Proud to serve New Zealanders

Discipline, patience and hard work over a sustained period paid off this year as The Warehouse Group recorded an impressive result. Tangible signs of progress show that the hard yards have been worth it and that the company’s focus over recent years can now start to be seen on the bottom line.

Accelerating our strategy through an ambitious transformation programme, relentlessly improving our business processes, focusing on what we offer, our Every Day Low Pricing pricing model, lifting brand performance across the board, and the ongoing development and roll-out of our digital future – these and other strategic initiatives have all improved our position significantly. The range and breadth of these measures speak to the complexity of the retail sector today: the rapidly evolving competitive environment, and the changing shopping behaviours of our customers.

No single answer is ever going to be enough given the dynamics of the retail sector, and so we have a broad portfolio of improvement initiatives running across our business. This has required our people to undertake significant change and I want to thank everyone for their hard work in getting us to this point. I’ve been impressed with the work and focus of the leadership team, and by the support from the Board.
Our drive to reduce inventory and improve working capital efficiency saw progress this year, translating through to a reduced net debt position following the renegotiation of offshore supplier trading terms and the reduction in aged inventory.

Good progress across our brands

It is particularly satisfying this year to see improvements across almost all of our brands.

The Warehouse is making good progress following the decision to move to Every Day Low Pricing and we saw clear benefits from the transformation initiatives, especially around merchandising and improvements in the cost of goods sold (COGS). This translated into a 19% increase in operating profit year on year for the Red Sheds. As well as improved profitability, we have also seen a six point increase in terms of perceived quality.

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Unit volume in the Red Sheds has remained flat this year as we continue to simplify our brand portfolio and further reduce our overall number of full stock keeping units (SKUs) by 17%. Continued focus on the optimisation of our product offering has delivered an enhanced shopping experience for Kiwis.

We are now starting to find the right balance between our ongoing commitment to Every Day Low Pricing and introducing some limited seasonal promotions to give us flexibility around driving foot traffic.
Revenue for The Warehouse increased by 0.6% to $1.7b, with gross margin up 70 basis points. Our best performing categories were General Merchandise and Home. Good progress was made following the move to Every Day Low Pricing and we saw clear benefits from the transformation initiatives.

Noel Leeming continues to impress, with another record result. The technology expertise offered to customers has made the brand experience more valuable to customers looking to incorporate more and more technology into their lives. Noel Leeming revenue grew by 5.0% to $924.6m this year, with operating profit up by 22.3% to $38.1m and gains in operating margins from 3.5% in FY18 to 4.1% in FY19.

Two important factors in the nature of the Noel Leeming offering point to a healthy future. The first is the continued rise of B2B on top of retail activity. Commercial sales continue to improve and we see this as a significant growth opportunity. The second is the ongoing growth of services, which increased 11.4% on last year. Growth in these areas demonstrate an increasing demand for more end-to-end life-cycle technology services from customers.

Warehouse Stationery made a welcome recovery this year after a poor FY18 as a result of internal systems integration and stock availability issues. Those issues are now behind us and Warehouse Stationery has performed well in FY19, reporting a record profit despite industry headwinds in its core stationery categories.

Revenue for Warehouse Stationery was up by 1.8% on the previous year to $268.6m in FY19. Operating profit also increased from $10.6m in FY18 to $16.7m this year. Operating margins kept pace with this, increasing from 4.0% last year to 6.2% this year.

We have continued to roll out the integration of The Warehouse and Warehouse Stationery. There are now 10 of these stores-within-a-store across the country, and both brands are benefiting from the strengths that the other can bring: foot traffic from Red, and high quality products and services from Blue.

Torpedo7 has continued to roll out more stores this year as we build scale and target new markets. Our overall view of the business is that it has considerable potential but that more focus is needed to turn good fundamentals into a profitable trading entity. To that end we recently announced the appointment of Simon West as CEO for Torpedo7, a move designed to focus on brand-specific issues.

Revenue for Torpedo7 increased again this year to $172.5m, up 5.6% on last year’s result of $163.4m; however, the company made an operating loss of $7.0m as we invested in greater market presence through 18 stores. As I have said for some time, expansion alone will not be enough because all stores have proven to be relatively profit-neutral in their first year of operation. This year we continued to build greater brand clarity and to refine our inventory.

Group online sales continued to grow this year, up 18% on last year to $239m. Currently, online sales represent 7.8% of our total sales, and are a critical part of our growth strategy. Digital initiatives enable us to create vehicles that reach beyond the specific constraints of the businesses that we own and operate. New Zealanders currently spend $4.2b online and that figure is only going to get bigger.

We launch a new digital era
After balance date, we launched our new digital platform TheMarket – part of the execution of a wider strategy to construct an enhanced ecosystem around our business. We’re very proud of the work that the team has done in a short period of time to release such an elegant platform to market.

Proof that we can do this and that there is capacity in the market for such initiatives can be seen in the fact that, at launch, we had welcomed 150 merchants onto the platform – offering more than a million products, including local brands Karen Walker, WORLD, Father Rabbit, Citta and Barkers, and Australian and international brands PE Nation, Cue, Billabong, Cotton On and The Nile. Key categories include fashion, footwear, kids and baby, toys, health and beauty, home, garden, electronics, sports and outdoor. TheMarket is independently operated but backed by The Warehouse Group.
The Market is a key investment for us in the digital future, one in which we see a much broader role for the Group in supporting a range of services to help New Zealanders live their lives better.

The next step will be the launch of a Group loyalty programme, and we have a number of services at various stages of consideration and development to expand the offering in order to become a true ecosystem.

Holding our own in an intense trading environment

These developments come not a moment too soon. We are more convinced than ever that without these changes we could not thrive in tomorrow’s retail environment. Our predictions of increased competition are being realised, with a number of fashion and lifestyle retailers having arrived or committed to come here. The presence of competitors such as Zara, H&M and the upcoming arrival of Costco, along with Amazon’s growing maturity in Australia which we think will start to affect us too, point to our need as a Group to make the most of our advantages as a New Zealand-based retailer with a significant footprint, loyal customers and deep relationships within communities.

As I said last year, scale and brand affinity are two of our greatest strengths, and we will continue to leverage them by recognising and rewarding the people who shop with us and offering them access to new and exciting digital initiatives, guided by sophisticated data, insights and capabilities. Looking at our performance against our current competitor set, we are satisfied that our strategy is headed in the right direction and our market data is showing significant progress against our close competitors.

Moving with speed

Speed, or rather the inability to respond to changing market dynamics at speed, has always been our greatest challenge. We are determined to move faster – and our Executive Team is focused on how we drive the business forward at an increased pace at the same time as we take care of our people. In light of what is happening around us, it is all the more important that we continue to put our house in order. Right now, we are moving towards peak investment mode in terms of systems and processes, and we’ll be looking for better ways to organise and drive customer-centricity, productivity and cultural change.

We’ve already lifted productivity in our stores by being more efficient and only focusing on those things that make a difference for customers. Boosting our wider productivity starts with addressing a significant under-investment in core systems and supply chain logistics capabilities. We need to make sure our systems of record are no longer a competitive disadvantage. The first step in getting that right is improving our fulfilment capability. Our new Warehouse Management System is the first expression of that. At this stage, it is greatly assisting us to serve our customers digitally.

In terms of our wider back office, we are also continuing to identify how we can use modern integrated systems to support our people, merchandising and finance systems and to reorganise our processes as part of that.
Transformation on a range of fronts

New systems and processes by themselves won’t be sufficient. Our RISE transformation programme has helped us change the way we work and has enabled us to lift our ability to execute, which is now reaping financial benefits. However, it’s also clear that we still need to make the full pivot from being a rigid, 20th century command and control organisation focused on supply to become a nimble, digital company focused on solving customer problems. With that goal in mind, we are assessing different operational models, adjusting our culture and looking to adopt lean principles such as speed-as-a-habit, agility, flexibility, minimum viable product and fail-fast as part of how we operate.

All of that requires further deep cultural change. We made the first steps towards that this year by redefining our values and examining the behaviours required to bring those values to life. While changing how we work is important, unlike some companies that have been through significant change, we don’t believe that is the extent of the transformation required. For us, it’s one part. We want to get the best value we can from it, of course, but we also need to use it as a lever to move the whole company forward.

Our transformation programme has been effective because it has been cross-functional and collaborative. We’ve recognised that we need to get better right across our Group, not just in some parts of the business, and the key to success is continuing to embed integrated solutions that lead to a far more collaborative style of working.

On top of that, the muscle that we’ve built in data science has enabled us to start building strength in areas such as price optimisation by category which will grow margins. We will continue to refine our understanding of our customers and their needs and to use that to inform our brand performance and our future investments.

Meeting our other responsibilities

Our core purpose to help Kiwis live better every day gives us both a responsibility and a remit to look beyond just making profits. Of course we must be as efficient and make the best returns as we can but we also serve the communities that we are part of, and there are other elements of value that are important to us and to other stakeholders. That’s why we have adopted Here for Good as a core value. It has prompted us to make stands on issues such as mental health and carbon neutrality this year. We believe this is fundamental to our values, to our operating principles, and supports our commitments to the community and the interests and priorities of New Zealanders.

This year we became a carboNZero™ company, and committed to 25 initiatives focused on reducing our carbon footprint. Our environment capital section in this report spells out what we are doing and the progress we are making in this space. We have three key focus areas: reducing our carbon emissions and waste; offsetting our carbon emissions through the regeneration of land and renewing native forests (this will become clearer as carbon trading legislation is finalised); and buying international Gold Standard carbon credits. We are reassessing our raw materials and enhancing our environmental performance by reducing packaging materials and purchasing responsibly produced products.

An integrated approach

Our commitment to a fully integrated report this year recognises that not everything we do is about financial value and we want to keep our stakeholders informed about the many non-financial initiatives we are undertaking and the progress we are making. It is also a reflection of the integrated way we are addressing our strategic priorities: integrating our capitals to give us a holistic view of our vulnerabilities and opportunities; building clear understandings of our progress on multiple fronts; and recognising, as I said earlier, that there is not a singular answer. We believe that’s also good business.
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Good progress
This year we had defined the key performance indicators (KPIs) that mattered to us as a leadership team: earnings for the year, product and retail experience, systems and processes, performance culture, mid-term strategy and eCommerce.

We have made good progress in each of these areas, but the work is far from done. And we know that major system and process change in the next year of our transformation, coupled with product changes and refinement of our ecosystem, is all part of refining our retail experience and testing new formats as we feel our way into a rapidly evolving competitive environment.

The investments we make going forward will be on that basis: looking for ways to bolster each brand so that it achieves its full potential and, at the same time, getting best leverage from what we do as a Group. With earnings rising and our balance sheet in good health, we are well placed to make some of the big investments in front of us. Having reduced our debt gearing, we now have the capacity to balance the demands on our capital and deliver a strong and sustainable future for our organisation across all our channels, current and emerging.

My thanks to everyone in the Group for your hard work this year.

Nick Grayston
Chief Executive Officer
The Warehouse Group