Group Chief Executive's Review

"The Group continued to make progress in 2019 in improving the fundamentals underpinning our businesses as part of our multi-year transformation. While we still have work to do to complete phase one of our transformation plan, we are pleased with the progress so far and are turning attention to some areas of phase two with the objective of delivering well consistently… The diversity of the Group's business mix from the perspective of both direct and indirectly managed businesses, formats and geography did provide some insulation from unprecedented market challenges."

Introduction

Overall, the Group continued to make progress in 2019 in improving the fundamentals underpinning our businesses as part of our multi-year transformation. While we still have work to do to complete phase one of our transformation plan which entails building a strong retail foundation, we are pleased with the progress so far and are turning attention to some areas of phase two with the objective of delivering well consistently across all facets of our business.

The Group's Grocery Retail profits increased significantly in the year, driven by an improvement in Southeast Asia Grocery Retail as the space optimisation plan delivered enhanced quality and operating standards. While the turnaround of the Southeast Asian businesses remains at an early stage, there are encouraging signs of improvement.

Underlying performance for our Convenience format was pleasing. We continued to invest in mainland China, with the network having now grown to almost 1,300 stores. We also continued to invest in IKEA, with two additional stores opened in 2019. E-commerce growth was also strong for IKEA as improvements were made to website functionality across the region.

The Group's investments in Yonghui and Robinsons Retail delivered good returns. Underlying profit growth in Yonghui was strong as it benefitted from the partial sell-down of their investment in the Yunchuang Technology business, which was announced in December 2018. Robinsons Retail successfully integrated the Rustan acquisition in 2019.

The diversity of the Group's business mix from the perspective of both direct and indirectly managed businesses, formats and geography did provide some insulation from unprecedented market challenges. In particular, the social unrest in Hong Kong materially impacted the performance of the Group's Health and Beauty division, as well as Maxim's.

Five strategic imperatives

1) Grow in China

7-Eleven delivered strong growth, with almost 1,300 stores now opened, and we are pleased with the underlying performance of the business with strong like-for-like sales growth throughout the year. Strong focus has been put on the development of the ready-to-eat offering, which has resulted in higher day time traffic and converted consumer behaviour to encourage eating at 7-Eleven. On-top of this, digital and other services – such as facial recognition payment – continue to be one of the key drivers in China. There remains significant opportunity for growth in the longer-term with Guangdong province home to over 100 million people. In the short-term, however, competition for site rentals has intensified and we will remain disciplined in our property growth strategy.

Mannings China reported good like-for-like sales growth in the second half due to strong O2O e-commerce growth as well as encouraging results from new format designs. We have also developed a revised cross-border e-commerce platform for Mannings, with an upgraded and integrated supply chain to support fulfilment and accessibility. Our scale of growth in Mannings China has not fulfilled its potential historically, but we see

* Including 100% of associates and joint ventures.

opportunities for further space development through a realignment programme which aims to identify the optimal store format and size. There will be a stronger focus on the Greater Bay Area where Mannings has strong brand awareness and where the business can leverage the existing scale of 7-Eleven in the region.

We continue to develop a strong and growing relationship with Yonghui. Projects to leverage the scale of both companies are beginning to bear fruit with partnerships in procurement enhancing efficiency and reducing costs. In addition, Mannings branded products have been introduced into almost 450 Yonghui stores. We anticipate further shared learning and idea generation between the two businesses going forward. We also continue to develop relationships with China's technology companies, with a series of trials taking place to better understand the changes in customer expectations as regards the use of technology in this market and beyond.

2) Maintain strength in Hong Kong

The social unrest in Hong Kong negatively impacted our operations in our home market last year. Reduction in tourist traffic has had the greatest impact on Mannings within our portfolio. Disruptions to stores have also impacted our key associate Maxim's. IKEA's Hong Kong operations were also disrupted by the social unrest.

However, even within Hong Kong, we benefitted to some extent from the diversified mix of our businesses. While there was disruption to stores, a clear trend towards more eating at home supported solid like-for-like sales growth for Wellcome Hong Kong. A combination of improvement programmes and a more disciplined approach to store space saw an improving trend in underlying profit performance. We remain confident about the future growth potential of our Grocery Retail business in Hong Kong.

Performance for our Convenience format was pleasing with sales and profit ahead of last year. This is despite challenging conditions in the second half. In order to continue to build store traffic and brand differentiation, aggressive development of ready-to-eat and the Own Brand range was a key focus. This will continue in 2020.

Faced with the current challenges, the Group is adopting a prudent approach to cost control. The challenges in Hong Kong were also difficult for our team members but their commitment towards putting customers first was nevertheless unwavering and I would like to thank all of them for their hard work and dedication.

3) Revitalise Southeast Asia

Profitability in our Southeast Asian Grocery Retail business improved significantly in 2019 as we execute our multi-year transformation plan. Greater efficiencies generated from improvement programmes as well as our space optimisation plan supported the strong growth in profits. While the turnaround remains at an early stage, there are encouraging signs.

Our upscale stores continue to show signs of recovery as we raise operating standards of quality, freshness, availability and range. Remodelled pilot stores have been developed and initial performance has been encouraging.

We continue to re-engineer our food offering within Giant to focus on improving the customer proposition and optimising space. A detailed plan is being executed and we are expecting to see continued progress in 2020.

We are taking a holistic view towards space optimisation, of which the conversion of a Giant hypermarket to an IKEA store in Sentul, Indonesia is a good example. The store was opened in November, only five months after handover and was the fastest IKEA store opening in history.

Group Chief Executive's Review

Our Guardian Health and Beauty business remains a significant opportunity for us in Southeast Asia. Over 1,000 stores have now been opened across the region, with the business achieving strong like-for-like sales growth overall in the region. Profits in Singapore, Malaysia and Indonesia each achieved double-digit percentage growth. Indonesia grew particularly strongly, driven by strong retail execution as we introduced better, more relevant range into stores and invested in store fitout in a cost-effective manner.

Guardian is leveraging its strong brand name in the region both from the perspective of Own Brand, as well as innovative partnerships. Guardian Own Brand performance for products introduced into Rose Pharmacy has been strong. Guardian Singapore also entered into an exclusive partnership in 2019 with leading Korean Health and Beauty retailer Olive Young to enhance its range in the K-beauty segment.

We are continuing to invest in growth of the IKEA network across the Group, but in particular in Indonesia. While this will have some short-term impact on profits due to new store startup costs and pre-opening expenses, we remain confident about our underlying profitability for IKEA and its growth potential in the markets where we operate the franchise.

Robinsons Retail made a positive contribution in 2019. The adoption of the new lease accounting standard, IFRS 16, led to Robinsons Retail reporting a decline in profits.

4) Build capability

Since the start of 2018, we have significantly changed the leadership team to assemble a group of people who have strong track records in the Retail and Consumer industries. In addition to the senior leadership team, we have also built management depth within the business. There have been close to 200 middle-management new hires since 2018. In addition, over 80% of senior managers have taken new or expanded responsibilities.

The result of the strengthening of our capabilities has driven a significantly different way of working and seen a significant improvement in our ability to collaborate across functions, banners and regions, which has led to successful execution of a number of improvement programmes. We plan to change our Store Support Centre to an open plan environment to facilitate better collaboration.

We are taking a proactive approach towards nurturing younger talent within the organisation and collaborating more closely with the Jardine Matheson Group. Graduates of the Jardine Executive Trainee programme have taken opportunities in key areas of the business including commercial operations, merchandising, digital and finance management. We are also working more closely with Jardines in developing a pipeline of junior talent and graduate trainees.

We now have the ability to drive considerable changes necessary to not only improve Dairy Farm's performance but to transform the business to a modern-day retailer focused on delivering what customers want, where and how they want it.

5) Driving digital innovation

Retail is rapidly changing and Dairy Farm has historically been slow to respond to the pace of digital change.

Since the appointment of our Chief Digital Officer and Chief Technology Officer in the fourth quarter of 2018, a significant review of the previous ad-hoc programmes has been undertaken. Focus and discipline in our IT investments has been enhanced and we are confident that returns on our IT investments will improve over the coming years.

We have now successfully consolidated our IT systems in Singapore by introducing SAP and removing a significant number of legacy systems.

We have invested in e-commerce across both our Home Furnishings and Health and Beauty businesses. Enhanced website functionality supported growth for IKEA. In addition, we have invested in e-commerce infrastructure to support the growth of online sales for our Health and Beauty businesses. E-commerce for Guardian Singapore was relaunched in early 2020 with significant improvement in the customer experience. We expect these investments to support online sales growth for Mannings Hong Kong later in 2020.

Significant investments have also been made to enhance the Group's own digital data analytics capabilities, which will support the future growth of our businesses. In addition, progress is also being made in our partnerships with technology companies, which will support our digital transformation.

Leveraging scale

The key objective of our transformation is to leverage our expertise and scale more effectively across our countries and banners. This will be achieved by operating more effectively as one company. While we fully recognise that there needs to be localisation of the offer and customer proposition at both a banner and a country level, we also believe there are significant opportunities for us to drive efficiency and lower costs through a more cohesive approach towards leveraging synergy and scale.

Improvement programmes have been a key area of focus to date and will continue to be in 2020 and beyond. We are continuing to make progress in improving consistency and lowering costs in areas such as Procurement, Category Management, People Development, Store Productivity, Supply Chain Optimisation and Business Process Re-engineering. At the store level, we have been working on a number of projects to improve the workflow for team members and remove unnecessary duplication of work. For example, auto-replenishment systems have been introduced into Mannings Hong Kong, which reduces the amount of manual labour required for store team members when re-ordering inventory. In addition, programmes to introduce new systems and processes to improve fresh food quality and lower waste are being implemented and have been introduced to over 300 stores across the company, which are also yielding significant cost savings. At the Store Support Centre level, we have also taken a more centralised approach across functions to leverage the scale of the organisation. As an example, we have taken a centralised approach to marketing by moving away from having different media agencies across each banner and country. This has yielded a 90% reduction in the number of agencies we use and considerable cost savings.

The Group is now adopting a more consistent approach to Own Brand. One example is with the launch of the Meadows brand in our Food businesses. The brand is common across markets and we are able to leverage its scale in common sourcing, as well as marketing. The number of SKUs brought to market has progressively increased with focus on increasing range over time. The value proposition is exceptional with high quality products introduced that are significantly cheaper than branded equivalent products, helping to support value-for-money in our store offer. In addition, customers can find Meadows branded products across multiple banners including our supermarkets and convenience stores. We are piloting other Own Brand development options across our Health and Beauty businesses and leveraging scale when opportunities arise.

Impactful growth

As the business transforms there is a great opportunity to improve the Group's impact on the communities it serves, by demonstrating that Dairy Farm's business and commercial objectives are closely correlated with addressing societal challenges and by creating a consistent approach across our businesses to how they address those challenges. The Group is developing an enduring sustainable business architecture that is aligned with its corporate strategy and commercial ambitions. There is much work to do but the journey is underway to become a truly purpose-led business.

Year ahead

The Dairy Farm transformation remains on track. Our efforts over the past two years to enhance capability, change the way in which we operate, to address underlying business challenges previously neglected and to focus on consistently improving retail basics across our business are all combining to enhance Dairy Farm's prospects for the future. This cultural change to drive Standardisation, Synergy and Scale is now integrated into our way of working.

We also benefit from the diversity of our portfolio, not only in terms of retail sector, format and geographical spread, but also in the balance between Dairy Farm managed businesses and Dairy Farm invested businesses. While we have seen some businesses with a Hong Kong bias adversely impacted in their 2019 performance, others have seen performance improve, most notably in Southeast Asia where our turnaround plans are beginning to bear fruit. In addition, the integration of our Rustan business into Robinsons Retail has proved to be a successful financial investment decision in its first year.

We are not ignoring the current short-term challenges and have been pro-active in adapting to a changing operating environment, seeking to optimise our current trading position in difficult circumstances. However, the diversity of our portfolio does provide the Group with greater resilience when facing external market uncertainties such as the events of 2019 and the current COVID-19 challenges of 2020.

All sustainable business transformations take time to execute and we are still in the early stages of that transformation. Nonetheless, we are encouraged by our underlying progress to date, remain resolute in our confidence in our turnaround plan and are grateful for the determination and effort of all our team members across Dairy Farm in their personal hard work to make a sustainable performance difference over time, both for our shareholders and most importantly, our customers.

Ian McLeod
Group Chief Executive
5th March 2020