CHAIR'S REP

Protecting our future in uncertain times
During a period of uncertainty that has tested New Zealanders' courage and determination, The Warehouse Group demonstrated its resilience by holding true to its course.

The financial year just completed posed challenges and complexity we could never have anticipated, testing our ability to comprehend changes, harness and deploy resources, and execute successfully in a dynamic and volatile environment.

I want to start my report to shareholders this year by paying tribute to the exemplary leadership demonstrated by Group Chief Executive Nick Grayston and his executive team, all our leaders across the business and our team members around the country who have continued, in this extraordinary year, to ensure we serve our customers and help Kiwis live better every day.

The Group's FY20 results provide evidence of the gains to be achieved by putting our customers at the centre of everything we do. We have not deviated from our strategy. Despite unprecedented disruption we have been able to build value for our customers, remain flexible in an unpredictable trading environment and weather the immediate effects of COVID-19 in a way that would not have been possible a few years ago.

"We are now on the cusp of the next stage in our evolution: becoming a business that is Agile, with the discipline, insights and confidence to adapt, focus and deliver even in times of global upheaval and economic contraction."

Joan Withers
Chair, The Warehouse Group

We are saying goodbye to old ways of doing things and pushing forward with transforming the way we work. We continue to apply a laser focus to fixing our retail fundamentals and are embracing opportunities to build a digital future – and we are intensifying these efforts.

We are now on the cusp of the next stage in our evolution: becoming a business that is Agile, with the discipline, insights and confidence to adapt, focus and deliver even in times of global upheaval and economic contraction.

While we have been laying the foundations for this move for a long time, the value of the Group's transformation has been put to the test in ways no one could have contemplated in the year under review.

The results
Our adjusted Net Profit After Tax (NPAT) result of $80.7m was a 9.0% increase on last year, with our reported NPAT being $44.5m. Adjusted NPAT excludes $36.3m in unusual items. This result is a testament to the underlying strength of our brands and operating performance. It is remarkable that the Group was able to deliver this result during a year in which our stores' doors were shuttered for seven weeks during New Zealand's initial lockdown in response to COVID-19.

Our Group retail sales over the course of FY20 provide a snapshot of the disruption inflicted by the global pandemic. We saw good momentum in the first half. We were on track and confident that our transformation efforts were delivering measurable and sustainable gains.

Our confidence was tested in the second half with the impact of COVID-19 lockdown trading restrictions which required an initial period of complete closure, followed by a gradual increase in online sales activity and the eventual reopening of all our stores on 14 May. This disruption had a significant impact on business performance in the third quarter: retail sales were down $128m or 17.9%.

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Consumers returned to our stores in force in the final quarter, lifting total retail sales for the year to $3.2b.

Reported net profit attributable to shareholders for the year was $44.5m - this compares to $65.4m last year.

On 26 March 2020, the Board considered the circumstances and uncertainty around the impact of COVID-19, and decided that it was in the best interest of the company to cancel the previously declared interim dividend for FY20 of 10 cents, which was due to have been paid on 17 April 2020.

Similarly, the Board determined not to pay a final dividend given the continued uncertainty around economic activity and our trading outlook.

Staying the same is not an option in retail. For more than three years, we have been dedicated to transforming our business so we can become New Zealand's most sustainable, convenient and customer-first company. An enormous amount of work has gone into that, and it has translated into a credible financial performance during a time of huge challenges and complexity. We are committed to leveraging the investment and organisational change we have made to ensure we are here for the next 100 years.

One important outcome of fixing our retail fundamentals has been our strengthened ability to capture, manage and utilise data. We are uniquely placed given the breadth and depth of our operations across the country. The insights the data provides are invaluable and innumerable.

We are now accessing customer insights that enable us to pinpoint shifting patterns of shopping behaviour so the business can respond with precision: decisions are well-informed, taken quickly and implemented at pace.

We can also more accurately and speedily track initiatives we implement and the Board and Executive have clear line of sight and maintain scrutiny to ensure investments are adding value.

COVID-19

The scale of the challenges presented by the arrival of COVID-19 in New Zealand cannot be overstated.

Our people at every level in the business had to rapidly adjust and do things differently. We were already well down the path of change. COVID-19 has not altered our direction, but it has accelerated the pace at which we travelled. Despite all the disruption, we have flipped to our new Agile way of working only one month later than originally planned. This has been a remarkable feat in the circumstances which demonstrates the increasingly important ability to pivot quickly to changing circumstances.

One of our early actions was to ensure our people continued to receive their pay during lockdown. The Group was granted the initial Government Wage Subsidy and claimed a total of $67.8m (after tax the total received was $48.8m). The subsidy was crucial to the Group maintaining its workforce through a time when we were closed to customers and faced significant sales uncertainty. This subsidy was paid in full to our team members who received 100% of their pay during this period. On average the wage subsidy equated to around 55% of our normal wage and salary expense over the period to which the subsidy applied.

As the nation prepared to enter alert level 4, the Government focused first and foremost on securing the nation's health and we completely supported that approach. We were, however, disappointed that the Group had to close its stores during alert levels 4 and 3. Senior officials and politicians engaged with the Group and we were receiving advice from them as New Zealand moved through the COVID-19 alert levels.

We hope we are through the worst of the pandemic in New Zealand. However, events in August showed that even with strict controls at our border, the virus can penetrate and spread in our communities. It is clear that the economic implications will reverberate here for years to come. All businesses need to react to the new and evolving reality and we are committed to weathering this storm and ensuring we can serve our customers through the channels that work for them.

What changed most potently during the COVID-19 crisis was the rapid escalation in online shopping.

After that initial period of complete closure, our brands moved to providing online sales of essential items during alert level 4 and then a full online range of products during alert level 3 for delivery or contactless Click & Collect.

Online sales ballooned and by the end of FY20 had increased by 55.2% on the prior year, representing 11.4% of total retail sales for the year.

COVID-19 has changed the way people work, engage socially and shop. We must continue to pay attention to what this means for our business.

We will keep adapting our business to meet the needs of this new normal for our customers. That means prioritising our resources to deliver in a retail environment that will continue to present challenges, as well as opportunities.

The successful launch of TheMarket.com in August 2019 is a case in point. It now offers over 2 million products and across more than 3500 brands and while it is still early days, its performance gives us confidence in the long-term value of this investment in the digital future.

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The Board is delighted with the progress and the efforts of the team to launch and operate what is effectively a start-up during a period of such profound upheaval.

It has also been a year in which we have had to acknowledge that our systems and processes have sometimes let us down. During the run-up to Christmas, our Warehouse Management System (WMS) did not perform to expectations, and that caused frustration for our customers.

The performance glitches were regrettable and showed that we had yet to complete fixing our retail fundamentals. The executive leadership team took full responsibility for getting WMS back on track. Subsequently, the enhanced performance and metrics meant the business was in much better shape to respond to and manage the tsunami of online orders during the COVID-19 lockdown through to early June.

There remains further work to do, but we are heading in the right direction.

Honouring our commitments

When we published our first Integrated Report last year, we described how we deploy our resources and manage our networks, expertise, relationships, environment and financial capital to create long-term sustainable value.

That commitment has not wavered, despite the challenges we faced during the second half because of COVID–19.

Initiatives include improving accessibility for people with disabilities, providing private-label period products for $1, partnering with IBM and schools to lift the digital skills of our future workforce through the P-TECH initiative, and increasing the range of products across our brands that have sustainable attributes – to name but a few. Further detail can be found on pages 42 and 43.

Capital management

Cancelling the interim dividend after it had been declared was a very unusual measure for any Board to take in New Zealand. However, it was the prudent course of action. Similarly our determination to not pay a final dividend was made after careful consideration of all the information available to us.

The ongoing transformation efforts and balance sheet initiatives during FY20 have reduced our debt levels significantly.

The Board is rigorous in its evaluation of the Group's capital structure. We work hard to ensure we are making appropriate investment in value-enhancing initiatives and we are also highly cognisant of our responsibility to our shareholders.

In March the Group increased its banking facilities by $150m, extending total banking facilities to $330m – allowing for the redemption of the Group's NZX listed bond of $125m on 15 June.

As at year-end, the Group is in a strong financial position with a cash balance of $168m, and therefore access to funds of $498m.

Board activity

Two of our long-standing Directors due to retire by rotation have confirmed that they will not seek re-election and will step down at the Group's Annual Shareholders' Meeting in November.

The Warehouse Founder Sir Stephen Tindall and Deputy Chair and Chair of the Audit and Risk Committee Keith Smith have served as Directors since 1982 and 1988 respectively.

The Board has been fortunate in having Sir Stephen and Keith contribute their significant experience and wisdom to the governance of the business during a period of ongoing change, increasing competition and major technological developments.

We have specific aknowledgement of Sir Stephen and Keith's service to The Warehouse board on pages 10 and 11. However, I would like to add my personal gratitude to them both for the enormous support and guidance they have given me over the years.

The Board welcomed non-executive Director Dean Hamilton to his first meeting in May 2020. Dean has significant CEO and financial markets experience and is a valuable addition to the Board. He will, if elected at the Annual Shareholders' Meeting, become the Chair of the Audit and Risk Committee following Keith's retirement.

Robbie Tindall has been nominated as a Director of the Group and will also stand for election at the Annual Shareholders' Meeting. Robbie was appointed as Sir Stephen's alternate in July 2011 and has represented him since Sir Stephen took leave of absence from the Board in October 2017.

A special call out to Julia Raue who chairs our Health, Safety and Wellbeing Committee. The work this year, in tandem with our Health and Safety team in the business, was of particular importance under the shadow of COVID–19.

During her first year in our Future Director programme, Renee Mateparae has made an excellent contribution. The knowledge Renee gained in her leadership role at Spark during the organisation's transition to Agile ways of working has been of particular value.

We have undertaken an independently facilitated, comprehensive Board performance review, canvassing Board behaviours and culture as well as individual directorial performance. Senior executives who interact with the Board provided input.

The review culminated with a facilitated workshop to share the findings and most importantly to commit to the actions we will take as a result of those.

The review should give shareholders confidence that the Board is committed to the highest standards of corporate governance. It also provides a focused opportunity to look at our skills mix and succession planning.

Looking ahead

The business' own insights show that in the wake of the first COVID–19 lockdown, six out of seven consumers are now looking to save money with 64% of customers consciously cutting their spending.

We anticipate significantly reduced retail demand as the full economic impact of COVID–19 is felt by consumers over the course of FY21.

In June 2020 the Group confirmed it would accelerate some of the changes already planned – including some store closures and operational changes – due to the uncertainty associated with COVID–19.

While we are currently in a solid position, by making changes now in the way we organise ourselves and assist our customers, we will protect our future in very challenging times.

As I said in my introduction, the contribution of Nick Grayston and his executive leadership team has been outstanding. My thanks on behalf of the Board to all those who have worked so hard during a year beset by the impacts of a pandemic that has touched every corner of our planet.

My sincere thanks, too, to the Board, which has gone above and beyond, engaging in frequent virtual meetings and discussions during the height of COVID–19 alert levels and providing unfailing support for the Group throughout the financial year.

To our shareholders, I want to offer our thanks for their continued support during a year when they had to manage the impacts on their personal and professional lives of immense change. The Board is confident the investment we have made in the last three years to position the Group will provide sustainable competitive advantage and long-term shareholder value.

Joan Withers – Chair