

Pumpkin Patch Limited

Address to the 2014 Annual Shareholders Meeting

Tuesday 25th November 2014

The following document contains the addresses given by Peter Schuyt (Chairperson) and Di Humphries (Chief Executive Officer) to the 2014 Annual Shareholders Meeting.

Chairperson's address (Peter Schuyt)

The 2014 financial year proved to be another challenging year for Pumpkin Patch. This has been a constant theme presented to our shareholders and we want to shift the focus to what can be done and what will be done to address some fundamental issues with the business.

We have, however, had to contend with difficult retail environments in our core markets in New Zealand and Australia. This negatively impacted revenue, margins and the level of earnings achieved. Short term initiatives around product, supply chain, organisation restructuring and cost reduction were successfully executed. These were not sufficient to address margin erosion. We have not been alone in the retail clothing sector to face these issues.

Supply chain disruptions also had a negative impact on our ability to meet both customer demand and expectations at key times during the year.

The market has changed and continues to change. This company must adapt and meet changing demands from our customers and the growing competition of international

brands. This adaption will be reflected in changes to our supply chain, distribution networks, customer interactions, processes and information systems.

With external assistance we undertook a comprehensive strategic and operational review of the business. This has enabled us to identify and prioritise the initiatives required to drive performance improvement above their currently unacceptable levels and to take advantage of the long term growth opportunities.

In particular, the review did highlight a number of core strengths that create opportunities for us going forward. Most critically and supported by our research, our brand remains strong particularly in our Australasian markets. We also have substantial, but underutilised customer information that can be used to grow customer relationships.

These core strengths provide the basis for making the changes; invest in the business and to leverage those strengths into a more profitable business.

The review did however highlight the need for further development of the omni-channel business model.

There are fundamental changes and improvements that we need to make particularly in relation to the refresh of our product ranges and branding strategy, greater leveraging of our existing customer databases, the implementation of new supply chain and distribution arrangements, and improving our product value equation.

We also believe that the store footprint of the past is not what the business needs and fewer, more targeted stores are necessary. Di will talk further about these initiatives.

To effect those changes we need to invest in information systems to ensure we have product visibility, can better manage our supply and distribution chains and allow far more effective decision making.

In recognition of the change process, the Board elected to make provisions against store assets, inventory and IT assets at financial year end.

The business transformation process involves a two-year timeframe to complete and requires considerable work across all parts of the business, but we believe that these changes are required in order to deliver results that stakeholders of the Company are expecting.

This does not mean that we cannot effect faster change to deliver benefits. This sector moves quickly and the status quo for the next two years is not acceptable. The Board will make decisions and invest in quick win opportunities that will either reduce our cost structure or improve the top line numbers.

I would like to make clear that we see trading conditions in this hugely competitive market in the coming twelve months to remain difficult. The financial benefits from the various business transformation projects will be realised progressively and there is no silver bullet.

Those challenging trading conditions have been reflected in our first quarter results. Retail and Direct revenue is in line with last year but below target. Wholesale revenue is below last year mainly due to the timing of shipments. Our first quarter net profit before tax from continuing operations is in line with both targeted and last year's results, however our key trading periods are to come. Margin shortfalls have been offset by cost savings. Competition and product discounting continues to put pressure on revenue targets and margins.

We have a long term and positive relationship with our bankers – the ANZ Banking Group. We have had, and continue to have the support of the bank over this challenging trading and change period. We are currently in compliance with our banking covenants.

We are also currently part way into a seasonal peak trading period. The outcome of this trading period will materially affect our financial result and the outlook for the remainder of the year. Should trading not deliver to expectations over this period, or worsen over the first half of next year, then there is a risk that the company may breach banking covenants in the latter part of this financial year noting that the seasonal trading results will become clearer over the next 3-4 weeks. These matters are subject to ongoing review by the Board.

Against the backdrop of the trading challenges and the business transformation program, the Board has been undertaking a review of its capital structure and other strategic alternatives. The Board has engaged Goldman Sachs to assist in that process.

We have not declared a final dividend for FY14 as the reduction of bank debt continues to remain a key priority area. The payment of dividends will be reviewed once certainty around achieving the strategic milestones underlying the transformation process becomes apparent, particularly in relation to the debt reduction plan.

Investment will be required to deliver the transformation program.

During the year a review of the Board was also undertaken to refresh the Board membership and align the skills and experience on the Board to support the future strategies being implemented. Jane Freeman, Maurice Prendergast and Sally Synnott elected to step down from the Board with Luke Bunt, Bruce Cotterill and Josette Prince newly appointed. Their extensive experience will be invaluable as we move through the change process we have embarked on. We are delighted to have people of their calibre join the Board.

On behalf of the Board and shareholders I would like to acknowledge the significant contribution and huge level of commitment that Jane, Maurice and Sally have made to the organisation over the years.

Finally, on behalf of the shareholders and the Board of Directors I would like to thank Di and her team for their hard work and dedication they have shown during what has been a very tough year. As a Board we have clear sight of the effort that Di and her team are applying to travel through a very challenging retail environment as well as drive major change in the organisation. I will now hand over to Di who will outline her thoughts on the 2014 financial year and transformation program that is being undertaken.

Chief Executive Officer's address (Di Humphries)

Thanks Peter.

As Peter has said it certainly has been a challenging year.

The 2014 financial result was disappointing for both me and the entire team, however we have embarked on a major transformation process to build the core capabilities. I will expand on the transformation process later in my address...but firstly let's look at this year's result.

The company recorded a trading profit of \$1.2m in 2014, which I agree with Peter is by no means satisfactory.

The 2014 financial year did not begin well with sales of summer season being materially impacted by major supply chain disruptions resulting from the failure of two core suppliers and major flooding in a key supply region in China. An immense amount of effort has been put into supply chain management during the year to ensure the issues experienced last year from late deliveries of stock are not repeated.

I am pleased to report that new season summer product is running on schedule. However we are now heading into the busiest trading period of the year and we will have a better understanding of sales and margin in the next few weeks and we will look to update the market.

Market conditions in Australia and New Zealand remained very challenging. Both markets were again characterised by high levels of promotional activity, increased international competitor injection and subdued consumer sentiment. A stronger New Zealand dollar also had a negative impact and resulted in lower overseas earnings in New Zealand dollar terms.

Our debt position at July 2014 was up \$16 million on last year which is simply to ensure timely delivery of new season stock in order to avoid the issues experienced last year from late deliveries. The late delivery of new season stock in the prior year resulted in artificially

low inventory and debt levels in FY13, so the increase in debt position this year is not as significant once this is taken into account.

Nevertheless, working capital management and strengthening our balance sheet position remain key priorities.

During the 2014 year we undertook a restructure of our Head Office functions. In order to build the team capability required to move forward into the future (which resulted in a net annualised saving of around \$3m. A number of roles were disestablished and a number of key appointments also were made, namely; **Brenda Pennycuick** (ex Glassons) as Chief Operating Officer, **Kellie Nathan** (ex Telecom) as General Manager of Marketing, and more recently **Steve Mackay** (ex Ezibuy) as Chief Financial Officer.

As mentioned earlier, the Executive team and I completed a review of the business during the year and we now have embarked on a comprehensive business transformation program in order to improve the Group's financial position into the future. In recognition of the extent of the change identified during the strategic review provisions totalling \$12.6m were recorded in the 2014 result against store assets, inventory and IT assets.

While the full impact of the strategic transformation process will not start to be seen until the 2016 financial year, through a continued disciplined approach to capital expenditure and inventory management, we are expecting bank debt in the latter part of FY15 to be lower than this year.

I would like to now lead you through the key aspects of the transformation program.

During this strategic planning phase our business aspirations were clear.

1. Enhanced shareholder value
2. Enhanced customer loyalty and engagement
3. To meet EBITDA and working capital objectives
4. Market leadership status in specialty childrenswear in NZ and Australia
5. Fully Engaged employees.

To deliver our aspiration we need to urgently implement and invest in order to drive our business transformation forward. The key strategic pillars of our business transformation are:

- Product Positioning aligned to customer demands.
- Customer Connection
- Cost efficiency
- Omni-channel
- IT systems

I'll now talk to you in more detail about each of these strategic priorities.

The first Product positioning aligned to customer demands.

To have great product, good quality, good fit, great styling at a value our customers are prepared to pay is only the admission ticket in today's market. We must also tailor our product offering to align it to customer demands. So fundamentally we must have the right product at the right price in the right quantities at the right time and right place is key for our future.

Some of the key initiatives underway are:

1. Improved unit cost in products.
2. Improve critical path - time taken of our end to end process which is speed to market.
3. Re-engineering of our product and pricing landscape.
4. Development of tools to enhance and support accuracy on category and department forecasting.

Our next strategic priority is around customer connection, and this is fundamental to helping us connect better with customers in a more relevant, personal way.

Some of the initiatives that we have under way in this space include:

- Creating an engaging in-store experience with exceptional customer service as well as a refreshed store layout and presentation.
- Developing a Customer Contact Strategy that allows us to communicate with customers based on their previous purchase behaviour. This is a big shift from our current mass approach to email communications, and provides us with opportunities to target and segment customers in meaningful ways.
- Initiating a data capture programme to enhance the value of our database.
- Also develop a Loyalty proposition moving forward.

Strategic priority number 3 relates to Cost efficiency.

We understand the cost of running the business, we question spend decisions and actively review processes to ensure efficiencies.

Examples of specific initiatives include:

- Supply chain optimization including reduction of inventory holdings
- The closure of non-profit making stores
- Streamlining head office functions (across all departments) and recognising any process efficiencies

Priority Number 4 – Omni Channel.

Omni channel retailing is critical to our long term business success.

Being a true omni-channel retailer requires us to offer continuity of experience across brands, channels and devices.

Future Omni-channel initiatives include:

- Developing a 360 degree real time view of all stock
- Creating a content rich e-commerce website that increases transactions and also tells our brand story.

- Mobile strategy – mobile devices are becoming more and more central to our customers life, and as a brand we need to make it as easy and seamless as possible for customers to engage with us via their mobile phone.

And finally we need to develop a single view of customer data that allows more targeted customer communications.

The last key strategic priority for Pumpkin Patch is our IT Systems.

We need our systems to be enablers of our strategic priorities, automated, dynamic and seamlessly connected.

In particular we are focused on reviewing our Product Planning system, ERP and planning and implementing broader systems changes that support our move to be an Omni-channel retailer.

Finally I would like to thank the entire Pumpkin Patch team for their hard work and dedication. They are very focussed on both managing the day to day operations of the business and supporting the Business Transformation.

I have seen the passion the team has for our brands and the commitment they have to bringing our short and long term goals to fruition. They are focussed on profitability and taking advantage of the growth opportunities that exist for us, and primarily to make Pumpkin Patch the company we know it can be.

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