

Chief Executive's Review



Group sales from continuing businesses increased by 11.7 per cent to £4,975.6 million and profit before tax and exceptional items was up 3.2 per cent to £553.2 million. In an uncertain economic climate we continued to find new ways to grow our businesses and generate value for shareholders.

Cash flow Operating cash flow was £605.6 million, an increase of 17.6 per cent on the previous year. In addition to the cash flow generated by the businesses, we benefited from buoyant demand in the retail property market; this enabled Boots Properties to generate cash flow totalling £233.7 million from property disposals.

Businesses Boots The Chemists increased sales by 7.9 per cent and profits by 4.1 per cent to £443.8 million. Customers have responded enthusiastically to the Advantage Card, and incremental sales are already covering its ongoing operating costs. By tailoring store formats to locations, Boots The Chemists is still managing to extend its UK store network profitably, and in The Republic of Ireland its rapid growth – both organic and through acquisition – has made it the country's largest retail pharmacy chain.

Our pilot international retail programme is making good progress, with nine Boots Health & Beauty stores now trading successfully in Thailand and The Netherlands. Since the year end we have announced further investment in Thailand, where we plan to open another 40 stores over the next two years.

Halfords maintained strong profit growth, with operating profit up 27.6 per cent to £34.2 million on sales up 5.4 per cent. Margins were boosted by further expansion of own brand sales; profits also benefited from the continuing recovery of the garage servicing business, which came close to breaking even in the year and showed a profit in the second half.

Boots Opticians accelerated its sales and profits growth with sales up 23.5 per cent and operating profit before exceptionals up 23.2 per cent to £17 million. This outstanding result was achieved against fierce competition. The competitive strength of Boots Opticians comes from its success in attracting and retaining scarce qualified staff and its use of technology to provide high quality customer service. Our confidence in the business is clear from the fact that in 1998/99 we are stepping-up the rate at which it opens new stores.

In its first full year of ownership by Boots, Do It All is on the mend and has produced an excellent result – making a profit of £2.5 million compared with a £7.6 million loss in the previous year. The disposal of underperforming stores was virtually complete by the end of the year. Although this resulted in an overall sales reduction of 3.2 per cent, the ongoing stores achieved encouraging sales growth of 6.8 per cent.

At Boots Healthcare International, the investment of previous years is now bearing fruit: sales grew 12.4 per cent and the business turned a 1996/97 operating loss before exceptionals of £6.6 million into an operating profit before exceptionals of £1.2 million. Our confidence in its ability to achieve sustained growth and value creation is demonstrated by our continued investment in this business.

Boots Contract Manufacturing grew sales by 21.3 per cent and increased profits by 25.4 per cent to £24.7 million. This was a considerable achievement given the strength of sterling against other currencies and

reflected flexible use of the company's manufacturing operations in France, Germany and Spain.

Boots Properties delivered an outstanding return on previous years' investment, capitalising on the latest turn of the market cycle. The business took the opportunity of a buoyant market to sell some shopping centres and retail parks at premium prices – raising a total of £301.1 million.

Understanding our customers Continued profitable growth, particularly in our retail businesses, has always depended on knowing and understanding our customers. Today we are using increasingly sophisticated technology to achieve this – through the database marketing system being introduced by Boots Opticians, for example, and most significantly through the new Boots The Chemists Advantage Card. Already being used by eight million people, the Advantage Card is the first loyalty card from a major retailer to use smartcard technology. By giving us much deeper knowledge of our customers it will greatly refine the way we target and market products.

Making the most of our people The quality of our customer service and the imagination and flexibility with which we drive forward every part of our business, depend entirely on attracting, retaining and developing outstanding people at every level in the organisation. As a group, we are fortunate in being able to offer managers a broad range of experience and career opportunities; and we are encouraging all our business units to find their own ways of making the most of their people's potential and providing them with attractive, challenging careers.

Outlook With the UK economy showing signs of slowing down we see some evidence of weaker retail sales in what is an increasingly fragile domestic market. We know that our core businesses are resilient and capable of withstanding such conditions more robustly than many other retail businesses. Whilst continuing to exploit opportunities for expansion in the UK and to capitalise on strengths in own brands and information technology, we are directing more of our attention to overseas opportunities. At home our stable and loyal customer base underpins our confidence that we shall continue creating value for shareholders.

Lord Blyth of Rowington
Deputy Chairman and Chief Executive