News Release

Wesfarmers

15 March 2018

Intention to demerge Coles and senior leadership change

Wesfarmers today announced its intention to demerge its Coles division, subject to shareholder and other approvals.

It is anticipated that the proposed demerger would create a new top 30 company listed on the Australian Securities Exchange, with leading positions in supermarkets, liquor and convenience, strong cash generation capability to underpin dividend distributions, and an earnings profile which is expected to be resilient through economic cycles.

The decision follows a review of the Wesfarmers portfolio and an assessment of the composition of its capital employed to support higher levels of future growth and total shareholder returns. As at 31 December 2017, Coles accounted for approximately 60 per cent of the Group's capital employed and 34 per cent of Group divisional earnings.

Wesfarmers Managing Director Rob Scott said the Group was repositioning its portfolio to target a higher capital weighting toward businesses with strong future earnings growth prospects.

"Wesfarmers acquired Coles as part of Coles Group in 2007 and since then has successfully turned around the business and restored its position as a leading Australian retailer," Mr Scott said.

"We believe Coles has developed strong investment fundamentals and is of a scale where it should be operated and owned separately. It is now a mature and cash generative business, which is expected to have a strong balance sheet and dividend paying capacity. Coles will be well positioned to continue to deliver long-term earnings growth, with an earnings profile that is expected to be resilient through economic cycles.

"A demerger of Coles will facilitate greater focus by Wesfarmers on growth opportunities within its remaining businesses and the pursuit of value accretive transactions. The capacity to act opportunistically will be retained through a strong balance sheet and a cash generative portfolio. The Group expects to retain its current strong credit ratings and the dividend policy will remain unchanged."

Wesfarmers Chairman Michael Chaney said the demerger would extend the Group's long history of actively managing its portfolio.

"Wesfarmers' operating model has benefited our shareholders over the long term and will continue to provide the framework for future capital allocation decisions," Mr Chaney said.

Wesfarmers post the proposed demerger

Wesfarmers' remaining operating divisions include a number of world-class businesses and leading Australian brands, including Bunnings, Kmart, Officeworks, and its Industrials portfolio. The remaining divisions in Wesfarmers, excluding Resources, delivered compound annual growth in earnings of 8.9 per cent since FY2009 and generated a return on capital, excluding significant items, of 23.6 per cent, as at 31 December 2017. Organic and inorganic growth opportunities position these businesses well to deliver continued growth in earnings and returns.

Wesfarmers proposes to retain a minority ownership interest of up to 20 per cent in Coles following the demerger to support strategic alignment between Wesfarmers and Coles in relation to various growth initiatives, including in the areas of data and digital. Wesfarmers also proposes to retain a substantial ownership stake in flybuys to support continued access to the loyalty program and continued investment in data analytics capabilities.

If the proposed demerger proceeds, Wesfarmers' objective will remain the delivery of satisfactory returns to shareholders over the long term through active management of a diversified portfolio of businesses and strong financial discipline.

Coles post the proposed demerger

Coles is one of Australia's largest retailers, providing fresh food, groceries, general merchandise, financial services, liquor, hotels and fuel. It employs more than 109,000 people across Australia and processes 21 million customer transactions on average per week through a national network of approximately 2,500[1] stores and through online platforms.

Businesses to be included in the proposed demerger would include a national network of 806[1] supermarkets as well as Coles Online; 894[1] liquor stores nationally through Liquorland, Vintage Cellars and First Choice Liquor; Coles Express which operates 712[1] fuel and convenience store outlets under an exclusive alliance with Viva Energy; Coles Financial Services, which offers general insurance and credit cards; and Spirit Hotels, a chain of 88[1] hotels predominantly in Queensland.

Under Wesfarmers' ownership, over $8 billion of capital has been invested in the business across the store network, supply chain and online channel. Long-term collaborative partnerships have been developed with many suppliers, and prices have been reduced for customers for eight consecutive years.

Coles is well-placed to continue to execute its customer-led strategy and achieve growth over the long-term as demand increases for quality fresh food at great value, further supply chain efficiencies are identified and executed, the transformation of the liquor business progresses, and through the opportunities to drive growth in online, convenience and financial services.

Further detail, including Coles' proposed capital structure, dividend policy, separation, and governance arrangements will be announced in due course.

Demerger mechanics, timing and execution

If the demerger is implemented, Wesfarmers shareholders will receive shares in Coles proportional to their existing Wesfarmers holdings, after taking into account any shares to be retained by Wesfarmers. It is expected that the distribution of Coles shares to shareholders will qualify for demerger tax relief, subject to an Australian Tax Office ruling being obtained.

The demerger is subject to final Board approval, third party consents, and regulatory and shareholder approvals. If approved, the demerger would be expected to be completed in the 2019 financial year.

Coles leadership succession

Wesfarmers also announced that Steven Cain will be the next Managing Director of Coles, succeeding John Durkan, who will step down later this year after 10 years in senior leadership positions at Coles, including four as Managing Director.

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[1] As at 31 December 2017.

Mr Scott said Mr Durkan had decided it was the appropriate time for a leadership transition as Coles entered its next chapter. He will remain in an advisory capacity following the leadership change to ensure a seamless transition.

"John has made an enormous contribution to the successful turnaround of Coles under Wesfarmers' ownership and we look forward to him continuing to lead the business as we prepare for demerger," Mr Scott said.

Mr Cain is currently Chief Executive Officer of Supermarkets and Convenience at Metcash (ASX:MTS) and will bring significant local and international business experience when he joins the Group.

Mr Cain began his career with Bain & Co before moving into retail with UK retail group Kingfisher plc, later helping to transform supermarket chain Asda, where his roles included Group Marketing Director, Store Development Director and Grocery Trading Director. Later roles included being CEO of FTSE 100 media group Carlton Communications plc, Managing Director of food, liquor and fuel at Coles Myer, and Operating Director and portfolio company chairman at private equity firm Pacific Equity Partners, before joining Metcash in 2015. Steven was also an adviser to Wesfarmers on its takeover of the Coles Group in 2007.

Steven has attended management programs at Harvard and London Business Schools and has a Master of Chemical Engineering Degree from Imperial College London.

"Steven brings a wealth of experience in international and Australian retailing with organisations such as Asda, Kingfisher, Coles and Metcash," Mr Scott said. "This, combined with his experience as a listed company CEO, positions Steven well to lead Coles post the demerger."

Mr Cain said he was very excited at the opportunity to join Coles as it embarked on the next phase of its evolution as a great Australian retailer.

Mr Scott said Mr Durkan had spearheaded lowering the cost of the weekly grocery shop for Australian families over the past decade, and consequently led food retailers more broadly into a period of giving customers greater value for their money.

"The fact that food at Coles has been in deflation for eight consecutive years is in no small part due to John's determination to provide Australians with great quality food at great value," Mr Scott said.

"Coles' customers, regardless of where they live in Australia, have access to the best of Australian fresh produce, meat, deli and dairy, and market-leading prices on grocery. John has been instrumental in this fundamental change in Australian retailing.

"Under his leadership we have also seen the turnaround of Coles Liquor, a business that was in structural decline for many years, a much improved convenience offer through Coles Express, the establishment of the $50 million Coles Nurture Fund, the transformation of a number of key digital enablers across our store network, supporting the exponential growth of Redkite and SecondBite, and myriad initiatives to attract and retain great talent, including establishing one of the largest graduate programs in Australia."

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