

CHIEF EXECUTIVE OFFICER'S REPORT



MAURICE
PRENDERGAST

While the retail conditions across all our markets were challenging in 2008 we again grew sales and earnings across our all important Australian and New Zealand markets and continued to develop the brand in the United Kingdom, the United States and other markets around the world.

Total group operating revenue increased 12.3% to \$410.4m. Australia and New Zealand continued to deliver strong sales performances even when faced with more challenging retail conditions. This reflects the market leading position of the Pumpkin Patch brand in the two markets. Sales in the developing United States and United Kingdom market grew through new store openings. The Wholesale and Direct divisions again generated sales growth.

Group NPAT was \$17.1m compared to \$23.5m in 2007. Strong earnings growth from the Australian and Wholesale segments was offset by higher interest charges, higher quota costs, and losses from the United States and United Kingdom segments.

AUSTRALIA RETAIL

Although the Australian segment faced more challenging retail conditions in the latter part of the year full year sales continued to grow strongly up 11.4% to \$198.5m. This strong sales performance reflects the strength of the Pumpkin Patch brand in the market, the very strong summer and winter ranges offered to customers, and a more favourable average AUD/ NZD exchange rate.

Australian retail EBIT was up 16.1% to \$41.0m. EBIT margins were positively impacted by the ongoing focus on controlling product margins in a softening market and continued economies of scale benefits. Increased promotional activity was seen across the market in 2H08 as general retail conditions softened however this did not materially impact EBIT margins.

During the period we opened 5 new stores (2007: 13) taking total stores to 107.

NEW ZEALAND RETAIL

New Zealand retail sales grew 2.0% to \$65.6m a very solid performance considering the general retail environment was poor for much of the year. Sales softened in the latter part of year however the market leading position Pumpkin Patch holds lessened the impact of the slowdown.

We opened three stores in the year (2007: 4) and merged 1 Urban Angel store into an existing Pumpkin Patch store (2007: 3 mergers). Store numbers at July totalled 52.

	2008	2007	
	\$000	\$000	
Turnover AUD	163,401	156,945	4.1%
Turnover NZD	198,452	178,119	11.4%
EBIT NZD	41,031	35,349	16.1%
	20.7%	19.8%	
Stores			
Pumpkin Patch	95	90	
Outlet	11	11	
Urban Angel	1	1	
	<u>107</u>	<u>102</u>	

	2008	2007	
	\$000	\$000	
Turnover NZD	65,633	64,334	2.0%
EBIT	12,586	12,500	0.1%
	19.2%	19.4%	
Stores			
Pumpkin Patch	32	32	
Outlet	11	8	
Urban Angel	9	10	
	<u>52</u>	<u>50</u>	

UNITED KINGDOM RETAIL

United Kingdom retail sales grew to GBP 22.7m up 15.8%, or NZ\$59.4m up 9.4%. The retail environment across the year was very soft compared to 2007. Conditions slowed as the year progressed and as the economic outlook for the consumer worsened. This was reflected in the disappointing sales results from retail market leaders.

On 1 January 2008 the European Union quota ceased and as a consequence all unused quota at that time was written off leading to a one off \$1.0m quota expense for the United Kingdom Retail segment. Total quota costs for the year including the write off were \$2.2m (2007: \$1.6m). Supply chain and quota management complexities at times lead to stock mix and volume issues which meant some sales opportunities were lost especially earlier in the year. The ending of quota and the implementation of a number of supply chain initiatives will lessen the complexity of managing inventory in the future.

Of the 30 stores open longer than 12 months 18 stores generated positive EBIT contributions at store level before quota costs.

During the period we opened 5 new stores (2007: 7) taking the total number of stores at July to 35.

	2008	2007	
	\$000	\$000	
Turnover GBP	22,654	19,564	15.8%
Turnover NZD	59,369	54,258	9.4%
Before quota costs:			
EBITDA NZD	3,015	5,465	
	5.1%	10.1%	
EBIT NZD	(399)	2,639	
	(0.6%)	4.9%	
After quota costs:			
EBITDA NZD	793	3,889	
	1.3%	7.2%	
EBIT NZD	(2,621)	1,063	
	(4.4%)	2.0%	
Stores			
Pumpkin Patch	33	29	
Outlet	2	1	
	<u>35</u>	<u>30</u>	

UNITED STATES RETAIL

United States retail sales were US\$20.9m up 63.2%, or NZ\$27.3m up 50.6%. The translation of sales into NZD was impacted by the higher USD/NZD exchange rate during the year.

The United States retail environment was very tough with market leaders reporting extremely difficult trading conditions. Some industry rationalisation is occurring with many retailers closing stores and slowing store roll out plans, and in some cases closing entire operations. Such conditions are difficult for new entrants who do not have an established brand presence.

During the period we opened 16 stores (2007: 11) taking total stores to 34 across 8 states. On average stores have been opened for 16 months.

The EBIT loss was NZ\$6.6m before quota and NZ\$9.2m after quota. EBIT was significantly impacted by the very poor retail environment and increased quota costs. Quota costs for the period were \$2.6m (2007: \$1.1m). The increase is due to both an increase in the volume of product shipped to the United States and a significant increase in the per unit price of quota during the year.

As with the United Kingdom the complexities of working with quota at times led to stock levels and mix not being ideal and some sales opportunities were lost. A number of supply chain initiatives currently being implemented and the scheduled ending of quota on 1 January 2009 will help reduce the complexity of managing inventory in coming years.

Of the 18 stores open for greater than 12 months 10 stores made positive EBIT contributions at store level before quota costs.

	2008	2007	
	\$000	\$000	
Turnover USD	20,898	12,805	63.2%
Turnover NZD	27,310	18,137	50.6%
Before quota costs:			
EBITDA NZD	(3,375)	1,488	
	(12.4%)	8.2%	
EBIT NZD	(6,587)	(371)	
	(24.1%)	(2.0%)	
After quota costs:			
EBITDA NZD	(5,968)	340	
	(21.9%)	1.9%	
EBIT NZD	(9,180)	(1,519)	
	(33.6%)	(8.4%)	
Stores			
Pumpkin Patch	<u>34</u>	<u>18</u>	

WHOLESALE AND DIRECT

Wholesale and Direct turnover was up 17.8% to \$59.4m. Sales growth was achieved in local currency terms across most markets however this growth was negatively impacted by the high exchange rates when sales were converted back to NZD.

EBIT excluding quota for the year was \$17.4m up 11.7% on last year. EBIT including quota was up 10.6% to \$15.5m.

Quota costs for the period were \$1.8m (2007: \$1.5m) including a one off \$0.2m write off of unused European Union quota on hand when the quota ended on 1 January 2008. Quota costs will reduce in 2009 due to the ending of European Union quota and will be nil in 2010 following the end of United States quota in January 2009.

The development of our mail order and internet businesses in the United Kingdom and the United States is showing good early signs with solid sales growth coming from both markets.

	2008	2007	
	\$000	\$000	
Turnover NZD	59,380	50,410	17.8%
EBIT (before quota costs)	17,388	15,562	11.7%
	29.3%	30.9%	
EBIT NZ	15,541	14,048	10.6%
	26.2%	27.9%	

CASH FLOWS AND BALANCE SHEET

We continue to maintain a strong balance sheet with net assets of \$96.7m at July.

Inventory holdings at July were \$35.8m higher than the same time last year. Although additional inventory was held for stores opened during the year the majority of the increase related to inventory purchased to provide a buffer against ongoing supply chain disruptions into the United Kingdom and the United States. The impact of the additional stock purchased was accentuated by the softening of the retail environment in those two markets. A number of stock reduction and supply chain strategies are being implemented which will lead to lower inventory holdings on an average store basis over the next 18 months. The stock reduction strategies are not expected to materially impact margins over this period.

Fixed assets increased \$18.2m from 2007 reflecting the capital expenditure on the 29 stores opened in 2008 less ongoing depreciation charges.

We had total bank debt of \$81.3m at July (2007: \$37.1m). The movement is mostly the result of the increased inventory holdings.

Capital expenditure cash flows totalled \$35.6m (2007: \$35.8m). Although new store openings were lower in 2008 there was a change in the mix of new stores towards the more expensive United States stores.

TRADING OUTLOOK FOR 2009

AUSTRALIA

We are expecting trading conditions to be difficult throughout 2009 as a result of the tougher retail environment. However the strength of the Pumpkin Patch brand in the Australian market will position us well for when consumers come back to the market.

We plan to open at least 4 stores in 2009 including 1 Outlet store.

NEW ZEALAND

The retail environment is expected to remain very challenging throughout 2009 and store level profitability is likely to be impacted due to the fixed nature of store overheads.

It is expected that 4 new stores will open in 2009 including 3 Outlet stores.

UNITED KINGDOM

The current difficult retail conditions are expected to continue as general consumer sentiment remains at historically low levels. However customer awareness of the Pumpkin Patch brand continues to grow and trading at the more recently opened stores is expected to improve during 2009.

We will focus on enhancing margins through better inventory management and building further the brand awareness that is developing. Continued refinement of logistics systems and the removal of quota will improve segment EBIT margins however the impact of these will not be noticeable until overall retail trading conditions improve which is not expected until at least 2010.

As previously reported we are following a more cautious roll out program while market conditions remain soft. We will maintain our normal disciplined approach to site selection and new stores will only be considered when landlord contributions significantly cover capital expenditure costs. Currently one new store has been committed to for 2009.

UNITED STATES

The current tough retail environment is expected to continue throughout 2009 and into 2010. This is delaying the store sales growth profile that would normally be expected from a maturing network of stores. As a result the segment is expected to continue to generate EBIT losses for the foreseeable future.

While market conditions remain as they are we will focus on bedding down existing stores, increasing brand awareness, building a customer database, and ensuring the supply chain is operating efficiently to reduce costs and improve the management of inventory.

We plan to follow a more cautious expansion plan with 1 store committed for opening in 2009.

Medium term strategies for the United States operation continue to be developed. With an average store age of only 16 months it is still very early in the market's development life cycle.

We believe the best strategy in the near term while general retail conditions remain very difficult is to continue to drive store level cost efficiencies, enhance supply chain and inventory management processes, promote the brand within the market place, and open new stores only when stringent lease criteria are met.

WHOLESALE

The Wholesale Division is expected to be impacted by the current global retail weakness with lower sales forecasted from major wholesale customers in the United States, United Kingdom, and Australia. In addition softer retail conditions across many of our newer wholesale markets are expected to lead to slower growth rates in 2009. Softer global retail markets are also expected to lead to increased margin pressure from customers in 2009.

We continue to research other Asian and European markets and develop strategies for a number of these. However it is unlikely that any new markets will be entered in 2009.

The Direct operation will continue to grow especially in the United States and the United Kingdom however noticeable earnings will not be seen until 2010 and beyond.

EXECUTIVE TEAM CHANGES

As previously reported Greg Muir will soon be standing down from his executive role as General Manager Wholesale. I would like to thank him for the effort he has put in nurturing the Wholesale Division and developing relationships with customers over the last 5 years. The division is now a major earnings generator for the Company and is an important part of Pumpkin Patch's long term global strategy.

Neil Cowie, our Chief Operating Officer, is to take over the day to day responsibility of the Wholesale Division. This includes the management and coordination of existing Wholesale markets and the ongoing research and development of new markets around the world. Having Neil responsible for the Retail and Wholesale Divisions, while working closely with the Direct Division, will mean a full multi channel approach can be applied to all current and future markets

SUMMARY

The very strong sales performance across Australasia reflects the market leading position the Pumpkin Patch brand holds in Australia and New Zealand. Although 2009 will be more difficult than 2008 we are well placed to withstand challenges that will arise.

The continued development of new Wholesale markets shows that Pumpkin Patch is well on the way to become a truly global fashion brand.

Although the trading conditions are likely to remain very difficult in the United States and the United Kingdom and short term earnings will continue to be impacted by those conditions we are very confident that these markets play a very important role in the overall global strategies of Pumpkin Patch.

Once again I would like to thank all of the team spread out over many markets around the world. They are facing challenging times but are working even harder every day to continue the development of the Pumpkin Patch brand. Their level of commitment and dedication to the long term strategies of the business are as strong as ever and I look forward to working with them into the future.



Maurice Prendergast - CEO