience they value.

API's sustainability is affected by the Federal Government's policies on the Pharmaceutical Benefits Scheme (PBS) and the associated Community Service Obligations (CSO) Agreement. Under the CSO, API is recompensed for providing the service of suppling any PBS medicines to any pharmacy in Australia within 24 hours, ensuring that all Australians have access to the full range of the PBS listed medicines.

PRODUCT QUALITY AND SAFETY

When API engages a new supplier, we ensure that its products meet all applicable Australian Laws and Standards and seek an indemnity from the supplier to ensure that API has recourse in the event that products do not meet applicable Australian Standards or need to be recalled.

Where deemed necessary, API will physically inspect new suppliers' manufacturing facilities. API's preference is to source from Australian distributors of overseas products to reduce the risk of poor quality goods.

API's New Zealand manufacturing plants, include a Government approved and audited pharmaceutical facility.

API has a focus on reducing waste, with its Distribution Centres having a recycling program. Further, all Distribution Centres have installed LED lighting to help reduce the impact on the environment. The Company is in the process of moving away from plastic bags in its retail stores.

DIRECTORS' REPORT

SUSTAINABILITY REPORT *(Continued)*

EMPLOYEE ENGAGEMENT

API measures employee engagement with a survey every three to five years. Employee engagement was measured at 63% in 2016, which was considered average compared to benchmark data.

Since the 2016 Engagement survey, API has invested in leadership development and career planning with employees. API has developed five levels of leadership training, from first time leader courses to senior management training.

API plans another Engagement survey in 2020 with the target to improve on the 2016 employee engagement score.

EMPLOYEE RECOGNITION

API has a dedicated reward and recognition program - *We Love Your Work*. Team members are encouraged to nominate their colleagues for outstanding demonstration of Company values of Respect, Initiative, Unity and Excellence and for Safety. Outstanding nominations are recognised quarterly and annual winners are celebrated at an awards night held in November each year.

SAFETY

In 2016, API commenced working to become accredited with the Australian and New Zealand standard for safety management, AS/NZS 4801. The aim was to clearly demonstrate that API has the knowledge of, and control over, all relevant hazards and that the Company could demonstrate its strong commitment to ongoing improvements in its safety performance. API sets out to:

- increase its ability to identify and control safety risk;
- reduce injuries and incidents;
- enhance its reputation as a safe organisation;
- start the process to possible self-insurance; and
- comply with the National Occupational Health and Safety Insurance Audit Tool (NOHSSIAT).

The Company's key areas of focus were:

- **leadership** throughout the business to develop a culture of independent, sustainable Safety Health & Wellbeing (SH&W) practices focusing on Risk Management, Consultation & Communication, and Reporting;
- **process** focusing on Policies & Standards, Safe Work Processes, Training, Induction & On-boarding, and Emergency Preparedness; and
- **workplace** focus on Incident Management, Injury Management, Contractor Management and Auditing.

The following chart illustrates API's Safety, Health and Wellbeing framework.

DIRECTORS' REPORT

SUSTAINABILITY REPORT *(Continued)*

Safety, Health & Wellbeing Framework

Legislative Requirements

All of us. All the time.

Organisational Strategy
A safer place to work every day

SH&W Management System
(Compliant with AS/NZ4801)

Leadership

Supporting **every day leaders** to develop a culture of interdependence and working towards sustainable SH&W practices. Strong **safety leadership** involves active engagement of Team Members and embedding API values into the day to day.

Risk Management
Risk Management is the cornerstone of our SH&W management system and is an integral part of management, culture and day to day operations.

It involves understanding the hazards in the workplace that cause harm, the likelihood of incidents eventuating, and the activities and controls to protect and prevent our Team Members from being injured.

Example: Hazard Identification, Risk Assessments, Incident Investigations

Consultation & Communication
Not only is consultation a legislative requirement, it contributes to a culture of openness, respect and trust. By drawing on the knowledge and experience of Team Members, better decisions can be made to reduce the risk of injuries and incidents. The SH&W Team facilitates effective consultation and the sharing of information, emphasizing active participation by Team Members in dealing with SH&W problems.

Example: SH&W Committees Meetings, Connect, Team Talks, SH&W News Alerts

Reporting
The SH&W Team are responsible for monitoring SH&W performance and reporting to the operational and leadership teams. This drives accountability and responsibility for SH&W objectives across the organisation.

Example: Monthly & Weekly SH&W Reports, Board Report

Process

Continually improving our SH&W Management System to build intelligent processes and effective risk mitigation strategies. This involves intentional planning **activities** aimed at ensuring that operating processes are aligned with SH&W **policies** and **standards**.

Policies & Standards
These documents display API's commitment and what the organisation intends to achieve. They are developed through a consultative process and establish the standards and expectations for our Team Members, processes and workplace.

Example: SH&W Policy, Drug & Alcohol Policy, Risk Management Standard

Safe Work Processes
Across the organisation we continuously develop and follow safe work processes to ensure work tasks are performed safely.

Example: Standard Operating Procedures

Training, Induction & Onboarding
Through training, induction and onboarding we ensure that our Team Members have the right knowledge, qualifications and capabilities to perform tasks safely.

Example: Onboarding , Induction for forklift drivers

Emergency Preparedness
Planning, training and practising responses to emergency situations and enhancing the readiness of our Team Members to respond in actual emergencies.

Example: Emergency Risk Assessment, Evacuation Plans & Exercises

Workplace

All of us, all the time are working toward creating a safe workplace through proactive activities and collaboration with our SH&W Committees. Both the **implementation** and **monitoring** of processes are essential to maintaining a safe working environment.

Incident Management
By learning from incidents that occur, we find the root causes of hazards so that corrective actions can be implemented to prevent it from occurring in the future. This involves reporting, analysing, investigating, and sharing learnings about incidents.

Example: Incident reporting and investigations

Injury Management
Care, support and guidance provided to facilitate the return to work for our injured workers. Early intervention is the key getting our Team Members back to work sooner.

Example: Return to Work Programs

Contractor Management
Our SH&W duties and responsibilities extend to contractors and sub-contractors. The same level of care and due diligence is required.

Example: Contractor Management System, Work Method Statement

Auditing
Audits are conducted to check the effectiveness of our SH&W Management System. At set intervals we examine if the processes perform as intended.

Example: Self-assessments

A safer place to work every day

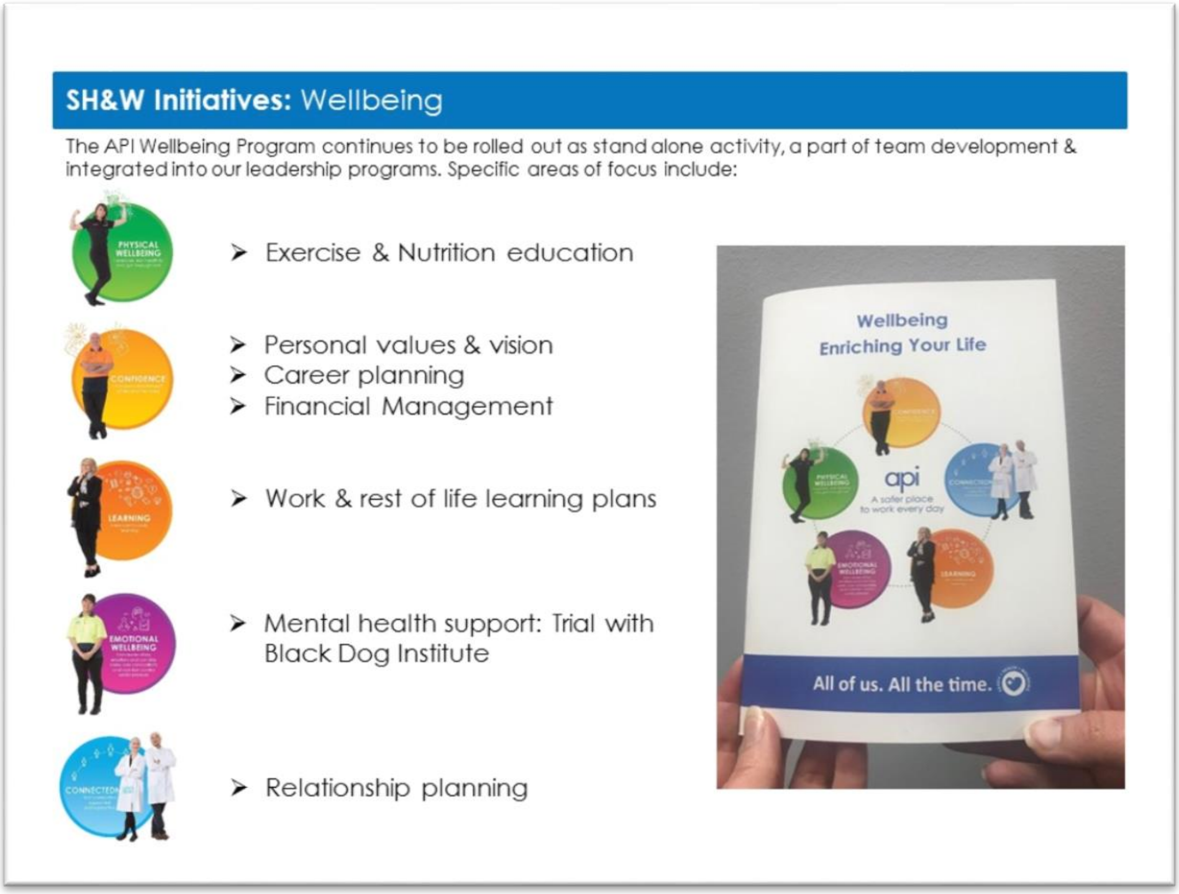
DIRECTORS' REPORT

SUSTAINABILITY REPORT *(Continued)*

AS/NZS 4801 accreditation was achieved in November 2017. The Company's safety results have improved significantly since this process began. Since 2015, the Total Reportable Injury Frequency Rate (TRIFR) has reduced by 60%, with the most significant decrease in medically treated injury rate by 70%.

However, despite the reduction since 2015, this year saw an increase in mental health issues reported in its results. Initiatives to address this such as a trial of mental health support through the Black Dog Institute and a focus on training for its leaders are part of API's focus on Wellbeing in its workforce. There are five areas of focus:

- Physical wellbeing, with exercise and nutrition education;
- Confidence building with a focus on personal values and visions, career planning, and financial management;
- Learning;
- Emotional wellbeing with a trial of mental health support through the Black Dog Institute; and
- Connectedness.



DIRECTORS' REPORT

SUSTAINABILITY REPORT *(Continued)*

TARGETS AND MEASUREMENT

API measures safety through both leading and lag indicators. Leading indicators include safety scans and hazard reporting, hazard closure rates, and safety business plan implementation. These indicators build on its 2017 accreditation to AS/NZS 4801 standard. API believes that this focus on the inputs into safety will lead to improvements in lagging indicators.

Lagging indicators include injury rates, both medically treated and lost time injuries. API has set a challenging goal to reduce Lost Time and Medically Treated Injury Frequency rates by 10% year on year.

The next step is to become compliant with the National Occupational Health and Safety Self Insurance Audit Tool (NOHSSIAT). This step will not only further improve its safety performance, but will also give API the ability to target self-insurance should it choose to. To achieve compliance, API will work on the 108 criteria over the next three years.

The following table is a summary of key indicators and objectives in improving API's Safety, Health and Wellbeing targets.

DIVERSITY AND GENDER

API sees gender diversity as a key driver of growth and is committed to ensuring diversity across the entire Company.

Across API, women make up 63.5% of its managers, with 52% of its promotions being women in the 2018 financial year, a slight increase on the prior year.

API is committed to improving gender diversity on its Board, which currently sits at 28.6%. The API Board has two female directors and 5 male directors, including the CEO. As Board vacancies arise, API is committed to increasing the female representation on its Board. In this context, the Board has committed to the objectives of the 30% Club, and the Australian Institute of Company Directors target for 30% female directors.

The following table is a summary of API's progress is achieving female diversity in its workforce and on its Board.

	FY15	FY16	FY17	FY18
Women on the Board	28.6%	28.6%	28.6%	28.6%
Women in senior leadership team	37.5%	20.0%	22.2%	20.0%
Women in management positions	59.4%	59.4%	68.5%	63.5%
Women in workforce	77.1%	77.1%	81.7%	78.6%
Promotions – women	NA	80.5%	50.0%	52.0%
Manager promotions - women	NA	82.6%	43.5%	48.5%

Source: API reports to Workforce Gender Equality Agency

ITS PARTNERS SHARING ITS VALUES

FRANCHISEES

Due to Federal Government regulations requiring pharmacist only ownership of the dispensary, each Priceline Pharmacy is franchised by pharmacists with the API Group.

Pharmacists are selected on the basis of stringent criteria, who share the API values and who are committed to operating the franchise in compliance with all applicable laws, including the recently enacted vulnerable workers legislation.

Each year API uses an independent survey of its franchisees to gauge their level of advocacy, commitment and engagement to the franchise. The survey assesses both the view of company performance and issues such as work-life balance for franchise partners. The results suggest its franchise partners are happy to advocate the franchise to others, committed to staying for the long-term, and are enthusiastically engaging with brand initiatives. In 2018 franchise partner sentiment improved relative to the prior year.

DIRECTORS' REPORT

SUSTAINABILITY REPORT *(Continued)*

THE PRICELINE SISTERHOOD FOUNDATION

The Priceline Sisterhood Foundation was initiated in 2011 and was formally established in 2014, as an independent incorporated Foundation that can receive tax deductible donations. It has its own Board of Directors, with the API CEO as its Chairman. The Board includes independent directors, in addition to API executives.

The Priceline Sisterhood Foundation has a set of selection criteria and principles for deciding on its charity partners. These selection criteria include:

- Alignment with women and their families' wellbeing;
- Promote principles of equity and diversity;
- "Real Need" charities and proposals – financial dependency on fundraising and volunteer pro bono ethics and not necessarily charities that receive large Government or Corporate funding;
- Preference for Australian focus (city and regional); and
- No conflicts (e.g. alcohol, tobacco, gambling).

Based on these criteria, the Priceline Sisterhood Foundation recently added the Raise Foundation as a charity partner. The Raise Foundation provides youth mentoring programs and personal development workshops for vulnerable young Australians facing profound challenges in their lives. This includes mental health issues, teen pregnancy/young parent families, sexual health issues or challenging home environments.

The Priceline Sisterhood Foundation is registered with the Australian Charities and Not-for-profits Commission (ACNC) and is compliant with all ACNC requirements.

PROTECTING ITS REPUTATION

CYBERSECURITY AND FRAUD

API understands the importance of privacy and data protection. The Company has internal policies and procedures in place that highlight the importance of data protection within API. API has dedicated staff that can deal with any mandatory reporting of data breaches.

The Company has a strong internal audit process in place with fraud controls regularly assessed.

DIRECTORS' REPORT

OTHER MATTERS

INSURANCE AND INDEMNIFICATION OF DIRECTORS AND OFFICERS

During the year the Company paid a premium in respect of a contract insuring the Directors and officers against all liabilities to another person, other than the Company or a related body corporate, that may arise from their position, except where the liability arises out of conduct involving a lack of good faith.

The contract covers any past, present or future Director, Secretary, Executive Officer or employee of the Company and the Group. Further details have not been disclosed due to confidentiality provisions of the contract of insurance. The Directors are each parties to a Director's Access, Indemnity and Insurance Deed. This Deed includes an indemnity by the Company (subject to and to the fullest extent permitted by applicable law) summarised as follows:

a) for any liability incurred by the Director as an officer of the Company;

b) for legal costs incurred by the Director in defending proceedings for a liability incurred as an officer of the Company, or in seeking relief from that liability under applicable law; and

c) for any liability for legal costs incurred by the Director in connection with legal proceedings of a Government or Regulatory authority which is brought against the Director because of their present or former capacity as on officer of the Company.

ENVIRONMENTAL REGULATION

The operations of the Group are subject to environmental regulation under Commonwealth, State and New Zealand Government legislation in relation to its manufacture of pharmaceutical products, retail stores and pharmaceutical distribution facilities. In respect of:

- Pharmaceutical and toiletries product manufacture – manufacturing plants operate under licence requirements relating to waste disposal, water and air pollution; and
- Wholesale distribution – distribution facilities operate under licence requirements relating to waste disposal, water and air pollution.

The Board believes that the Group has adequate systems in place for the management of its environmental requirements and is not aware of any significant breach of the environmental requirements as applied to the Group.

CORPORATE SOCIAL RESPONSIBILITY

The Group has continued its involvement with the Priceline Sisterhood Foundation. More information can be found in the preceding sustainability report.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

There were no significant changes in the nature of the activities of the Group during the year, other than the acquisition of the Clearskincare Clinics and Products business on 31 July 2018.

DIVIDENDS

A dividend was paid during the year ended 31 August 2018 in respect of the year ended 31 August 2017 on 8 December 2017. The dividend was at the rate of 3.5 cents per share, fully franked and totalled $17.229 million.

An interim dividend of 3.5 cents per share amounting to $17.235 million, fully franked in respect of half year ended 28 February 2018 was paid out of Profit Reserves on 1 June 2018.

LIKELY DEVELOPMENTS

The Group will continue to pursue its policy of improving the profitability and market share of each of its major operating businesses during the next financial year, including delivering on the strategies and initiatives outlined in the operating and financial review.

DIRECTORS' REPORT

OTHER MATTERS *(CONTINUED)*

Further information regarding the business strategies of the Group and the expected results of those operations in future financial years have not been included in this report as disclosure of this information would likely result in unreasonable prejudice to the Group.

NON-AUDIT SERVICES

During the year KPMG, auditors of the Group, have performed certain other services, mainly financial and tax due diligence services relating to the acquisition of the Clearskincare Clinics and Products business, in addition to their statutory duties.

The Board has considered the non-audit services provided during the year by the auditor and in accordance with written advice provided by resolution of the Audit and Risk Committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the Corporations Act 2001 for the following reasons:

- All non-audit services were subject to the corporate governance procedures adopted by the Company and have been reviewed by the Audit and Risk Committee to ensure they do not impact the integrity and objectivity of the auditor; and
- The non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 Code of Ethics for Professional Accountants, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision making capacity for the Company, acting as an advocate for the Company, or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Group, KPMG, and its related practices for audit and non-audit services provided during the year are set out in Note 23 to the financial statements.

The Board reviews and approves any non-audit services provided by the auditor having regard to market benchmarks and ensuring that the provision of these services delivers value efficiencies to the benefit of shareholders and does not impact the independence of the audit.

LEAD AUDITOR'S INDEPENDENCE DECLARATION

The Lead Auditor's Independence Declaration is set out on page 33 and forms part of the Directors' report.

The Company is of a kind referred to in ASIC Corporations Instrument 2016/191 dated 24 March 2016 and in accordance with that Class Order, amounts in the consolidated financial report and Directors' Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

Dated at Sydney, 17 October 2018

Signed in accordance with a resolution of the Directors:

Mark G Smith

Mark Smith

Chairman

DIRECTORS' REPORT

REMUNERATION REPORT

OVERVIEW OF REMUNERATION FOR FY 18

A summary of the matters impacting the Group's remuneration structure and strategy for FY18 are:

- No changes to the Short Term Incentive Plan (STIP) or the Long Term Incentive Plan (LTIP) have been made during the financial year.
- The financial performance of the Group for FY18 did not meet the minimum requirement for any STIP payments. Accordingly, no member of the Key Management Personnel (KMP) will receive an STI award in respect of FY18.
- The three year performance period for the 2015 LTIP ended on 31 August 2018. Vesting was subject to an aggregate Return on Equity (ROE) hurdle and an Earnings Per Share (EPS) Compound Annual Growth Rate (CAGR). The performance conditions were tested and audited with the following outcomes:
    - actual aggregate ROE for the performance period was 27.83% for an achievement of 34.4% of half the grant; and
    - actual CAGR EPS was 3.42% for an achievement of 0% of the other half of the grant.
    - The combined achievement of the 2015 LTIP for performance measured over a 3 year period resulted in 17.2% of the total grant vesting.

REMUNERATION SUMMARY – 'TAKE HOME PAY'

The table below shows the key elements of total reward received by each KMP for FY18. This includes the cash component elements paid to each executive for the year as well as the value of equity that has vested for services provided to 31 August 2018, and equity from previous years that vested in FY18 which was originally reported in accordance with the accounting standards in the year the equity was granted.

Executive	Fixed Remuneration	STI paid in FY18		LTI vested(i)	Total Remuneration Received
		Cash STI(ii)	Deferred STI(iii)		
In AUD ($)					
Mr R Vincent – Managing Director and Chief Executive Officer					
	1,061,667	3,085	66,104	359,658	1,490,514
Mr P Mendo – Chief Financial Officer					
	485,666	2,345	50,261	-	538,272

(i) Consists of the total cash value of the Performance Rights vested during FY18. These related to the 2014 grant, for which 239,772 shares were issued to Mr Vincent on 3 November 2017. The share price on that date was $1.50. This does not represent the statutory expense recognised in the profit and loss. The expense was recognised over a three year period in accordance with AASB 2 Share Based Payments.

(ii) STIP cash payment for Mr Vincent and Mr Mendo relates to payment in lieu of the dividend entitlements relating to the deferred FY2016 STIP equity.

(iii) Represents the vesting of the deferred 2016 STIP Performance Rights. 44,069 shares were issued to Mr Vincent and 33,507 shares were issued to Mr Mendo on 3 November 2017. The share price was $1.50 per share on that date. This does not represent the statutory expense recognised in the profit and loss.

A full breakdown of executive remuneration details has been prepared in accordance with statutory requirements and accounting standards. This detailed disclosure including statutory tables is included in Section 2 of the Remuneration Report.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

REMUNERATION REPORT – AUDITED

This report details the processes used in remuneration decisions and their outcomes for Key Management Personnel (KMP) for the 2018 financial year (FY18) and is prepared in accordance with Section 300A of the Corporations Act 2001 (as amended) for the Company and its subsidiaries.

KEY MANAGEMENT PERSONNEL

As defined under AASB 124, KMP have the authority and responsibility for planning, directing and controlling the activities of the Group, and comprise:

1. Non-executive Directors;
2. Managing Director and Chief Executive Officer; and
3. Chief Financial Officer.

NON-EXECUTIVE DIRECTOR KMP

Mark Smith	Chairman
Lee Ausburn	Director
Gerard Masters	Director
Robert Millner	Director
Kenneth Gunderson-Briggs	Director
Jennifer Macdonald	Director
Peter Robinson	Chairman and KMP for the period 1 September 2017 until retirement on 24 January 2018

EXECUTIVE KMP

Richard Vincent	Managing Director and Chief Executive Officer (appointed 15 February 2017)
Peter Mendo	Chief Financial Officer

This report has been audited by the Company's Auditor, KPMG as required by Section 308(3C) of the Corporations Act 2001.

The Remuneration Committee is governed by its Charter (available on www.api.net.au) which was developed in line with ASX Corporate Governance Principles and Recommendations. The Charter specifies the purpose, authority, membership and activities of the Remuneration Committee, and the Charter is annually reviewed by the Committee to ensure it remains consistent with regulatory requirements.

Membership of the Committee consists of Non-executive Directors. During the year members of the Committee were Mr Gerard Masters (Chairman), Mr Robert Millner and Mr Kenneth Gunderson-Briggs.

The Remuneration Report is in sections as follows:

Section 1 Non-executive Director KMP Remuneration

A. Policy and Principles
B. Remuneration of Directors (excluding the Managing Director and CEO)

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

Section 2 Executive Remuneration including the Managing Director and CEO

A. Policy and Principles
B. Remuneration Structure
C. Short Term Incentive Plan
D. Long Term Incentive Plan
E. Employment Contracts
F. Remuneration of Executives including the Managing Director and CEO

Section 3 Other matters required by Section 300A Corporations Act 2001

A. Movement in shares held by the KMP
B. Comments on Remuneration Report at the most recent AGM of the Company
C. Engagement of Remuneration Consultant
D. Related party transactions

SECTION 1 NON-EXECUTIVE DIRECTOR KMP REMUNERATION

A Policy and Principles

Non-executive Directors' fees are determined within an aggregate fee pool limit. An annual total fee pool of $1,200,000 was approved by shareholders at the 25 January 2017 Annual General Meeting. Total Non-executive Directors remuneration including Board Committee fees, non-monetary benefits and superannuation paid at the statutory rate for the year ended 31 August 2018 was $808,322. The average increase per Director was 3%. The total amount excludes the $220,000 retirement benefit paid to Peter Robinson under the Directors' Retirement Scheme (details below).

The remuneration of Non-executive Directors is determined having regard to the data provided by independent remuneration consultants, the need to attract and retain appropriately qualified Directors, fee levels applied in similarly sized companies, and board judgement as to whether any adjustments are appropriate. Non-executive Directors do not receive performance related remuneration.

Under the Board's Retirement Scheme, which was approved by Shareholders at the 1994 AGM, retiring Non-executive Directors are paid on a pro-rata basis up to ten (10) years' service to a maximum of three (3) times the average annual remuneration in the three (3) years preceding retirement. The retirement benefit is capped at $220,000 per Director and applies only to Directors appointed prior to 9 September 2003. The Directors have agreed to freeze this benefit as at 31 August 2009. During the year, Peter Robinson retired and received this benefit.

Annual Board fees (including superannuation) were structured as follows, with effect from 1 January 2018:

Role	Annual Fee Structure
Board chairman	$216,300
Board member	$92,700
Audit and Risk Committee chair	$35,000
Audit and Risk Committee member	$8,240
Remuneration Committee chair	$16,480
Remuneration Committee member	$8,240
Nomination Committee chair	(no fee)
Nomination Committee member	(no fee)
Senior Independent Director	$15,450

The Board Chairman does not receive Committee fees.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

B Remuneration of Directors (excluding the Managing Director and CEO)

Name	Year	Short term benefits ($)		Post-employment benefits ($)		Total remuneration ($)
		Director fees	Project remuneration	Retirement benefits	Superannuation benefits	
Mark Smith(i)	**2018**	**153,640**	**-**	**-**	**14,409**	**168,049**
	2017	-	-	-	-	-
Robert D. Millner	**2018**	**91,288**	**-**	**-**	**8,672**	**99,960**
	2017	86,692	-	-	8,236	94,928
Lee Ausburn	**2018**	**91,288**	**-**	**-**	**8,672**	**99,960**
	2017	86,692	-	-	8,236	94,928
Gerard J. Masters	**2018**	**98,700**	**-**	**-**	**9,380**	**108,080**
	2017	93,605	-	-	8,893	102,498
Ken Gunderson-Briggs	**2018**	**134,788**	**16,393(v)**	**-**	**14,362**	**165,543**
	2017	116,382	-	-	11,056	127,438
Jennifer Macdonald(ii)	**2018**	**74,337**	**-**	**-**	**7,063**	**81,400**
	2017	-	-	-	-	-
Peter R. Robinson(iii)	**2018**	**76,810**	**-**	**220,000**	**8,520**	**305,330**
	2017	181,279	-	-	17,222	198,501
E. Carol Holley(iv)	**2018**	**-**	**-**	**-**	**-**	**-**
	2017	43,924	-	-	4,173	48,097

(i) For period 6 September 2017 (date of appointment) until 31 August 2018.
(ii) For period 9 November 2017 (date of appointment) until 31 August 2018.
(iii) For period 1 September 2017 until 24 January 2018 (date of retirement).
(iv) For period 1 September 2016 until 25 January 2017 (date of retirement).
(v) Remuneration as chair of the Board committee for merger and acquisition activities during the year.

SECTION 2 EXECUTIVE REMUNERATION INCLUDING THE MANAGING DIRECTOR AND CEO

A Policy and Principles

The remuneration strategy of API is to:

- Offer a remuneration structure that will attract, focus, retain and reward highly capable people;
- Ensure that remuneration decisions are based on a fair and transparent job evaluation process that is linked to comparable market data and the experience of the individual in the position;
- Have a clear and transparent link between performance and remuneration outcomes;
- Encourage and integrate risk management within the reward framework; and
- Build employee engagement and align management and shareholder interests through the ownership of Company shares.

Executive remuneration is set with regard to the size and nature of the position with reference to market median benchmarks and the performance of the individual.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

The total remuneration of an Executive will incorporate variable "at risk" elements to:

- Link Executive reward with the achievement of the business objectives and financial performance of the Group; and
- Ensure total remuneration is competitive by market standards.

The role of the Remuneration Committee includes reviewing and making recommendations to the Board on Executive remuneration. The Remuneration Committee may seek independent advice on the appropriateness of remuneration levels. The Remuneration Committee is authorised to seek advice if and when required.

B Remuneration Structure

The Executive Remuneration Framework as it applies to the Managing Director and CEO, and Executives comprises:

- Fixed Remuneration; and
- Performance linked remuneration in the form of STIP and LTIP opportunities.

Fixed Remuneration

Fixed remuneration is a guaranteed salary level inclusive of any Fringe Benefits Tax (FBT), charges related to employee benefits including motor vehicles and employer contributions to superannuation funds.

Fixed remuneration levels are reviewed annually and set with regard for each position and the median market level for comparable roles. Any adjustment needs to also consider individual segment results and overall performance of the Group. In addition, external consultants provide analysis and advice to ensure that Executive remuneration is appropriate in the context of market practice and stakeholder expectations.

At Risk Remuneration

Performance linked remuneration includes both short term and long term incentives and is designed to reward KMP for meeting or exceeding their financial and non-financial objectives. The short term incentive is provided in the form of a cash payment and deferred rights to acquire shares while the long term incentive is provided as rights to acquire shares. Rights to acquire shares are termed as "Performance Rights".

The Group has a policy prohibiting recipients of share-based payments from entering into arrangements to hedge their exposure to losses arising from share price decreases. Entering into such arrangements has been prohibited by law since 1 July 2011.

C Short Term Incentive Plan

The STIP is an annual at risk incentive plan for Executives and certain other senior employees.

The objectives of the STIP are:

- Provide a clear link between individual and organisational performance and executive reward;
- Reinforce the link between individual, team and Company performance;
- Reinforce the interdependencies between business units and functions;
- Align the interests of Executives who are most able to positively impact profitability; and
- Drive a high performance leadership culture.

Prior to the start of the financial year the Remuneration Committee makes a recommendation to the Board for approval of the maximum STIP pool.

Prior to any payment under the STIP, Company performance must pass a minimum gateway requirement of Group Net Profit After Tax (NPAT).

At the start of each year the Remuneration Committee sets a 'scorecard' of performance conditions for the STIP as follows:

- NPAT; and
- Other financial and non-financial measures tailored for each business segment.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

Other performance measures vary by business segment, however each scorecard includes a measure related to Earnings Before Interest and Tax (EBIT), Return on Capital Employed (ROCE) and individual performance measures. Multiple measures of performance help diversify risk.

Each year, the Board establishes NPAT performance hurdles at which threshold, target and maximum STIP entitlements will be payable. The current practice is that the minimum STIP pool is established at 90% of NPAT budget (being the NPAT gateway), the target STIP pool is at budget and the maximum STIP pool is achieved at 110% of budget.

After the conclusion of the financial year, the Board assesses performance against Group and Segment Scorecards with 80% of the maximum percentage based on key financial objectives and 20% based on individual objectives. Prior to any consideration of a STIP payment, the Company must meet a minimum NPAT performance. The Board has discretion for a STIP payment where achievement is 90% of target NPAT levels.

Fifty percent of any STIP awarded to the Executive Leadership Team is deferred for 12 months in the form of performance rights. Performance rights are exercised for fully paid shares after the 12 months deferral period. In addition, participants will be eligible to receive at the time of vesting a cash payment equal to the dividends paid during the 12 month vesting period on shares resulting from the exercise of rights at vesting.

The number of performance rights is determined by dividing the value of the deferred component of the STIP award by the volume weighted average closing price of API shares on the ASX in the 10-day period after announcement of full year results of the initial grant year.

The deferred component of the STIP award is designed to manage risk by ensuring that decisions taken in the previous 12 months have resulted in sustainable Company benefit. The Board has the discretion to forfeit any unvested rights due to excessive risk taking, material misstatement of financial statements or fraudulent or gross misconduct.

More broadly, the Board retains absolute discretion over all awards made under the incentive award plans, including the STIP.

Managing Director and Chief Executive Officer

The Managing Director and CEO's STIP is equal to 32.5% of his fixed remuneration at threshold, 65% of fixed remuneration at target, and if NPAT is 110% or more of budget, the STIP provides for a maximum payment of 100% of fixed remuneration.

The STIP scorecard is determined by the Board each year and is drawn from financial measures such as NPAT, Return on equity (ROE) and Return on Capital Employed (ROCE). Non-financial measures may include retail sales growth, Priceline Pharmacy network growth, pharmacy distribution market share and improvement targets relating to workplace safety.

The performance measures and weightings for FY18 were as set out below.

Performance measure	Weighting
NPAT and ROCE	60%
Operational performance	25%
Safety performance (LTIFR)	5%
Succession	5%
Strategic projects	5%

The NPAT result for FY18 did not exceed the NPAT gateway and accordingly the Board did not approve a STIP award for the Managing Director and CEO.

Other Executive KMP

The STIP award at threshold for other Executive KMP STIP is equal to 10% of fixed remuneration, 20% of fixed remuneration at target and if NPAT is 110% or more of budget, the STIP provides for a maximum payment of 40% of fixed remuneration. The Remuneration Committee recommends to the Board, the financial measures for Executive KMP STIP which includes NPAT and ROCE.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

The following table summarises the basis of the calculation of the STIP award for Executive KMP.

	NPAT gateway	Financial Measure 1 40% weighting	Financial Measure 2 40% weighting	Personal Measure 20% weighting
Target	90% of NPAT Target	Business unit EBIT	Company ROCE Target	Individual Targets

The NPAT result for FY18 did not exceed the NPAT gateway and accordingly the Board did not approve a STIP award for other Executive KMP.

D Long Term Incentive Plan

The Remuneration Committee has responsibility for the Long Term Incentive Plan (LTIP). The Plan was established during the year ended 30 April 2006. The Remuneration Committee is responsible for awards granted under the Plan and overseeing administration of the Plan. The LTIP involves the grant of rights to acquire fully paid ordinary shares in API for no consideration.

The key features and implications of the LTIP are:

- Performance rights ("Rights") are granted to the Managing Director and CEO (which are subject to shareholder approval at the Annual General Meeting) and to certain Executives as soon as practicable after the full year results are announced. This ensures the allocation of Rights reflects the best informed assessment by the market of Company value and share price;
- The number of Rights granted is derived by dividing the participant's LTIP value by the 10-day Volume Weighted Average Closing Price (VWAP) of API shares immediately after announcement of full year results – that is, the 'face value' methodology;
- Vested Rights convert to API shares on a one-for-one basis. No dividends are received by Executives on unvested rights during the vesting period;
- If performance conditions are not fully met, the Rights lapse;
- The LTIP provides for shares to be purchased on market on behalf of the participant or new shares issued by the Company;
- Performance conditions will be tested only once and any Rights that do not meet the performance conditions will lapse and will not be re-tested;
- The Company has a policy prohibiting Directors and employees from dealing in financial products issued or created over or in respect of securities (e.g. hedges or derivatives) that have the effect of reducing or eliminating the risk associated with any equity incentives that may be offered from time to time;
- If an LTIP participant ceases to be employed before the end of the Performance Period for reasons other than redundancy, death, disability or illness, the Rights will automatically lapse, subject to Board discretion. If a participant ceases to be employed, before the end of the Performance Period and the date of employment ceasing is on or after the first anniversary date of the Commencement Date, due to redundancy, death, disability or illness, the number of Rights will be reduced pro-rata to reflect the length of time during the Performance Period the employee was employed;
- More broadly, the Board retains absolute discretion over all awards made under the incentive award plans, including the LTIP;
- Grants made include a target measure of three year EPS CAGR and the cumulative ROE achieved by the Group during the three year period commencing at the beginning of the performance period when compared to the target ROE set by the Board for the same period (Target ROE) measure. Each of the two measures (EPS and ROE) contribute equally to a LTIP award. If ROE is achieved and EPS is not achieved, or vice versa, then the total available award is halved. This means 50% of the award is dependent on the ROE metric, and 50% of the award is dependent on the EPS metric. ROE is expressed as a percentage created

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

by dividing NPAT for the relevant financial period by total shareholder equity for the relevant financial year. Target ROE is derived from the Corporate Plan for the three years commencing at the beginning of the performance period. EPS is derived from the Corporate Plan for the three years commencing at the beginning of the performance period. The EPS performance condition compares the actual EPS growth achieved during a three year performance period, against the target amount of EPS growth set by the Board. The EPS is the basic earnings per share disclosed in the Consolidated income statement of the Financial Statements. The initial benchmark EPS that serves as the basis for calculating EPS growth, and the target EPS may be varied by the Board in its absolute discretion;

- In determining whether the LTIP awards will vest the Board will have regard for a range of factors to ensure alignment to long-term overall Company performance and is consistent with:
  - strategic business drivers; and
  - long term shareholder return.

  Subject to commercial sensitivity, the Board intends to provide full details of performance against specified hurdles upon those conditions being tested and upon vesting of the relevant rights; and
- The value of the LTIP awarded to Executive KMP is:
  - Managing Director and CEO: equal to 60% of Fixed Remuneration;
  - Other Executives: 30% of Fixed Remuneration.

2015 grant

On 13 January 2016, performance rights (the "2015 Grant") were granted with a performance period commencing on 1 September 2015 and ending 31 August 2018. The performance conditions, being ROE and EPS CAGR for the exercise of performance rights were assessed after the results for the period were finalised with the following outcomes:

- actual aggregate ROE for the performance period was 27.9% resulting in 34.4% of this tranche vesting; and
- actual EPS CAGR was 3.4% resulting in 0% of this tranche vesting.
- The combined achievement of the 2015 LTIP is 17.2% of the opportunity.

2016 grant

On 1 February 2017, performance rights (the "2016 Grant") were granted with a performance period commencing on 1 September 2016 and ending 31 August 2019. Shareholder approval for any LTIP performance rights to be offered to Mr Vincent in the role of Managing Director and CEO was received at the January 2018 Annual General Meeting.

The performance conditions, being ROE and EPS CAGR for the exercise of performance rights will be assessed after 31 August 2019 once the results are finalised.

The ROE performance condition has the effect that:

- if a cumulative ROE of 26.96% is achieved for the three year period, 20% of the Rights subject to the ROE Performance Condition will vest;
- if a cumulative ROE of 43.81% is achieved for the three year period,100% of the Rights subject to the ROE Performance Condition will vest; and
- if the cumulative ROE is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

The EPS CAGR performance condition has the effect that:

- if CAGR of 7.5% is achieved for the three year period, 20% of the Rights subject to the CAGR Performance Condition will vest;
- if a CAGR of 10.0% is achieved for the three year period, 100% of the Rights subject to the CAGR Performance Condition will vest; and
- if the CAGR is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

2017 grant

On 29 January 2018, performance rights (the "2017 Grant") were granted with a performance period commencing on 1 September 2017 and ending 31 August 2020.

Shareholder approval for any LTIP performance rights offered to Mr Vincent in the role of Managing Director and CEO was received at the January 2018 AGM.

The performance conditions, being ROE and EPS CAGR for the exercise of performance rights will be assessed after 31 August 2020 once the results are finalised.

The ROE performance condition has the effect that:

- if a cumulative ROE of 24.32% is achieved for the three year period, 20% of the Rights subject to the ROE Performance Condition will vest;
- if a cumulative ROE of 39.52% is achieved for the three year period,100% of the Rights subject to the ROE Performance Condition will vest; and
- if the cumulative ROE is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

The EPS CAGR performance condition has the effect that:

- if CAGR of 7.5% is achieved for the three year period, 20% of the Rights subject to the CAGR Performance Condition will vest;
- if a CAGR of 10.0% is achieved for the three year period, 100% of the Rights subject to the CAGR Performance Condition will vest; and
- if the CAGR is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

E Employment Contracts

The Company has entered into Executive Service Agreements ("agreements") with Executive KMP. These agreements outline the components of remuneration to be paid. Remuneration levels are reviewed each year to take into account any change in the scope of the role performed, and any other changes required to meet the principles of the remuneration policy.

The employment conditions and remuneration of the KMP are formalised in the agreements. No fixed terms are specified within the agreements and the following termination provisions apply:

- Mr Vincent may resign from the Company by giving three months written notice. The Company may terminate Mr Vincent's agreement without cause by providing twelve months written notice, or making a payment in lieu of the notice period. The agreement provides for a non-compete restriction of up to twelve months after cessation of employment.
- Peter Mendo may resign from the Company by giving six months written notice. The Company may terminate Mr Mendo's agreement without cause by providing six months written notice, or making a payment in lieu of the notice period. The agreement provides for a non-compete restriction of up to six months after cessation of employment.

The Company may summarily terminate the KMP's employment in specified circumstances with immediate effect and no termination benefits will apply other than accrued entitlements.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

F Remuneration of Executives including the Managing Director and CEO

Details of the nature and amount of each major element of remuneration of each of the Key Management Personnel of the Group (including the Chief Executive Officer) are as follows:

	Short Term										
	Salary and Fees Cash -Short-term incentive	Cash -Short-term incentives(iv)	Total	Post-employment Superannuation contributions	Long Service Leave	Final benefits	Equity Value of rights granted under STIP	Equity Value of rights granted under LTIP(i)	Total	Proportion of remuneration performance related	Value of rights as proportion of remuneration (%)
EXECUTIVES	$	$	$	$	$	$	$	$	$	%	%
Mr R Vincent – Managing Director and CEO(ii)											
31 August 2018	1,041,537	3,085	1,044,622	20,129	25,780	-	-	124,330	1,214,861	10.5	10.2
31 August 2017	871,917	-	871,917	19,688	114,808	-	41,866	227,028	1,275,307	21.1	21.1
Mr S Roche – Managing Director and CEO(iii)											
31 August 2018	-	-	-	-	-	-	-	-	-	-	-
31 August 2017	466,282	-	466,282	19,288	12,623	986,988	198,896	316,655	2,000,732	25.8	25.8
Mr P Mendo – Chief Financial Officer											
31 August 2018	463,161	2,345	465,506	20,129	1,270	-	-	(17,362)	469,543	(3.2)	(3.7)
31 August 2017	439,013	-	439,013	19,688	4,775	-	31,832	87,749	583,057	20.5	20.5

(i) The value of performance rights is calculated at grant date using the Black-Scholes Option Pricing model. The value is allocated to each reporting period evenly over the performance period.

(ii) Mr Vincent commenced as Managing Director and CEO on 15 February 2017. His 2017 remuneration includes remuneration for his previous role as KMP, as well as his new role as the Managing Director and CEO.

(iii) Mr Roche's ceased being a KMP on 15 February 2017. His final benefits were in consideration of entitlements due under his Executive Service Agreement and calculated based on an average of the last three years' Total Employee Compensation (TEC). In addition, Mr Roche was paid accrued leave entitlements.

(iv) STIP cash payment for Mr Vincent and Mr Mendo relates to payment in lieu of the dividend entitlements relating to the deferred FY2016 STIP equity.

Analysis of Performance Rights over Equity Instruments granted as Compensation

Details of the performance rights awarded as remuneration to each Executive KMP are below.

Executive	Tranche	Number	Fair value - per share $	Total value $	Included in FY18 remuneration $	As at the date of this report % vested %	% forfeited (i) %
Richard C. Vincent							
	2015 LTIP	99,180	1.82	180,508	(89,291)	17.2%	82.8%
	2016 LTIP - in previous role	44,877	1.68	75,393	5,931	0.0%	0.0%
	2016 LTIP - as CEO	177,895	1.81	321,990	25,330	0.0%	0.0%
	2017 LTIP	402,264	1.36	547,079	182,360	0.0%	0.0%
Peter Mendo							
	2015 LTIP	75,410	1.82	137,246	(67,891)	17.2%	82.8%
	2016 LTIP	75,000	1.68	126,000	9,912	0.0%	0.0%
	2017 LTIP	92,311	1.32	121,851	40,617	0.0%	0.0%

(i) The % forfeited in the year represents the reduction from the maximum number of performance rights available to vest due to the performance criteria not being achieved.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

LTIP summary

- LTIP performance rights were granted on 13 January 2016 with a performance period commencing on 1 September 2015 and ending 31 August 2018 (the 2015 grant). The performance conditions for the exercise of performance rights were assessed resulting in 17.2% of the grant vesting. The fair value of the performance rights is dependent upon the ROE and EPS performance conditions for the entire grant and is $1.82 per share.
- LTIP performance rights were granted on 1 February 2017 with a performance period commencing on 1 September 2016 and ending 31 August 2019 (the 2016 grant). The performance conditions for the exercise of performance rights will be assessed shortly on or after the year ending 31 August 2019. The fair value of the performance rights is dependent upon the ROE and EPS performance conditions for the entire grant and is $1.68 per share.
- LTIP performance rights were granted on 29 January 2018 with a performance period commencing on 1 September 2017 and ending 31 August 2020 (the 2017 grant). The performance conditions for the exercise of performance rights will be assessed shortly on or after the year ending 31 August 2020. The fair value of the performance rights is dependent upon the ROE and EPS performance conditions for the entire grant and is $1.32 per share.

STIP summary

- Performance rights relating to the STIP program commencing on 1 September 2015 and ending 31 August 2016 were granted on 7 November 2016. The performance rights were valued at $1.90 per share reflecting the volume weighted average closing price of API shares on the ASX in the 10-day period after announcement of full year 31 August 2016 results. These rights fully vested and were satisfied by the issue of fully paid ordinary shares in the Company on 3 November 2017.
- The performance rights were provided at no cost to the recipient.
- No STIP was approved for FY17 and FY18.

Performance rights over equity instruments

The movement during the reporting period in the number of performance rights held directly or beneficially, by each KMP, including their related parties, is as follows:

	Number of performance rights				
Executive	**Held at the beginning of the year**	**Granted as compensation(i)**	**Vested during the year**	**Other changes(ii)**	**Held at the end of the year**
Financial year 2018					
Richard C. Vincent	663,465	402,264	(283,841)	(57,672)	724,216
Peter Mendo	183,917	92,311	(33,507)	-	242,721

(i) Total KMP grants of 494,575 rights during the period over new issue shares were equal to 0.1% of common shares outstanding.

(ii) Other changes represent performance rights that expired or were forfeited during the year

At the end of the year, no rights held by KMP have become vested but not exercisable.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

SECTION 3 OTHER MATTERS REQUIRED BY SECTION 300A CORPORATIONS ACT 2001

A Movements in shares held by the KMP

The movement during the year in the number of ordinary shares of the Company, held directly, indirectly or beneficially by each executive and non-executive KMP, including their personally related parties is as follows:

	Number of shares			
KMP	Held at the beginning of the year	Purchases or issues	Sale of shares	Held at the end of the year
Financial year 2018				
Mark Smith(i)	-	170,000	-	170,000
Robert D. Millner	1,755,620	-	-	1,755,620
Lee Ausburn	83,334	-	-	83,334
Gerard J. Masters	218,000	-	-	218,000
Ken Gunderson-Briggs	10,000	10,000	-	20,000
Jennifer Macdonald(ii)	-	35,000	-	35,000
Peter R. Robinson(iii)	302,168	-	-	302,168
Richard C. Vincent	145,444	283,841 (iv)	-	429,285
Peter Mendo	-	33,507(v)	-	-

(i) Mark Smith appointed as a Director and KMP on 6 September 2017.
(ii) Jennifer Macdonald appointed as Director and KMP on 9 November 2017.
(iii) Peter R. Robinson ceased to be a Director and KMP on 24 January 2018. Only shareholdings as at that date are included.
(iv) Issued in November 2017 pursuant to the LTIP for the year ended 31 August 2014 and the STIP for the year ended 31 August 2016.
(v) Issued in November 2017 pursuant to the STIP for the year ended 31 August 2016.

Consequences of Performance On Shareholders' Wealth

In considering the performance of the Group and the benefits for shareholder wealth, the Remuneration Committee has regard to a range of indicators in respect of senior executive remuneration and have linked these to the previously described short and long term incentives.

The following table presents these indicators over the past 5 financial years, taking into account dividend payments, share price changes and returns of capital during the financial years:

	31 August 2018	31 August 2017	31 August 2016	31 August 2015	31 August 2014
Net profit/(loss) $'000	48,202	52,371	51,670	43,126	(90,771)
Dividends declared – cents per share	7.5	7.0	6.0	4.5	3.5
Share price as at $	1.85	1.47	1.77	1.62	0.59

B Comments on Remuneration Report at the most recent AGM of the Company

The Company's previous AGM was held on 24 January 2018. At this meeting:

(a) no comments were made on the Remuneration Report that was considered at this AGM;

(b) when the resolution that the Remuneration Report be adopted, at least 75% of the votes cast were in favour of adoption of that report.

DIRECTORS' REPORT

REMUNERATION REPORT *(CONTINUED)*

C Engagement of Remuneration Consultant

While the Remuneration Committee seeks external advice from advisers who are independent of management of remuneration matters, it did not require a remuneration recommendation as defined under Section 9B of the Corporations Act 2001 by an external adviser during the year ended 31 August 2018.

D Related party transactions

Transaction with Related Parties are set out in Note 19. The Company has not entered into any loan arrangements.

THE REMUNERATION REPORT CONCLUDES AT THIS POINT.

Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To the Directors of Australian Pharmaceutical Industries Limited

I declare that, to the best of my knowledge and belief, in relation to the review of Australian Pharmaceutical Industries Limited for the year ended 31 August 2018 there have been:

i. no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and

ii. no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

Maurice Bisetto
Partner

Melbourne

17 October 2018

FINANCIAL REPORT

CONSOLIDATED INCOME STATEMENT

		Year ended 31 August	
In thousands of AUD	**Note**	**2018**	**2017**
Revenue	3	4,026,302	4,061,200
Cost of sales		(3,529,592)	(3,567,573)
Gross profit		**496,710**	**493,627**
Other income and expense	3	8,890	5,961
Warehousing and distribution expenses		(140,056)	(135,152)
Marketing and sales expenses		(190,098)	(188,120)
Administration and general expenses		(93,049)	(87,040)
Profit from operating activities (EBIT)		**82,397**	**89,276**
Finance income		181	309
Finance expenses	4	(12,551)	(13,173)
Net finance costs		**(12,370)**	**(12,864)**
Profit before tax		**70,027**	**76,412**
Income tax expense	5	(21,825)	(24,041)
Profit for the year		**48,202**	**52,371**
Attributable to:			
Ordinary shareholders of the Company		48,056	52,371
Non-controlling interest		146	-
Profit for the year		**48,202**	**52,371**
Earnings per share for profit attributable to the ordinary shareholders of the Company:		**cents**	**cents**
Basic earnings per share	6	9.8	10.7
Diluted earnings per share	6	9.7	10.6

Notes to the Consolidated Income Statement are annexed.

FINANCIAL REPORT

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

		Year ended 31 August	
In thousands of AUD	Note	2018	2017
Profit for the year		**48,202**	**52,371**
Other comprehensive income/(loss)			
Items that will not be reclassified subsequently to the income statement			
Remeasurements of the defined benefit asset, post tax		64	(22)
Total items that will not be reclassified		**64**	**(22)**
Items that may be reclassified subsequently to the income statement			
Exchange fluctuations on translation of foreign operations, post tax		926	(1,804)
Effectiv e portion of changes in fair v alue of cash flow hedges, post tax		272	149
Total items that may be reclassified		**1,198**	**(1,655)**
Total other comprehensive income/(loss) for the year		**1,262**	**(1,677)**
Total comprehensive income for the year		**49,464**	**50,694**
Attributable to:			
Ordinary shareholders of the Company		49,318	50,694
Non-controlling interest		146	-
Total comprehensive income		**49,464**	**50,694**

Notes to the Consolidated Statement of Comprehensive Income are annexed.

FINANCIAL REPORT

CONSOLIDATED BALANCE SHEET

		As at 31 August	
In thousands of AUD	Note	2018	2017
Current assets			
Cash and cash equivalents	26	35,948	39,776
Trade and other receivables	8	654,661	681,620
Inventories	8	395,219	399,344
Total current assets		**1,085,828**	**1,120,740**
Non-current assets			
Trade and other receivables	8	28,279	21,187
Deferred tax assets	5	21,916	20,210
Property, plant and equipment	9	101,015	95,280
Intangible assets	11	265,718	193,659
Total non-current assets		**416,928**	**330,336**
Total assets		**1,502,756**	**1,451,076**
Current liabilities			
Trade and other payables	8	774,920	804,473
Loans and borrowings	13	2,679	2,765
Provisions	12	29,851	26,896
Income tax payable	5	7,141	16,899
Total current liabilities		**814,591**	**851,033**
Non-current liabilities			
Trade and other payables	8	97,826	7,903
Deferred tax liabilities	5	292	364
Loans and borrowings	13	89,214	29,834
Provisions	12	5,637	7,696
Total non-current liabilities		**192,969**	**45,797**
Total liabilities		**1,007,560**	**896,830**
Net assets		**495,196**	**554,246**
Equity			
Share capital	15	566,461	566,461
Reserves	15	46,987	92,449
Accumulated losses		(104,664)	(104,664)
Total equity attributable to members of API Limited		**508,784**	**554,246**
Non-controlling interest in controlled entities		**(13,588)**	**-**
Total equity		**495,196**	**554,246**

Notes to the Consolidated Balance Sheet are annexed.

FINANCIAL REPORT

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Attributable to ordinary shareholders of API Limited									
In thousands of AUD	Share Capital	Accumulated Losses	Profits[(i)] Reserve	Translation Reserve	Hedging Reserve	Equity Reserve	Control Reserve[(iii)]	Total	Non-controlling interest	Total Equity
Balance at 1 September 2017	**566,461**	**(104,664)**	**86,155**	**(189)**	**(204)**	**6,687**	**-**	**554,246**	**-**	**554,246**
Profit after tax	-	-	48,056	-	-	-	-	48,056	146	48,202
Total other comprehensive income	-	-	64	926	272	-	-	1,262	-	1,262
Total comprehensive income for the year	-	-	48,120	926	272	-	-	49,318	146	49,464
Transactions with owners, recorded directly in equity										
Purchase of treasury shares [(ii)]	(362)	-	-	-	-	-	-	(362)	-	(362)
Dividends to equity holders	-	-	(34,464)	-	-	-	-	(34,464)	-	(34,464)
Consideration payable to non-controlling interests	-	-	-	-	-	-	(59,900)	(59,900)	(11,605)	(71,505)
Proportionate share of business assets acquired	-	-	-	-	-	-	-	-	(2,129)	(2,129)
Shares vested under the STIP and LTIP	362	-	-	-	-	(532)	-	(170)	-	(170)
Share based payments	-	-	-	-	-	116	-	116	-	116
Total contributions by and distributions to owners	-	-	(34,464)	-	-	(416)	(59,900)	(94,780)	(13,734)	(108,514)
Balance at 31 August 2018	**566,461**	**(104,664)**	**99,811**	**737**	**68**	**6,271**	**(59,900)**	**508,784**	**(13,588)**	**495,196**
Balance at 1 September 2016	**566,461**	**(104,664)**	**68,092**	**1,615**	**(353)**	**5,544**		**536,695**	**-**	**536,695**
Profit after tax	-	-	52,371	-	-	-	-	52,371	-	52,371
Total other comprehensive income/(loss)	-	-	(22)	(1,804)	149	-	-	(1,677)	-	(1,677)
Total comprehensive income for the year	-	-	52,349	(1,804)	149	-	-	50,694	-	50,694
Transactions with owners, recorded directly in equity										
Purchase of treasury shares [(ii)]	(493)	-	-	-	-	-	-	(493)	-	(493)
Dividends to equity holders	-	-	(34,286)	-	-	-	-	(34,286)	-	(34,286)
Shares vested under the STIP and LTIP	493	-	-	-	-	(493)	-	-	-	-
Share based payments	-	-	-	-	-	1,636	-	1,636	-	1,636
Total contributions by and distributions to owners	-	-	(34,286)	-	-	1,143	-	(33,143)	-	(33,143)
Balance at 31 August 2017	**566,461**	**(104,664)**	**86,155**	**(189)**	**(204)**	**6,687**	**-**	**554,246**	**-**	**554,246**

(i) The profits reserve represents current year profits transferred to a reserve to preserve the characteristic as a profit and not appropriate those profits against prior year accumulated losses. Such profits will be available to enable payment of franked dividends in the future.

(ii) Shares were purchased on market and issued to the previous Managing Director for the vesting of the 2014 and 2015 STIP.

(iii) The control reserve represents the cost of future instalments for the purchase of the shares held by non-controlling interest in Clearskincare clinics, subject to the put and call option exercisable on 1 September 2020 and 1 September 2021. Refer Note 20.

Notes to the Consolidated Statement of Changes in Equity are annexed.

FINANCIAL REPORT

CONSOLIDATED STATEMENT OF CASH FLOWS

		Year ended 31 August	
In thousands of AUD	Note	2018	2017
Cash flows from operating activities			
Cash receipts from customers (inclusive of GST)		4,446,366	4,445,196
Cash payments to suppliers and employees (inclusive of GST)		(4,347,655)	(4,315,384)
Cash generated from operations		**98,711**	**129,812**
Interest received		181	309
Finance costs paid		(12,397)	(13,610)
Income taxes paid		(32,844)	(21,029)
Net cash inflows from operating activities	26	**53,651**	**95,482**
Cash flows from investing activities			
Proceeds from sale of stores, property, plant and equipment		-	513
Acquisition of property, plant and equipment and intangibles		(25,698)	(28,290)
Payment for business acquired, net of cash acquired	20	(56,608)	-
Net cash used in investing activities		**(82,306)**	**(27,777)**
Cash flows from financing activities			
Proceeds from borrowings		2,720,235	1,598,000
Repayment of borrowings		(2,660,000)	(1,615,198)
Payment of finance lease liabilities		(941)	(1,601)
Dividends paid		(34,464)	(34,286)
Net cash inflows/(outflows) from financing activities		**24,830**	**(53,085)**
Net increase/(decrease) in cash and cash equivalents		(3,825)	14,620
Cash and cash equivalents at the beginning of the year		39,776	25,489
Effect of exchange rate fluctuations on cash held		(3)	(333)
Cash and cash equivalents at the end of the year		**35,948**	**39,776**

Notes to the Consolidated Statement of Cash Flows are annexed.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

About This Report

1. About This Report

Australian Pharmaceutical Industries Limited (the 'Company') is a for-profit public company limited by shares incorporated and domiciled in Australia. The financial report was authorised for issue by the Directors on 17 October 2018.

Significant accounting policies adopted in preparing the financial report have been consistently applied to all the years presented, unless otherwise stated and are described in the note to which they relate. Accounting policies relevant to understanding the financial report as a whole are set out below.

a) Basis of preparation

This general purpose financial report has been prepared in accordance with Australian Accounting Standards adopted by the Australian Accounting Standards Board (AASB) including Australian Interpretations and the Corporations Act 2001. The financial report also complies with International Financial Reporting Standards (IFRS) and interpretations adopted by the International Accounting Standards Board.

The financial report has been prepared on the historical cost basis except for derivative financial instruments and employee defined benefit plan which are carried at their fair value and is presented in Australian dollars, which is the functional currency of the Company.

b) Consolidation

The financial report of the Company comprises the Company and its subsidiaries (together referred to as the 'Group'). Subsidiaries are all entities over which the Group has control as defined in AASB 10 Consolidated Financial Statements. Control exists when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the power, directly or indirectly, to affect those returns. Detail of controlled subsidiaries are set out in Note 16.

The financial report includes information and results of each subsidiary from the date on which the Group obtains control until such time as the Group ceases to control the entity. In preparing the financial report, all intercompany balances, transactions and unrealised profits arising within the Group are eliminated in full. Accounting policies of the Company and all subsidiaries in the Group are consistently applied.

c) Foreign currency

Translation of foreign currencies into Australian dollars is as follows:

- Transactions in foreign currency are translated at the exchange rate at the date of the transactions.
- Financial assets and liabilities are translated at the exchange rate on balance date.
- Non-financial assets and liabilities are translated at historical rates at the date of the transaction.

Exchange gains and losses on translation are recognised in the income statement, unless they relate to qualifying cash flow hedges which are deferred in equity and recognised in other comprehensive income.

Assets and liabilities, including goodwill and fair value adjustments on consolidation, of foreign subsidiaries are translated to Australian dollars at the exchange rate on balance date. Foreign exchange differences on translation are recognised in other comprehensive income and foreign currency translation reserve.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

About This Report *(continued)*

d) Key estimates and judgements

Preparation of the financial report requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts in the financial reports. The estimates and judgements are continually evaluated and reviewed based on historical experience and other factors, including reasonable expectations of future events. Changes in the assumptions underlying the estimates may result in a significant impact on the financial statements. Management believes the estimates used in preparing the financial statements are reasonable and in accordance with the accounting standards.

Key assumptions and judgements that have the most significant impact on the amount recognised in the financial report are set out in the following notes:

Note	Judgement area
Note 8 Working Capital	Carrying value of trade receivables Carrying value of inventories
Note 11 Intangible assets	Impairment of goodwill and brand names
Note 12 Provisions and Contingencies	Determination of exposure under financial guarantees
Note 20 Business acquisitions	Determination of contingent consideration Determination of fair value of purchase consideration Determination of fair value of net identifiable assets and liabilities acquired

e) Notes to the financial statements

The notes include information that is required to understand the financial statements and is material and relevant to the operations, financial position and performance of the Group. Information is considered material and relevant if, for example:

- The amount to which to the information relates is significant because of its size or nature;
- The information is important for understanding the results of the Group;
- It helps to explain the impact of significant changes in the Group's operations; or
- It relates to an aspect of the Group's operations that is important to its future performance.

The notes have been organised in five separate sections based on their nature. The beginning of each section describes the information presented.

f) Rounding

The amounts shown in this Financial Report, including the Directors' report, have been rounded off, except where otherwise stated, to the nearest thousand dollars as the Company is in a class specified in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 dated 24 March 2016.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Financial Performance

This section provides information about the Group's financial performance during the year including performance of its operating segments and the Group's financial results including revenue and other income, expenses, earnings per share, taxation and dividends.

2. Segment report

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to the transactions with any of the other segments. AASB 8 Operating Segments requires disclosure of segment information on the same basis as that used for internal reporting provided to the Chief Operating Decision Maker (CODM) of the Group. The CODM has been identified as the CEO.

Segment information is presented to the CEO for the following segments:

Segment	Principal activities
Australia	Distribution of pharmaceutical, medical, health, beauty and lifestyle products to pharmacies, the purchase and sale of health, beauty and lifestyle products within the retail industry and provider of retail services to pharmacies. Also includes the Clearskincare business which specialises in non-invasive cosmetic products and procedures. The Group predominantly operates within Australia. Monthly management reports provided to the CEO report Australian reportable segment profit.
New Zealand	Manufacturer and owner of rights of pharmaceutical medicines and consumer toiletries. Products are sold in both New Zealand and exported.

	Year ended 31 August							
	Australia		New Zealand		Eliminations		Consolidated	
In thousands of AUD	2018	2017	2018	2017	2018	2017	2018	2017
Revenue								
External sales	3,828,323	3,863,605	48,358	45,204	-	-	3,876,681	3,908,809
External services	149,621	152,391	-	-	-	-	149,621	152,391
Inter-segment revenue[i]	-	-	10,935	5,442	(10,935)	(5,442)	-	-
Total segment revenue	3,977,944	4,015,996	59,293	50,646	(10,935)	(5,442)	4,026,302	4,061,200
Reportable segment gross profit	469,970	471,586	26,740	22,041	-	-	496,710	493,627
Reportable segment profit	**79,587**	**88,576**	**2,810**	**700**	**-**	**-**	**82,397**	**89,276**
Unallocated amounts								
Net financing costs							(12,370)	(12,864)
Profit before tax							**70,027**	**76,412**
Income tax expense							(21,825)	(24,041)
Profit for the year							**48,202**	**52,371**
Attributable to:								
Ordinary shareholders of API							48,056	52,371
Non-controlling interest							146	-
Other segment information:								
Depreciation and amortisation	26,614	27,279	1,562	1,345	-	-	28,176	28,624
Additions of property, plant and equipment and intangible assets	104,340	29,021	3,055	1,391	-	-	107,395	30,412

(i) All inter-segment sales are on arm's length basis

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Financial Performance *(Continued)*

3. Revenue and other income

In thousands of AUD	Year ended 31 August 2018	2017
Revenue		
Sales revenue	3,876,681	3,908,809
Service revenue	149,621	152,391
Total revenue	**4,026,302**	**4,061,200**
Other income		
Gain on disposal of stores, property, plant and equipment	-	50
Interest fee income	8,887	5,978
Net foreign exchange gain/(loss)	3	(67)
Total other income	**8,890**	**5,961**

Accounting policies

Category	Revenue stream	Recognition policy
Sales revenue	Sale of goods	Revenue from the sale of goods is recognised when the significant risks and rewards of ownership have been transferred to the buyer, usually when goods are delivered to manufacturing and wholesale customers or the point of sale for retail customers. Revenue is recognised net of returns, allowances, trade discounts and volume rebates.
	Loyalty program (Sister Club) – deferred revenue	Under the loyalty card programme deferred revenue is recognised as a reduction in sales revenue when the products or services are sold. The deferred revenue liability is recognised based on historical loyalty card redemption data and a weighting of possible outcomes against their associated probabilities. Revenue is earned when loyalty card awards are redeemed.
Service revenue	Membership and brand fees	The Group receives membership and brand fees from franchisees of Priceline stores, and Soul Pattinson and Pharmacist Advice banner stores in return for access to the brand names, special discounts, catalogue advertising and other benefits. This revenue is recognised over the period over which services are rendered.
	Franchise service fees	This relates to service income received from franchisees for operational services including store development, lease negotiation, human resource and information technology assistance. This revenue is recognised when the service has been performed.
	Marketing services and promotional income	The Group receives income from suppliers for promotional and marketing services rendered. This revenue is recognised once the service obligations have been performed.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Financial Performance *(Continued)*

3. Revenue and other income *(Continued)*

Category	Revenue stream	Recognition policy
	Community Service Obligation (CSO)	CSO income is received from the Federal Government in recognition for the Group providing the communities access to full range of PBS medicines to their local pharmacies within a short timeframe. CSO income is recognised when the Group has complied with the conditions attached to the obligation and has reasonable assurance that the income will be received.
Other income	Interest income	Interest fee revenue includes interest earned on loans to customers and interest charges on overdue debtors and is recognised on an accrual basis.

4. Expenses

	Year ended 31 August	
In thousands of AUD	**2018**	**2017**
Wages and salaries expense	187,329	180,407
Superannuation expense	14,206	13,882
Share based payments expense	116	1,636
Other employee expenses	18,656	18,455
Total employee benefits expense	**220,307**	**214,380**
Interest expense	7,731	8,057
API rewards	4,710	4,871
Finance expense on leased assets	110	245
Finance expenses	**12,551**	**13,173**
Depreciation and amortisation	28,176	28,624

Accounting policies	
Employee benefits	Employee benefits includes wages, salaries, superannuation benefits, personal leave, annual leave, long service leave and any non-monetary benefits paid to employees in consideration of services rendered. These are expensed as incurred. Refer to Note 12 for details on calculation of employee benefits provisions. Refer to Note 22 for accounting policies on share based payments.
Finance costs	Finance costs are recognised as expenses in the period as incurred and include: • interest on bank overdrafts, short-term and long-term borrowings; • interest payable on securitisation programs; • interest charges on finance leases; • amortisation of ancillary costs incurred in connection with the arrangement of borrowings; and • net interest charges on the API rewards programme.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Financial Performance *(Continued)*

5. Taxation

	Year ended 31 August	
In thousands of AUD	**2018**	**2017**
(a) Income tax expense recognise in the income statement		
Current tax expense	23,637	25,279
Deferred tax expense	(1,617)	(1,352)
Adjustments in current year tax relating to prior year	(195)	114
Total income tax expense	**21,825**	**24,041**
Reconciliation of prima facie tax expense to income tax expense		
Profit before income tax	70,027	76,412
Prima facie income tax at 30%	21,008	22,924
Tax effect of items which increase/(decrease) tax expense:		
Share based payments expense	(52)	341
Entertainment and other sundry expense	111	279
Expenses paid in foreign jurisdictions	-	255
Other	952	128
Adjustment for prior years	(194)	114
Income tax expense	**21,825**	**24,041**
(b) Deferred tax recognised directly in equity	**(119)**	**36**

	As at 31 August	
In thousands of AUD	**2018**	**2017**
(c) Current tax liability[(i)]	**7,141**	**16,899**
(d) Deferred tax assets/(liabilities)		
Employee benefits	6,982	6,726
Provisions	2,429	13,731
Property, plant and equipment	(5,635)	(7,150)
Other	17,848	6,539
Net deferred tax asset	**21,624**	**19,846**
Comprised of:		
Entities incorporated in Australia - net deferred tax asset	21,916	20,210
Entities incorporated in New Zealand - net deferred tax liability	(292)	(364)
Net deferred tax asset	**21,624**	**19,846**
Movements in deferred tax		
Balance at 1 September	19,846	19,223
Expense recognised in the income statement	1,617	560
Deferred tax recognised directly in equity	(119)	36
Deferred tax recognised on business acquisition	280	-
Employee benefits transferred from store acquisitions	-	27
Balance at 31 August	**21,624**	**19,846**

(i) Represents income taxes payable in respect of current and prior financial years.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Financial Performance *(Continued)*

5. Taxation (*Continued*)

Accounting policies	
Income tax expense	Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.
Current tax liability	Current tax liability is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.
Deferred tax	Deferred tax is recognised using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. No temporary differences are recognised on goodwill or differences arising from the initial recognition of assets or liabilities (unless in a business combination) in a transaction that affects neither accounting nor taxable profit at the time of the transaction. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. The carrying amount of deferred income tax assets is reviewed at each reporting period and reduced to the extent that it is no longer probable that the sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilised. If certain criteria are met deferred tax assets and liabilities are offset in the financial statements.
Tax consolidation	Australian Pharmaceutical Industries Limited is the head entity of the Australian tax consolidated group. The head entity and the members of the tax consolidated group have entered into a tax funding arrangement which sets out the funding obligations of members in respect of tax amounts. The head entity recognises the tax effects of its own transactions and the current tax liabilities and the deferred tax assets arising from unused tax losses and unused tax credits assumed from the subsidiaries. Members of the tax consolidated group have also entered into a tax sharing agreement that provides for the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations. The entities that form part of the Clearskincare Clinic business are not part of the API tax consolidated group as they are not 100% owned subsidiaries.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Financial Performance *(Continued)*

6. Earnings per share

	Year ended 31 August	
In thousands of AUD	**2018**	**2017**
Profit attributable to shareholders of the Group	**48,056**	**52,371**
In thousands of shares		
Basic weighted average number of ordinary shares for the year	491,975	489,704
Effect of potential ordinary shares on issue	2,684	4,935
Diluted weighted average number of shares for the year	**494,659**	**494,639**
In cents		
Basic earnings per share	9.8	10.7
Diluted earnings per share	9.7	10.6

7. Dividends

	Year ended 31 August	
In thousands of AUD	**2018**	**2017**
Dividends paid during the year		
Final dividend for 2017 financial year of 3.5 cents per share fully franked (2017: Final dividend of 3.5 cents per share fully franked)	17,229	17,143
Interim dividend for 2018 financial year of 3.5 cents per share fully franked (2017: Interim dividend of 3.5 cents per share fully franked)	17,235	17,143
Total dividends paid during the year	**34,464**	**34,286**
Dividend franking account		
Franking credits available to shareholders for subsequent financial years based on tax rate of 30% [i]	53,867	52,943

(i) The ability to utilise the franking credits is dependent upon there being sufficient available profits to declare dividends. The future reduction in the dividend franking account of dividends proposed after the balance sheet date but not recognised as a liability at balance date is $8,441,632 (31 August 2017: $7,347,006).

Accounting policies

Dividends are recognised as a liability when an obligation to pay a dividend arises. The obligation arises following declaration of the dividend by the Board.

Dividends declared after balance date

On 17 October 2018, the Directors declared that a final dividend of4.0 cents per share amounting to $19,697,141 will be paid in respect of the 2018 financial year. The dividend will be payable out of the Profits Reserve and will be fully franked to be paid on 7 December 2018. The financial effect of this dividend is not included in the financial statements for the year ended 31 August 2018 and will be recognised in the 2019 financial statements.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities

This section provides information about the Group's operating assets and liabilities, including working capital, tangible and intangible assets, provisions and commitments.

8. Working capital

	As at 31 August	
In thousands of AUD	**2018**	**2017**
Current		
Trade and other receivables	683,775	708,455
Provision for impairment	(29,114)	(26,835)
Net trade and other receivables	**654,661**	**681,620**
Inventories		
Raw materials and consumables	5,846	5,746
Finished goods	395,730	402,153
Provision for obsolescence and shrinkage	(6,357)	(8,555)
Net inventories	**395,219**	**399,344**
Trade and other payables	(774,920)	(804,473)
Net working capital - current	**274,960**	**276,491**
Non-current		
Non-current trade receivables	27,467	20,486
Defined benefit plan asset	812	701
Lease payable	(8,114)	(7,903)
Financial liabilities payable to non-controlling shareholders [(i)]	(89,712)	-
Total non-current	**(69,547)**	**13,284**
(a) Movement in provision for impairment losses		
Balance at beginning of the year	(26,835)	(18,688)
Amounts provided for during the year	(5,047)	(10,716)
Amounts written off during the year	2,768	2,569
Balance at end of the year	**(29,114)**	**(26,835)**

(i) Details relating to financial liabilities payable to non-controlling shareholders are set out in Note 20.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

8. Working Capital (Continued)

Accounting policies

Trade receivables

Trade receivables are initially recognised at invoice value (fair value) and subsequently measured at amortised cost, less allowance for impairment losses. The majority of trade debtors are settled within 40-120 days of the invoice date. Trade debtors are presented as current assets unless collection is not expected for more than 12 months after the reporting date, in which case they are recognised at their present value discounted using the appropriate interest rate.

Securitised receivables are recognised on the balance sheet as the Group assumes the risks and rewards of these receivables.

Key accounting estimate and judgement – carrying value of trade receivables

Management judgement is applied to assess the recoverability of trade debtors on an ongoing basis and at each reporting period. Recoverability of debtors is assessed with reference to the customer's ability to repay amounts due, which includes an assessment of:

- The anticipated cash flows of the customer;
- the estimated security valued held by the Group over the customer's property and assets;
- estimated value of other security held such as retention of title of inventory and;
- the ranking of the Group's debt compared to other creditors of the customer.

A provision for impairment losses is recognised when there is objective evidence that the amounts due may not be fully recovered.

Objective evidence includes default or delinquency by a debtor, restructuring of an amount due on unfavourable terms to the Group, and indications that the debtor will enter administration or bankruptcy.

Where the likelihood of recovery is remote, the amount due is provided for through the provision for impairment losses. In instances where there is a reasonable prospect of recovery, management will make their best estimate based on all available information, on the most likely outcome as at the reporting period. Any provision for impairment for trade debtors is recognised against profit during the reporting period. Trade receivables that are deemed uncollectible are written off.

Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price less estimated selling expenses.

Inventories are recognised on the weighted average cost basis including the purchase price of inventories and associated costs, net of rebates and trade discounts. Cost of manufactured goods includes direct labour, direct material and overhead expenses based on normal operating capacity.

Key accounting estimate and judgement – carrying value of inventories

Management judgement is applied to determine the net realisable value of inventories. Provisions are established for all obsolete or slow moving inventories, taking into consideration the ageing profile of inventories, discontinued lines, sales trends and forecast sales.

Trade payables

Liabilities are recognised as amounts to be paid in the future for goods or services received or provided prior to the end of the reporting period. Trade accounts payable are normally settled within 30-60 days of the invoice date.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

9. Property, plant and equipment

	As at 31 August				
In thousands of AUD	Land and buildings	Plant and equiment	Finance leases	Capital work in progress	Total
Financial year 2018					
Cost	10,397	226,335	7,887	7,560	252,179
Accumulated depreciation and impairment	(5,833)	(138,134)	(7,197)	-	(151,164)
Net book value	**4,564**	**88,201**	**690**	**7,560**	**101,015**
Balance 1 September 2017	4,795	83,992	1,796	4,697	95,280
Additions	-	1,323	-	24,046	25,369
Additions from business acquisitions	-	10,160	-	-	10,160
Disposals	-	(2,047)	(52)	-	(2,099)
Depreciation expense for the year	(266)	(15,445)	(1,054)	-	(16,765)
Rev ersal of impairment	-	452	-	-	452
Reclassification of assets	-	9,729	-	(9,729)	-
Transfer of assets to intangibles	-	-	-	(11,469)	(11,469)
Foreign currency exchange differences	35	37	-	15	87
Balance at 31 August 2018	**4,564**	**88,201**	**690**	**7,560**	**101,015**
Financial year 2017					
Cost	10,318	207,294	8,065	4,697	230,374
Accumulated depreciation and impairment	(5,523)	(123,302)	(6,269)	-	(135,094)
Net book value	**4,795**	**83,992**	**1,796**	**4,697**	**95,280**
Balance 1 September 2016	5,210	88,232	3,889	2,798	100,129
Additions	-	2,121	-	24,374	26,495
Disposals	-	(2,513)	(210)	-	(2,723)
Depreciation expense for the year	(273)	(14,885)	(1,883)	-	(17,041)
Rev ersal of impairment	-	1,163	-	-	1,163
Reclassification of assets	57	10,081	-	(10,138)	-
Transfer of assets to intangibles	-	-	-	(12,244)	(12,244)
Foreign currency exchange differences	(199)	(207)	-	(93)	(499)
Balance at 31 August 2017	**4,795**	**83,992**	**1,796**	**4,697**	**95,280**

Accounting policies

Acquisitions and disposals

Property, plant and equipment is stated at cost less accumulated depreciation and impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be reliably measured. Assets under construction are not depreciated until ready for use.

Profit and losses on disposal of property, plant and equipment are recognised in the income statement.

Dismantling provisions relating to an obligation for site closure or restoration are recognised as part of the cost of the asset.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

9. Property, plant and equipment (*Continued*)

Accounting policies	
Depreciation	Property, plant and equipment, other than land, is depreciated on a straight-line basis over the estimated life of each asset to the Group. Estimated useful lives of each class of asset are as follows: • Buildings 40 years • Plant and equipment 3 to 15 years • Fixtures and fittings 10 years
Impairment of assets	The carrying amounts of tangible and intangible assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the recoverable amount of the asset or the Cash Generating Unit (CGU) it belongs to is estimated. If the carrying amount exceeds the recoverable amount, an impairment loss is recognised in the income statement. Impairment losses at the CGU level are allocated first to reduce the carrying amount of the goodwill allocated to that CGU. The recoverable amount of an asset or cash-generating unit is the greater of its fair value less costs to sell and its value in use calculated as the estimate of future cash flows discounted to present value using a post-tax discount rate. An impairment loss is reversed, except impairment losses relating to goodwill, if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the carrying amount of the asset does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.
Leases	Leases on which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Other leases are classified as operating leases. Finance lease assets are capitalised at the amount of the lower of fair value or the present value of the minimum lease payments and are amortised on a straight-line basis. A finance lease liability is recognised as future rental obligations net of finance charges. Lease liabilities are reduced by payments of principal, with interest expenses recognised in the income statement as finance expenses. Operating leases are not capitalised. Payments are recognised as expenses as incurred, on a straight line basis, including any lease incentives received.

10. Commitments

	As at 31 August	
In thousands of AUD	**2018**	**2017**
Non-cancellable operating leases - Group as lessee		
Less than one year	47,291	42,301
Between one and five years	86,741	97,033
More than five years	28,992	36,417
Total operating leases	**163,024**	**175,751**
Leases expense during the year	**67,215**	**67,231**
Capital expenditure contracted but not provided for or payable	**786**	**446**

The Group leases property and plant under non-cancellable operating leases expiring from two to fifteen years. Leases generally provide the Group with a right of renewal at which time all terms are renegotiated. With certain franchise

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

10. Commitments (*Continued*)

arrangements, the Group holds the head lease and recharges the franchisee the rental charge on an arm's length basis, in advance, and offsets this against the rental charge on the head lease.

Certain leases are subject to contingent rental clauses calculated as a percentage of revenue earned in excess of pre-determined thresholds set out in the lease agreements. The Group recognises these amounts as an expense in the period where it is anticipated these thresholds will be reached.

11. Intangible assets

	As at 31 August				
In thousands of AUD	Goodwill	Brand names	Software	Development costs	Total
Financial year 2018					
Cost	178,355	99,000	123,728	1,996	403,079
Accumulated amortisation	(56,360)	(2,640)	(77,240)	(1,121)	(137,361)
Net book value	**121,995**	**96,360**	**46,488**	**875**	**265,718**
Balance 1 September 2017	50,019	96,360	46,929	351	193,659
Transfer from property, plant and equipment	-	-	10,711	758	11,469
Additions from business acquisitions	70,849	-	-	-	70,849
Additions from stores acquired	1,017	-	-	-	1,017
Disposals	-	-	(2)	-	(2)
Amortisation expense for the year	-	-	(11,171)	(239)	(11,410)
Foreign currency exchange differences	110	-	21	5	136
Balance at 31 August 2018	**121,995**	**96,360**	**46,488**	**875**	**265,718**
Financial year 2017					
Cost	106,379	99,000	112,759	1,225	319,363
Accumulated depreciation and impairment	(56,360)	(2,640)	(65,830)	(874)	(125,704)
Net book value	**50,019**	**96,360**	**46,929**	**351**	**193,659**
Balance 1 September 2016	46,973	96,360	46,266	376	189,975
Transfer from property, plant and equipment	-	-	12,202	42	12,244
Additions from stores acquired	3,917	-	-	-	3,917
Disposals	-	-	(3)	-	(3)
Amortisation expense for the year	-	-	(11,464)	(119)	(11,583)
Foreign currency exchange differences	(871)	-	(72)	52	(891)
Balance at 31 August 2017	**50,019**	**96,360**	**46,929**	**351**	**193,659**

(a) Assets with indefinite useful lives

The Group has identified the following cash generating units to which goodwill and brand names with indefinite useful lives have been allocated, as follows:

	As at 31 August							
	Australia		New Zealand		Clearskincare(i)		Total	
In thousands of AUD	2018	2017	2018	2017	2018	2017	2018	2017
Goodwill	**34,690**	**33,673**	**16,456**	**16,346**	**70,849**	**-**	**121,995**	**50,019**
Brand names								
Soul Pattinson brand name	37,500	37,500	-	-	-	-	37,500	37,500
Priceline brand name	58,860	58,860	-	-	-	-	58,860	58,860
Total brand names	**96,360**	**96,360**	**-**	**-**	**-**	**-**	**96,360**	**96,360**

(i) The accounting for the Clearskincare acquisition is provisional at balance date. The identification of intangible assets and determination of useful lives will be completed during the 12-month measurement period. Refer Note 20.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

11. Intangible assets (*Continued*)

Accounting policies

Identifiable intangible assets are recognised at cost less accumulated amortisation and impairment losses where applicable. Intangible assets acquired separately are capitalised at cost or, if arising from a business combination, at fair value as at the date of acquisition.

Unidentified intangible assets are recognised as goodwill when the fair value of the consideration paid for a business acquisition exceeds the fair value of the identifiable net assets acquired.

Below are the key accounting policies and criteria for recognition of each category of intangible assets.

Intangible asset	Capitalisation criteria	Useful life
Goodwill	Business combinations are accounted for by applying the acquisition method. Goodwill represents the excess of the consideration transferred over the fair value of the net identifiable assets acquired. Acquisition-related costs are recognised in the income statement as incurred. Goodwill is tested for impairment on an annual basis and is stated at cost less any accumulated impairment losses. An impairment loss recognised for goodwill cannot be reversed in subsequent periods.	Indefinite
Brand names	Brand names acquired are recognised initially at fair value, using independent valuations obtained in the year of acquisition. Brand names assessed to have a finite useful life are amortised and subsequently recognised at cost less accumulated amortisation. Brand names that are assessed to have indefinite useful lives. as they have an unlimited legal life and risk to become commercially or technically obsolete, are assessed for impairment at least on an annual basis.	Indefinite
Research and development	Expenditure on research activities, undertaken with the prospect of gaining new technical knowledge and understanding, is recognised in the income statement as an expense as incurred. Expenditure on development activities, where research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised if the product or process is technically and commercially feasible and the Group has sufficient resources to complete development. The expenditure capitalised includes the cost of materials, direct labour and appropriate proportion of overheads. Other development expenditure is recognised against profit as an expense as incurred.	1 to 4 years
Software	Capitalised software are initially recorded at cost and amortised on a straight line basis over the estimated useful lives but not greater than a period of 7 years.	1 to 7 years

(c) Impairment assessment for cash generating units (CGU) with indefinite life intangible assets

Indefinite life intangible assets are tested for impairment at least annually by calculating the recoverable amount of the CGU to which they belong. They are then compared to the carrying value of that CGU. Refer to Note 9 for accounting policies and determination of recoverable amount.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

11. Intangible assets (*Continued*)

Key accounting estimate and judgement – carrying value of indefinite life intangibles

Management judgement is applied to identify the CGUs and determine the recoverable amounts using a "value in use" calculation, as outlined in Note 9. These judgements include establishing forecasts of future financial performance, as well as the assessment of earnings growth rates, discount rates and terminal growth rates based on past experience and expectations for the future. The cash flow projections are based on a maximum of five-year Board approved budgets and strategic plan. The forecasts use management estimates to determine revenue, expenses, working capital movements, capital expenditure and associated cash flows for each CGU.

The key assumptions for impairment assessment of each of the Australian and New Zealand CGU's are as follows:

Key assumption	Australia CGU	New Zealand CGU
Budgeted EBITDA growth for the next five years	Based on budgets and five year strategic plans approved by the Board and includes: Pharmaceutical distribution business growth reflects the Board approved financial plan and is based on recent history. New store rollout estimates derived from the analysis by management of the likely net annual increase in stores in the five-year forecast period, based on recent past history, applications from prospective franchisees currently under consideration and the potential pool of new franchisees, after adjusting for the risks associated with execution of the strategic plan and the potential for loss of existing franchisees. The cash flow contribution from new stores is based on the estimates by management of net contribution from individual stores, including working capital, marketing and supply chain costs. Comparable stores sales growth is based on management estimates and recent history for the period in FY19 to FY23.	Based on budgets and five year strategic plans approved by the Board and includes: Contracts entered into with new local and international customers, that will provide annual sales increases. Leveraging and increasing synergies with the Australian business to achieve growth within the supply business.
Discount rate	Pre-tax discount rate of 14.4%, based on a market-determined, risk adjusted post-tax discount rate of 10.1%, representing the post-tax weighted average cost of capital (WACC) including specific risks relating to the CGU.	Pre-tax discount rate of 15.7%, based on a market-determined, risk adjusted post-tax discount rate of 11.2%, representing the WACC.
Terminal long term growth rate	The terminal growth rate of 2.5% represents the growth rate applied to extrapolate cash flows beyond the five year forecast period. The terminal growth rate is based on management expectations of the CGU's long term performance after considering current conditions and available external market data.	

Reasonably possible change

The impairment assessment for both of the above CGUs, including sensitivity analysis on the key assumptions, did not result in any impairment being recognised. The recoverable amount of the NZ CGU assumes the achievement of annual sales growth, profit and working capital targets in the period from FY 2019 to FY 2023. Holding all other assumptions constant, if NZ actual annual sales were below targets by greater than 20%, this may result in an impairment of goodwill for the NZ CGU. A reasonably possible change in the discount rate, holding all other assumptions constant, would not result in an impairment for the NZ CGU.

Clearskincare CGU

The recently acquired Clearskincare business is a separate CGU within the Group. The recent arm's-length purchase price is used as a proxy for the recoverable amount of the Clearskincare business.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

12. Provisions and contingencies

In thousands of AUD	As at 31 August 2018	2017
Current provisions		
Employee benefits	21,608	18,989
Other provisions	8,243	7,907
Total current provisions	**29,851**	**26,896**
Non Current provisions		
Employee benefits	2,374	3,834
Other provisions	3,263	3,862
Total non current provisions	**5,637**	**7,696**

Other provisions

As at 31 August *In thousands of AUD*	Directors' retirement scheme	Provision for dismantling costs	Provision for loyalty programs	Total other provisions
Financial year 2018				
Balance 1 September 2017	351	4,394	7,024	11,769
Provisions made during the year, net of writeback	-	518	6,601	7,119
Provisions used during the year	(205)	(550)	(6,732)	(7,487)
Unwinding of discount	-	105	-	105
Balance at 31 August 2018	**146**	**4,467**	**6,893**	**11,506**

Accounting policies

Recognition of provision — A provision is recognised when there is a legal or constructive obligation as a result of a past event it, is probable that a future outflow of economic benefits will occur to settle the obligation and the amount can be reliably estimated. The amount recognised is the best estimate of the consideration required to settle the present obligation. If a provision is material, it is discounted to present value of the expected future cash outflow and the unwind of the effect of discounting is recorded in finance expenses.

Employee benefits — Liabilities for annual leave are accrued based on statutory and contractual requirements, including related on-costs, measured using the rates expected to be paid when the obligations are settled.

Liabilities for long service leave are accrued at the present value of expected future payments to be made resulting from services provided by employees. The provision is calculated using expected future increases in wage and salary rates including related on-costs and expected settlement dates, discounted using Australian corporate bond rates at the reporting date. Liabilities for long service leave entitlements, which are not expected to be paid or settled within twelve months, are accrued at the present value of future amounts expected to be paid.

Liabilities for bonuses are accrued over the period of service to which the bonus relates, based on the expectation and actual achievement of pre-determined bonus targets.

Dismantling provisions — The Group recognises a provision for the estimated costs to cover its obligations to lessors to restore premises to the condition that existed when leases of real property were entered.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Operating Assets and Liabilities *(Continued)*

12. Provisions and contingencies (*Continued*)

Contingencies

Contingent liabilities

	As at 31 August	
In thousands of AUD	**2018**	**2017**
Financial guarantees to pharmacists	9,907	10,459

Financial guarantees of $9,907,000 (2017: $10,459,000) have been provided to financial institutions of individual debtors and debtor groups. The Group has strict controls over the approval of guarantees of pharmacy customers and takes security over the assets of the relevant pharmacy or pharmacy group.

Key accounting estimate and judgement – financial guarantee contingent liabilities

Management judgement is applied to assess likely net exposures relating to financial guarantees provided in respect of pharmacy customers. These assessments take into account total amounts owed by pharmacy customers to third-party financiers and trade debts owed to API. In addition, pharmacy valuations and the assessed value of any security offered by pharmacy customers to API is included in determining whether a net exposure to API is likely. The Group only recognises a provision if an event has occurred that give rises to a present obligation and it is probable that a loss will eventuate.

At balance date, Directors are of the opinion that provisions are not required in respect of these guarantees, as it is not probable that a future loss will occur.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Capital and Risk Management

This section provides information about the Group's capital structure, funding arrangements, exposure to financial risks and how the Group manages these risks.

13. Loans and borrowings

	As at 31 August	
In thousands of AUD	**2018**	**2017**
Current liabilities		
Insurance premium funding	1,972	1,608
Finance lease liabilities	707	1,157
Total current liabilities	**2,679**	**2,765**
Non current liabilities		
Finance lease liabilities	701	1,192
Securitisation of trade receivables	18,000	25,000
Cash advance facilities - secured	5,513	3,642
Interest bearing loans	65,000	-
Total non current liabilities	**89,214**	**29,834**

Accounting policies

Interest-bearing liabilities are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing liabilities are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the term of the liabilities on an effective interest method basis.

Amortised cost is calculated by taking into account any issue costs and any discount or premium on issuance. Gains and losses are recognised in the income statement in the event that the liabilities are derecognised.

Interest bearing liabilities are classified as current liabilities unless there is an unconditional right to defer settlement of the liability for at least twelve months after reporting date.

Financing facilities

	As at 31 August		
In thousands of AUD	**Facilities utilised(i)**	**Facilities unutilised(ii)**	**Total facilities**
Financial year 2018			
Bank overdraft	-	8,749	8,749
Cash advance facilities	5,513	22,506	28,019
Securitisation of trade receivables	18,000	257,000	275,000
Interest bearing loans	65,000	-	65,000
Total at 31 August 2018	**88,513**	**288,255**	**376,768**
Financial year 2017			
Bank overdraft	-	8,732	8,732
Cash advance facilities	3,642	29,821	33,463
Securitisation of trade receivables	25,000	250,000	275,000
Total at 31 August 2017	**28,642**	**288,553**	**317,195**

(i) Average used facilities during the year, excluding interest bearing loans relating to the Clearskincare acquisition, was $187,298,010 (2017: $171,509,399).

(ii) Average unused facilities during the year was $123,573,348 (2017: $146,155,209).

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Capital and Risk Management *(Continued)*

13. Loans and borrowings (*Continued*)

Financing facilities	
Bank overdraft	The Company is a guarantor to a bank facility agreement which provides a total overdraft facility of $8,749,000 (31 August 2017: $8,732,000) to entities within the Group. The facility is subject to set off arrangements between companies within the Group. Interest on bank overdrafts is charged at prevailing market rates. The bank overdraft is repayable on demand and subject to annual review.
Finance lease facility	The lease liabilities of the Group are secured by the leased assets. In the event of default, the assets revert to the lessor.
Cash advances	The consolidated cash advance facilities of $28,019,000 (31 August 2017: $33,463,000) are secured by fixed and floating charge over the assets of the Group. Interest is based on the bank-bill reference rate plus a margin charged by the lender.
Securitisation	The Group has access to funds through the securitisation of current trade receivables provided the receivables meet certain criteria. The securitisation facility of $275 million consists of a daily redraw overdraft facility of $100 million and a term facility of $175 million. The facilities are interest bearing, based on a variable interest plus margin. At 31 August 2018 the weighted average rate was 3.52% (31 August 2017: 3.51%). The funds available under securitisation facility are capped at the amount of the qualifying trade receivables. The trade receivables are collateralised in full against amounts drawn. The facility imposes rights and obligations on the Group with respect to the quality and maintenance of the receivables, collection of receivables, settlement and reporting to the financier. The Group has complied with its obligations under the facility throughout the financial year.
Interest bearing loans	The interest bearing loan facilities pertain to the acquisition of the Clearskincare business and are revolving loan facilities with an expiry of 31 July 2021. The facilities are secured by way of a fixed and floating charge over the assets of the Group. Interest is based on the bank-bill reference rate plus a margin charged by the lender.

14. Financial risk management

The Group has exposure to various financial risks as part of its operating activities. The Group's risk management program seeks to mitigate these risks and reduce the volatility of the Group's financial performance through use of various financial instruments.

The Board has overall responsibility for the establishment and oversight of the risk management framework of the Group. The Audit and Risk Committee ("Committee") of the Board is responsible for assessing and monitoring the risk management program and making recommendations to the Board.

The risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the activities of the Group.

The Committee oversees the monitoring of compliance with the risk management policies and procedures by management and reviews the adequacy of the risk management framework in relation to the risks, with assistance from the internal audit function.

The Group has exposure to the following principal financial risks:

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Capital and Risk Management *(Continued)*

14. Financial risk management (*Continued*)

(i) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk arises principally from the Group's receivables from customer sales and financial guarantees the Group has provided for certain trade debtors. The maximum exposure to credit risk is the carrying value of trade receivables.

The Group has established credit policies that ensure new customers are subject to credit worthiness verification including review of external credit ratings, financial position, past experience and industry reputation. Purchase limits are established for each customer. Customers that fail to meet the benchmark credit worthiness only transact with the Group on a prepaid basis. In monitoring customer credit risk, customers are grouped by state and reviewed monthly. "High risk" customers are placed on "credit hold", with orders manually released as appropriate. All goods sold are subject to retention of title clauses, so that in the event of non-payment the Group may have a secured claim in respect of the goods sold.

The ageing profile of current and non-current trade and other receivables, including provision of impairment assessment at balance date is set out below:

	As at 31 August	
In thousands of AUD	**2018**	**2017**
Not past due	559,261	622,746
Past due 0 - 30 days	28,456	32,808
Past due 31+ days	124,337	74,088
Total gross trade and other receivables - current and non-current	**712,054**	**729,642**
Provision for impairment losses	(29,114)	(26,835)
Net trade receivables	**682,940**	**702,807**

(ii) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The approach to managing liquidity is to ensure, as far as possible, that there will be sufficient liquidity to meet liabilities when due, under both normal and stressed conditions.

The Group has varying borrowing levels based on seasonal requirements of the business, and also has access to its borrowing facilities. The following are the contractual maturities of financial liabilities, including interest payments and excluding the impact of netting arrangements.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Capital and Risk Management *(Continued)*

14. Financial risk management (*Continued*)

	As at 31 August					
In thousands of AUD	Carrying Amount	Contractual cash flows	0 - 1 year	1 - 2 years	2-5 years	More than 5 years
Financial year 2018						
Finance lease liabilities	1,408	1,478	1,137	341	-	-
Insurance premium funding	1,972	1,972	1,972	-	-	-
Trade and other payables	783,034	783,034	774,920	1,151	4,024	2,939
Cash advance facility	5,513	5,513	-	5,513	-	-
Securitisation of trade receivables	18,000	18,000	-	18,000	-	-
Interest bearing loans	65,000	65,000	-	-	65,000	-
Payable to Non-controlling interest	89,712	98,213	4,518	5,099	88,596	-
Balance at 31 August 2018	**964,639**	**973,210**	**782,547**	**30,104**	**157,620**	**2,939**
Financial year 2017						
Finance lease liabilities	2,349	2,518	1,266	1,212	40	-
Insurance premium funding	1,608	1,608	1,608	-	-	-
Trade and other payables	812,376	812,376	804,473	646	3,357	3,900
Cash advance facility	3,642	3,642	-	3,642	-	-
Securitisation of trade receivables	25,000	25,000	-	-	25,000	-
Balance at 31 August 2017	**844,975**	**845,144**	**807,347**	**5,500**	**28,397**	**3,900**

(iii) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates, will affect the income of the Group or the value of the financial instruments held by the Group. The objective of market risk management is to manage and monitor market risk exposures within acceptable parameters, whilst optimising the return on risk.

(a) Currency risk

The Group had no material exposure to foreign currency risk on sales and purchases that are denominated in a currency other than the respective functional currencies of the entities within the Group.

(b) Interest rate risk

The Group is exposed to interest rate risk on its financing facilities. The Group adopts a policy that up to 85% of its exposure to the changes in interest rates on its long term variable rate borrowings relating to the securitised trade receivables may be hedged on a fixed rate basis. At 31 August 2018, the Group had interest rate swaps with a notional contract amount of $36,000,000, with a maturity date of September 2019 and weighted rate of 1.99%.

The Group classifies interest rate swaps as cash flow hedges. The notional contracted interest cash flows are consistent with highly probable forecast interest cash flows to August 2019 based on the forecast of used facilities for the securitised trade receivables.

Effective interest rates

The following table shows the effective interest rates for the financial assets and interest bearing financial liabilities at reporting date.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Capital and Risk Management *(Continued)*

14. Financial risk management (*Continued*)

As at 31 August	Effective interest rate	Total amount ($'000)
Financial year 2018		
Financial assets[(i)]	3.15%	63,415
Financial liabilities - fixed rate	3.71%	(37,408)
Financial liabilities - variable rate	3.66%	(54,485)
Balance at 31 August 2018		**(28,478)**
Financial year 2017		
Financial assets[(i)]	3.78%	60,017
Financial liabilities - fixed rate	4.23%	(27,349)
Financial liabilities - variable rate	4.05%	(5,250)
Balance at 31 August 2017		**27,418**

(i) Includes cash and cash equivalents which have a variable interest rate. Other financial assets have fixed rates.

(iv) Financial instruments at fair value

The only financial assets or financial liabilities carried at fair value are derivative financial instruments designated as cash flow hedges. The Company considers the derivatives to be Level 2 financial instruments because their measurement is derived from inputs other than quoted prices that are observable for the assets or liabilities, either directly (as prices) or indirectly (derived from prices). There have been no transfers between levels 1, 2 and 3 for recurring fair value measurements during the year. The derivative fair values have been obtained from third party valuations derived from forward interest rates at the reporting date. The following table indicates the periods in which the cash flows and profit and loss impact associated with derivatives that were designated as cash flow hedges existing as at balance date are expected to occur.

As at 31 August *In thousands of AUD*	Fair value	Expected cash flows	0 - 1 year	1 - 2 years	2-5 years	More than 5 years
Financial year 2018						
Interest rate swap	34	34	-	34	-	-
Foreign exchange forward	63	63	63	-	-	-
Net asset/(liability)	**97**	**97**	**63**	**34**	**-**	**-**
Financial year 2017						
Interest rate swap	(130)	(130)	(83)	(47)	-	-
Foreign exchange forward	(162)	(162)	(162)	-	-	-
Net asset/(liability)	**(292)**	**(292)**	**(245)**	**(47)**	**-**	**-**

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Capital and Risk Management *(Continued)*

14. Financial risk management (*Continued*)

(iv) Financial instruments at fair value (continued)

Sensitivity analysis

A strengthening by 100 basis points in interest rates at balance date would have had the following impact:

In thousands of AUD	As at 31 August 2018			As at 31 August 2017		
	Impact on profit/(loss)	Impact on equity	Impact on cash flows	Impact on profit/(loss)	Impact on equity	Impact on cash flows
Interest rate swap - 100bp increase	-	51	51	-	79	79
Interest rate swap - 100bp decrease	-	(51)	(51)	-	(79)	(79)

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit and loss, nor has any fair value hedges. Therefore a change in interest rates would not affect fixed rate instruments.

(v) Fair value estimation

The carrying amounts and estimated fair values of the Group's financial statements recognised in the financial instruments are materially the same. The methods and assumptions used to estimate the fair values are:

	Financial instrument	Fair valuation technique
Carrying value approximates fair value	Loans and borrowings	Calculated based on discounted expected future principal and interest cash flows using market rates of interest.
	Finance lease liabilities	Present value of future cash flows, discounted at market interest rates
	Put and call option liability	The put and call option liability recognised on the acquisition of Clearskincare business (CSC), refer Note 20, has been measured at the present value, discounted using a risk adjusted discount rate, of the exercise price of the option which is a fixed amount.
	Trade receivables / payables	For receivables / payables with a remaining life of less than one year, the notional amount is deemed to reflect fair value. All other receivables / payables are discounted at market interest rates to determine the fair value.
Measured at fair value	Interest rate swaps	Determined using present value of estimated future cash flows based on observable yield curves and marked implied volatility.
	Foreign exchange forwards	Fair value is determined using prevailing forward exchange rates.
	Other financial liabilities (Amounts payable to non-controlling interests)	The amounts payable include liabilities relating to the mandatory dividend payments and contingent consideration payable to non-controlling shareholders of CSC, refer Note 20 for details. The Group has assessed these liabilities as Level 3 financial instruments as there are no observable market inputs. The Group has determined fair value using the present value technique based on the probability weighted expected cash outflows, discounted using an appropriate risk adjusted discount rate. Probability assessment includes estimating the likelihood of performance hurdles being met for the payment of contingent consideration, and the expected level of future profitability of the CSC business for the payment of mandatory dividends.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Capital and Risk Management *(Continued)*

14. Financial risk management (*Continued*)

Capital Management

The policy of the Board is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business.

The Board seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position.

There were no changes in the approach of the Group to capital management during the year. The details of the various financing facilities the Group uses to manage its debt facilities are set out in Note 13.

15. Capital and reserves

Share capital

	Ordinary Shares as at 31 August	
In thousands of shares	**2018**	**2017**
Shares on issue at beginning of the period - fully paid	489,800	489,097
Ordinary shares issued during Nov ember 2017 pursuant to the Company's Long Term Incentiv e Plan	2,336	703
Ordinary shares issued during Nov ember 2017 pursuant to the Company's Short Term Incentiv e Plan	292	-
Shares on issue at the end of the period - fully paid	**492,428**	**489,800**

Equity item	Description and accounting policy
Ordinary shares	The Company does not have authorised capital or par value in respect of its issued shares. All issued shares are fully paid and are recognised at the fair value of the consideration received by the Company, net of post-tax share issue costs. Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders meetings. In the event of a winding up of the Company, ordinary shareholders rank after all other creditors and are fully entitled to any proceeds of liquidation.
Translation reserve	The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations where the functional currency is different to the presentation currency of the Company.
Equity reserve	The equity reserve relates to share-based payment transactions measured at fair value.
Hedging reserve	The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments relating to hedged transactions that have not yet occurred.
Control reserve	The control reserve represents additional consideration to be paid for acquisition of non-controlling shareholders' interests in acquired businesses.
Non-controlling interest	Represents the non-controlling interest in the acquiree that is held by other minority shareholders. The Group recognises the non-controlling interest at the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Group Structure

This section provides information about the Group's structure, subsidiaries and business acquisitions.

16. Subsidiaries

The Group's financial statements include the consolidated information on assets, liabilities and results of the following subsidiaries.

(a) Entities that are 100% owned in current and previous financial year:

Entity name	Entity name	Entity name
API Services Australia Pty Ltd	New Price Retail Services Pty Ltd	Synapse Finance Pty Ltd(i)
API Victoria Pty Ltd(i)	Soul Pattinson (Manufacturing) Pty Ltd	New Price Retail Finance Pty Ltd(i)
Canberra Pharmaceutical Supplies Trust	API Financial Services Australia Pty Ltd(i)	Australian Pharmaceutical Industries (Queensland) Pty Ltd(i)
Pharma-Pack Pty Ltd	Priceline Unit Trust	New Price Retail Pty Ltd
API (Canberra) Pty Ltd	Priceline Proprietary Ltd(i)	PSM Healthcare Ltd(ii)
Making Life Easy - Mobility and Independent Living Superstores Pty Ltd	Pharmaceutical Sales and Marketing Ltd(ii)	Healthcare Manufacturing Group Ltd(ii)
Stevens KMS Equities Ltd(ii)	MLE Unit Trust	The Medicine Shoppe Ltd(ii)
API Healthcare Holdings (NZ) Ltd(ii)	Priceline (NZ) Pty Ltd(ii)	PAF (New Zealand) Ltd(ii)
Garrett Investments Ltd(ii)	Second Priceline Unit Trust	

(i) *These controlled entities have entered into a Deed of Cross Guarantee with the parent entity, refer Note 17, in respect of relief granted from accounting and financial reporting requirements in accordance with the ASIC Corporations (Wholly-owned Companies) Instrument 2016/785.*

(ii) *Entities incorporated in New Zealand. All other entities are incorporated in Australia.*

(b) Entities acquired or incorporated as part of the acquisition of Clearskincare Australia

Entity name	Entity name	Entity name
CSC Holdings Australia Pty Ltd(i)	Clearskincare Adelaide Street Pty Ltd	Clearskincare Bendigo Pty Ltd
CSC Products Pty Ltd(i)	Clearskincare Collins St Pty Ltd	Clearskincare Carindale Pty Ltd
Clearskincare Clinics Australia Pty Ltd(i)	Clearskincare South Yarra Pty Ltd	Clearskincare Chermside Pty Ltd
Clearskincare Cockburn Gateway Pty Ltd	Clearskincare Macarthur Square Pty Ltd	Clearskincare Macquarie Centre Pty Ltd
Clearskincare Parramatta Pty Ltd	Clearskincare Southport Pty Ltd	Clearskincare Norwood Pty Ltd
Clearskincare Warringah Mall Pty Ltd	Clearskincare Cronulla Pty Ltd	Clearskincare South Australia Pty Ltd
Clearskincare Clarence St Pty Ltd	Clearskincare Brighton Pty Ltd	Clearskincare Robina Pty Ltd
Clearskincare Miranda Pty Ltd	Clearskincare Quentin Ave Pty Ltd	Clearskincare Bondi Beach Pty Ltd

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Group Structure (Continued)

16. Subsidiaries (*Continued*)

Entity name	Entity name	Entity name
Clearskincare Cremorne Pty Ltd	Clearskincare Moonee Ponds Pty Ltd	Clearskincare West End Pty Ltd
Clearskincare Leichhardt Pty Ltd	Clearskincare Sunshine Plaza Pty Ltd	Clearskincare Claremont Pty Ltd
Clearskincare Rockdale Pty Ltd	Clearskincare Fremantle Pty Ltd	Clearskincare Northland Pty Ltd
Clearskincare Toowong Pty Ltd	Clearskincare QV Melbourne Pty Ltd	Clearskincare Southland Pty Ltd
Clearskincare Canberra City Pty Ltd	Clearskincare Bondi Junction Pty Ltd	Clearskincare Chirnside Park Pty Ltd
Clearskincare Chatswood Pty Ltd	Clearskincare Carousel Pty Ltd	Clearskincare Mt Lawley Pty Ltd
Clearskincare Doncaster Pty Ltd	Clearskincare Hurstville Pty Ltd	Clearskincare Newmarket Ltd(ii)
Clearskincare Clinics Payroll Pty Ltd	Clearskincare Tokapuna Ltd(ii)	
Clearskincare Clinics Pty Ltd	CSC Ventures Pty Ltd	

(i) These entities are 100% owned. All other entities are 50.2% owned.
(ii) Entities incorporated in New Zealand. All other entities are incorporated in Australia.

17. Deed of Cross Guarantee

Entities which are party to the Deed of Cross Guarantee (Closed Group), entered into in accordance with ASIC Corporations (Wholly owned Companies) Instrument 2016/785, are disclosed in Note 16.

The summarised statement of comprehensive income, retained profits and reserve and the Statement of financial position of the Closed Group, after eliminating all transactions between members of the Closed Group, at 31 August 2018 is set out as follows:

(a) Summarised statement of comprehensive income, retained profits and reserves

	Year ended 31 August	
In thousands of AUD	**2018**	**2017**
Profit before tax	64,938	76,519
Income tax expense	(20,904)	(17,143)
Profit after tax	**44,034**	**59,376**
Other comprehensive income	336	127
Total comprehensive income for the year	**44,370**	**59,503**
Movement in accumulated losses		
Accumulated losses at the beginning of the year	(120,516)	(120,516)
Profit after tax(i)	-	-
Accumulated losses at the end of the year	**(120,516)**	**(120,516)**
Movement in Reserves		
Reserves at the beginning of the year	41,544	15,184
Profit after tax for the year(i)	44,034	59,376
Dividends paid from profits reserve	(34,464)	(34,286)
Other comprehensive income	336	127
Share based payments expense, recorded in equity reserve	(416)	1,143
Reserves at the end of the year	**51,034**	**41,544**

(i) Profit after tax is recognised in the profits reserve which represents current year profits transferred to a reserve to preserve the characteristic as a profit and not appropriate those profits against prior year accumulated losses.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Group Structure (Continued)

17. Deed of cross guarantees (*Continued*)

(b) Closed group balance sheet

	As at 31 August	
In thousands of AUD	**2018**	**2017**
Current assets		
Cash and cash equivalents	20,018	32,878
Trade and other receivables	711,281	677,181
Inventories	291,842	296,083
Total current assets	**1,023,141**	**1,006,142**
Non-current assets		
Trade and other receivables	26,396	48,150
Investments	133,530	133,530
Deferred tax assets	1,475	1,300
Property, plant and equipment	42,605	48,980
Intangible assets	111,260	111,241
Total non-current assets	**315,266**	**343,201**
Total assets	**1,338,407**	**1,349,343**
Current liabilities		
Trade and other payables	793,644	794,962
Loans and borrowings	1,833	1,978
Provisions	13,181	11,470
Income tax payable	5,188	16,807
Total current liabilities	**813,846**	**825,217**
Non-current liabilities		
Trade and other payables	5,895	5,466
Loans and borrowings	18,213	25,365
Provisions	3,474	5,806
Total non-current liabilities	**27,582**	**36,637**
Total liabilities	**841,428**	**861,854**
Net assets	**496,979**	**487,489**
Equity		
Share capital	566,461	566,461
Reserves	51,034	41,544
Accumulated losses	(120,516)	(120,516)
Total equity	**496,979**	**487,489**

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Group Structure (Continued)

18. Parent entity disclosures

(a) Summarised statement of comprehensive income

	Year ended 31 August	
In thousands of AUD	2018	2017
Profit after tax	**50,201**	**57,310**
Other comprehensive (loss)/income	64	(22)
Total comprehensive income for the year	**50,265**	**57,288**

(b) Summarised balance sheet

	As at 31 August	
In thousands of AUD	2018	2017
Current assets	186,914	367,814
Non-current assets	854,031	678,234
Total assets	**1,040,945**	**1,046,048**
Current liabilities	554,869	568,003
Non-current liabilities	23,083	30,853
Total liabilities	**577,952**	**598,856**
Net assets	**462,993**	**447,192**
Equity		
Share capital	566,461	566,461
Reserves	86,915	71,114
Accumulated losses	(190,383)	(190,383)
Total equity	**462,993**	**447,192**
Capital commitments of the parent entity	**349**	**95**

Details of guarantees and contingencies of the parent entity are included in Note 12.

19. Related party transactions

(a) Parent entity

The parent entity of the Group is Australian Pharmaceutical Industries Limited.

(b) Equity interests in related parties

Details of the percentage of ordinary shares held in subsidiaries are disclosed in Note 16.

(c) Key management personnel

Disclosures relating to key management personnel are set out in Note 21.

(d) Transactions with related parties other than key management personnel or entities related to them

Sales to, and purchases from, related parties for goods and services are made on an arm's length basis at normal prices and on normal commercial terms.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Group Structure (Continued)

20. Business acquisitions

On 25 June 2018, the Group announced that it had entered binding agreements to acquire the assets of Clearskincare Clinics and Products business, consisting of a separate clinics and products business. On 31 July 2018, the acquisition was completed and the Group took control of the business.

Clearskincare Clinics is a leading provider of non-invasive aesthetic services such as laser hair removal, skin treatments and cosmetic injectables with 42 clinics in Australia and 2 in New Zealand. The Clearskincare products business is a provider of an exclusive skincare product range.

The acquisition was structured as follows:

- On 31 July 2018 the Group paid cash consideration to acquire a 50.2% controlling interest in the clinic operations and 100% interest in the skincare product business;
- In September 2020 the Group is due to pay $32.9 million to acquire an additional 25% interest in the clinic operations;
- In September 2021 the Group is due to pay $32.9 million to acquire the remaining 24.8% interest in the clinic operations; and
- The Group may be required to pay an additional capped cash consideration of up to $20 million subject to certain performance hurdles being met in 2020 and 2021 ('contingent consideration').

In accordance with AASB 10, the Group assessed that it had control of the entities on 31 July 2018. The results of the acquired businesses have been consolidated in the Group results from close of business on 31 July 2018.

Details of the purchase consideration, the net assets acquired and goodwill are as follows:

In thousands of AUD	Fair value
(a) Purchase consideration	
Cash paid	49,650
Financial liabilities	2,348
Contingent consideration (i)	18,207
Total purchase consideration	**70,205**
(b) Net identifiable assets/(liabilities) acquired based on the provisional fair value at the date of acquisition:	
Provisional net identifiable assets/(liabilities) acquired	**(2,773)**
Less: interest retained by non-controlling shareholders	**2,129**
Provisional net identifiable assets/(liabilities) acquired, net of non-controlling interest	**(644)**
Provisional goodwill on acquisition (a - b)	**70,849**

(i) Determined as the fair value of the contingent consideration payable at acquisition date, being the discounted present value of the amount that may become payable, adjusted for the probability of performance hurdles being met.

The goodwill recognised relates to the value of expected synergy benefits from the business combination, future earnings prospects, skills and technical talent of the acquired business. The goodwill is not expected to be deductible for tax purposes.

As of the date of this report due to the acquisition completing near balance date, the accounting for the net identifiable assets is provisional and has not been finalised due to the ongoing work to be carried out on the identification and valuation of the net assets acquired. Therefore, the amounts recognised maybe subject to change. Finalisation is expected no later than 31 July 2019.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Group Structure (Continued)

20. Business acquisitions (*Continued*)

(c) Other information in relation to the acquisition

In thousands of AUD	Amount
Cash outflows on acquisition:	
Cash consideration paid on acquisition	49,650
Cash outflows on settlement of existing debt	11,924
Less: cash and cash equivalent balances acquired	(4,966)
Outflow of cash - investing activities	**56,608**
Contribution of revenue by the acquired business from acquisition date to year end	3,459
Contribution of profit by the acquired business from acquisition date to year end	274
Acquisition costs expensed in the profit and loss	3,064

(d) Financial liabilities recognised on acquisition

The Group has recognised the following financial liabilities from the acquisition. A summary of these financial liabilities and related accounting treatment is set out below:

Item	Nature and recognition	Carrying amount (AUD $'000)
Contingent consideration	Contingent consideration, subject to certain performance hurdles being met, has been recognised by the Group as a financial liability being the discounted present value of the amount that may become payable.	$18,207
Put and call option	The acquisition includes a symmetrical put and call option with a fixed $32.9 million payable on each of 1 September 2020 and 1 September 2021 for the Group to acquire the remaining 49.8% of Clearskincare Clinics shares not initially acquired. The Group has assessed that the put and call option is virtually certain to be exercised. In accordance with AASB 132 requirements, this liability has been measured at the present value, discounted using a risk adjusted discount rate, of the exercise price of the option which is a fixed amount.	$59,900
Other liabilities	Financial liabilities relating to the mandatory distribution of profits to the non-controlling shareholders have been recognised at fair value.	$11,605
Total liabilities payable to non-controlling shareholders		**$89,712**

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Group Structure (Continued)

20. Business acquisitions (*Continued*)

Business combinations are accounted for using the acquisition method under AASB 3. Key accounting policies and judgements applied by the Group in accounting for the business acquisition are set out below:

Item	Accounting policy
Purchase consideration	The consideration transferred for the acquisition of a subsidiary includes the fair value of the assets transferred, including cash, the liabilities incurred and any equity instruments issued by the Group. Liabilities include any deferred consideration payable, as well an estimate for any future payments that may be payable on future performance of the business. This amount is classified as contingent consideration. Any subsequent changes in the fair value of contingent consideration are recognised in profit or loss. Acquisition related transactions costs are expensed and do not form part of the consideration.
Identifiable net assets	Identifiable assets, liabilities and contingent liabilities acquired are measured at fair value at the acquisition date, which is the date the Group obtains control over the business acquired. If the initial accounting for a business combination is incomplete at the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. The provisional amounts are subsequently adjusted during the measurement period (not exceeding 12 months from acquisition date) to reflect the fair value at acquisition.
Goodwill	The excess of consideration transferred and the amount of any non-controlling interest in the acquiree over the fair value of the net identifiable assets is recognised as goodwill. The Group has elected to apply the proportionate goodwill method, where only the Group's share of goodwill has been recognised, with remaining goodwill allocated to non-controlling interests.
Non-controlling interests	The Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

Key accounting estimate and judgement – business acquisitions

Management judgement has been applied in accounting for the business acquisitions during the year as follows:

- The determination of control and whether the Group has control over the acquired subsidiaries requires judgement. The Group has assessed its ability to govern the financial and operating activities of the acquiree to determine control.
- As part of the acquisition, the Group has entered into a reciprocal put and call arrangement to acquire the remaining non-controlling interest of the clinics business. This liability is recorded at present value.
- The Group has assessed that non-controlling shareholders continue to have present access to returns from ownership of the acquiree. Therefore, the Group has recognised non-controlling interests on a proportionate share basis.
- Fair value of the purchase consideration includes contingent consideration payable subject to certain performance hurdles being met. The Group has assessed the likelihood of these performance hurdles being met and determined the fair value of this contingent consideration.
- The Group has applied judgement with respect to determination of the fair value of net identifiable assets and liabilities acquired with reference to internal and external information.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures

This section provides information on other disclosures that are required by the Australian Accounting Standards or the Corporations Act 2001.

21. Key management personnel disclosures

(a) Key Management Personnel (KMP) compensation summary

In accordance with the requirements of AASB 124 Related Party Disclosures, the KMP included Non-Executive Directors and members of the Group Executive team who have authority and responsibility for planning, directing and controlling the activities of the Group. A summary of KMP compensation, included in personnel expenses, is set out below:

	Year ended 31 August	
In AUD	**2018**	**2017**
Short term employee benefits	2,247,402	2,385,786
Other long term employee benefits	138,389	248,685
Final payouts	220,000	986,988
Share based payments	106,967	904,026
Total KMP compensation	**2,712,758**	**4,525,485**

(b) Individual Directors and Executives compensation disclosures

Information regarding individual Directors and Executives' compensation and equity instruments disclosures as required by Corporations Act S300A and Corporations Regulations 2M.3.03 are provided in the Remuneration report section of the Directors' Report.

Apart from the details disclosed in this note, no Director has entered into a material contract with the Company or its subsidiaries since the end of the previous financial year and there were no material contracts involving Directors' interests existing at year end.

(c) Other Key Management Personnel transactions with the Company or its Controlled Entities

A Director of the Company is a director of a company that have entered into transactions with the Group during the financial year. These transactions are on the same terms and conditions as those entered into by other entities, employees or customers.

No shares were granted during the period to Directors.

Mr R D Millner is a Director of Washington H Soul Pattinson and Company Limited. Washington H Soul Pattinson and Company Limited holds 95,068,472 shares (31 August 2017: 95,068,472 shares) in the Company at year end. In addition, Mr Millner holds 1,755,620 shares in the Company.

During the year, further performance rights were issued by the Company to key management personnel and certain Executives. Share rights forfeited by and issued to key management personnel have been disclosed in the Remuneration report contained within the Directors' Report of this report.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures *(Continued)*

22. Share based payments

	Year ended 31 August	
In thousands of AUD	**2018**	**2017**
Short term incentive plan (STIP)		
Deferred component - 2016 STIP	51	488
Long term incentive plan (LTIP)[(i)]		
2014 grant	-	231
2015 grant	(527)	399
2016 grant	40	518
2017 grant	552	-
Total share based payments expense	**116**	**1,636**

(i) In accordance with AASB 2 Share-based Payment, this amount represents the expense incurred, net of any writebacks, during the year in respect of current incentive allocations to employees. The amounts are therefore not amounts actually received by the employees during the year. Whether the employees receive any equity instruments in the future will depend on the performance of the Company over the vesting period.

(a) Long term incentive plan (LTIP)

The Group has granted equity settled performance rights that entitle key management personnel and senior employees to receive shares in the Company if defined performance conditions are achieved (the LTIP). The LTIP has been established to incentivise employees to generate shareholder wealth and align the interests of the employees with those of the shareholders. Detailed remuneration disclosures, including the link between the LTIP and shareholder wealth, are provided in the Remuneration Report section of the Directors' Report.

Under the LTIP, the performance conditions are assessed by the Remuneration Committee at the next meeting immediately after the end of the vesting period. If the performance conditions are met, the employees are granted shares in the Company proportionate to the level of performance achieved. If the minimum performance hurdles are not met, no shares are granted. The table below summarises the movement in the number of performance rights granted under the LTIP.

Tranche	Grant date	Number of performance rights granted	Balance at start of year	Granted during the year	Exercised during the year	Lapsed during the year	Balance at end of year
Financial year 2018							
2014 LTIP	16 Dec 2014	2,970,348	2,970,348	-	(2,337,905)	(632,443)	-
2015 LTIP[(i)]	13 Jan 2016	1,103,290	1,103,290	-	-	(43,244)	1,060,046
2016 LTIP	1 Feb 2017	924,512	924,512	-	-	-	924,512
2017 LTIP	29 Jan 2018	1,241,012	-	1,241,012	-	-	1,241,012
Total		**6,239,162**	**4,998,150**	**1,241,012**	**(2,337,905)**	**(675,687)**	**3,225,570**
Financial year 2017							
2014 LTIP	16 Dec 2014	2,970,348	2,970,348	-	-	-	2,970,348
2015 LTIP	13 Jan 2016	1,103,290	1,103,290	-	-	-	1,103,290
2016 LTIP	1 Feb 2017	924,512	-	924,512	-	-	924,512
Total		**4,998,150**	**4,073,638**	**924,512**	**-**	**-**	**4,998,150**

(i) Since the end of the financial year, the Remuneration Committee has assessed the performance conditions of this grant which resulted in the vesting of 17.2% of this grant.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures *(Continued)*

22. Share based payments (*Continued*)

Fair value of performance rights granted

Fair value of the performance rights at grant date is independently determined using Black-Scholes option pricing model developed by external consultants. Share performance rights are granted under a service condition and market and non-market performance conditions. Non-market performance conditions are not taken into account in the grant date fair value measurement of the services received.

The fair value calculated through the model and inputs into the model are set out below. Note there were two grants under the 2017 LTIP:

	Tranche 1	Tranche 2
Grant date	29 Jan 2018	13 Feb 2018
Fair value at measurement date	$1.32	$1.36
Model inputs:		
Share price at grant date	$1.43	$1.47
Expected volatility (expressed as weighted average)	35%	35%
Performance rights vesting life	Three years	Three years
Expected dividend yield	4.50%	4.50%
Risk free interest (based on Government bond rates)	2.21%	2.10%

(b) Short term incentive plan (STIP)

The short term incentive plan (STIP) for Executives of the Group is designed to drive key performance measures aligned to strategy and financial objectives. For STIP performance scorecard measures established after 1 September 2012, 50% of any resulting STIP payment is converted from cash to rights to acquire API shares and is deferred for 12 months to encourage employee retention. It is also designed to manage risk by ensuring that decisions taken in the previous reporting period have resulted in sustainable benefit for the Group. Further details of the STIP are set out in the Remuneration Report.

Set out below is a summary of the performance rights granted under the STIP:

Tranche	Grant date	Number of performance rights	Balance at start of year	Granted during the year	Exercised during the year	Lapsed during the year	Balance at end of year
Financial year 2018							
2016 STIP (deferred)	7 Nov 2016	512,718	512,718	-	(512,718)	-	-
No STIP granted in 2017 (deferred component) or 2018 financial years							
Financial year 2017							
2015 STIP (deferred)	21 Oct 2015	983,725	983,725	-	(971,477)	(12,248)	-
2016 STIP (deferred)	7 Nov 2016	512,718	-	512,718	-	-	512,718
Total		**1,496,443**	**983,725**	**512,718**	**(971,477)**	**(12,248)**	**512,718**

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures *(Continued)*

23. Auditors' remuneration

During the year, the Group's auditors, KPMG Australia, provided the following services:

	Year ended 31 August	
In AUD	**2018**	**2017**
Audit services - audit and review of financial reports		
KPMG Australia	538,125	475,000
Overseas KPMG firms	36,000	36,000
Total audit services	**574,125**	**511,000**
Other services		
Due diligence services for business acquisitions - KPMG Australia	774,175	585,000
Other assurance services - KPMG Australia	32,015	61,314
Taxation services - KPMG Australia	35,494	41,205
Taxation services - Overseas KPMG firms	8,640	22,916
Total non audit services	**850,324**	**710,435**

24. New accounting standards

Except as described in this report, the accounting policies adopted by the Group in these consolidated financial statements are the same as those applied by the Group in its financial statements for the financial year ended 31 August 2017.

The Group has adopted the following new and amended accounting standards.

Pronouncement	Date adopted
AASB 2016-1 *Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses*	1 September 2017
AASB 2016-2 *Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107*	1 September 2017
AASB 2017-2 *Amendments to Australian Accounting Standards – Further Annual Improvements 2014-2016*	1 September 2017
AASB 1048 *Interpretation of Standards*	1 September 2017

The adoption of the accounting standards did not have any material financial or disclosure impact on the financial statements.

The Group is required to adopt AASB 9 *Financial Instruments* and AASB 15 *Revenue from Contracts with Customers* from 1 September 2018.

The Group has not early adopted the new or amended standards in preparing the consolidated financial statements. The Group's provisional assessment of the impact of these standards on the financial statements for the year ending 31 August 2019 is set out below.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures *(Continued)*

24. New accounting standards (Continued)

Estimated impact of the adoption of AASB 9 and AASB 15 in the financial year beginning 1 September 2018

The provisional estimated impact of the adoption of these standards on the Group's equity as at 1 September 2018 is based on assessments undertaken to date and is summarised below. The actual impact on adoption at 1 September 2018 may vary to the estimates below because the Group is yet to fully implement the changes resulting on adoption.

	Estimated impact of adoption of AASB 9 and AASB 15			
	As reported 31 August 2018	**Estimated adjustments on adoption of AASB 9**	**Estimated adjustments on adoption of AASB 15**	**Estimated adjusted opening balance at 1 September 2018**
Profits reserve	$99.8 million	Decrease in reported profit reserves of between $0.5 million to $3 million	Increase in reported profit reserves of between nil to $2 million	$99.3 million to $98.8 million

More information on the detailed impacts are summarised below.

AASB 9 Financial Instruments (2014) – to be adopted on 1 September 2018

AASB 9 replaces the existing guidance in AASB 139 Financial Instruments: Recognition and Measurement and prescribes revised guidance on the classification and measurement of financial instrument. This includes a new expected credit loss model for calculating impairment on financial assets, and new general hedge accounting requirements.

The impact on adoption by the Group is summarised below:

Impairment of financial assets

AASB 9 replaces the 'incurred loss' model in AASB 139 with a forward-looking 'expected credit loss' (ECL) model. This requires judgement about how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. The new model will apply to the assessment of impairment of trade receivables held by the Group.

The Group plans to adopt the simplified approach in applying the ECL model. The Lifetime ECL will be determined at each reporting period with reference to the historical credit loss rates across the trade receivables portfolio, adjusted for forward looking observable macroeconomic data that may impact on the Group's future credit risk.

Forward looking observable data used to determine Lifetime ECLs may include:

- Financial conditions of specific counterparties on expected settlement;
- Macroeconomic indicators including consumer spending, GDP growth, unemployment and inflation forecasts; and
- Regulatory or industry specific changes impacting on the retail and pharmaceutical sectors.

The Group has assessed that the impact of applying the ECL model and concluded that the provision for impairment of trade receivables will increase upon the expected adoption of AASB 9 on 1 September 2019 through earlier recognition of potential credit losses. Additional disclosures regarding credit risk and expected credit loss will also be required.

The Group will recognise the effect on the new model upon the expected adoption of AASB 9 at 1 September 2018, with the effect of initial application being recognised as an adjustment in opening profit reserves.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures *(Continued)*

24. New accounting standards (Continued)

AASB 9 Financial Instruments (2014) – to be adopted on 1 September 2018	
Hedge accounting	AASB 9 will require the Group to ensure that hedge accounting relationships are aligned with the Group's risk management objectives and strategies and to apply a more qualitative and forward-looking approach to assessing hedge effectiveness. The disclosures in the financial statements will also include the Group's risk management objectives and strategies. The types of hedging arrangements that the Group currently implements will continue to qualify for hedge accounting under the new standard and are aligned with the entity's risk management strategy and objectives. The current accounting treatment applied by the Group regarding effective cashflow hedges is consistent with the requirements of AASB 9. On initial application of AASB 9, the Group will adopt the transitional arrangements of the standard for all continuing hedge relationships, including assessment of the hedge ratio and rebalancing if required, on 1 September 2018. Any new hedge arrangements entered into on or after 1 September 2018 will be assessed for qualification for hedge accounting under the AASB 9 requirements.
Classification of non-derivative financial assets and liabilities	As at 31 August 2018, the Group's non-derivative financial assets include trade receivables, and cash & cash equivalents. The non-derivative financial liabilities comprise interest bearing liabilities, trade payables and financial guarantees. Based on its assessment, the Group does not expect a significant impact on its accounting for non-derivative financial assets and liabilities.

AASB 15 Revenue from Contracts with Customers – to be adopted on 1 September 2018

AASB 15 establishes a comprehensive framework for determining revenue recognition. It replaces existing revenue recognition guidance, including AASB 15 Revenue, and AASB Interpretation 13 Customer Loyalty Programmes. This new standard is based on the principle that revenue is recognised when performance obligations in the contract are satisfied. The transaction price is allocated to each distinct performance obligation and recorded as the performance obligation is completed. The Group intends to adopt the cumulative effect transition method.

The impact on adoption by the Group is summarised below.

Franchise fees	The Group receives franchise and membership fee income from its franchisees. These include: • Upfront fees received at the commencement of a franchise arrangement, which are currently recognised as revenue upon the signing of the franchise agreement. The Group has assessed that there is no distinct performance obligation that is satisfied at the beginning of a franchise arrangement, therefore under AASB 15 these fees will be deferred and recognised over the term of the franchise agreement. • Brand fees are received from franchisees that include fixed incremental increases over the term of the contract. Under AASB 15, the Group has assessed that there are no significant changes in the performance obligations delivered by the Group over the contract. Therefore, the revenue will be recognised evenly over the term of the contract.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures *(Continued)*

24. New accounting standards (Continued)

AASB 15 Revenue from Contracts with Customers – to be adopted on 1 September 2018	
Return of goods	AASB 15 requires the Group to include an estimate of probable return of goods from its customers, which represents variable consideration of the transaction price. This return obligation is recognised as a liability on the balance sheet. A corresponding asset is recognised where the Group estimates that it will be able to either return the goods to its suppliers, or subsequently sell the returned goods to customers. The application of AASB 15 requirement on variability to the transaction price will not have a material impact on the Group's balance sheet.
Presentation and classification	Through the adoption of AASB 15, the Group has performed a review of the presentation and classification of the revenue streams. There may be changes to the presentation and classification of contributions and rebates received from suppliers within the consolidated income statement. This is expected to have no impact on the net profit of the Group.

AASB 16 Leases – to be adopted on 1 September 2019

AASB 16 replaces the existing guidance on leases and introduces a single, on-balance sheet accounting model for lessees. A lessee recognises a right-of-use (ROU) asset representing the lessee's right to use the underlying asset and a lease liability representing its obligation to make lease payments. The ROU asset is depreciated over the term of the lease and finance charges are recognised on the lease liabilities. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting remains unchanged by the current standard with lessors continuing to classify leases as finance leases or operating leases.

As at 31 August 2018, the Group's future minimum lease payments under non-cancellable operating leases amounted to $163 million. AASB 117 does not require the recognition of any right-of-use asset or liability for future payments for these leases; instead, certain information is disclosed as operating lease commitments in Note 10 of this financial report. The initial impact assessment indicates that these arrangements will meet the definition of a lease under AASB 16 and that the Group will recognise new assets and liabilities for the operating leases held by the Group.

The Group is continuing to assess the impact of adopting the standard. It is expected that the Group's balance sheet will be materially "grossed-up" by the recognition of ROU assets and lease liabilities for all current operating leases, and in turn the key financial ratios will be impacted. The Group has established a project team to continue the assessment and implementation of the standard comprising representatives from the Finance, Treasury, and Property functions. The project team is in the process of progressing the implementation plan, identifying system, data and control changes required.

25. Subsequent events

Details of the final dividend declared since balance date is set out in Note 7.

The Directors have not become aware of any other significant matter or circumstance that has arisen since 31 August 2018, that has affected or may affect the operations of the Group, the results of those operations, or the state of affairs of the Group in subsequent years, which has not been covered in this report.

FINANCIAL REPORT

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Other Disclosures *(Continued)*

26. Reconciliation of cash flows from operating activities

	Year ended 31 August	
In thousands of AUD	**2018**	**2017**
Profit before tax for the year	70,027	76,412
Depreciation and amortisation	28,176	28,624
Reversal of impairment loss on property, plant and equipment	(452)	(1,163)
Foreign exchange loss/(gain)	(3)	67
Net (gain)/loss on sale of stores, property, plant and equipment	1,190	615
Non-cash share based payments	116	1,636
Net finance costs	12,370	12,864
Operating profit before changes in working capital and provisions	**111,424**	**119,055**
Decrease/(increase) in trade and other receivables	19,867	(2,315)
Decrease/(increase) in inventories	4,125	14,438
(Decrease)/increase in trade and other payables[i]	(37,601)	4,655
(Decrease)/increase in provisions and employee benefits	896	(6,021)
Cash generated from operations	**98,711**	**129,812**
Net interest paid	(12,216)	(13,301)
Income taxes paid	(32,844)	(21,029)
Net cash inflows from operating activities	**53,651**	**95,482**

(i) Excluding the effects of acquisition of Clearskincare business.

Reconciliation of cash and cash equivalents to net debt

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the cash management for the Group. The reconciliation of cash and cash equivalents to net debt is included below.

	As at 31 August	
In thousands of AUD	**2018**	**2017**
Cash and cash equivalents	35,948	39,776
Loans and borrowings - current	(2,679)	(2,765)
Loans and borrowings - non current	(89,214)	(29,834)
Net debt	**(55,945)**	**7,177**

DIRECTORS' DECLARATION

1. In the opinion of the Directors of Australian Pharmaceutical Industries Limited ('API'):

    a. the consolidated financial statements and notes set out on pages 34 to 78, and the Remuneration Report set out on pages 20 to 32 in the Directors' Report, are in accordance with the Corporations Act 2001, including:

        i. giving a true and fair view of the financial position of the consolidated entity as at 31 August 2018 and of its performance, for the financial year ended on that date; and

        ii. complying with Australian Accounting Standards and the Corporations Regulations 2001;

    b. the consolidated financial report also complies with International Financial Accounting Standards as disclosed in Note 1(a); and

    c. there are reasonable grounds to believe that API will be able to pay its debts as and when they become due and payable.

    There are reasonable grounds to believe that API and the controlled entities identified in Note 16 will be able to meet any obligations or liabilities to which they are or may become subject to by virtue of the Deed of Cross Guarantee between the Company and those controlled entities pursuant to ASIC Corporations (Wholly owned Companies) Instrument 2016/785.

2. The Directors have been given the declarations by the Chief Executive Officer and Chief Financial Officer for the financial year ended 31 August 2018 pursuant to Section 295A of the Corporations Act 2001.

Dated at Sydney, 17 October 2018

Signed in accordance with a resolution of the Directors:

Mark G Smith

Mark Smith
Chairman

Independent Auditor's Report

To the shareholders of Australian Pharmaceuticals Industries Limited

Report on the audit of the Financial Report

Opinion

We have audited the ***Financial Report*** of Australian Pharmaceutical Industries Limited (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the ***Group's*** financial position as at 31 August 2018 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The ***Financial Report*** comprises:

- Consolidated balance sheet as at 31 August 2018
- Consolidated income statement, Consolidated statement of comprehensive income, Consolidated statement of changes in equity, and Consolidated statement of cash flows for the year then ended
- Notes including a summary of significant accounting policies
- Directors' Declaration.

The ***Group*** consists of the Company and the entities it controlled at the year end and from time to time during the financial year.

Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Group in accordance with the *Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

KPMG

Key Audit Matters

The ***Key Audit Matters*** we identified are:

- Asset valuation (carrying value of goodwill and brand names for Australia and carrying value of goodwill for New Zealand);
- Valuation of receivables (including assessment of financial guarantees); and
- Acquisition accounting of Clearskincare clinics business.

Key Audit Matters are those matters that, in our professional judgement, were of most significance in our audit of the Financial Report of the current period.

These matters were addressed in the context of our audit of the Financial Report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Asset valuation (carrying value of goodwill and brand names of $131.1m for Australia and carrying value of goodwill of $16.5m for New Zealand)

Refer to Note 11 to the Financial Report

The key audit matter	How the matter was addressed in our audit
Asset valuation of the Group's indefinite useful life assets is a key audit matter due to the significant forward-looking assumptions the Group applied in its value in use models being inherently difficult to determine with precision. We focused on the following significant assumptions which impact forecast cash flows: • EBIT growth rates – These are impacted by non-market related factors such as personal care and healthcare sales growth in consumer brands, net franchise store growth, and like-for-like store sales growth in pharmacy and retail sales detailed in the Group's Strategic Plan; • Discount rates which are inherently subjective and vary according to the conditions and environment the specific cash generating unit (CGU) is subject to from time to time and the valuation models approach to incorporating risks into the cash flows or discount rates; and • Terminal growth rates are impacted by market-related factors such as inflation rates which contribute to variability in pharmacy and retail, and consumer brands sales.	Our audit procedures included: • Evaluating the appropriateness of the value in use method applied by the Group to perform impairment testing against the requirements of accounting standards; • Assessing the integrity of the value in use models used, including the mathematical accuracy of the underlying calculation formulas; • Assessing the Group's underlying methodology and documentation for the allocation of corporate costs to the forecast cash flows contained in the value in use models, for consistency with our understanding of the business and the criteria in accounting standards; • Comparing the EBIT growth rates to the Group's Strategic Plan, published industry growth rates and market research reports. We also compared the carrying value and value in use Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) multiples to comparable companies; • Comparing the forecast cash flows contained in the value in use model to the Strategic Plan approved by the Board; • Working with our valuation specialists, we independently developed a discount rate range using publicly available market data for comparable entities, adjusted by risk factors specific to the Group, such as variability in pharmacy and retail sales and the uncertain outcome of government reforms to the Pharmaceutical Benefits Scheme;

The Group's model is sensitive to changes in EBIT growth rates. This drives additional audit effort specific to the feasibility and consistency of application to the Group's strategy. Reasonably possible changes to key assumptions increases the possibility of non-current assets being impaired, plus the risk of inaccurate forecasts or a wider range of possible outcomes for us to consider. The valuation models used to perform impairment assessments include a range of internally and externally sourced inputs. Valuation models, particularly those containing judgemental allocations of corporate costs to CGUs, and forward-looking assumptions tend to be prone to greater risk for potential bias, error and inconsistent application. These conditions necessitate additional scrutiny by us, in particular to address the objectivity of sources used for assumptions, and their consistent application. In addition, the Group has not met forecasts, in particular the New Zealand Consumer Brands business, raising our concern for the reliability of current forecasts. Given the inherent complexity of this key audit matter, we involved valuation specialists to supplement our senior audit team members.	• Working with our valuation specialists, we compared the terminal growth rates to inflation rates published by the Reserve Bank of Australia and NZ Reserve Bank and external economic outlook reports; • Considering the sensitivity of the model by varying key assumptions, such as EBIT growth rates within a reasonably possible range, to identify those CGUs at higher risk of impairment and to further focus our procedures; • Assessing the Group's prior accuracy in forecasting EBIT growth rates, in particular the New Zealand Consumer Brands business. EBIT growth rates are driven by personal care and healthcare sales growth in consumer brands, net franchise store growth, and like-for-like store sales growth in pharmacy and retail sales. We compared historical forecasts detailed in Group Strategic Plans to actual results. We did this to inform our evaluation of forecasts incorporated in the models. We applied additional focus to forecasts in the areas where previous forecasts were not achieved; • Assessing the disclosures in the financial report using our understanding of the issue obtained from our testing and against the requirements of the accounting standards.

Valuation of receivables of $654.7m (including assessment of financial guarantees of $9.9m)	
Refer to Notes 8 and 12 to the Financial Report	
The key audit matter	**How the matter was addressed in our audit**
The Group is exposed to credit risk in relation to overdue trade receivables and long term loans provided as financial assistance to certain pharmacy customers. The recoverable value of these receivables from customers was a key audit matter due to the audit effort to address multiple and varying credit conditions across a large pool of customers. We focused on: • Amendments to standard terms of trade with certain customers, such as long term funding arrangements;	Our audit procedures included: • Assessing the Group's valuation of receivables methodology against the requirements of relevant accounting standards. • Identifying customers with receivables balances which were at greater risk of non-recovery by reading the Group's credit committee reports and inspecting aged debtors ledgers. For those customers at greater risk of non-recovery, our audit procedures included: o Assessing the amendments to standard terms of trade with customers against signed long term funding arrangements. We also assessed patterns of customer's repayments since the amendments for consistency. We followed up unusual or inconsistent patterns;

• The value of security held by the Group over the customers' assets and its impact to the Group's credit risk exposure. In particular, the value of the retention of title on inventory held by the customers, the value of the formal charges over customer's assets used as collateral, and the ranking of the Group's debt compared to other creditors; and • Assessing the Group's subjective judgements related to the customers' ability to repay amounts and the timing of these repayments. The specific trading situations of those customers was critical to our assessment. In addition, the Group disclosed the expected impact of AASB 9 *Financial Instruments*, which will be first adopted by the Group on 1 September 2018. Under AASB 9, credit losses are recognised on an Expected Credit Loss (ECL) basis. Given the subjective judgements by the Group applied in calculating the expected credit losses on an ECL basis, additional audit effort was applied to these disclosures.	o Assessing the value of the security held by the Group over the customer's pharmacy assets by comparing the Group's analysis of value to conclusions of external valuation reports obtained by the Group in relation to similar pharmacy businesses; o Evaluating the objectivity, competence and scope of work undertaken by the external valuation expert appointed by the Group; o Assessing the Group's analysis of the value for other security held by the Group such as retention of title of inventory, formal charges over customer's assets and the ranking of the Group's debt compared to other creditors. This involved comparing the Group's estimates to customer inventory records, property mortgage documents and other information; o Challenging assumptions made about the ability of customers to repay amounts due and the associated timing of repayments. This included assessing the customer's current trading status, payment history, payments made subsequent to year end for its effect in reducing the balance outstanding at year end, and evaluating the actions taken by the Group to recover overdue amounts; • Assessing the ECL model developed by the Group against the criteria in AASB 9, in particular the forward looking assumptions, the outputs compared to the historical write off rates, and the Group's disclosures to the results of the ECL model.

Acquisition Accounting of Clearskincare clinics business	
Refer to Note 20 to the Financial Report	
The key audit matter	**How the matter was addressed in our audit**
The Group's acquisition of 50.2% of the Clearskincare clinics business (clinics business) is a key audit matter due to the: • Size and pervasiveness of the acquisition to the financial statements and consequently was a significant part of our audit; • Judgemental aspects of the Group's accounting for the acquisition of the clinics business, including: o The Group's determination of control and impact on consolidation accounting. This is due to the relatively low ownership interest of 50.2%. Judgement was required by the Group in assessing its power over the relevant activities of the clinics business. o Accounting for the non-controlling interest in the clinics business. Put and Call Option deeds increased the complexity of the accounting for the non-controlling interest due to the interpretation of the key terms and conditions. o Measurement of the provisional contingent consideration relating to meeting earnings targets as per the Sale and Purchase Agreement. This required judgement by the Group to forecast performance of the acquired clinics business, which is inherently difficult given the clinics business is new to the Group. o Provisional fair value of the acquired assets and liabilities recognised at acquisition date. We focused on the fair value of acquired liabilities and property, plant and equipment (PPE) due to the size of these compared to other assets and liabilities acquired. In addition, the Group engaged an external expert to value the PPE. These conditions resulted in significant audit effort and additional scrutiny by us. We involved our senior team members, including technical accounting and valuation specialists in assessing this key audit matter.	Our audit procedures included: • Reading the Sale and Purchase Agreement and Put and Call Option Deeds to understand the terms and conditions of the acquisition. • Working with our technical accounting specialists, we assessed the Group's analysis of control and accounting for non-controlling interest against the criteria in the accounting standards. We did this with reference to the key terms and conditions of the Sale and Purchase Agreement and Put and Call Option Deeds, and our understanding of the acquisition; • Assessing the measurement of the contingent consideration by comparing the earnings targets in the Sale and Purchase Agreement to forecast performance used in the business case for the acquisition, adjusted for changes on integration of the clinics business into the Group; • Examining the provisional fair value of assets and liabilities recorded by the Group in the provisional purchase price allocation calculations, including: o Working with our valuation specialists to assess the valuation methodology used to fair value PPE. We did this by comparing the valuation methodology used by Group's external expert to accepted market practices. o Assessing the scope, competence and objectivity of the Group's external expert with respect to Property Plant and Equipment. o Checking the underlying documentation of subsequent cash payments to extinguish shareholder loans and other third party liabilities acquired. • Assessing the Group's disclosures in respect of business acquisitions, including the provisional accounting, against the requirements of the accounting standards and our knowledge of the acquisition.

Other Information

Other Information is financial and non-financial information in Australian Pharmaceutical Industries Limited's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error
- assessing the Group and Company's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Group and Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with *Australian Auditing Standards* will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the Financial Report.

A further description of our responsibilities for the audit of the Financial Report is located at the *Auditing and Assurance Standards Board* website at: http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf. This description forms part of our Auditor's Report.

Report on the Remuneration Report

Opinion

In our opinion, the Remuneration Report of Australian Pharmaceutical Industries Limited for the year ended 31 August 2018, complies with *Section 300A* of the *Corporations Act 2001*.

Directors' responsibilities

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with *Section 300A* of the *Corporations Act 2001*.

Our responsibilities

We have audited the Remuneration Report included in pages 20 to 32 of the Directors' report for the year ended 31 August 2018.

Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with *Australian Auditing Standards*.

KPMG

KPMG

M. Bisetto

Maurice Bisetto
Partner
Melbourne
17 October 2018

SHAREHOLDER INFORMATION

ASX ADDITIONAL INFORMATION

Additional information required by the ASX Listing Rules and not disclosed elsewhere in this report is set out below.

Shareholdings as at 16 October 2018

Substantial shareholders

The number of shares held by substantial shareholders and their associates as notified to the ASX are set out below:

Washington H Soul Pattinson and Company Limited	95,068,472	ordinary shares
Commonwealth Bank of Australia	25,193,835	ordinary shares
UBS Group AG	24,523,392	ordinary shares

Voting rights

The voting rights attaching to the ordinary shares, as set out in clause 16.2 of the Company's Constitution, are:

a) on a show of hands:
   - (i) if a member has appointed two proxies, neither of those proxies may vote;
   - (ii) a member who is present and entitled to vote and is also a proxy, attorney or representative of another member has one vote; and
   - (iii) subject to paragraphs (a)(i) and (a)(ii), every individual present who is a member, or a proxy, attorney or representative of a member, entitled to vote has one vote;

b) on a poll every member entitled to vote who is present in person or by proxy, attorney or representative:
   - (i) has one vote for every fully paid share held; and
   - (ii) subject to paragraph (c), in respect of each partly paid share held has a fraction of a vote equal to the proportion which the amount paid bears to the total issue price of the share; and

c) unless:
   - (i) permitted under the Listing Rules; and
   - (ii) otherwise provided in the terms on which shares are issued, in calculating the fraction of a vote which the holder of a partly paid share has, the Company must not count an amount:
   - (iii) paid in advance of a call; or
   - (iv) credited on a partly paid share without payment in money or money's worth being made to the Company.

On-market share buy-back

There is no current on-market share buy-back.

FINANCIAL REPORT

SHAREHOLDER INFORMATION *(CONTINUED)*

Shareholders information continued

Distribution of Shareholders as at 16 October 2018

Category

Ordinary Shares	Number of Shareholders
1 – 1,000	3,045
1,001 – 5,000	4,004
5,001 – 10,000	1,732
10,001 – 100,000	2,071
100,001 and over	196
	11,048

The number of shareholders holding less than a marketable parcel at 16 October 2018 was 730 (17 October 2017: 760).

Stock Exchange

The Company is listed on the Australian Securities Exchange. The Home Exchange is Melbourne.

Other Information

Australian Pharmaceutical Industries Limited, incorporated and domiciled in Australia, is a publicly listed company limited by shares.

Twenty largest Shareholders as at 16 October 2018 *

Name	Number of Ordinary shares held	Percentage of Capital held
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	117,738,202	23.91
WASHINGTON H SOUL PATTINSON AND COMPANY LIMITED	95,068,472	19.30
J P MORGAN NOMINEES AUSTRALIA LIMITED	55,093,545	11.18
CITICORP NOMINEES PTY LIMITED	48,831,260	9.91
NATIONAL NOMINEES LIMITED	27,169,617	5.51
PRUDENTIAL NOMINEES PTY LTD	7,000,000	1.42
BNP PARIBAS NOMS PTY LTD	4,971,742	1.01
BNP PARIBAS NOMINEES PTY LTD	4,720,514	0.95
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED – GSCO ECA	1,602,906	0.32
JUM PTY LIMITED	1,567,286	0.31
MR FREDERICK BENJAMIN WARMBRAND	1,460,000	0.29
CS THIRD NOMINEES PTY LIMITED	1,220,822	0.24
MR RAYMOND FRANCIS FREW & MRS GILLIAN MARGARET FREW	1,200,000	0.24
CITICORP NOMINEES PTY LIMITED	1,110,648	0.22
SOPHIA PTY LTD	736,245	0.15
DE BRUIN SECURITIES PTY LTD	725,000	0.14
MR JOHN JOSEPH MURPHY	681,879	0.13
MRS PATRICIA JUNE MURPHY	681,371	0.13
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	653,267	0.13
AMP LIFE LIMITED	615,013	0.12
	372,847,789	75.61

*As shown on the register, beneficial holdings may differ.

FINANCIAL REPORT

SHAREHOLDER INFORMATION *(CONTINUED)*

Shareholder Communications

Enquiries or notifications by shareholders regarding their shareholdings or dividend should be directed to API's share registry:

Boardroom Pty Limited

Grosvenor Place

Level 12

225 George Street

Sydney NSW 2000

GPO Box 3993

Sydney NSW 2001

Telephone 1300 737 760

International +61 2 9290 9600

Facsimile 1300 653 459

Shareholders can also send queries to the share registry via email: enquiries@boardroomlimited.com.au

You can access information about your API shareholding and download forms via the internet by visiting: www.boardroomlimited.com.au

Dividends

If you wish your dividends to be paid directly to a bank, building society or credit union account in Australia contact the share registry or visit the website of Boardroom at www.boardroomlimited.com.au for an application form. The payments are electronically credited on the dividend payment date and confirmed by payment advices sent through the mail to the shareholder's registered address. All instructions received remain in force until amended or cancelled in writing.

Tax File Number (TFN), Australia Business Number (ABN or exemption)

You are strongly advised to lodge your TFN, ABN or exemption with the share registry. If you choose not to lodge these details, then API is obliged to deduct tax at the highest marginal rate (plus the Medicare levy) from the unfranked portion of any dividend. Certain pensioners are exempt from supplying their TFN's. You can confirm whether you have lodged your TFN, ABN or exemption via the Boardroom website.

Uncertificated Forms of Shareholdings

Two forms of uncertificated holdings are available to API shareholders:

Issuer Sponsored Holdings:

This type of holding is sponsored by API and provides shareholders with the advantages of uncertificated holdings without the need to be sponsored by any particular stockbroker.

Broker Sponsored Holdings ('CHESS'):

Shareholders may arrange to be sponsored by a stockbroker (or certain other financial institutions) and are required to sign a sponsorship agreement appointing the sponsor as their 'controlling participant' for the purposes of CHESS. This type of holding is likely to attract regular stock market traders or those shareholders who have their share portfolio managed by a stockbroker.

Shareholders communicating with the share registry should have their Security Holder Reference Number (SRN) at hand or Holder Identification Number (HIN) as it appears on the Issuer Sponsored/ CHESS statements or dividend advices. For security reason, shareholders should keep their Security Holder Reference Numbers confidential.

Annual Report Mailing List

Shareholders (whether Issuer or Broker Sponsored) wishing to receive the Annual Report should advise Boardroom in writing so that their names can be added to the mailing list. Shareholders are able to update their preference via the Boardroom website. Shareholders can also elect to receive the Annual report by e-mail or by accessing the Company website.

FINANCIAL REPORT

SHAREHOLDER INFORMATION *(CONTINUED)*

Change of Address

Shareholders who are Issuer Sponsored should notify any change of address to the share registry promptly in writing quoting their Security Holder Reference Number, previous address and new address. Application forms for Change of Address are also available for download via the Boardroom website. Broker Sponsored (CHESS) holders must advise their sponsoring broker of the change.

Share Trading and Price

API shares are traded on the Australian Securities Exchange . The stock code under which they are traded is 'API' and the details of trading activity are published in most daily newspapers under that abbreviation.

Off-Market Share Transfers

Stamp duty on transfer of listed shares was abolished on 1 July 2001.

Information on API

API has an internet site featuring news items, announcements, corporate information and a wide range of product and service information. API's internet address is www.api.net.au

The Annual Report is the main source of information for shareholders. Other sources of information include:

- Interim results;
- Annual results;
- The Annual General Meeting (the Chairman and the Managing Director address the meeting);
- ASX announcements.

Financial Calendar*

Half year end	28 February 2019
Half year profit announcement	18 April 2019
Year end	31 August 2019
Full year profit announcement	24 October 2019
Annual General Meeting	22 January 2020

*Timing of events is subject to change.

Requests for publications and other enquiries about API's affairs should be communicated to:

Company Secretary

Australian Pharmaceutical Industries Limited

Level 5

250 Camberwell Road

Camberwell, Vic 3124

FINANCIAL REPORT

SHAREHOLDER INFORMATION *(CONTINUED)*

Corporate Directory

Offices and Officers

Company Secretary

Mr Peter Sanguinetti B.Juris, LLB, GAICD

Ms Kylie Barrie LLB (Hons), AAICD

Registered Office

Australian Pharmaceutical Industries Limited

Level 5

250 Camberwell Road

Camberwell Vic 3124

Locked Bag 3002

Hawthorn BC

Vic 3122

Telephone: (03) 8855 3000

International: +61 3 8855 3000

Facsimile: +61 3 8855 3406

Email: legal@api.net.au

Location of Share Registry

Boardroom Pty Limited

Grosvenor Place

Level 12

225 George Street

Sydney NSW 2000

GPO Box 3993

Sydney NSW 2001

Telephone: 1300 737 760

International: +61 2 9290 9600

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