



Australian Pharmaceutical Industries Limited
2011 Annual General Meeting
17 January 2012

Address by Stephen Roche, CEO & Managing Director

Welcome again to today's AGM and thank you for joining us this afternoon.

Peter has talked you through API's progress and achievements over the past year and given you an overview of our financial results.

I would like to talk to you about the business in a strategic context.

I'm going to split this presentation into two parts. Firstly, I'm going to talk to you about the business itself, the significant market opportunity we're pursuing, the regulatory situation and finally the strategy we are embarking on.

I will then talk to you about why we're so confident that our strategy will succeed.

API is uniquely positioned as a domestic market leader in both health and beauty retail and pharmaceutical distribution.

1. As you all know, API owns and operates the Priceline and Priceline Pharmacy brand, that is a leading health and beauty brand in Australia. Operating largely through a franchisor model, Priceline provides pharmacist franchisees with a total retail model. Combined with the traditional Priceline stores that the company owns, API has a health and beauty offer that meet the needs of its consumers, even when under intense competition.



2. API also has additional pharmacy brands Soul Pattinson & Pharmacist Advice along with a substantial independent pharmacy API Member Program.
3. API is also Australia's leading pharmaceutical distributor

API is uniquely positioned to capitalise on two powerful consumer trends within the retail sector.

The first is that customers are increasingly becoming more "health conscious" and the second is that given the current economic environment, they are increasingly "cost conscious".

There is no doubt that customers want to look and feel good, but they are looking to spend less on their favourite brands and they are also looking for cheaper alternatives.

Consumers are also looking for preventative health solutions and advice from a trusted health professional – a pharmacist; and they are looking for a network of stores that delivers a consistency of offer.

Whilst there has been a reduction in total retail spend in Australia over the past couple of years, the health and beauty sector has delivered underlying growth.

People continue to buy health and beauty products.

Here we are at an advantage over other retailers – we are building a uniquely attractive revenue profile which has underlying growth and is defensive.

The pharmaceutical industry continues to be highly regulated, but the regulatory framework provides both commercial advantages and restrictions.



API is fortunate in that it has 101 years of experience of working within this framework. For the foreseeable future, deregulation of pharmacies is unlikely. The Pharmacy Guild continues to strongly oppose it. They have a strong voice where it matters. Secondly, the current regulatory position has the bi-partisan support of the major political parties.

API supports the ownership of pharmacies by pharmacists.

Importantly, I believe that the positive impacts of PBS reforms are under-appreciated. A reduced dispensary income will accelerate the need for Pharmacists to diversify their customer offering and lead to an increased level of interest by Pharmacists for brands. We believe Priceline is well placed to benefit from this need, which in turn should lead to accelerated store roll out growth.

We also expect to see further growth in Soul Pattinson and Pharmacist Advice.

Now that the market opportunity and regulatory environment has been outlined, I would like to talk about where our business is positioned in the market. Priceline Pharmacy is uniquely placed with what we believe to be a compelling customer offer. On one hand, we have the major department stores which focus on service and range, over price. On the other hand we have the supermarkets and discount chemists which focus on price over service.

Priceline occupies the middle ground, with a strong focus on both customer service and price. We deliberately centre our mass market offer on service, value and a great in store experience.

We seek to provide our customers with an enjoyable in-store experience with health and beauty specialists on hand to assist as needed and a wide range of branded products that are priced competitively.



Our rationale is simple – providing the best offering to customers will ultimately result in commercial success for our franchisees and our business.

API has been refining its strategy over the last five years, and has, we believe, a significant first mover advantage.

API has made substantial investments in both our infrastructure and our people and we are in a position where we can support a doubling of store numbers without further material investment in these fixed costs.

We have an extensive site network and franchisee base already secured, an existing loyal customer base and a low cost, low risk growth plan established and working.

Another of our key advantages is the strength of our brands Priceline, Soul Pattinson and Pharmacist Advice. They are recognised and trusted throughout Australia and our Priceline brand in particular is a key asset for both retaining and attracting new customers. Our Priceline loyalty program Clubcard moves from strength to strength, with currently 3.6 million members and is arguably the 4th largest loyalty program in Australia. This program is not easily replicable and is a significant point of difference.

In addition to our retail offering, API is also the market leader for pharmaceutical distribution and the Company continues to provide valued services to our independent pharmacy customer base through our API Member and Premium programs.

API's vision is to become the dominant mass market health and beauty retailer and best franchise partner in Australia

We have already made significant steps towards achieving this vision. There is always more to do but our strategy will take us there.



We will:

1. Pursue growth in our brands, however, the Priceline Pharmacy brand has clear point of difference –
 - Capitalising on the expected surge in pharmacists' needs
 - Continue to provide an attractive retail channel for multi-national brands in health and beauty
 - With the increased interest in brands, we also expect growth in Soul Pattinson and Pharmacist Advice.
2. Maintain a leading market position in Australian pharmaceutical distribution
3. Be the best franchise partner for our customers, branded or independent
4. Provide tailored health and beauty products through our manufacturing and marketing capabilities

We are confident that our strategy has all of the elements required for success.

Firstly, it is important to remember that this is not uncharted territory. If we look further afield at our peers overseas, we can see examples of successful strategies being implemented by companies such as:

Superdrug in the UK,
Clicks in South Africa, and;
Shoppers Drug Mart in Canada

We have taken the “best of breed” strategies from these offshore peers and adapted them to the nuances of the Australian market. This approach significantly de-risks our business model and provides confidence that our strategy will succeed.



Secondly Priceline Pharmacy offers an exceptionally appealing franchisee proposition for independent pharmacies.

- Franchisees have a significantly greater earnings potential – Priceline Pharmacy provides an offer that reduces the reliability on dispensary income,
- The Priceline brand, Clubcard with 3.6 million members and its marketing spend significantly increases store traffic and builds customer loyalty,
- Priceline is able to provide competitive pricing and margins for its franchisees through its scale and supplier relationships with leading brands
- There is significant business and retail expertise support available to franchisees which they are able to benefit and learn from.

Our on-line store is currently under construction and is due for launch in the second quarter of this calendar year.

It has been based on 'best in class' international health and beauty stores and customer research. It will feature over 10,000 unscheduled products for purchase.

Each year we conduct an independent survey of our franchisees and this year the results show outstanding franchisee satisfaction levels, increasing each year since its inception three years ago.

The third reason which gives strength to our strategy is that we have a distinctive offering which sets Priceline Pharmacy apart from its competitors.

As noted previously, we believe we have an attractive customer offer in the market by selling mid-mass market branded products at competitive prices. We also know that customers value having a pharmacist and beauty specialists on hand. They also



want to touch, feel and try products before they buy. The majority of our customers, largely women, want an enjoyable in-store experience when shopping for health and beauty products, and we work very hard to create this environment in our stores.

An added benefit is that the product ranges that we offer are very complimentary in nature and we find that customers tend to browse once in store making additional purchases.

So on top of value pricing, and excellent customer service, customers are also rewarded for their loyalty through using our successful Priceline Clubcard.

We are extremely proud of the loyalty program which is now arguably the fourth most popular loyalty card in Australia. It has over 3.6 million members, and we have thousands of new members joining up every week.

The benefit of the card for Priceline is easy to see, with basket size an average 50% larger than non-Clubcard holders and sales by loyalty card customers accounting for over 40% of overall store sales, including prescriptions.

The final key reason why we are confident that our strategy will be successful, lies in the robustness of the commercial model we have developed.

We have invested heavily in our competency and capability over recent years, as we recognised the potential and strength of the business. This investment has been made in the necessary business infrastructure required to cater for a network double the size we have today. This includes everything from our supply chain, merchandise and marketing programs to our highly skilled people.

The impact of this up-front investment is that we have now built significant scalability in our earnings base. This will mean that our



retail margins will expand significantly as store numbers increase and future earnings will represent a “J curve“ profile.

API is a company which I believe has strong investment appeal and is currently significantly undervalued by the market.

We are poised for a better earnings year in 2012, free hopefully from the one-off items which impacted our profitability in 2011. Through Priceline, the company has excellent exposure to the sustained underlying growth, yet defensive health and beauty retail market. As you have already heard from the Chairman, comparable sales for December were up 7.4% and for the year to date up 2.8% which demonstrates my point.

But perhaps most importantly, we expect that a mix of factors will drive an uplift in store numbers, our key earnings driver.

As Priceline Pharmacy grows its store numbers, the company's earnings mix will change dramatically. As a result we increasingly view ourselves as being a specialty retailer rather than a healthcare company. As the chart on the slide shows, when compared to a range of specialty retailer peers, API's valuation appeal is substantial. API is currently trading on the highest dividend yield of this group and also the lowest price earnings multiple. We think this combination clearly highlights the investment appeal of the company.

We clearly respect our 100 year heritage in pharmacy and are confident that experience will enable us to manage the economic and environmental impacts challenging pharmacy.

We look forward to working with our pharmacist customers to provide a product and or a service offer that meets both their and their consumers needs.

We are confident in our ability to provide value to shareholders.



In conclusion, and on a personal level I would like to thank all our employees for their very hard work over the past twelve months. It has not been easy but they have always delivered. I would also like to extend my thanks and appreciation to members of my management team and the Board. Their ongoing support has been greatly valued by me.

Thank you.