



**ASX Release
30 April 2008**

Half year result and supply chain program

- API established as leading pharmaceutical wholesaler
- Priceline Pharmacy store footprint increased
- Strong revenue growth in Pharmacy and Retail
- Underlying operating margins grow as business improvement continues
- Launch of Revitalise supply chain program expected to deliver annualised savings of \$18 million a year from the 2011 financial year

Australian Pharmaceutical Industries Limited (API) today reported its results for the six months to the end of February 2008*. API generated sales of \$1,605 million, earnings before interest, tax and depreciation (EBITD) of \$29.7 million and a net profit after tax of \$6.1 million.

Managing Director and Chief Executive Officer, Stephen Roche, said the results demonstrated that API was on track with its business improvements and its strategic position was sound, with better returns from the Pharmacy division while also growing the Priceline Pharmacy brand.

"We are now the number one pharmaceutical wholesaler in Australia, we're continuing to improve underlying margins and the demand for the Priceline brand is growing because we have a unique retail offer," Mr Roche said.

"Sales growth of 19.8% over the same six month period to February last year and earnings margin growth from the previous reporting periods, show that once we stabilised the business we have continued to build on our core strengths," he said.

"We expect our improved performance will flow into the second half, particularly with the full benefit of the Alphapharm partnership and the planned sale of corporate stores to transition to Priceline Pharmacies.

"The increase in underlying sales has led to higher working capital requirements and a higher interest charge than initially anticipated. Growth has come at a cost and we believe we are managing that well, however our new supply chain program, Revitalise, will help us to address these issues in future.

"To capitalise on the growth momentum we are commencing Revitalise to service the future demands of our Priceline brand and independent pharmacies at a lower cost.

"Revitalise has been designed in conjunction with leading supply chain experts, XAct Solutions, and will take three years to complete and is tailored to maintain excellent service levels while reducing our overall cost base."

* API has commenced a new financial year from 1 September and as such does not have a matching reported prior corresponding period. The Appendix 4D references the last recorded half year result ended 31 October 2006.



The Board has determined it prudent that the company not pay a dividend for the first six month period of the financial year, although directors have indicated they will review this position at the end of the second half.

Divisional reviews

Pharmacy

The Pharmacy division revenue was \$1,208.5 million, up 24.7% on the six months to February last year. Underlying sales growth exceeded that of the industry, excluding the Alphapharm sales that were included for the last four months of the period. EBITD margins improved to 1.9% from the four month period to August 2007 of 1.8% and are expected to continue growing in the second half.

"We have managed this business very well during the period with continued underlying growth and better margins. We also integrated the Alphapharm business, which incurred one-off start up costs and also delayed other planned initiatives to reduce operating costs, and these factors won't be present in the second half," Mr Roche said.

"The market conditions have been highly competitive but we have been careful to manage new business without diluting margins," he said.

The division has continued to focus on working capital and debtors, and has kept trading terms in check.

Retail

The Retail division encountered a volatile and fluctuating market during the period under review but maintained very good like-for-like growth as the division further developed the Priceline Pharmacy platform.

"We are continuing our transition from a predominantly corporate store portfolio to a majority of franchise stores as it is the central plank in our strategic development. In addition to new sites, during previous periods we transferred our Priceline corporate stores into franchises to maintain a rapid Priceline Pharmacy store roll out which has affected our margins in the short term as we continue to develop the brand aggressively," Mr Roche said.

"Our underlying EBITD margin of 4.8% was improved on previous periods which is pleasing. The process to transition more Priceline corporate stores to Priceline Pharmacies will occur in the second half now that the peak trading period is completed," he said.

The Priceline Pharmacy roll out is continuing well, with another 18 stores scheduled to open in coming months.

Total revenue for the period was \$331.3 million, up 6% on the six months to February last year. Like for like combined comparable store growth during the period was 7.3%, with Priceline Pharmacy front of store comparable growth at 12.9% and traditional Priceline stores at 5.1%.



"The new marketing programs commenced during the period were highly beneficial, providing well planned promotions to lift the brand profile at critical times," he said.

The fluctuating demand from month to month also provided management challenges in matching demand with staffing and inventory needs and this will continue to be closely monitored during the second half.

Consumer Brands

The Consumer Brands division has continued to record positive earnings and is developing its offering, particularly in the Australian pharmacy market. It is on track to build on last year's earnings position.

Revitalise – API's supply chain program

During the period API undertook a thorough review of its supply chain requirements with specialist supply chain advisers, XAct Solutions. A new network plan has been developed that forecasts an \$18 million annualised cost reduction when the program is completed in three years, although benefits are expected to start in the 2010 financial year. Revitalise will require an investment of approximately \$60 million until its completion in 2011.

"Revitalise will make API highly efficient, enabling us to meet growth targets and competitive or industry changes. In addition it means we'll be holding stock closer to stores thereby making us more responsive but at a lower cost," Mr Roche said.

"We expect that the investment would provide an internal rate of return of 33% from a conservative business case, and the investment is not anticipated to be dilutive to earnings during the program," he said.

API currently supports the infrastructure for two supply chains. One consists of 14 distribution centres (DCs) supplying pharmaceuticals and front of store products to pharmacies. The other is one DC at Dandenong that supplies products (excluding pharmaceuticals) to all Priceline branded stores in Australia. A significant portion of inventory is duplicated, as are freights costs across the company.

Under Revitalise API's existing two supply chains will be combined to a single system to reduce inventory holdings and freight costs. Under the program API will:

- Increase automation at the DCs in Melbourne, Sydney and Brisbane which will also hold the total product range required to service all pharmacies and Priceline stores;
- Adelaide, Perth, Cairns and a new Launceston DC will hold an expanded range of products;
- Establish one new DC in Melbourne, consolidating the two existing sites;
- Establish a larger DC in Brisbane and also assess the impact on the existing Sydney DC; and,
- Install a Warehouse Management System to enable both division to access all products in a single DC.



The current DCs in Brisbane and both Melbourne sites would have required investment or relocation regardless of Revitalise to cope with the increases in the current volume.

Outlook

The Board is evaluating the best options for the company's capital management position, as advised at the Annual General Meeting in December 2007. This work continues with particular focus on the funding requirements of API's strong organic growth rate and the Revitalise program. The Board has engaged advisers to examine the best options to ensure shareholder value is maximised while maintaining the growth momentum.

Retail trading conditions have been more volatile during recent months with interest rate rises appearing to slow overall economic growth and the impact will be closely monitored and managed in stores.

API is confident that with a full period of Alphapharm sales; the transfer of further Priceline corporate stores to franchises, and the continued focus on costs the business will further improve in the second half. API remains comfortable with consensus forecasts of earnings before interest and tax of approximately \$49.5 million.

"Our focus is to drive our organic growth in pharmacy and our unique retail offering. Revitalise is a key pillar for us in delivering a better, more efficient service that enables this growth to continue. We are also preparing the company for any potential changes to the PBS funding mechanisms before the next Community Pharmacy Agreement in 2010," Mr Roche said.

"We are still open to industry consolidation, but regardless of that issue we are driving strategic growth options that are right for API and that will return value for shareholders."

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About API

Australian Pharmaceutical Industries Limited (API) is one of Australia's leading health and beauty companies. API's Pharmacy business provides wholesale distribution, business and marketing services to community pharmacies across Australia. The Retail division is a leader in the health and beauty market through its retail brands Priceline and Priceline Pharmacy. The Consumer division is a niche player in over-the-counter pharmaceuticals and is based in New Zealand.

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