

NZX and Media Release

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FINANCIAL RESULTS FOR THE YEAR TO 30 APRIL 2019

Smiths City result improves as transformation continues

Overview

- Revenue falls 4.4% to \$206.4 million from \$215.9 million following store closures and slower trading in the second half of the financial year
- Same store sales - excluding store closures - rose 2.8% to \$192 Million – reflecting strong growth in the online channel and operational improvements across the network.
- Net losses before tax narrow to \$1.9 million from a net loss of \$9.9 million in the prior year with the group benefiting from growth in same store sales and a strong performance from Smiths City Finance.
- Transformation programme continues with the rationalisation of the store footprint and investments in store formats and systems

National furniture and appliance retailer Smith City (NZX.SCY) today reports improvements in earnings and same-store performance as it makes progress in its transformation programme.

In the year to 12 months to 30 April 2019, same store sales (store revenue excluding stores closed during the year) rose 2.8% to \$192 million from \$187 million as the group starts to see results from a strategic reset initiated in the first half of the financial year.

The online store was the standout performer. It grew its sales very strongly to make it one of Smiths City's larger stores. Meanwhile, in the first half of the year the company benefitted from a strong contribution its commercial operation, which provides furniture and appliances to businesses across the country.

However, group revenue for the year fell 4.4% to \$206.4 million from \$215.9 million with the fall largely reflecting store closures as part of the broader transformation programme to drive the regeneration of the Smiths City brand. It also reflected a softening in New Zealand retail demand in the second half of the year, particularly in Smiths City's core furniture and electronic goods categories.

Group net losses before tax narrowed to \$1.9 million from \$9.9 million in the prior year. Earnings in the finance business partially offset the impact of weaker trading, the ongoing pressure on margins and one-off items of \$1.1 million associated with a strategic decision to close, and eventually relocate, the Wairau Park store on Auckland's North Shore.

Chair Alastair Kerr said: “Over the last year Smiths City has accelerated its transformation. The strong gains we saw in the first half of the year – when we celebrated our centenary – have not been sustained in the second half. This was particularly the case during the crucial Christmas trading period and it continued into the remainder of the financial year, partly reflecting the softening in house prices and consumer confidence.

“It is clear Smiths City must continue to build resilience in its business to respond to these variable market conditions. Key initiatives this year have included the closure of underperforming stores across the country and investment in those stores where we see strong potential.

“Since the end of the financial year this programme has included the rationalisation of the Auckland footprint. This decision does not diminish our commitment to the upper North Island. The challenge remains - in Auckland and in other regions - to better articulate our proposition in store and online and do so in stores that are in the right locations and of a size most suitable to that location. In this way we can ensure we deliver an offer that resonates with regional tastes and plays to our strengths as both a bricks-and-mortar and online retailer.

“At the same time, we must continue to work to overcome a legacy of systems, processes and values that are not aligned with the aspirations and operations of modern retail brand. The board and a refreshed management team are now aligned with the task we face to return Smiths City to its rightful place as New Zealand’s most trusted retailer.

“We are a brand that stands for value, integrity, honesty and fairness and while there is plenty of work to do, we are making progress.”

Balance sheet and dividend

As at 30 April 2018 the company had \$6.4 million of cash on hand, up from the \$6.2 million held at the same time a year ago and \$2.3 million at the end of October. Net interest-bearing debt stood at \$65.0 million, up \$4.1m on the same time a year ago.

The increase in debt was used to fund working capital. All borrowings are secured against finance company receivables.

In light of these results and the continuing need to invest in the business, the board retains its view that it is not yet appropriate to pay a dividend. The board will continue to review Smiths City’s dividend policy but at present it believes the company is unlikely to resume paying dividends in the current financial year.

Outlook

“Retailing is never easy. Large international discount and big-box retailers are coming to New Zealand and are focused on the attractive upper North Island market. Even though the economy is still performing strongly and demand for housing is strong, consumers remain uncertain.

“We understand that, faced with these conditions, we must differentiate ourselves by building enduring relationships of trust and service and delivering an excellent customer experience. Through steady investment in infrastructure and systems and people, Smiths City is putting in place the foundations to support a return to generating sustainable improvements in earnings and profits.

“Gross margins recovered in the final month of the 2019 financial year and this positive sentiment has continued in the first months of the new financial year. It is still too early to provide guidance on the first six months of the 2020 financial year, let alone the full year results. We will provide an update at the company’s annual shareholders meeting in September.”

Operational review

Chief Executive Roy Campbell said: “Smith’s City’s 2019 financial year was a game of two halves. In the first six months we generated strong growth in revenue flowing from the company’s centenary celebrations, strong sales in the commercial business, and growth in the online channel.

“The momentum in sales continued early into the second half, reflecting the growing importance of Black Friday and Cyber Monday¹ to the Christmas trading period. However, it was not maintained for the remainder of the period.

The strong trading early in the period came at the expense of post-Christmas sales and this was compounded by the disruption that followed a reset to our sales incentives programme. Margins, meanwhile, have remained under pressure, but we remain determined to meet the market to maintain our share.”

Revenue in the 12 months to 30 April 2019 in the retail business fell 4.6% to \$198.3 million from \$207.9 million in the same period a year ago, while trading losses from retail decreased 51.7% to \$-5.6 million from \$-11.6 million. The losses in the prior year were worsened by provisions recognising onerous leases on a number of our stores as well as a number of large one-off items.

“Store closures also impacted our top line performance. We closed stores in Queenstown and Gisborne taking the total to 32 from 34 in the same period a year ago. These followed on the closure of stores in Ngauranga Gorge and Riccarton during the prior financial year.

“The Auckland stores showed strong revenue and profitability improvements over the prior year, particularly in appliances, which is a new category for Smiths City in this region. Despite this, they are not configured as we require in this market. Consequently, we decided to exit and look to relocate from our Wairau Park location and to reduce our footprint of our Mount Wellington location. We are working to identify our next sites in the Auckland region and expect to announce these in the coming months.

“It has now become clear that we can meet this demand in the region with smaller stores, supported by our online presence. Online performs strongly in this region reflecting the important role it plays in this market in customer fulfilment and allowing easy comparison of products and prices.

Across the network, we are working to better recognise these regional differences in both customer behaviour and tastes and tailor our offer accordingly. The Auckland stores, for instance, are moving to cater for a much more diverse and urbanised population than we see in our South Island heartland.

“Conversely in our Christchurch stores and many across provincial New Zealand, larger stores with broader ranges play a much greater role in influencing customer behaviour. We have worked to improve in-store execution to ensure products are well presented with a focus on a “whole of house” offer. We have also

¹ The Friday and Monday after the US thanksgiving holiday, which last year fell on 22 November 2018

worked with our people to ensure they delight customers, but this is a journey and we still have some way to go.

“Over the coming year we are looking to back up these initiatives with improvements to our systems to better understand our customers, to inform our buying decisions, our negotiations with suppliers and our management of inventory.

“Recognising the pivotal role our people play in bringing this vision to life we have also continued to build our culture and invested in training to ensure our people model our values and the spirit of the Smiths City brand.

“We continue to align our recruitment induction and training to our guiding principles of integrity, accountability and care. We have refreshed and realigned our key performance indicators for our staff that align with these principles and the broader aspirations of the company.”

Smiths City Finance

“Smiths City Finance turned in a creditable performance despite the competition that has seen interest free finance extending to periods only recently seen in the sector. Revenue increased 16.5% to \$10.6 million from \$9.1 million in the same period a year ago, while trading profits increased 72.4% to \$5.0 million from \$2.9 million in the same period a year ago.

“We continue to see strong opportunities to grow the finance company by building deeper relationships with our customers. Over the coming year we will be investing in our finance company system to better realise these.

“Key goals of the upgrade include: a streamlined application and faster approval process; better reporting to customers; improved links with customer relationship management systems and over the longer-term greater personalisation of the finance offer.”

Outlook

“Our long term success and return to a sustainable profit are dependent on the company’s progress with four priorities for the year ahead: continuing to transform the company culture; gaining a better understanding of, and engaging with, our customers; making the store network a destination of choice and ranging locally, while still taking advantage of our national footprint,” Mr Campbell said.

“Smiths City understands that price will never be a sustainable point of difference for the company. We must deliver value and a compelling and engaging shopping experience that combines the best online and bricks-and-mortar retail experience with the added value of an in-house finance offer. We must continue to build on our strong kiwi heritage and our reputation, consistently demonstrating that we are a company that our customer can trust.

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About Smiths City Group Limited

Smiths City Group (NZX.SCY) was founded in Christchurch in 1918 and has a proud tradition as one of New Zealand's oldest and largest retail chains. The company floated on the stock exchange in 1972 and operates 35 stores (including 3 clearance centres) nationwide. The group comprises Smiths City Retail, Smiths City Finance and Smiths City Commercial. On the web: www.smithscity.co.nz and www.smithcitygroup.co.nz.