



## DAVID JONES ANNOUNCES ITS FUTURE STRATEGIC DIRECTION

**DAVID JONES HAS MANY EXISTING STRENGTHS:** It has a distinctive positioning in the Australian market, a loyal customer base, a strong service ethic, a profitable and well positioned store portfolio, a strong Balance Sheet, robust cashflows and a high dividend payout ratio - all of which position the Company well to leverage the many opportunities that exist for future growth outlined below.

### DESPITE ITS STRENGTHS THE COMPANY FACES CHALLENGES

- **Structural Changes** – the internet is globalising & changing retailing;
- **Macro Economic Headwinds** – retail sales have been flat and rents, labour, utilities & financing costs are increasing;
- **Challenging Australian Consumer Credit Markets** - the Company's card portfolio is exposed to prevailing weak discretionary retail spending. This could result in a halving of EBIT contribution from this business in FY14 when the alliance with American Express converts to a share of underlying profits.

### DAVID JONES WILL ADDRESS THESE CHALLENGES & GROW VIA A “3 POINT STRATEGY”

1. **Transformation:** The Company is in the process of transforming:
  - into an **Omni Channel Retailer (OCR)** modelled on international department store best practice. The Company is investing in technology and realigning its processes & structures. The Company will increase its online SKUs from 9,000 to 90,000 before Christmas 2012. Its OCR offering will integrate the shopping experience across sales channels (i.e. physical stores, web-store, mobile applications, contact centre, social commerce platforms) to enable customers to choose how and when they engage with David Jones, supported by integration and investment in its marketing channels (traditional and digital);
  - its **Customer Service & Engagement** proposition by further investing in customer service & experiences that will differentiate it from competing retailers;
  - its **Pricing** by managing (with its suppliers) the transition to global Cost Price Harmonisation over time;
  - its **Technology capabilities** by increasing its investment & resources in this area with projects such as a new POS system, new traffic analytics, a new end-to-end OCR solution platform, new customer analytic capabilities, new merchandise planning system & a new staff rostering & scheduling system; and
  - its **Management Composition** to ensure its skill base is aligned to its future strategic direction. To date 200 new dedicated (internal & external) staff have been added across the Company's IT, Digital and Operations divisions.
2. **Growing its Store Network:** The Company is planning to:
  - **Open 6 New Stores** in high value locations, all of which are signed up with the landlords & will increase the Company's store foot print to 42 stores nationally. Two of these, Highpoint (Vic) and Indooroopilly (Qld) have commenced construction and are due to open for trade in FY 13 & FY14 respectively. These 2 stores are expected to generate approximately \$10 million p.a. in incremental EBIT. The remaining 4 stores are expected to generate approximately \$20 million p.a. of incremental EBIT when they open.
  - **Open several Smaller Format Stores** (based on the Company's successful Claremont Quarter store) which are expected to deliver at least \$2 million each p.a. of incremental EBIT.
3. **Strengthening the Core Business:** The Company is implementing initiatives that will:
  - continue its track record of offering the **best national and international brands**;
  - reduce its **CODB** by approximately \$30 mil over 3 years to offset some of the expected cost increases;
  - restore its **GP Margins** to a long term sustainable range of 39.5% - 40%;
  - generate incremental Sales and EBIT through **Refurbishments**; and
  - consolidate & grow the revenue generated from the Company's **Financial Services** business.

**FUNDING:** Implementation of the Company's Strategy will require Capex of approximately \$70-\$80 million p.a. This will be largely funded from the Company's Cashflows.

### OUTLOOK & SHAREHOLDER DELIVERABLES

- The Company has implemented a number of new operational and strategic initiatives which will impact total costs in the balance of FY12. These together with the expected continuing challenging trading conditions and the cost of clearing excess Inventory are expected to result in a decline in FY12 PAT of 35-40%;
- Thereafter (assuming no further deterioration in trading conditions and relatively flat LFL sales) **moderate growth** is expected in the **Company's PAT** until there is sustained improvement in consumer sentiment and an improved market outlook in retail sales.
- The Company expects that its Growth & Core Business Strengthening initiatives will deliver incremental EBIT in **FY14** that **offsets** the impact of **rising costs** & the **decline in its FY14 Financial Services EBIT**.
- Whilst the **Transformation** of the Company will take time & initially involve major investment without immediate return, it will provide the Company with a **sustainable business model that can deliver medium – long term PAT growth**. As and when the macro economic environment improves, we expect the Company will be well placed to leverage the sales growth upside and thereby positively impact PAT growth.
- The Board has reaffirmed it's '**not less than 85% of PAT Dividend Payout Policy**'.

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David Jones Limited (DJS) today unveiled its future strategic direction following a detailed review. This review identified:

- The existing strengths of the business;
- The challenges the business faces;
- Opportunities for growth that exist;
- Areas that the Company can improve on that are fundamental to its transformation (eg. Omni Channel Retailing, investment in technology, customer service and customer engagement).

The Company has embarked on a “Three Point Strategy” that builds on its existing strengths, leverages opportunities for growth and addresses the challenges facing the business. Its Strategy involves significant investment and resources which in the short term will impact the Company’s financial performance. The short term financial impacts (2H12 and 1H13) however are outweighed by the benefits that the Company’s transformation are expected to deliver, positioning it as a successful Omni Channel Retailer (OCR) on par with its international peers, building a platform for sustainable future growth in the medium to long term.

## DAVID JONES TODAY – EXISTING STRENGTHS

David Jones today has:

- established itself as the **leading branded department store** in Australia offering a high level of distinctive benefits with its “Home of Brands” strategy;
- **strong brand affinity** with consumers and 174 years of heritage;
- a **strong customer service ethic** and reputation— David Jones was awarded “**Department Store of the Year 2011**” by Roy Morgan Research based on customer satisfaction;
- a **loyal and attractive customer base** that covers three generations (daughter, mother, grandmother);
- a **profitable and well positioned store portfolio**;
- **the best national and international brands** (many on a department store exclusive basis);
- a **department store card/credit card business** that is a profit contributor to the business and delivers customer analytics capabilities;
- **direct ownership of its flagship Sydney & Melbourne CBD stores**;
- a **strong Balance Sheet** with low debt levels and solid cashflows – the Company’s leverage ratio is among the lowest of its peer group with net debt of \$120 million at the end of FY11. The Company generated ~\$350 million of free cashflow over the past 3 years; and
- an **experienced department store team** who know the business well, complemented by people new to the Company with additional skill sets and fresh ideas.

## CHALLENGES FACING THE AUSTRALIAN RETAIL SECTOR

The Company recognises that it (in conjunction with the Australian Retail Sector as a whole) faces a number of serious challenges. These can be divided into three categories:

- Structural changes;
- Macro Economic headwinds; and
- Challenging Australian Consumer Credit markets.

The **Structural Changes** that Australian retailers face relate to the growth of online and the fact that it is changing the way consumers shop by offering new shopping channels and opening up retail competition to not only online retail pure-plays but also bricks and clicks retailers (locally and internationally), domestic and international websites, brands selling through aggregator websites and their own websites, as well as established international retailers opening stores in Australia.

Online retailing has also resulted in greater global price comparisons as well as putting pressure on traditional bricks and mortar retailers to differentiate themselves from online retailers by enhancing their customers’ in-store experiences and improving their customer service.

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The **Macro Economic Headwinds** that Australian retailers are facing are best demonstrated by the fact that department store industry sales have experienced the worst two year period in more than 20 years with cumulative sales down 3.3% over the 2009 to 2011 period<sup>i</sup>. This recent experience has created a more cautious short term outlook, taking account of the current strong \$A, deflation, high levels of household savings and increased net outbound tourism. This has resulted in the Company taking a conservative assessment of recovery in LFL sales in the near term.

Overlaying this is an environment of increasing costs for Australian retailers in areas such as labour, utilities, rent and financing.

David Jones' store and credit card members are retail oriented consumers and as such the performance of the Company's credit card portfolio is connected both to the performance of the discretionary retail environment and the consumer credit environment. Since the launch of the David Jones American Express card in September 2008 growth in the **Australian Consumer Credit Card Market** has deteriorated substantially as has the Australian Discretionary Retail Environment. Since 2008 the year-on-year growth of the number of the Australian credit cards issued has declined by 48% (from 7.1% (the 10 year average until 2008) to 3.6% p.a (the average since 2008))<sup>ii</sup>. The year-on-year growth of Australian average spend per account has dropped by 89% (from 11% (the 10 year average until 2008) to 1.2% p.a (the average since 2008))<sup>iii</sup>.

Over the past three and a half years the Company has introduced a number of initiatives to improve the performance of its Financial Services business. These initiatives however have not been sufficient to overcome the impact of the prolonged downturn in the discretionary retail and consumer credit markets. As a result the Company has not achieved the underlying Financial Services growth it had anticipated in 2008 when it entered into its alliance with American Express. In FY14 when the alliance between David Jones and American Express converts to a sharing of underlying profit, David Jones expects the EBIT contribution from its Financial Services business to broadly halve.

## ADDRESSING THE CHALLENGES & GROWING THE BUSINESS

The Company acknowledges the challenges it faces and is implementing a "Three Point Strategy" to address these issues and to build the foundation for a successful and sustainable long term business. This strategy involves:

### 1. TRANSFORMATION

The Company recognises that the way customers wish to interact and shop with retailers has fundamentally changed and will continue to evolve over the coming years.

In order to succeed and prosper in this environment, retailers must adapt to the changes taking place. David Jones has embraced the need to change and is focussed on transforming into an OCR based on international department store best practice, including the successful Nordstrom model (which in 2009 generated 10% of its Sales and more than 20% of its EBIT from its online business<sup>iv</sup>) as well as transforming its physical store experience by investing significantly in customer service and engagement, technology and management expertise.

#### 1.1 Omni Channel Retailing (OCR)

The transformation of David Jones into an OCR will enable the Company's customers to choose how they engage with David Jones, knowing they will receive a seamless experience across all sales channels.

This transformation will take time and require investment and resources. The Company is investing in technology, people and processes with a focus on integrating the shopping experience across all of David Jones' marketing channels (traditional and digital) and sales channels (physical stores, contact centre, webstore, mobile applications and social commerce).

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David Jones CEO Paul Zahra said, “Whilst we acknowledge that our transformation into an OCR will take time, given online retailing in Australia in 2011 accounted for 4.9%<sup>v</sup> of total retail sales we are confident we can move at the right pace to capitalise on this opportunity.

“The success of international department stores such as Nordstrom (US) and John Lewis (UK) who have adopted OCR business models clearly demonstrates that there is great potential for well managed Omni Channel department store businesses that build on their existing network of stores, their existing customer base and their existing brand positioning to offer customers new ways to shop and different shopping experiences.

“This is further reinforced by the fact that in the United States 17 of the top 25 online retailers are domestic “bricks and clicks” businesses<sup>vi</sup>. The US experience indicates that having a physical presence enhances your online offer and provides customers more flexibility and choice in the way they wish to shop – making it a preferred model from the customer’s perspective.

“International experience suggests that Omni Channel shoppers are four to six times more valuable than single channel customers<sup>vii</sup>, which demonstrates the size of the opportunity for us.

“We are confident that the transformation we have commenced is the right framework for our Company’s ongoing future success. Over time we expect approximately 10% of our total sales to be generated through our web-store, mobile applications and social commerce site. We also expect improved service and sales in our physical stores through greater inventory visibility, an integrated Gift and Bridal offer and improved customer service and in-store experience,” Mr Zahra said.

### **Progress to Date in Transforming David Jones into an OCR**

David Jones’ has already made progress in its transformation into an OCR.

**In September 2011** the Company launched a bespoke **Mobile Site** featuring functionality focused on enhancing the in store experience. Already 15% of all traffic to the Company’s web address is coming via this mobile site.

**In November 2011 free delivery** for David Jones’ American Express and store card holders for standard purchases either online or in-store was introduced by the Company. This resulted in the online share of tender doubling. David Jones is leading the way in Australia by offering free standard delivery across all channels for selected customers.

**In late November 2011 the David Jones online “Gift Finder” & “Christmas Hub”** were launched and proved to be the most visited areas of the Company’s website.

**In December 2011 the Company launched its “Brand finder”** on its website and mobile site which enables customers to search for their favourite brands across the store network.

**On 10 February 2012** the Company announced that it had **appointed IBM** to provide an end-to-end OCR solution platform and it is now focussed on delivering a seamless, consistent and enriched shopping experience anywhere, anytime, every time across its physical stores, web-store, mobile applications and social commerce channels – all of which are designed around what customers need and want.

**On 15 February 2011** the Company **live-streamed the David Jones Autumn/Winter Collections** launched to a live public audience of approximately 5000 people. David Jones currently has **over 120,000 Facebook fans** and this is growing rapidly. The Company’s Facebook community is larger than any comparable Australian retailer. More importantly David Jones’ Facebook fans are highly engaged compared to retailers locally and internationally with 10% of the Company’s fans talking about David Jones compared to 2% for Nordstrom and 3% for Selfridges<sup>viii</sup>.

### **Next Steps in the Company’s OCR Transformation & Customer Deliverables**

The next steps in David Jones’ transformation into a fully integrated OCR are as follows:

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**BY CHRISTMAS 2012: LAYING THE FOUNDATION**

The primary focus of the Company is to lay the foundation for future growth and development as an OCR by implementing the systems platforms, organisational structure and processes required to support the Company's transformation. The new systems to be implemented by Christmas 2012 will include the new IT system provided by IBM including a new web-store, content management system, order management system and warehouse management system.

Progressively throughout 2012 the David Jones customer experience will improve through the **introduction of incremental sales channels** including:

- a. **The New David Jones Webstore:** in 1Q13 a new web-store will be launched featuring approximately 90,000 SKUs. This compares favourably to Macy's which has 50,000 SKUs online and Nordstrom's which has 138,000 SKUs online<sup>ix</sup> and is a major improvement on the current offering of only 9,000 SKUs. A further extension of the web-store will be rolled out in 2Q13 with enhanced functionality such as customer reviews and ratings, additional carrier options and additional payment plans. This will ensure that David Jones' online offer is competitive from both a local and international perspective.
- b. **Launch of a transactional mobile web-store:** The new David Jones web-store will be optimised by enabling customers to utilise their mobile devices to research, browse and shop on the go across all major mobile devices.
- c. **Launch of Native Mobile Applications:** David Jones customers will have the ability to browse, purchase and organise delivery via a native application designed for their mobile device.
- d. **Launch of Social Commerce Store:** Customers will be able to browse, purchase and organise delivery all within the social commerce channel via the Company's Facebook platform.

**These sales channels will be integrated via:**

- a. **Integrated Marketing Program:** The Company has commenced integrated marketing across both traditional and digital marketing. Social marketing will continue to be a focus via Facebook and there will be a realignment of marketing spend towards the digital channel with greater emphasis on search engine marketing.
- b. **Integrated Product Offer & Content.**
- c. **Integrated View of Inventory and Fulfilment across all Channels** enabling customers to:
  - Browse and review stock levels across all stores;
  - Organise delivery or pick up in store of choice;
  - Arrange shipment of big ticket items directly;
  - Process returns via any channel.
- d. **Integration with David Jones' Corporate site:** in line with the launch of the new David Jones webstore the Company's website corporate pages will also be upgraded.
- e. **Integration of store-based activities:** such as appointment bookings and Gift Registry purchase capture across all sales channels.

**2013 ONWARDS: SETTING NEW EXPECTATIONS**

David Jones recognises that implementation and development of its Omni Channel strategy will be an ongoing process. The Company is planning to invest, learn and respond to its customer's needs and to continue evolving.

Significant capital has been set aside in the Company's Capex allocation each year to address components of its OCR offer. With the foundations laid by Christmas 2012 the next stage looks to deliver on new expectations. The web-store will continue to be enhanced through the roll-out of initiatives such as new customer offers, 3D product gallery and integrated gift vouchers offer. The Company will also launch a fully integrated Gift and Bridal offer including the ability to set up and maintain a list across all channels, develop

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A.B.N. 75 000 074 573



a '**store of the future**' format that fully integrates new technology and services and continues to focus on customer analytics and trigger marketing across all channels.

## 1.2 Customer Service & Engagement

The Company recognises that as part of its transformation into a successful OCR it also needs to focus on customer service and customers' shopping experience. As various channels of retailing emerge and gain popularity customers are increasingly expecting more in terms of service and experience when they venture into physical stores.

To address this expectation the Company is investing significantly in Customer Service and Engagement initiatives.

Examples of the initiatives that the Company has or is rolling out include:

- Investment in **increased floor staff hours** as a relative proportion to sales;
- The creation of **100 new floor staff supervisor roles**;
- The creation of over **200 new, innovative frontline service roles** across the entire store portfolio that will deliver differentiated and specialised services to customers;
- The continuation of investment in **frontline training** to improve selling and conversion skills;
- The provision of better **performance reporting** to frontline staff to enable tracking against targets;
- An **increase** in the Company's **Incentive program** for frontline staff to drive sales and reward high performance. **All David Jones floor staff** (not incentivised directly by brands) are **eligible to earn performance based incentives** over and above their base salary;
- Adding resources to other **critical customer service touch points** for example additional staff in fitting rooms;
- **90 additional new in-store customer events** and promotions per annum (over and above the Company's existing calendar of events);
- Australia's **first ever department store Bridal suite "Bridal at David Jones"** – the Australian Bridal market is valued at \$4.3 billion in 2012 and is expected to grow by 1.7% p.a. over the next few years<sup>x</sup>. David Jones is well positioned to carve out a profitable share of this market with the introduction of the Bridal at David Jones suite, the Company's newly refurbished Gift registries and the newly introduced David Jones Celebration Card.

The Company's investment in Customer Service will continue recognising and responding to emerging trends in customer shopping habits (e.g. OCR) as well as more traditional expectations of training and supervision.

## 1.3 Cost Price Harmonisation Initiative & Deflation

Price differentials have always existed in the Australian retail sector when compared to international retailers. This has however become increasingly transparent (to both consumers and retailers) due to the growth of online retailing, the strong A\$ and increased outbound tourism.

International Price Differentials are the result of four factors:

1. The **A\$** which is trading at all time highs. This is something that the Company cannot control. The Company acknowledges that the dollar fluctuates, however if it falls this will adversely impact the attractiveness of offshore online shopping and outbound tourism.
2. The **GST and tariff exemption** that offshore purchases under \$1000 enjoy, which creates an 'unfair playing field' in the Australian market. The Productivity Commission has acknowledged that this threshold is too high and has established a task force to review cost efficient ways of collecting the GST and tariff on a lower threshold.
3. The third factor is in the Company's control and relates to **negotiating with suppliers** to ensure that the wholesale price it buys at is comparable to that paid by offshore department stores. A

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A.B.N. 75 000 074 573



report on the Australian Retail sector prepared by the Productivity Commission in 2011 examined the issue of price differentials between Australian and offshore retailers and concluded that this was not the result of Australian retailers having higher gross margins. The Commission concluded that Australian department store gross margins are on par with their international peers.

4. Australian retailers supporting Australian workers and Australian working conditions.

Addressing price harmonisation is important in order to protect its customer value proposition and to avoid sales leakage. This does however involve working with suppliers and addressing existing and entrenched distribution channels, which will entail lengthy and complicated negotiations.

The Company has commenced a detailed work program to address the cost price harmonisation issue. Suppliers to whom the issue of price transparency relates have been advised of the Company's concerns and proposed next steps.

The Company is not alone in initiating these discussions with suppliers as price harmonisation is becoming a worldwide initiative. Bricks and mortar retailers in Canada and US such as Target USA have commenced these discussions, so suppliers are well aware of the issue and recognise that it needs to be addressed<sup>xi</sup>. In fact some suppliers such as Yves Saint Laurent, Kiehl's, Lancome, Fossil and DNKY have already taken the initiative to decrease their Australian cost prices.

David Jones CEO Mr Paul Zahra said, "The concept of price harmonisation around the world is well understood and applied by international luxury brands. These brands understand that in order to preserve the value and positioning of their brands they cannot have material price discrepancies in different geographic markets as it will focus consumers on price as opposed to the allure, status and fashionability of the brand".

Whilst the Company recognises that Price Harmonisation is a clear objective it does carry with it the issue of deflation. As a result in working towards Price Harmonisation the Company's objectives are to:

- Ensure its Gross Profit margin percentages are preserved as part of the negotiations with suppliers; and
- Capture extra volume as a result of the decreased retail price, with a view to help offset the impact of deflation on the Company's NPAT.

## **1.4 Technology Focus**

The Company is placing significant focus on and investment in Technology in order to improve service, generate efficiencies and savings within its business.

Key projects being invested in and rolled-out include:

- A new Point of Sale System (POS);
- A new end-to-end OCR solution platform;
- Traffic analytics enabling store management to be accountable to new key retail Key Performance Indicators (KPIs) relating to sales conversion rates;
- Workforce Management enabling real-time scheduling and costing of labour to ensure the best service option is implemented;
- A Merchandising Planning Tool; and
- Automation of calculation and collection of rebates, mark-downs, advertising etc.

## **1.5 Management Composition**

Given the future strategic direction of the Company and the increased emphasis on OCR, Digital Marketing, Technology, Customer Service and Customer Engagement the composition of the management team needs to be realigned to ensure expertise and capability in these areas are adequately covered.

**DAVID JONES**

David Jones Limited A.C.N. 000 074 573  
A.B.N. 75 000 074 573



**200 dedicated, new staff** (comprising permanent employees, contractors and consultants) have been added to strengthen the Company's IT, Digital and operations capabilities.

The Company has created a new Executive Committee position dedicated to the development, implementation and integration of the Company's OCR strategy across all parts of the Company. David Robinson was appointed to this role in August 2011 and since that date a strong OCR team has been established.

The Company has also restructured its Information Technology and Property Areas into Retail Services (headed by Antony Karp) to reflect the Company's transformation into a fully integrated OCR. The Information Technology team has been bolstered through the addition of IT specialists.

A new Digital Marketing team has been established comprised of **11 externally appointed experts** in this area. In addition Visual Jazz (a digital creative agency) have been appointed to work with the new Digital Marketing Team to deliver the David Jones Facebook page, Fashion Hub and the look, feel and functionality of the new David Jones web-store.

The Company is continuing to review its Management composition to ensure its skill base is aligned to the future strategic direction of the Company.

## 2. GROWING STORE NETWORK

Unlike its Australian peers David Jones has a relatively small footprint in terms of physical stores. The Company currently has 36 department stores, all of which are profitable and located in high value areas with strong demographics and growth potential.

Given the relatively modest size of the Company's store portfolio there is significant scope to open more stores in attractive locations in which David Jones should be represented which will in turn support the Company's OCR strategy and enable customers to choose where, how and when they wish to shop.

### 2.1 New Full Line Department Stores

The Company has announced six new stores that will increase the Company's footprint to 42 stores nationally. These are Highpoint (Vic) which is scheduled to open in the first quarter of calendar 2013 and Indooroopilly (Qld) which is scheduled to open in the first quarter of calendar 2014 – both of which are under construction. In addition the Company has signed "Agreements to Lease" for new stores at Macquarie (NSW), Whitford (WA), Pacific Fair (Qld) and Sunshine Plaza (Qld) which are scheduled to open subject to the landlords' development schedules.

All of these new stores are in high value, high growth areas and will result in the Company's store portfolio increasing to 42 stores. The expanded physical store network is part of the Company's fully integrated OCR strategy and each new store (starting with Highpoint) will be specifically designed as a "store of the future" that complements and enhances the Company's OCR strategy.

The existing stores in the Company's portfolio are all profitable and the six new stores to be opened are expected to generate incremental Sales of at least \$280 million p.a. and an additional \$30 million p.a. of EBIT by maturity.

### 2.2 New Smaller Format Stores

In addition to the new full line department stores the Company also plans to open several **smaller format David Jones stores** in attractive locations. These stores will be approximately 7000 sq. m in size and will be based on the format of the successful David Jones Claremont Quarter (WA) store. Each small format store opened is expected to deliver \$2 million of incremental EBIT.

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David Jones Limited A.C.N. 000 074 573  
A.B.N. 75 000 074 573





Possible locations are in areas with good demographics which do not have major shopping centres located within the area. It is expected that the cost of opening these smaller format stores will be borne by a combination of the landlords, David Jones and suppliers.

The smaller format stores are consistent with the Company's core business, leveraging existing merchandising, operating and service capabilities as well as the David Jones brand and will be designed as "stores of the future" that complement and enhance the Company's OCR strategy.

### 3. STRENGTHENING THE CORE BUSINESS

In addition to generating revenue through its Growth Initiatives the Company has significant scope to generate incremental EBIT by improving areas of its core business. Set out below are details of the initiatives the Company is undertaking in this regard.

#### 3.1 Best National & International Brands

The Company is continuing to invest in and add to its brand portfolio. It is focussed on adding new national and international brands that customers want and that ensure its brand offering remains fresh, exciting and new. Over the past 15 months the Company has introduced 138 new brands into its business.

The Company has a strong and capable merchandise team with a successful track record of being able to identify and secure the best brands across all of David Jones' categories.

#### 3.2 Cost of Doing Business (CODB) Reductions

The Company has identified a number of CODB reductions that are expected to deliver approximately \$30 million of incremental EBIT over the next 3 years. This \$30 million will go some way to offset the Company's expected cost increases in terms of labour, rental, utilities and financing costs without impacting service levels.

These CODB reductions will be derived from a variety of areas and will ensure that customer service is further enhanced. Examples of the CODB reductions include:

- Elimination of store administration tasks through the introduction of a new workforce management tool for rostering and scheduling;
- Interface the production of all shelf-talker price tickets with our inventory management system to eliminate manual processes;
- Automating store reconciliation tasks through the interface of cash management equipment with the Company's financial systems; and
- Reducing supply chain costs base focussing on big ticket deliveries, import processing and logistics costs and recoveries.

#### 3.3 Gross Profit (GP) Margin Improvements

The Company is implementing five gross margin initiatives which are expected to return its GP margins to a long term sustainable range of 39.5% to 40%.

The expected improvement in GP Margins will primarily be delivered by:

- Investment in a new all-encompassing merchandise planning system
- Improve trading terms and exclusive arrangements by reviewing all vendors against benchmarks
- Improving the efficiency of rebate collection by automating the process.
- Low Profit Department Review.
- Ongoing investment in securing exclusive, unique partners and allocation of space to high margin departments.

#### 3.4 High Value Refurbishments

Whilst the Company has over the past eight years significantly refreshed its store portfolio there is scope for the **refurbishment of five high-value stores** over the next few years. These

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David Jones Limited A.C.N. 000 074 573  
A.B.N. 75 000 074 573



refurbishments are expected to deliver approximately \$10 million of incremental EBIT upon completion.

The stores that will be refurbished are:

- Miranda (NSW);
- Elizabeth Street (NSW) (Ground & Lower Ground floors);
- Karrinyup (WA);
- Burwood (NSW); and
- Toowong Village (Qld).

Mr Zahra said, "Our store refurbishments have delivered a significant positive contribution and high return on investment. We intend to continue this track record with our High Value Refurbishment Program by ensuring that each proposed refurbishment is EBIT positive immediately upon completion of the refurbishment.

"Our objective with each refurbishment is to leverage the improving wealth demographics of our existing store locations by:

- reallocating space to higher margin categories and brands hence improving profitability;
  - reinforcing our "Home of Brands" positioning through our brand installations;
  - improving space productivity by converting existing non-productive space into selling space;
- and
- generating long-term Sales and EBIT growth," Mr Zahra said.

The impact of all of the planned refurbishments has been factored into the Company's Future strategic direction. The refurbishment program is structured so that as the Company completes one refurbishment it moves into another so that there is no net adverse impact to Company EBIT in any year.

Most importantly the Company's physical stores will be refurbished and tailored as part of its transformation into an OCR. Highpoint (Vic) which will open in early 2013 will be the first physical store that encapsulates the "store of the future" concept and has been designed to incorporate the features required for OCR. Highpoint will represent the prototype store format that will be rolled out in all future new stores and adapted to existing stores to ensure they are "OCR friendly".

### **3.5 Financial Services Initiatives**

David Jones' Financial Services business is important in that not only does it provide highly valuable customer analytics capabilities but it also delivers an annual revenue and profit stream for the Company.

In April 2012 the Company will implement a **new customer database** that will give David Jones improved capability to tailor offers that customers value based on their spending behaviour at a product level across categories.

From 2008 (when the Company entered into its alliance with American Express) to the end of FY13 the Company will have received more than **\$230 million of EBIT** from this business as well as retaining ownership of its customer base and being entitled to an ongoing revenue stream through its profit sharing arrangement with American Express which comes into effect in FY14.

Whilst the growth of the Company's Financial Services business has not been in line with what was anticipated in 2008 due to the deterioration of the discretionary retail environment and the consumer credit card market, the Company now expects **flat EBIT growth** in its **Financial Services business in 2H12 and FY13**. The difference between 7.5% EBIT growth and flat growth during this period equates to **\$7.5 million**. These funds will be **reinvested** in the Financial Services business to implement several initiatives.

When the David Jones/American Express alliance converts to a share of underlying profits in FY14 the Company expects its share of the EBIT generated by this business to be broadly half the EBIT contribution in FY13.

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In order to increase the revenue generated by the Company's Financial Services business the following initiatives are planned to be implemented:

- **Launch Platinum Card:** The David Jones Platinum card is planned to be launched in the second half of calendar 2012. It is targeted to a premium customer segment that values unique and retail oriented benefits and will provide these customers with a premium rewards program and unique retail in-store benefits and experiences.
- **Drive Everyday & External Spend:** The Company launched its new "3,2,1" value proposition on 10 October 2010 which offers higher point earn rates for everyday spend categories and expanded redemption options. This has been well received by card-members and has driven a 30% uplift in spend on everyday categories at major supermarkets and petrol stations. Approximately 75% of spend on the David Jones American Express cards now occurs outside David Jones stores. The focus is on promotions and bonus points rewarding spend, new customer sign ups, engagement initiatives and an increased focus on the issue of supplementary cards. In addition in the second half of calendar 2012 the Company plans to further improve the rewards program on the David Jones American Express Card.
- **New Events & Promotions:** More than 40 new in-store card customer events and promotions are being introduced to leverage David Jones' unique retail assets in order to drive in-store spend and customer retentions.
- **Re-Focus on Store Card:** Initiatives focused on improving the value of the David Jones store card and better benefits for store card holders have commenced including new rewards for store-card customers which are being rolled out in the second half of calendar 2012.
- **Expand Card Related Insurances:** Increased focus on consumer insurances (such as travel, secure ID and personal accident cover) which provide additional services to the Company's cardmembers.

## FUNDING

Implementation of all of the key components of the Company's future strategic direction will be predominantly funded by the Company's cashflows as well as landlord and supplier contributions. The Company's Capital Expenditure (Capex) is expected to be between \$70 - \$80 million p.a.

## OUTLOOK

The Company's "Future Strategic Direction" has been formulated on the basis that the recent macro economic conditions impacting LFL sales growth will continue and that certain costs such as labour, occupancy and utilities will increase. The Company expects a recovery in retail sales will arise during the planning period but, as its timing is uncertain, this has not been taken into account in the plan.

As and when the macro economic environment improves we expect the Company will be well placed to leverage the sales growth upside and thereby positively impact PAT growth.

The "Transformation" component of the Company's future strategic direction will require significant investment over the next 18 months. This investment will have short term financial implications for the Company in 2H12 and 1H13.

In addition, the Company's "Growth Initiatives" will require capital and the initiatives implemented to "Strengthen the Core Business" will result in certain costs being incurred over the next 12 months.

The Company's PAT Guidance for FY12 is a decline of 35% - 40% on FY11. This outlook for the full year reflects both current trading performance and the cost of new strategic initiatives. The two key components affecting the expected result are:

- A sales decline in 2H12 and clearing costs associated with excess inventory:

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- Transformational initiatives with direct and indirect costs associated with 200 new personnel in IT, a new IT platform, a new POS system, a new Merchandise Planning Tool and Traffic Analytics, an increased investment in customer service, as well as restructuring costs

Other components impacting the expected result include:

- Financial Services EBIT growth slowing from 7.5% p.a. over the past 3.5 years to flat;
- Interest Costs increasing substantially due to the establishment of the new bank facility, reflecting current funding margins;
- Increasing costs relating to the Company's labour, occupancy and utilities cost;
- The cycling of one-off benefits to Profit in 2H11 resulting from the significantly reduced employee incentives paid that half due to the downturn in performance in that period.

The Company expects its Growth Initiatives and the Strengthening of its Core Business to deliver incremental EBIT in FY14 that will offset the adverse impacts on EBIT of increasing Costs and the conversion of the Financial Services business into a sharing of underlying profits.

The Company's plan beyond FY12 is formulated on the basis that LFL sales growth is relatively flat and on that basis, expects moderate PAT growth. Upon a recovery in retail sales, the Company is well placed to enjoy an acceleration in that growth.

## **SHAREHOLDER DELIVERABLES**

David Jones CEO Paul Zahra said, "David Jones today has many key strengths from which we can build the platform for our transformation into a successful Omni Channel Retailer. We have a distinctive brand and market position as Australia's leading branded department store, a loyal and attractive customer base, a unique brand portfolio, a profitable 36 store portfolio, low debt levels, ownership of our flagship Sydney and Melbourne CBD stores, healthy cashflows and a strong Balance Sheet.

"We have entered an era which is both challenging and full of opportunity and are well positioned and prepared to adapt to the changing environment around us. Based on the success of international Omni Channel department stores we are confident that we have the right strategy in place to deliver sustainable future growth for our shareholders.

"Our "Three Point Strategy" will enable us to create a strong business model from which the Company will be well positioned to deliver year on year sustainable PAT growth. It will provide us with enormous leverage to generate sales and PAT growth as and when the macro-economic environment improves," Mr Zahra said.

The Board of Directors has reaffirmed the Company's dividend pay-out ratio of not less than 85% of Profit after Tax and the growth of Dividends in line with PAT.

ENDS

### **FOR FURTHER INFORMATION CONTACT:**

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A.B.N. 75 000 074 573



NOTES:

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<sup>i</sup> ABS series 5206 Table 3, 8501 Table 1

<sup>ii</sup> RBA (Credit cards with an interest free period excluding charge cards and cards issued to businesses), Dec 2011, ABS 8501, Table 1, Jan 2012

<sup>iii</sup> RBA (Credit cards with an interest free period excluding charge cards and cards issued to businesses), Dec 2011, ABS 8501, Table 1, Jan 2012

<sup>iv</sup> Nordstrom Annual Report, 2009

<sup>v</sup> NAB/Quantum :NAB Online Retail Sales Index: 27 February, 2012

<sup>vi</sup> US Top 500 Online Guide, PJP analysis

<sup>vii</sup> Saks' Incandela: Multi Channel Retailing is Critical by Sharon Edelson 8 Feb 2012

<sup>viii</sup> Facebook Insights, 29 February 2012

<sup>ix</sup> Internet Retailer Portal to e-Commerce Intelligence, 2011 Edition, Vertical Web Media, BPA Worldwide

<sup>x</sup> IBISWorld 2010

<sup>xi</sup> Target takes aim at web-only retailers", Internet Retailer, 23 January, 2012

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