API CEO AGM ADDRESS
WEDNESDAY, 23 JANUARY 2019

Thank you Mark and good afternoon everyone. Thank you especially for making the time to be here, or to listen online.

I will first cover our 2018 financial year operational performance, followed by the main strategic developments and then our current outlook.

In the 2018 financial year, we recorded a slight increase in underlying net profit after tax compared to the prior year. While general trading conditions remained subdued in our major operating businesses, a creditable result was delivered from focussed, diligent management across the company. This focus is demonstrated by the cost of doing business as a percentage of sales again being reduced on the prior year.

The highlights of the performance for the year were:

- Underlying net profit after tax -NPAT - was $54.7 million, up 0.9 per cent on the prior year.
- Underlying earnings before interest and tax – EBIT – came in at $90.5 million, a decrease of 1.5 per cent on the prior year.
- Underlying return on equity rose 51 basis points to 10.29 per cent.
- Underlying return on capital employed was 35 basis points lower at 16.54 per cent.
- Pharmacy distribution achieved underlying sales growth of 6.4 per cent with total revenues of $2.9 billion.
- Priceline Pharmacy total network sales grew 2.1 per cent to $2.1 billion. Like for like sales were down by 1.1 per cent reflecting the pressures that consumers are facing, as Mark referred to in his introduction. This was improved 60 basis points from the first half result.
- The Priceline Pharmacy network stood at 475 stores at the year end, up by a net 13 stores on the previous year.

It is worth noting that these results were achieved in a year where we saw the statutory price changes to the Pharmaceutical Benefits Scheme (PBS) and exclusive direct distribution arrangements reduce our gross profit by more than $10 million – far above the long-term trend and the impact on earnings was well recovered in the circumstances.

At the outset I would like to say that while recent attention has been on our acquisition of Clearskincare and our proposal to merge with Sigma, it is important to note that we have established, sustainable positions in both pharmaceutical wholesaling and in retailing. We are confident that with all our assets we are well placed to leverage our asset base to create further value.

On that note, I want to share with you the new-look API which is building the growth assets that the Chairman mentioned in his address.

Our heritage Pharmacy Distribution business is a steady performer that generates a good return on capital employed and is a source of cash. It plays an important role in enabling growth in other areas, especially Priceline Pharmacy. Critically, Priceline Pharmacy's store growth comes from the relationships we leverage across our thousands of independent pharmacies that we deal with every day in Pharmacy Distribution. The fact we have a broader relationship with our potential partners is highly advantageous.

Clearskincare is a good, emerging business, but one that needs the specialist expertise we have in Priceline Pharmacy in fields such as property development, franchise development and marketing to accelerate its growth. Clearskincare products will also be ranged in Priceline Pharmacy.

Finally, the Consumer Brands product portfolio is ranged in Priceline Pharmacy and is also being leveraged back through our Pharmacy Distribution network of independent pharmacies. We expect that in future Consumer Brands will manufacture products for Clearskincare.

As you can see, there is logic to the horizontal and vertical integration through this portfolio that we seek to maximise. Management focus is on extracting the value from these assets first and foremost so I will now address our operational results.

Let's start with Priceline Pharmacy, where we saw total network sales increase by 2.1% to $2.1 billion. Register like-for-like sales were down 1.1% reflecting retail sales that have been patchy for some time. Having said that, across the health and beauty categories we held market share in the 2018 financial year. We delivered an improved gross margin percentage during the year, we optimised stock levels, saw growth in transactions and basket size, all of which was offset by deflation, mostly from increased consumer purchases on promotion.

While we see ongoing pressure on consumer spending, we have a clear strategy to strengthen our customer offering with a focus in key categories to return sales ahead of market growth rates.

As an example, Beauty is a staple category for us to regenerate growth and we are moving from having a focus on only mass-market brands to extending into selected niche and prestige ranges that the customer is demanding.

During the year we secured the Napoleon Perdis range, which resonates with our customer base and is proving to be a good contributor to sales. We also announced at our full year that we continue to have first to market and exclusivity with highly popular brands such as Bondi Sands, Kristin Ess, Andalou, The Base Collective and Alya. We have further internationally famous brands on the cusp of joining our range that will reinforce the new direction and help to cement that in the minds of our customers.

Across the rest of the store dispensary, skincare and over-the-counter health categories have all showed growth on the prior year. In skincare and health, we continued to expand our ranges and exclusive offerings to take advantage of our market position, which we are carrying into the current year.

Our Sister Club program remains the pre-eminent health and beauty loyalty program in Australia and our key marketing tool. During the year we went beyond 8 million members, and their contribution to total sales increased as we create more value for members. Further investment in this program in 2019 will allow us to better service our members needs and to increase our use of targeted offers. This investment will mean we can be more responsive to prevailing market conditions with the best, targeted offers to drive foot traffic and basket size.

We also expect to commence our 'click and collect' trial later in calendar 2019. This will allow our customers to order online and collect from the Priceline Pharmacy store that is most convenient for them.

Our annual franchise partner satisfaction survey showed that sentiment had improved on the prior year and our Priceline Pharmacy store network expansion continued. We ended the year at 475 stores, up 13 on the prior year. We took a tougher position in our negotiations with landlords; overall this has proved positive in rental outcomes, but it meant we closed uneconomic stores during the year. We see network expansion continuing in the 2019 financial year with demand for new franchise stores remaining constant.

In addition to the developments in Priceline Pharmacy, our Consumer Brands business is experiencing pleasing expansion. Almost two years ago we invested in new management capability and with their achievements to date we are now expecting much more consistent and stronger earnings contributions in the future. In the 2018 financial year EBIT was up $2.1 million on the 2017 financial year of $700,000.

Consumer Brands will be predominantly driven by an excellent portfolio of over-the-counter health products that has no equivalent in the domestic market. The manufacturing and sourcing of product has delivered this extensive range at a highly competitive and sustainable cost. Our confidence comes from a strong pipeline of contracts that will be complemented by new product development and line extensions.

Our toiletries products with brands such as Health Basics and Only Good grew. We are moving these products into new international markets which is embryonic but promising and worth the investment.

In our heritage business of Pharmacy Distribution we managed the PBS price reductions which saw a $10 million gross profit impact which our team almost entirely offset by new business wins and cost savings. When you exclude these impacts of PBS reforms and the effect of Hepatitis C medicines, where sales declined by $155 million, underlying revenue growth was 6.4 per cent. In addition, we maintained our gross profit margin at 7.8 per cent.

To assist our competitive positioning, we established more new stores in our Soul Pattinson and Pharmacist Advice banner brands during the year. We have invested in new professional programs, merchandise and marketing developments and new leadership which has garnered a very positive reaction from independent pharmacies.

The improved offer for independent pharmacies combined with strategic relationships with major groups and retail expertise provides us with the opportunity to continue to hold or improve our market position.

The most significant issue for this business is the regulatory environment. Late in calendar 2018, the Department of Health released new Community Service Obligation (CSO) operational guidelines for the distribution of PBS medicines. The updated Community Service Obligation Deeds, which are a series of distinct agreements between individual wholesalers and the Department of Health, outline how the strict service levels and reporting standards will be maintained across the pharmaceutical wholesaling sector. I'd like to acknowledge the Minister and the Department for recognising the value of the CSO and the principles which underpin it that are critical to the delivery of the National Medicines Policy.

The CSO funding pool remains at the same level as prior years until June 2020, with an option to extend for another two years. It hasn't addressed the rising operational costs that we all face nor fully resolved the issue of having equal access for the distribution of PBS medicines. Nonetheless it does prevent exclusive direct distributors also being in the CSO, which is a step in the right direction.

API, in conjunction with other members of the National Pharmaceutical Services Association, will continue to engage with the Department of Health and the Minister to advocate for the policy settings after 2020 that will allow us to deliver on the Government's commitment to the Australian public.

Finally, I am really delighted to introduce you to the new addition to API, the Clearskincare business. It adds to our portfolio by giving us access to a highly complementary service and product sector, with good potential for us to accelerate its growth. It is a leading provider of non-invasive cosmetic services such as skin treatments, laser hair removal and cosmetic injectables.

It is differentiated from its major competitors in that it has a focus on specialised skin solutions and has an exclusive skincare product range. Importantly, it is not subject to the vagaries of government funding and we can see strong opportunities to grow core treatments within the existing network and to expand into a number of under-serviced geographical markets in both Australia and New Zealand. We have already scoped a number of potential sites in both these markets.

Clearskincare currently has 43 clinics in Australia and two in New Zealand, including the first clinic opened since acquiring the business in the Melbourne suburb of Mordialloc. In the medium term, we see significant opportunities to grow its network and increase its market penetration, in particular by applying our existing customer relationship capabilities.

We are already beginning to reap the benefits of Priceline Pharmacy and Clearskincare's common customer base, via exclusive offers to our Sister Club members.

Overall, Clearskincare's trading is in line with our expectations pre-the acquisition, with EBITDA margins at a very healthy 28 per cent.

In other matters that are important to our company and its performance, API's commitment to the health and safety of its team members is a key focus for management. Last year API achieved the accreditation for AS4801 and this year we achieved the international standard, ISO45001 as we have continued to build our high standards across the company during 2018. The accreditation takes ongoing commitment and diligence from all our team members and is a credit to the safety and wellbeing leadership team.

Like safety, we also take the role of community contribution seriously, and I'd like to share with you some exciting news about our Priceline Sisterhood Foundation. It had a stellar year in 2018, raising more than $1 million for our chosen charities in the month of June. This was achieved by the '*Misterhood for Sisterhood'* campaign, led by the irrepressible Merv Hughes. Merv was ably supported by our dedicated Priceline sisters and the foundation's patron Ita Buttrose.

In total now, since the formation of the foundation just seven years ago, we've raised more than $4.8 million. This year, the charities that will benefit are Dementia Australia, Look Good Feel Better, the Children First Foundation, Perinatal Anxiety and Depression Australia and Raise Foundation. These are wonderful charities with whom we work very closely to ensure that our funding is helping them to meet their strategic goals.

So, a huge thank you is due to our Ambassadors, API staff, and most importantly, our Priceline Pharmacy franchise partners and their staff and customers for what is an outstanding commitment to helping these fantastic charities. API's vision of enriching life as the most inspirational choice for health, beauty and wellbeing is lived through our everyday operations and through the Priceline Sisterhood Foundation the difference we can make is magnified.

In wrapping up, my final comments are directed toward our current trading performance. As I indicated in December, retail trading remained patchy and since then the consumer data and media reports have indicated that has been the case through this period. In the Priceline Pharmacy network like-for-like sales in December were flat on the prior year despite the general weakness reported across retail. To the middle of January like-for-like sales for the year were 0.7% down on the prior year while overall health and beauty market share has been held over the year to November 2018.

Our Priceline Pharmacy and Clearskincare networks will record growth at the end of the February. In Priceline Pharmacy we continue to focus on the right store fit for the most economic benefit and in Clearskincare we will add more clinics to complement the Mordialloc clinic opened at the end of 2018. Consumer Brands is also on track with our expectations for another significantly improved result in the 2019 financial year.

Pharmacy Distribution continues to achieve underlying revenue growth but is still absorbing the PBS reforms impact and issues such as exclusive direct distribution.

Due to our growth assets trading in line with our expectations we expect earnings before interest and tax in the first half of this financial year to reflect 5% growth on the prior year. We expect this operational performance to remain sound, bearing in mind that results for the first half will also see an increase in financing costs, largely due to funding required for the acquisition of shares in Sigma.

Before handing back to Mark I would like to thank him and the Board for their support in pursuing new options for API and also to the management team and all of our team members at API who I know are committed to our direction and often go above and beyond in the work they do.

I look forward to meeting with you later today after the close of the meeting and please feel free to talk to me or any of the other management team that is here today.

Thank you.