



api

2017
ANNUAL
REPORT

Australian Pharmaceutical Industries Limited

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ANNUAL REPORT 2017

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**Enriching life as the most
inspirational choice for health,
beauty and wellbeing.**

The Directors present their report together with the financial report of Australian Pharmaceutical Industries Limited ('the Company') and of the consolidated entity, being the Company and its controlled entities, for the year ended 31 August 2017 and the Auditor's report thereon.

MESSAGE FROM THE CHAIRMAN AND CEO

PETER ROBINSON AND RICHARD VINCENT



We are pleased to present to shareholders the Company's annual report for the financial year ended 31 August 2017

API has a focused growth strategy centred on two key objectives.

The first is building Priceline Pharmacy's position as Australia's favourite mass market health and beauty retailer. In the face of subdued consumer sentiment and intensified competition we continued to evolve all aspects of our customer offering, particularly our in-store product range and service capabilities, in both health and beauty.

The second is ensuring that our pharmacy distribution business continues to deliver steady and sustainable growth in the face of ongoing Pharmaceutical Benefits Scheme (PBS) reforms. We increased our investment in the development of professional services as this area is increasingly important for pharmacists'

future remuneration and we also expanded our distribution footprint to help deliver more timely and efficient stock management for our growing customer base.

API's significant infrastructure investments in prior years meant we could further streamline our business to weather the challenging conditions in both retailing and pharmacy distribution.

Of equal importance to our operating results is that our focus on capital management has seen us achieve further improvements in working capital and record zero reported net debt ahead of schedule. We continue to evaluate a range of options for future capital allocation to optimise value for shareholders.

MESSAGE FROM THE CHAIRMAN AND CEO

CONTINUED

Underlying NPAT of \$54.2 million was up 5.4% on the prior year.

OPERATIONAL PERFORMANCE

Financial highlights

- Underlying¹ net profit after tax of \$54.2 million, up 5.4% on the underlying NPAT for the prior year;
- Underlying earnings before interest, tax, depreciation and amortisation of \$120.5 million, an increase of 6.1% on the prior year;
- Underlying return on capital employed up 140 basis points to 16.9%;
- Underlying return on equity up 20 basis points to 9.8%;
- Net cash was positive by \$7.2 million; and,
- Dividends paid to shareholders were up 17% for the year to 7.0 cents per share.

The Priceline Pharmacy network finished the financial year at 462 stores, increased by a net 20 stores on the previous year. Retail register sales¹ for the period were up 2.0% to \$1.15 billion, but like for like store sales¹ were down on the previous year by 0.4%. Including dispensary, total retail sales for the network were \$2.1 billion for the financial year, up 5% on the last financial year.

The store network grew both revenue and market share in health, with both dispensary and over-the-counter medicines delivering positive results. The beauty category also grew during the year but at a slower rate than previous years due to depressed consumer sentiment which has a more pronounced impact in discretionary categories.

During 2017 we implemented phase-one of our Sister Club relaunch, introducing tiering and increased benefits for members. We have since commenced phase two, an investment that will maximise our ability to deliver timely, personalised offers to 7.1 million members. Our 'new generation' store format roll-out is gathering pace, further differentiating the brand from its competitors via dedicated service counters and personal spaces to test and try new products. Ensuring our store experience remains superior is particularly important in the current trading environment.

Our pharmacy distribution business delivered very pleasing revenue growth of 7.3%. When normalised for the effect of PBS reforms and Hepatitis C medicines, sales revenue was up 7.5% on the previous financial year.

We opened a new Distribution Centre in Western Australia at a total cost of \$5 million. The new DC will service our growing base of independent pharmacists in that State. Our Soul Pattinson, Pharmacist Advice and our program for independent pharmacies, Club Premium, expanded their membership base during the year.

Our New Zealand manufacturing business improved earnings in the 2nd half of the year as the benefits of new manufacturing contracts flowed through, but overall sales declined by 5.4% and gross profit by 6.8% compared to the prior year. The decline in performance was largely due to the change in scheduling of codeine-based products in Australia. We have responded with a range of over-the-counter alternatives which we expect to improve our performance in 2018.

1. To be read in conjunction with FY17 Results Announcement 19 October 2017.



Underlying NPAT

↑ **5.4%**

Underlying EBITDA

↑ **6.1%**

Full year dividends

↑ **17%**

Our Brands



MESSAGE FROM THE CHAIRMAN AND CEO

CONTINUED

The Company has increased total dividend payments by a compound annual growth rate of 29.3% in the last three years.

PBS Landscape

The Government initiated review into Pharmacy Remuneration and Regulation handed down an Interim Report, with the Final Report now pending. Unfortunately, the Interim Report largely ignored the wholesaling sector's evidence-based recommendations on the policy settings required to ensure a cost effective and sustainable pharmaceutical distribution system that delivers equality of access to vital medicines for all Australians. We have been heartened by subsequent discussions with the Department and the Minister and we are optimistic that we will achieve a satisfactory outcome.

Group summary

We ended the financial year with a reduction in reported net debt at balance date of \$33.1m which has been a source of constant improvement. This was achieved by improvements in our working capital and cash conversion cycle. The latter was down another 1.9 days to 22 days at the year end. The cost of doing business as a percentage of revenue declined to 9.45%, a 20 basis points improvement on last year.

The Company generated \$102 million in free cash, up 22% on FY16, which enabled the payment of debt and ongoing investments in the Company's key programs. Other than stay-in-business capital expenditure, such as store refits, future investments will be focussed on furthering our in-store retail offer and on our Sister Club infrastructure.

The Company has increased total dividend payments by a compound annual growth rate of 29.3% in the last three years. This reflects the ongoing improvement in the overall financial position of the Company. The dividends of 7.0 cents per share in 2017 represented a 65% payout ratio, increasing from 60% in 2016.

It is also worth recognising that the Company's long term focus is making API a safer place to work. The emphasis on this in our stores, Distribution Centres and offices has yielded further reductions in both the Total Recordable Injury Frequency Rate as well as Lost Time Injury Frequency Rate over the last financial year. Safety is the responsibility of every staff member at API so we can create the safest environments for our teams and anyone visiting our premises.

Corporate Social Responsibility

The Priceline Sisterhood Foundation is API's major Corporate Social Responsibility program. During the year approximately \$400,000 dollars was raised for the Foundation due to the joint efforts of API staff and our Priceline Pharmacy franchisees. The Foundation actively supported five key charities during the year: Dementia Australia, Look Good Feel Better, Hear to Listen, The Children First Foundation, and Perinatal Anxiety and Depression Australia. The Foundation has raised more than \$3.4 million since its inception in 2011 and is an integral part of the API and Priceline Pharmacy culture.



Leadership succession

After ten years Stephen Roche stepped down as CEO and Managing Director and the Board appointed API's General Manager of Business Development, Operations and Strategy, Richard Vincent to the role. The Board reiterates its thanks to Stephen for his leadership of the Company and for the smooth transition to our new CEO and Managing Director.

The Company announced in September of this year that Mark Smith had been appointed as a Non-executive Director and, subject to Mr Smith's election at the 2017 Annual General Meeting, the Board intends to confirm Mark's appointment as Chairman of the Board, effective from that date.

Finally, on behalf of all API Directors, our congratulations and thanks to all our people for their commitment and dedication to delivering another solid result in such a dynamic operating environment. We look forward to their ongoing commitment to implementing our strategy as we face into another challenging year.

Peter R Robinson
Chairman

Richard C Vincent
Managing Director
and Chief Executive Officer

Priceline Sisterhood Foundation™

HELP US HELP WOMEN

MORE THAN
\$3,400,000
RAISED SO FAR

The Priceline Sisterhood was initially formed in 2011 with its purpose being to give back to the community and, specifically, to provide support to women and their families.

Charity Partners were selected that covered a range of causes that were close to the hearts of women; coming from the results of a national survey that had more than 25,000 female respondents.

In 2014 the Priceline Sisterhood Foundation Limited was established to allow for tax deductible donations. The Foundation has an independent Board of Directors and the patron of the Foundation is Ita Buttrose. More than \$3 million has been raised since inception and all funds raised go directly to our Charity Partners.

The Priceline Sisterhood Foundation today

The Foundation has a desire to help more Australian women and their families by supporting those who are affected by conditions such as cancer and mental health. The Foundation also aims to increase awareness of the work the charities are undertaking as this can lead to greater understanding, better treatment, and, in some cases, prevention.

In reality there is only one degree of separation for many Australians who know people affected by these conditions and the Foundation is working to support all those affected, either directly or indirectly.

More information about the Priceline Sisterhood Foundation can be found at <https://www.priceline.com.au/sisterhood>



Who does the Foundation help?

The Charity Partners help thousands of Australians every day. This is what the causes are about and a snapshot of who they help:

Dementia Australia

Alzheimer's Australia has rebranded to **Dementia Australia**. The change represents a shift in focus from Alzheimer's, the most common form of dementia, to now include all 100+ types of dementia that exist in Australia. Dementia Australia's main challenge will be to raise awareness and understanding of dementia while the condition continues to grow in prevalence nationally. By unifying all forms of dementia, the organisation can deliver consistent support services, strengthen their capacity for advocacy and enhance their ability to raise awareness, fundraise and facilitate research and education into the prevention, delay and cure of dementia.

Children First Foundation

The Children First Foundation was established in 1999 to provide seriously injured or unwell children from developing countries with the opportunity to have lifesaving/ changing surgery. Our two programs support the belief that excellent medical care is a basic right of every child regardless of where they are born:

- *Miracle Smiles* brings children from developing countries to Australia for profoundly life-changing, or life-saving surgery that is not available in their country of birth
- *Between the Gaps* supports Australian families with disabled or chronically ill children by providing the 'gap' funding for equipment and services that are only partially funded by government and other support agencies.

Hear to Listen

Hear to Listen is a pilot program being run in South Australia to improve hearing for Aboriginal children. Remarkably more than 60% of all Aboriginal children at schools in Australia have a hearing issue, which can significantly impair their ability and willingness to learn. This program aims to address this issue with clinical assistance and will be run over two years coordinated by the Cora Barclay Centre in Adelaide and supported by Port Power's community program.

Look Good... Feel Better

Look Good... Feel Better (LGFB) is a free community service program dedicated to helping Australians living with cancer cope with the side effects of chemotherapy. By addressing hair loss and skin changes through the use of skin care, make-up, hats, turbans and wigs, they help to restore patients' appearance and self-image.

In Australia, more than 118,000 people have participated in the program, which now offers approximately 1,000 workshops nationwide in more than 180 venues.

Today, the program is managed by a small team of staff and together with the support of 1,500 trained and certified cosmetic, beauty and hairdressing professionals who volunteer their time and expertise to help deliver workshops across Australia.

1. Source: <https://fightdementia.org.au>
2. Source: <https://accf.org.au>
3. Source: <http://corabarclay.com.au/our-services/hear-to-listen-program>
4. Source: <http://childrenfirstfoundation.org.au>
5. Source: <http://lgfb.org.au>
6. Source: <http://www.panda.org.au>

Perinatal Anxiety & Depression Australia

Perinatal Anxiety and Depression Australia (PANDA) is committed to a community where post and antenatal mood disorders are recognised and the impact on women and their families is minimised through acknowledgement, support and education.

- Up to 1 in 10 women & 1 in 20 men struggle with antenatal depression
- More than 1 in 7 new mums and up to 1 in 10 new dads experience postnatal depression each year in Australia
- Anxiety is thought to be just as common and many parents experience anxiety and depression at the same time.

Further information on the charity partners and the services they provide is available from:

- Dementia Australia <https://dementia.org.au>
- Children First Foundation <http://childrenfirstfoundation.org.au>
- Hear to Listen <http://corabarclay.com.au/our-services/hear-to-listen-program>
- Look Good Feel Better Foundation <http://lgfb.org.au>
- Perinatal Anxiety and Depression Australia <http://www.panda.org.au>

Our charity partners are:



DIRECTORS' REPORT

FOR THE YEAR ENDED 31 AUGUST 2017

DIRECTORS

The Directors of the Company at any time during or since the end of the financial year are:



Peter R. Robinson

Mr Peter R. Robinson Chairman

B.Com, FAICD
Non-executive director.
Director since 5 May 2000.
Appointed Chairman 8 July 2003.

Mr Robinson has held both executive and non-executive directorships for over 30 years. Mr Robinson also during this time has had extensive general management and chief executive officer experience in the pharmaceutical industry.

Other current listed company directorships:

- Clover Corporation Limited (resigned 21 September 2017)
- TPI Enterprises Ltd

Former listed company directorships in the past three years:

- Washington H Soul Pattinson and Company Limited (appointed 1984, resigned 31 March 2015)
- New Hope Corporation Limited (appointed August 1997, resigned 31 March 2015)



Robert D. Millner

Mr Robert D. Millner Non-executive Director

FAICD
Director since 5 May 2000.
Appointed member of the Remuneration Committee on 2 October 2007.

Appointed member of the Nomination Committee on 15 August 2012.

Mr Millner has had extensive management and public company experience across a number of industries.



E. Carol Holley

Other current listed company directorships:

- Brickworks Limited
- BKI Investment Company Limited
- Milton Corporation Limited
- New Hope Corporation Limited
- TPG Telecom Ltd
- Washington H Soul Pattinson and Company Limited

Ms E. Carol Holley Independent Non-executive Director

B.A, FCA, FAICD
Director since 19 December 2006.

Ceased being a Director on 25 January 2017.

Appointed Chair of the Audit and Risk Committee on 19 December 2006.

Ms Holley is a non-executive Director of the Australian Science and Technology Organisation and a member of the Audit and Risk Committee.

Ms Holley is also Chair of the Audit and Risk Committees of the NSW Department of Finance Services and Innovation, the NSW Property and Advisory Group, Service NSW, The Parliament of NSW and National Health Funding Body and a member of the committees of the NSW Mental Health Commission.

Mr Richard C. Vincent Executive Director

B.Bus, (Accountancy), CPA

Appointed Managing Director and Chief Executive Officer on 15 February 2017.

Mr Vincent started his professional career in finance with Bridgestone before moving to Britax Rainsfords where he was CFO. He joined FH Faulding & Co Limited in

1998 and remained with that company until 2005, during which time he held a number of senior leadership roles, including responsibility for the pharmacy distribution, retail merchandise and generic pharmaceutical development.

Mr Vincent joined API in 2005 where he has held a number of General Management roles that have included pharmacy business development, strategy, supply chain, franchise recruitment, IT, manufacturing and M&A.

Mr Vincent is the Deputy Chairman of the National Pharmaceutical Services Association and was also a Director of CH2 from 2006 to 2015.

Mr Stephen P. Roche Executive Director

B.Bus, FAICD
Managing Director and Chief Executive Officer since 14 August 2006.

Ceased being a Director on 15 February 2017.

Mr Roche joined API in March 2005. Previously he was Group General Manager, Health Services for Mayne Group Limited with responsibility for pharmacy distribution, pathology and other business units. Previous roles included Chief Operating Officer, Healthcare Services for FH Faulding & Co and a number of management roles at CSR.

In October 2016, Mr Roche was appointed a Director of The Myer Family Investments Pty Ltd.

Mr Roche is also Chairman of Priceline Sisterhood Foundation Limited.



Stephen P. Roche

DIRECTORS' REPORT

CONTINUED



Lee Ausburn

Ms Lee Ausburn Independent Non-executive Director

M.Pharm, B.Pharm,
Dip.Hosp.Pharm, FAICD
Director since 7 October 2008.

Appointed member of the Audit and Risk Committee on 7 October 2008.

Appointed member of the Nomination Committee on 15 August 2012 and appointed Chair on 8 April 2015.

Ms Ausburn is a pharmacist with experience in retail and hospital pharmacy and in academia. She had a long career in the pharmaceutical industry with Merck Sharp and Dohme (Australia) Pty Ltd and was previously Vice President, Asia, for Merck and Co Inc with responsibility for the company's operations across Asia.

Ms Ausburn is also President, Pharmacy Faculty Foundation, University of Sydney.

Other current listed company directorships:

- NIB Holdings Limited
- Somnomed Limited

Mr Gerard J. Masters Independent Non-executive Director

Director since 7 September 2010.

Appointed member of the Nomination Committee on 15 August 2012.

Appointed member and Chair of the Remuneration Committee on 30 January 2014.

Member (interim) of the Audit and Risk Committee from 1 March 2017 to 6 September 2017.

Mr Masters has had extensive experience in retailing. Until his resignation in early 2006, he spent more than 33 years with the Coles Myer Group. This included a 10 year period as Managing Director of Bi Lo, Coles and then the total Supermarkets Group which was Coles Myer's largest and most profitable business. His most recent role, until his resignation in 2009, was as the Managing Director and CEO of The Reject Shop Limited.

Mr Kenneth W. Gunderson-Briggs Senior Independent Non-executive Director

B.Bus, FCA, MAICD
Director since 6 May 2014.

Appointed member of the Audit and Risk Committee on 6 May 2014 and appointed Chair on 25 January 2017.

Appointed member of the Remuneration Committee on 8 April 2015.

Appointed Senior Independent Director on 2 September 2015.

Mr Gunderson-Briggs is a chartered accountant, registered company auditor and public company Director, with broad experience in finance and the retail franchise sectors.

Mr Gunderson-Briggs has been Chairman of Glenaeon Rudolf Steiner School Limited since 2013, having been a Director on the Board since 2009.

Other current listed company directorships:

- Harvey Norman Holdings Limited

Mr Mark Smith Independent Non-executive Director

Dip Business (Marketing),
FAICD,
FAIM, FAMI, CPM
Director since 6 September 2017.

Appointed member of the Audit and Risk Committee on 6 September 2017.

Mr Smith was previously the Chair of Patties Foods Limited for three years and a Non-executive Director of Toll Holdings Limited for eight years.

Mr Smith has extensive senior management experience in the fast moving consumer goods industry globally and was Managing Director of Cadbury Confectionery ANZ from 2001, Managing Director of Cadbury Schweppes Australia and New Zealand from 2003 to 2007, and a member of the Cadbury Schweppes Asia Pacific Regional Board.

He also has a strong commitment to not-for-profit organisations as Chair of Enactus Australia and Chair of the Humour Foundation Ltd.

Other current listed company directorships:

- GUD Holdings Limited



Gerard J. Masters



Kenneth W. Gunderson-Briggs



Mark Smith

DIRECTORS' REPORT

CONTINUED

COMPANY SECRETARY

Mr Peter Sanguinetti has been Company Secretary and General Counsel since November 2007. Mr Sanguinetti BJuris, LLB, GAICD has extensive experience and was previously Company Secretary and General Counsel of Kodak (Australasia) Pty Ltd for 9 years, responsible for legal and company secretarial activities for the Kodak group across Asia. Mr Sanguinetti was also a Non-executive Director of HPAL Limited (formerly listed on the ASX) from January 2005 to November 2007.

On 15 February 2017, Ms Kylie Barrie, Senior Legal Counsel, was appointed as Alternate Company Secretary. Ms Barrie, LLB (Hons) is a qualified lawyer and supports the Company Secretary. On 25 May 2017, Ms Genevieve Ryan resigned as Alternate Company Secretary.

DIRECTORS' MEETINGS

The number of Directors' meetings (including meetings of committees of Directors) and number of meetings attended by each of the Directors of the Company during the year were:

Director**	Board		Audit and Risk		Remuneration		Nomination	
	Number attended	Number Held*	Number attended	Number held*	Number attended	Number held*	Number attended	Number held*
Mr P R Robinson***	17	17	–	–	–	–	–	–
Mr R D Millner	15	17	–	–	1	1	1	1
Ms E C Holley (ceased being a Director on 25 January 2017)	5	5	1	1	–	–	–	–
Mr S P Roche*** (ceased being a Director on 15 February 2017)	5	5	–	–	–	–	–	–
Ms L Ausburn	16	17	4	4	–	–	1	1
Mr G J Masters	16	17	3	3	1	1	1	1
Mr K W Gunderson-Briggs	17	17	4	4	1	1	–	–
Mr R C Vincent*** (appointed as a Director on 15 February 2017)	12	12	–	–	–	–	–	–

* Number of meetings held during the time the Director held office or was a member of the committee during the year. (Excludes Mark Smith appointed 6 September 2017).

** All Directors who are not members of Committees are invited to attend Committee Meetings.

*** The Chairman and the Managing Director and CEO attended all Committee meetings by invitation.

OPERATING AND FINANCIAL REVIEW

As required by Section 299A(1) of the Corporations Act, and in accordance with ASIC Regulatory Guide 247 Effective Disclosure in an Operating and Financial Review (RG247) issued in March 2013, the Board is required to include in the Directors' Report an Operating and Financial Review (OFR) which includes information that shareholders would reasonably require to make an informed assessment of the consolidated entity's operations, financial position and business strategies, and prospects for future years. The OFR complements and supports the financial report.

DIRECTORS' REPORT

CONTINUED

Principal Activities

The principal activities of the consolidated entity were the wholesale distribution of pharmaceutical goods to pharmacies, and retail of health and beauty products to consumers through a network of Priceline Pharmacy franchise and Priceline company owned stores in Australia. The consolidated entity also manufactures and distributes pharmaceutical goods in New Zealand. There have been no significant changes in the nature of the principal activities during the year.

Financial Performance

- Underlying net profit after tax up 5.4% to \$54.2 million
- Reported net profit after tax up 1.4% to \$52.4 million
- Earnings before interest and tax up 2.5% to \$89.3 million
- Revenue up 5.8% to \$4.1 billion
- Overall cost of doing business reduced by 20 basis points
- Final declared dividend of 3.5 cents per share fully franked.

The consolidated entity reported an underlying net profit after tax of \$54.2 million, following an improved contribution from Pharmacy Distribution and Supply Chain optimisation combined with general cost management. The challenging retail conditions are reflected in the Retail Operations contribution, which was at a similar level to the previous year.

Priceline and Priceline Pharmacy recorded register sales (excluding the dispensary) growth of 2.0% to \$1.15 billion. With the challenging retail sales environment experienced in the second half of the year this result was in line with expectations, and reflects our strong customer offering. It should be noted that 'register' sales made by franchisees do not form part of the financial results of the consolidated entity.

Due to the strong brand proposition, demand for new stores from potential pharmacist franchise partners continues to be strong with new store openings contributing to the register sales result. The Priceline Pharmacy network numbers were 462, up from 442 at 31 August 2016. Engagement with customers across all forums, including online, social media and in store, is a key driver of loyalty for the brand, with the Sister Club loyalty program now having 7.1 million members. This loyalty program remains the leader in health and beauty membership programs in Australia.

Pharmacy Distribution performed to expectations with overall reported sales growth of 7.3% to \$2.96 billion. Excluding HepC, overall reported sales growth was 2.5%. To this, adding back Pharmaceutical Benefits Scheme (PBS) reforms, the underlying sales growth would have been 7.5%. The business grew independent accounts as well as particularly a number of large pharmacy groups, demonstrating that pharmacists are choosing to deal with API due to the choice of programs that are tailored to the individual needs of their businesses.

The New Zealand manufacturing segment recorded a profit of \$0.7 million. A strategic review has recently been undertaken to increase our focus on profitable market segments, resulting in new contracts and the stocking of products in a major supermarket chain. The business continues to grow its Healthcare product range which are provided to the Australian and New Zealand pharmacy markets, and its contract manufacturing business.

Capital expenditure for the year was \$26.5 million reflecting a range of projects to optimise inventory, improve the Sister Club offering, and further enhance profit.

The Company's cash from operating activities improved 15.2% to \$95.5 million as a result of sales growth and a reduction in finance costs which is reflective of improved cash and debt management.

Financial Position

The Company reported a net cash position of \$7.2 million, an improvement of \$33.1 million on the prior year. The Company is currently operating well within the Group's facility limits and associated banking covenants.

In line with the strong operational performance the Company has declared a fully franked final dividend of 3.5 cents per share, bringing the full year dividend to 7.0 cents per share fully franked, an increase of 17% on the prior year dividend of 6.0 cents.

DIRECTORS' REPORT

CONTINUED

Business strategies and prospects for future financial years

During the year the Board undertook a review of short and long term strategies. This review was performed to ensure that the strategies remained relevant and adaptable to the dynamic regulatory and economic environment in which the Company operates, and which may affect the future financial performance and position of the Company.

The strategic issues that the Company must address in order to achieve its vision are, by their very nature, long term issues and continue to evolve through changes in competitive pressures and technology advancements.

The strategic review analysed a range of internal and external environmental elements which will deliver a better customer experience and improve the experience of doing business with API to ensure longer term profitability. These objectives are supported by the Company's strategic goals and supporting initiatives across all business units and functions. The overall business strategies relevant to the Company's future financial position and performance include:

- Leveraging our health and beauty competitive advantage to optimise business and network growth
- A compelling business model for partners
- An agile API driving superior value
- Market insights driving innovation and the customer experience
- An enriched sustainable community
- Famous for energised, talented and committed people
- A safer place to work every day

These strategic goals and supporting initiatives are ultimately focused on the Company achieving its vision of *'Enriching life, as the most inspirational choice for health, beauty and wellbeing'*.

By applying the strategic goals to the Company's business plans, there will be a continued emphasis on capitalising on the strengths of the Company in the health and beauty retail market and to optimise its strong national community pharmacy wholesale distribution business. This means the Company intends to:

- Consistently deliver a differentiated and personalised experience for our customers, and continue to promote the Priceline Pharmacy Franchise proposition to grow the store network

- Priceline Pharmacy to continue to be a compelling proposition for pharmacists who wish to offset the impact of PBS reform, leverage pharmacy expertise, and drive further growth from integrated dispensary and retail programs
- Build loyalty and increase engagement of the Priceline Sister Club loyalty program, and promote increased customer engagement through all channels including the Priceline website and social media
- Optimise the size and value of the store network for all brands
- Deliver superior value and service to independent pharmacy customers
- Provide consistent, valued, and measurable service improvement to all customers and suppliers
- Optimise the value of our business portfolio through investment, divestment, and acquisition
- Be at the forefront of Health, Beauty and Wellbeing industry trends, insights and innovation, and use customer insight to drive connectivity of Beauty, Health, and the Dispensary
- Enrich the community by active support of our Sisterhood Foundation
- Enhance the employee value proposition, and to create an environment to generate, prioritise and execute innovation; and
- Increase lead indicator safety performance.

The Company expects to improve earnings performance through the implementation of its core strategies and supporting initiatives. This outlook is subject to there being no material change in consumer or customer demand, a stable economic climate and no unforeseen adjustments to either the regulatory environment or the PBS.

Specific details about the Company's business strategies and prospects that could give rise to likely material detriment to the Company, for example, information that is commercially sensitive, confidential or could give a third party a commercial advantage has not been included in this Annual Report. Other than the information set out in this document, information about other likely developments in the operations of the Company in future financial years has not been included.

DIRECTORS' REPORT

CONTINUED

Material Business Risks

The Company continues to be influenced by a number of general economic and business conditions including levels of consumer spending, interest and exchange rates and Government regulatory policies. The Company has a distinctive positioning in the Community Pharmacy wholesaling sector in Australia as well as being well positioned in the mass market Health and Beauty retail sector.

Despite the strengths in these sectors the Company faces challenges including:

- Ongoing Government reforms to the PBS in the Pharmacy sector; and
- Macro-economic factors contributing to less stable retail sales and increasing cost pressures in key areas such as labour.

As part of the risk management process, the risk profile of the Company is reviewed by management with the assistance of the Audit, Risk and Compliance team at least annually. The results of this review are provided to the Audit and Risk Committee for its consideration and recommendation to the Board.

The risk management process of the Company is integrated with the strategic planning process and involves identifying the risk universe and documenting those factors that contribute to the inherent risk environment. Inherent risk is determined by combining likelihood and consequences assessments determined in the absence of any controls within the business.

The effectiveness of current controls in place to manage the identified risks is then assessed to determine residual risk. Where residual risk is deemed to be greater than the business risk appetite, risk treatment plans are developed and specific personnel assigned responsibility for the management of those risks. The status of risk treatment plans is monitored and reported to the Audit and Risk Committee at regular intervals.

The most recent update in respect of risk profile and risk management plans was in June 2017 against a backdrop of continued PBS reforms, challenging retail trading conditions and the ongoing exploitation of the platforms of the Company.

The following is a summary of the contemporary risks facing the Company as assessed by the recent risk profile update of the Company:

- *Structural reforms within the Australian Community Pharmacy sector*
This relates to the risk of continued Government PBS reforms. The Company monitors the changes to PBS medicines and responds with a combination of reduced discounts to Pharmacy customers and operational adjustments. The Company also closely monitors costs associated with the Community Service Obligation (CSO).
- *Execution of Retail Pharmacy strategy with associated growth of Priceline Pharmacy stores.*
There is a risk that the expansion of the Priceline Pharmacy franchise network is unsuccessful or the expected growth in the next five years is slower than expected. Existing key business processes and responses to mitigate this risk include the continuation of dedicated Retail Pharmacy Business Development teams, and the inclusion of landlords, banks and industry accountants in pharmacist familiarisation and recruitment forums. Tracking measures to monitor growth rates are reported to the Managing Director and the Board on a monthly basis.
- *One Enterprise Restructure and Information systems upgrade.*
In 2011 the Company undertook a restructure of its Australian business and has transitioned from a multiple Business Unit structure to the One Enterprise functional structure. This transition included an upgrade of the Company's enterprise management information platforms of the enterprise in the latter part of the 2015 financial year.
The Company aims and continues to further optimise the platforms and realise greater potential. In this regard the Company monitors the allocation of resources to these projects through the tracking of performance against the initial business case including the realisation of benefits.
- *Financial Risk*
The activities of the Company expose it to a number of financial risks including customer payment defaults, financial guarantees supporting Pharmacy customers, and general retail trading conditions. The Company adopts a financial risk management program which seeks to minimise potential adverse impacts on the financial performance of the Company. The Company has undrawn funding lines throughout the year to manage any unforeseen financial risks.

DIRECTORS' REPORT

CONTINUED

OVERVIEW OF REMUNERATION FOR FY17

A summary of the matters impacting the Group's remuneration structure and strategy for FY17 are:

- Richard Vincent commenced as Managing Director (MD) & Chief Executive Officer (CEO) on 15 February 2017 after Stephen Roche ceased being the Managing Director and CEO on that date.
- No changes to the Short Term Incentive Plan (STIP) or the Long Term Incentive Plan (LTIP) have been made during the financial year other than those described in the Remuneration Report for the previous period.
- The financial performance of the consolidated entity for FY17 did not meet the minimum requirement for any STIP payments. Accordingly, no member of the KMP will receive an STI award in respect of FY17.
- The three year performance period for the 2014 LTIP ended on 31 August 2017. Vesting was subject to an aggregate Return on Equity (ROE) hurdle and an Earnings Per Share (EPS) Compound Annual Growth Rate (CAGR). The performance conditions were tested and audited with the following outcomes:
 - actual aggregate ROE for the performance period was 28.26% for an achievement of 61.22% of half the grant; and
 - actual CAGR EPS was 36.96% for an achievement of 100% of the other half of the grant.
- The combined achievement of the 2014 LTIP for performance measured over a 3 year period resulted in 80.6% of the total grant vesting.

The table on the following page shows the key elements of total reward received by each KMP for FY17. This includes the cash component elements paid to each executive for the year as well as the value of equity that has vested for services provided to 31 August 2017, and equity from previous years that vested in FY17 which was originally reported in accordance with the accounting standards in the year the equity was granted.

Executive	Fixed Remuneration \$	STI applicable to FY17			Final benefits*** \$	Total Remuneration Received \$
		Cash STI \$	Deferred STI \$	LTI vested** \$		
Mr R Vincent – Managing Director and CEO (Appointed 15 February 2017*)	891,605	–	–	198,984	–	1,090,589
Mr S Roche – Managing Director and CEO (Ceased being a Director on 15 February 2017)	485,570	–	–	664,728	986,988	2,137,286
Mr P Mendo – Chief Financial Officer	458,701	–	–	–	–	458,701

* Mr Vincent was appointed Managing Director and CEO on 15 February 2017 after Mr Roche ceased being the Managing Director and CEO on that date. His remuneration for the year is inclusive of his previous role and his current role held during the year.

** Consists of the total fair value of the Performance Rights vested during FY17. These relate to the 2014 grant which vested over a three year period. The expense was recognised over a three year period in accordance with AASB 2 Share Based Payments.

*** Excludes accrued leave entitlements.

A full breakdown of executive remuneration details has been prepared in accordance with statutory requirements and accounting standards. This detailed disclosure including statutory tables is included in Section 2 of the Remuneration Report.

DIRECTORS' REPORT

CONTINUED

REMUNERATION REPORT – AUDITED

This report details the processes used in remuneration decisions and their outcomes for Key Management Personnel (KMP) for the 2017 financial year (FY17) and is prepared in accordance with Section 300A of the Corporations Act 2001 (as amended) for the Company and its subsidiaries.

Key Management Personnel

As defined under AASB 124, KMP have the authority and responsibility for planning, directing and controlling the activities of the consolidated entity, and comprise:

1. Non-executive Directors;
2. Managing Director and Chief Executive Officer; and
3. Chief Financial Officer.

Non-executive Director KMP

Peter Robinson	Chairman
Lee Ausburn	Director
Gerard Masters	Director
Robert Millner	Director
Carol Holley	Director (ceased being a Director on 25 January 2017)
Kenneth Gunderson-Briggs	Director
Mark Smith	Director (appointed as a Director on 6 September 2017)

Executive KMP

Richard Vincent	Managing Director and Chief Executive Officer (appointed 15 February 2017)
Stephen Roche	Managing Director and Chief Executive Officer (ceased being a Director and CEO on 15 February 2017)
Peter Mendo	Chief Financial Officer

This report has been audited by the Company's Auditor, KPMG as required by Section 308(3C) of the Corporations Act 2001.

The Remuneration Committee is governed by its Charter (available on www.api.net.au) which was developed in line with ASX Corporate Governance Principles and Recommendations. The Charter specifies the purpose, authority, membership and activities of the Remuneration Committee, and the Charter is annually reviewed by the Committee to ensure it remains consistent with regulatory requirements.

Membership of the Committee consists of Non-executive Directors. During the year members of the Committee were Mr Gerard Masters (Chairman), Mr Robert Millner and Mr Kenneth Gunderson-Briggs.

The Remuneration Report is in sections as follows:

Section 1 Non-Executive Director KMP Remuneration

A Policy and Principles

B Remuneration of Directors (excluding the Managing Director and CEO)

DIRECTORS' REPORT

CONTINUED

Section 2 Executive Remuneration including the Managing Director and CEO

- A Policy and Principles
- B Remuneration Structure
- C Short Term Incentive Plan
- D Long Term Incentive Plan
- E Employment Contracts
- F Remuneration of Executives including the Managing Director and CEO

Section 3 Other matters required by Section 300A Corporations Act 2001

- A Comments on Remuneration Report at the most recent AGM of the Company
- B Engagement of Remuneration Consultant

SECTION 1 NON-EXECUTIVE DIRECTOR KMP REMUNERATION

A. Policy and Principles

Non-executive Directors' fees are determined within an aggregate fee pool limit. An annual total fee pool of \$1,200,000 was approved by shareholders at the 25 January 2017 Annual General Meeting. Total Non-executive Directors remuneration including Board Committee fees, non-monetary benefits and superannuation paid at the statutory rate for the year ended 31 August 2017 was \$666,390. This is a 3.6% decrease on the prior year. The remuneration of Non-executive Directors is determined having regard to the data provided by independent remuneration consultants, the need to attract and retain appropriately qualified Directors, fee levels applied in similarly sized companies, and board judgement as to whether any adjustments are appropriate. Non-executive Directors do not receive performance related remuneration.

Under the Board's Retirement Scheme, which was approved by Shareholders at the 1994 AGM, retiring Non-executive Directors are paid on a pro-rata basis up to ten (10) years' service to a maximum of three (3) times the average annual remuneration in the three (3) years preceding retirement. The retirement benefit is capped at \$220,000 per Director and applies only to Directors appointed prior to 9 September 2003. The Directors have agreed to freeze this benefit as at 31 August 2009.

Annual Board fees (including superannuation) were structured as follows with effect from 1 January 2017:

Role	Annual Fee Structure
Board chairman	\$210,000
Board member	\$90,000
Audit and Risk Committee chair	\$35,000
Audit and Risk Committee member	\$8,000
Remuneration Committee chair	\$16,000
Remuneration Committee member	\$8,000
Nomination Committee chair	(no fee)
Nomination Committee member	(no fee)
Senior Independent Director	\$15,000

The Board Chairman does not receive Committee fees.

DIRECTORS' REPORT

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B. Remuneration of Directors (Excluding the Managing Director and CEO)

Directors*	Short Term										Proportion of remuneration performance related	Value of rights as proportion of remuneration (%)
	Salary and Fees	Cash -Short-term incentives	Non-monetary benefits	Total	Post-employment superannuation contributions	Other long term	Final benefits	Equity Value of rights granted under STIP	Equity Value of rights granted under LTIP	Total		
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	%	%
Non-executive												
Mr P R Robinson												
31 August 2017	181,279	-	-	181,279	17,222	-	-	-	-	198,501	-	-
31 August 2016	158,718	-	23,012	181,730	15,078	-	-	-	-	196,808	-	-
Mr R D Millner												
31 August 2017	86,692	-	-	86,692	8,236	-	-	-	-	94,928	-	-
31 August 2016	80,294	-	-	80,294	7,628	-	-	-	-	87,922	-	-
Ms E C Holley (ceased being a Director on 25 January 2017)												
31 August 2017	43,924	-	-	43,924	4,173	-	-	-	-	48,097	-	-
31 August 2016	107,368	-	-	107,368	10,200	-	-	-	-	117,568	-	-
Ms L Ausburn												
31 August 2017	86,692	-	-	86,692	8,236	-	-	-	-	94,928	-	-
31 August 2016	80,294	-	-	80,294	7,628	-	-	-	-	87,922	-	-
Mr G Masters												
31 August 2017	93,605	-	-	93,605	8,893	-	-	-	-	102,498	-	-
31 August 2016	86,361	-	-	86,361	8,204	-	-	-	-	94,565	-	-
Mr K Gunderson-Briggs												
31 August 2017	116,382	-	-	116,382	11,056	-	-	-	-	127,438	-	-
31 August 2016	97,526	-	-	97,526	9,265	-	-	-	-	106,791	-	-

* Excludes Mark Smith appointed as a Director on 6 September 2017.

DIRECTORS' REPORT

CONTINUED

SECTION 2 EXECUTIVE REMUNERATION INCLUDING THE MANAGING DIRECTOR AND CEO

A. Policy and Principles

The remuneration strategy of API is to:

- Offer a remuneration structure that will attract, focus, retain and reward highly capable people;
- Ensure that remuneration decisions are based on a fair and transparent job evaluation process that is linked to comparable market data and the experience of the individual in the position;
- Have a clear and transparent link between performance and remuneration outcomes;
- Encourage and integrate risk management within the reward framework; and
- Build employee engagement and align management and shareholder interests through the ownership of Company shares.

Executive remuneration is set with regard to the size and nature of the position with reference to market median benchmarks and the performance of the individual.

The total remuneration of an Executive will incorporate variable "at risk" elements to:

- Link Executive reward with the achievement of the business objectives and financial performance of the consolidated entity; and
- Ensure total remuneration is competitive by market standards.

The role of the Remuneration Committee includes reviewing and making recommendations to the Board on Executive remuneration. The Remuneration Committee may seek independent advice on the appropriateness of remuneration levels. The Remuneration Committee is authorised to seek advice if and when required.

B. Remuneration Structure

The Executive Remuneration Framework as it applies to the Managing Director and CEO, and Executives comprises:

- Fixed Remuneration; and
- Performance linked remuneration in the form of STIP and LTIP opportunities.

Fixed Remuneration

Fixed remuneration is a guaranteed salary level inclusive of any Fringe Benefits Tax (FBT), charges related to employee benefits including motor vehicles and employer contributions to superannuation funds. It does not include long service leave entitlements.

Fixed remuneration levels are reviewed annually and set with regard for each position and the median market level for comparable roles. Any adjustment needs to also consider individual segment results and overall performance of the consolidated entity. In addition, external consultants provide analysis and advice to ensure that Executive remuneration is appropriate in the context of market practice and stakeholder expectations.

Performance Linked Remuneration

Performance linked remuneration includes both short term and long term incentives and is designed to reward KMP for meeting or exceeding their financial and non-financial objectives. The short term incentive is provided in the form of a cash payment and deferred rights to acquire shares while the long term incentive is provided as rights to acquire shares. Rights to acquire shares are termed as "Performance Rights".

The consolidated entity has a policy prohibiting recipients of share-based payments from entering into arrangements to hedge their exposure to losses arising from share price decreases. Entering into such arrangements has been prohibited by law since 1 July 2011.

C. Short Term Incentive Plan

The STIP is an annual at risk incentive plan for Executives and certain other senior employees.

The objectives of the STIP are:

- Provide a clear link between individual and organisational performance and executive reward;
- Reinforce the link between individual, team and Company performance;
- Reinforce the interdependencies between business units and functions;
- Align the interests of Executives who are most able to positively impact profitability; and
- Drive a high performance leadership culture.

Prior to the start of the financial year the Remuneration Committee makes a recommendation to the Board for approval of the maximum STIP pool. The size of the pool varies from year to year and is a percentage of target EBIT for the year.

Prior to any payment under the STIP, Company performance must pass a minimum gateway requirement of Group Net Profit After Tax (NPAT).

DIRECTORS' REPORT

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At the start of each year the Remuneration Committee sets a 'scorecard' of performance conditions for the STIP as follows:

- NPAT; and
- Other financial and non-financial measures tailored for each business segment.

Other performance measures vary by business segment, however each scorecard includes a measure related to Earnings Before Interest and Tax (EBIT), Return on Capital Employed (ROCE) and individual performance measures. Multiple measures of performance help diversify risk.

Each year, the Board establishes NPAT performance hurdles at which threshold, target and maximum STIP entitlements will be payable. The current practice is that the minimum STIP pool is established at 90% of NPAT budget (being the NPAT gateway), the target STIP pool is at budget and the maximum STIP pool is achieved at 110% of budget.

After the conclusion of the financial year, the Board assesses performance against Group and Segment Scorecards with 80% of the maximum percentage based on key financial objectives and 20% based on individual objectives. Prior to any consideration of a STIP payment, the Company must meet a minimum NPAT performance. The Board has discretion for a STIP payment where achievement is 90% of target NPAT levels.

Fifty percent of any STIP awarded to the Executive Leadership Team is deferred for 12 months in the form of performance rights. Performance rights are exercised for fully paid shares after the 12 months deferral period. In addition, participants will be eligible to receive at the time of vesting a cash payment equal to the dividends paid during the 12 month vesting period on shares resulting from the exercise of rights at vesting.

The number of performance rights is determined by dividing the value of the deferred component of the STIP award by the volume weighted average closing price of API shares on the ASX in the 10-day period after announcement of full year results of the initial grant year.

The deferred component of the STIP award is designed to manage risk by ensuring that decisions taken in the previous 12 months have resulted in sustainable Company benefit. The Board has the discretion to forfeit any unvested rights due to excessive risk taking, material misstatement of financial statements or fraudulent or gross misconduct.

More broadly, the Board retains absolute discretion over all awards made under the incentive award plans, including the STIP.

Managing Director and Chief Executive Officer

The Managing Director and CEO's STIP is equal to 32.5% of his fixed remuneration at threshold, 65% of fixed remuneration at target, and if NPAT is 110% or more of budget, the STIP provides for a maximum payment of 100% of fixed remuneration.

The STIP scorecard is determined by the Board each year and is drawn from financial measures such as NPAT, Return on equity (ROE) and Return on Capital Employed (ROCE). Non-financial measures may include retail sales growth, Priceline Pharmacy network growth, pharmacy distribution market share and improvement targets relating to workplace safety.

The FY17 STIP scorecard and performance measures were set by the Board at the beginning of the year for the former Managing Director and CEO who ceased being the Managing Director and CEO on 15 February 2017.

The performance measures and weightings for FY17 were as set out below.

Performance measure	Weighting
NPAT and ROCE	60%
Operational performance	25%
Safety performance (LTIFR)	10%
Strategic projects	5%

The NPAT result for FY17 did not exceed the NPAT gateway and accordingly the Board did not approve a STIP award for the Managing Director and CEO.

DIRECTORS' REPORT

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C. Short Term Incentive Plan (continued)

Other Executive KMP

The STIP award at threshold for other Executive KMP STIP is equal to 10% of fixed remuneration, 20% of fixed remuneration at target and if NPAT is 110% or more of budget, the STIP provides for a maximum payment of 40% of fixed remuneration. The Remuneration Committee recommends to the Board, the financial measures for Executive KMP STIP which includes NPAT and ROCE.

The following table summarises the basis of the calculation of the STIP award for Executive KMP.

	NPAT gateway	Financial Measure 1 40% weighting	Financial Measure 2 40% weighting	Personal Measure 20% weighting
Target	90 % of NPAT Target	NPAT Target	Company ROCE Target	Individual Targets

The NPAT result for FY17 did not exceed the NPAT gateway and accordingly the Board did not approve a STIP award for other Executive KMP.

EXECUTIVES	Maximum STIP as a % of Fixed Remuneration	STIP Award as a % of Fixed Remuneration	STIP Cash Entitlement	STIP Deferred Equity**
	%	%	\$	\$
Mr R Vincent – Managing Director and CEO (Appointed 15 February 2017*)				
31 August 2017	100%	–	–	–
31 August 2016	40%	27.7%	83,732	83,732
Mr S Roche – Managing Director and CEO (Ceased being a Director on 15 February 2017)				
31 August 2017	100%	–	–	–
31 August 2016	100%	78.4%	397,791	397,791
Mr P Mendo – Chief Financial Officer				
31 August 2017	40%	–	–	–
31 August 2016	40%	27.7%	63,664	63,664

* Mr Vincent's STIP scorecard relevant to his position of Managing Director and CEO has been pro-rated for time in that position from 15 February 2017.

** The STIP Deferred Equity is recognised in remuneration for FY17 in accordance with AASB 2 Share Based Payments.

DIRECTORS' REPORT

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D. Long Term Incentive Plan

The Remuneration Committee has responsibility for the Long Term Incentive Plan (LTIP). The Plan was established during the year ended 30 April 2006. The Remuneration Committee is responsible for awards granted under the Plan and overseeing administration of the Plan. The LTIP involves the grant of rights to acquire fully paid ordinary shares in API for no consideration.

The key features and implications of the LTIP are:

- Performance rights ("Rights") are granted to the Managing Director and CEO (which are subject to shareholder approval at the Annual General Meeting) and to certain Executives as soon as practicable after the full year results are announced. This ensures the allocation of Rights reflects the best informed assessment by the market of Company value and share price.
- The number of Rights granted is derived by dividing the participant's LTIP value by the 10-day Volume Weighted Average Closing Price (VWAP) of API shares immediately after announcement of full year results – that is, the 'face value' methodology.
- Vested rights convert to API shares on a one-for-one basis. No dividends are received by Executives on unvested rights during the vesting period.
- If performance conditions are not met, the Rights lapse.
- The LTIP provides for shares to be purchased on market on behalf of the participant or new shares issued by the Company.
- Performance conditions will be tested only once and any Performance Rights that do not meet the performance conditions will lapse and will not be re-tested.
- The Company has a policy prohibiting Directors and employees from dealing in financial products issued or created over or in respect of securities (e.g. hedges or derivatives) that have the effect of reducing or eliminating the risk associated with any equity incentives that may be offered from time to time.
- If an LTIP participant ceases to be employed before the end of the Performance Period for reasons other than redundancy, death, disability or illness, the Performance Rights will automatically lapse, subject to Board discretion. If a participant ceases to be employed, before the end of the Performance Period and the date of employment ceasing is on or after the first anniversary date of the Commencement Date, due to redundancy, death, disability or illness, the number of Performance Rights will be reduced pro-rata to reflect the length of time during the Performance Period the employee was employed.
- More broadly, the Board retains absolute discretion over all awards made under the incentive award plans, including the LTIP.
- Grants made include a target measure of three year EPS CAGR and the cumulative ROE achieved by the consolidated entity during the three year period commencing at the beginning of the performance period when compared to the target ROE set by the Board for the same period (Target ROE) measure. Each of the two measures (EPS and ROE) contribute equally to a LTIP award. If ROE is achieved and EPS is not achieved, or vice versa, then the total available award is halved. This means 50% of the award is dependent on the ROE metric, and 50% of the award is dependent on the EPS metric. ROE is expressed as a percentage created by dividing NPAT for the relevant financial period by total shareholder equity for the relevant financial year. Target ROE is derived from the Corporate Plan for the three years commencing at the beginning of the performance period. EPS is derived from the Corporate Plan for the three years commencing at the beginning of the performance period. The EPS performance condition compares the actual EPS growth achieved during a three year performance period, against the target amount of EPS growth set by the Board. The EPS is the basic earnings per share disclosed in the Consolidated income statement of the Financial Statements. The initial benchmark EPS that serves as the basis for calculating EPS growth, and the target EPS may be varied by the Board in its absolute discretion.
- In determining whether the LTIP awards will vest the Board will have regard for a range of factors to ensure alignment to long-term overall Company performance and is consistent with:
 - strategic business drivers; and
 - long term shareholder return.

Subject to commercial sensitivity, the Board intends to provide full details of performance against specified hurdles upon those conditions being tested and upon vesting of the relevant rights.

- The value of the 2017 LTIP awarded to Executive KMP is:
 - Managing Director and CEO: equal to 60% of Fixed Remuneration; and
 - Other Executives: 30% of Fixed Remuneration.

DIRECTORS' REPORT

CONTINUED

D. Long Term Incentive Plan (continued)

2014 grant

On 16 December 2014, performance rights (the "2014 Grant") were granted with a performance period commencing on 1 September 2014 and ending 31 August 2017. The performance conditions, being return on equity (ROE) and earnings per share (EPS) compound annual growth rate (CAGR) for the exercise of performance rights were assessed after the results for the period were finalised with the following outcomes:

- actual aggregate ROE for the performance period was 28.26% resulting in 61.22% of this tranche vesting; and
- actual EPS CAGR was 36.96% resulting in 100% of this tranche vesting.

The combined achievement of the 2014 LTIP is 80.6% of the opportunity.

2015 grant

On 13 January 2016, performance rights (the "2015 Grant") were granted with a performance period commencing on 1 September 2015 and ending 31 August 2018. The performance conditions, being ROE and EPS CAGR for the exercise of performance rights will be assessed after 31 August 2018 once the results are finalised.

The ROE performance condition has the effect that:

- if a cumulative ROE of 25.07% is achieved for the three year period, 20% of the Rights subject to the ROE Performance Condition will vest;
- if a cumulative ROE of 40.74% is achieved for the three year period, 100% of the Rights subject to the ROE Performance Condition will vest; and
- if the cumulative ROE is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

The EPS CAGR performance condition has the effect that:

- if CAGR of 7.5% is achieved for the three year, 20% of the Rights subject to the CAGR Performance Condition will vest;
- if a CAGR of 10.0% is achieved for the three year period, 100% of the Rights subject to the CAGR Performance Condition will vest; and
- if the CAGR is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

2016 grant

On 1 February 2017, performance rights (the "2016 Grant") were granted with a performance period commencing on 1 September 2016 and ending 31 August 2019. No LTIP performance rights were granted to Mr Roche. Shareholder approval for any LTIP performance rights to be offered to Mr Vincent in the role of Managing Director and CEO will be sought at the January 2018 Annual General Meeting.

The performance conditions, being ROE and EPS CAGR for the exercise of performance rights will be assessed after 31 August 2019 once the results are finalised.

The ROE performance condition has the effect that:

- if a cumulative ROE of 26.96% is achieved for the three year period, 20% of the Rights subject to the ROE Performance Condition will vest;
- if a cumulative ROE of 43.81% is achieved for the three year period, 100% of the Rights subject to the ROE Performance Condition will vest; and
- if the cumulative ROE is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

The EPS CAGR performance condition has the effect that:

- if CAGR of 7.5% is achieved for the three year period, 20% of the Rights subject to the CAGR Performance Condition will vest;
- if a CAGR of 10.0% is achieved for the three year period, 100% of the Rights subject to the CAGR Performance Condition will vest; and
- if the CAGR is between these two levels, the number of rights that vest will be calculated on a straight line proportional basis.

DIRECTORS' REPORT

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E. Employment Contracts

The Company has entered into Executive Service Agreements ("agreements") with Executive KMP. These agreements outline the components of remuneration to be paid. Remuneration levels are reviewed each year to take into account any change in the scope of the role performed, and any other changes required to meet the principles of the remuneration policy.

The employment conditions and remuneration of the KMP are formalised in the agreements.

Key terms of the Executive Service Agreement with the Chief Executive Officer

Mr Richard Vincent, the Managing Director and Chief Executive Officer, has an agreement dated 10 October 2016 with effect from 15 February 2017 which replaces the previous agreement dated 27 September 2006.

The material terms of the agreement between the Company and Mr Vincent are as follows:

Term	No fixed term. Ongoing until terminated by either party in accordance with the agreement.
Total Fixed Remuneration	\$1,040,000 per annum, inclusive of superannuation and reviewed annually.
Short term incentives plan (STIP)	Mr Vincent will participate in the STIP, in accordance with the details described in Section C above.
Long term incentives plan (LTIP)	Mr Vincent will be entitled to participate in the Company's LTIP. The terms of the LTIP are included in Section D above.
Termination	The agreement states the following in respect of cessation of his employment: <ul style="list-style-type: none"> – Mr Vincent may resign from the Company by giving three months written notice; – The Company may summarily terminate Mr Vincent's employment in specified circumstances with immediate effect and no termination benefits will apply other than accrued entitlements; and – The Company may terminate Mr Vincent's employment by the giving of twelve months written notice and may make a termination payment in lieu of notice of up to twelve months fixed remuneration.

Terms and notice periods of other KMP

No fixed terms are specified within the agreements of other KMP.

Peter Mendo may resign from the Company by giving six months written notice. The Company may terminate Mr Mendo's agreement without cause by providing six months written notice, or making a payment in lieu of the notice period. The agreement provides for a non-compete restriction of up to twelve months after cessation of employment.

The Company may summarily terminate the KMP's employment in specified circumstances with immediate effect and no termination benefits will apply other than accrued entitlements.

DIRECTORS' REPORT

CONTINUED

F. Remuneration of Executives including the Managing Director and CEO

Details of the nature and amount of each major element of remuneration of each of the Key Management Personnel of the consolidated entity (including the Chief Executive Officer) are as follows:

Executives	Short Term			Total	Post-employment Superannuation contributions	Long Service Leave	Final benefits	Equity Value of rights granted under STIP	Equity Value of rights granted under LTIP**	Total	Proportion of remuneration performance related	Value of rights as proportion of remuneration (%)
	Salary and Fees	Cash - Short-term incentives	Non-monetary benefits									
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	%	%
Mr R Vincent – Managing Director and CEO (Appointed 15 February 2017)***												
31 August 2017	871,917	–	–	871,917	19,688	114,808	–	41,866	227,028	1,275,307	21.1	21.1
31 August 2016	582,684	83,732	–	666,416	19,359	14,952	–	100,592	52,055	853,374	27.7	17.9
Mr S Roche – Managing Director and CEO (Ceased being a Director on 15 February 2017)												
31 August 2017	466,282	–	–	466,282	19,288	12,623	986,988**	198,896	316,655	2,000,732	25.8	25.8
31 August 2016	989,338	397,791	22,810	1,409,939	19,359	26,169	–	444,123	239,453	2,139,043	50.6	32.0
Mr P Mendo – Chief Financial Officer												
31 August 2017	439,013	–	–	439,013	19,688	4,775	–	31,832	87,749	583,057	20.5	20.5
31 August 2016	440,641	63,664	–	504,305	19,359	–	–	31,832	46,000	601,496	23.5	12.9

* The value of performance rights is calculated at grant date using the Black-Scholes Option Pricing model. The value is allocated to each reporting period evenly over the performance period. LTIP performance rights proposed to be offered to Mr R Vincent as Managing Director and CEO will be subject to shareholder approval at the January 2018 Annual General Meeting.

** Mr Roche's final benefits were in consideration of entitlements due under his Executive Service Agreement and calculated based on an average of the last three years' Total Employee Compensation (TEC). In addition, Mr Roche was paid accrued leave entitlements.

*** Mr Vincent's remuneration includes remuneration in his previous role as KMP, as well as his new role as the Managing Director and CEO which commenced on 15 February 2017.

DIRECTORS' REPORT

CONTINUED

Analysis of Performance Rights over Equity Instruments granted as Compensation

Details of the performance rights awarded as remuneration to each Executive KMP are below.

Executive Director	Performance Rights granted			Performance period commences	Performance period ends	Included in remuneration	As at the date of this report	
	Number	Fair Value – per share	Total Value				% vested	% forfeited*
Mr R Vincent – Managing Director and CEO (Appointed 15 February 2017)								
2014 LTIP	297,444	\$0.83	246,879	1 September 2014	31 August 2017	34,398	80.6%	19.4%
2015 LTIP	99,180	\$1.82	180,508	1 September 2015	31 August 2018	60,169	0%	0%
2016 LTIP – in previous role	44,877	\$1.68	75,393	1 September 2016	31 August 2019	25,131	0%	0%
2016 LTIP – as CEO	177,895	\$1.81	321,990	1 September 2016	31 August 2019	107,330	0%	0%
STIP Deferred Equity	64,182	\$1.83	117,452	1 September 2014	31 August 2016	–	100%	0%
STIP Deferred Equity	44,069	\$1.90	83,731	1 September 2015	31 August 2017	41,866	100%	0%
Mr S Roche – Managing Director and CEO (Ceased being a Director on 15 February 2017)								
2014 LTIP	993,644	\$0.83	824,725	1 September 2014	31 August 2017	114,912	80.6%	19.4%
2015 LTIP	332,543	\$1.82	605,228	1 September 2015	31 August 2018	201,743	0%	0%
STIP Deferred Equity	268,007	\$1.83	490,453	1 September 2014	31 August 2016	–	100%	0%
STIP Deferred Equity	209,364	\$1.90	397,792	1 September 2015	31 August 2017	198,896	100%	0%
Executive Officers								
Mr P Mendo								
2015 LTIP	75,410	\$1.82	137,246	1 September 2015	31 August 2018	45,749	0%	0%
2016 LTIP	75,000	\$1.68	126,000	1 September 2016	31 August 2019	42,000	0%	0%
STIP Deferred Equity	33,507	\$1.90	63,663	1 September 2015	31 August 2017	31,832	100%	0%

* The % forfeited in the year represents the reduction from the maximum number of performance rights available to vest due to the performance criteria not being achieved.

DIRECTORS' REPORT

CONTINUED

LTIP summary

- LTIP performance rights were granted on 16 December 2014 with a performance period commencing on 1 September 2014 and ending 31 August 2017 (the 2014 grant). The performance conditions for the exercise of performance rights will be assessed shortly on or after on 31 October 2017. The fair value of the performance rights is dependent upon the ROE and EPS performance conditions for the entire grant and is \$0.83 per share.
- LTIP performance rights were granted on 13 January 2016 with a performance period commencing on 1 September 2015 and ending 31 August 2018 (the 2015 grant). The performance conditions for the exercise of performance rights will be assessed shortly on or after on 31 October 2018. The fair value of the performance rights is dependent upon the ROE and EPS performance conditions for the entire grant and is \$1.82 per share.
- LTIP performance rights were granted on 1 February 2017 with a performance period commencing on 1 September 2016 and ending 31 August 2019 (the 2016 grant). The performance conditions for the exercise of performance rights will be assessed shortly on or after on 31 October 2019. The fair value of the performance rights is dependent upon the ROE and EPS performance conditions for the entire grant and is \$1.68 per share.

STIP summary

- Performance rights relating to the STIP program commencing on 1 September 2014 and ending 31 August 2016 were granted on 21 October 2015. The performance rights were valued at \$1.83 per share reflecting the volume weighted average closing price of API shares on the ASX in the 10-day period after announcement of full year 31 August 2015 results. These rights fully vested and were satisfied by the issue of fully paid ordinary shares in the Company on 9 November 2016.
- Performance rights relating to the STIP program commencing on 1 September 2015 and ending 31 August 2017 were granted on 7 November 2016. The performance rights were valued at \$1.90 per share reflecting the volume weighted average closing price of API shares on the ASX in the 10-day period after announcement of full year 31 August 2016 results. Performance rights will only vest if the Executive remains employed at the exercise date subject to forfeiture conditions and Board discretion.
- The performance rights were provided at no cost to the recipient.

Performance rights over equity instruments

The movement during the reporting period in the number of performance rights held directly or beneficially, by each KMP, including their related parties, is as follows:

	Held at 1 Sept 16	Granted as Compensation*	Exercised	Other changes**	Held at 31 Aug 17	Vested during the year
Directors						
Mr R Vincent	460,806	266,841	(64,182)	–	663,465	64,182
Mr S P Roche	1,594,194	209,364	(268,007)	–	1,535,551	268,007
Executives						
Mr P Mendo	75,410	75,000	–	–	150,410	–

	Held at 1 Sept 15	Granted as Compensation*	Exercised	Other changes**	Held at 31 Aug 16	Vested during the year
Directors						
Mr R Vincent	674,595	163,362	(81,262)	(295,889)	460,806	81,262
Mr S P Roche	1,770,732	600,550	–	(777,088)	1,594,194	–
Executives						
Mr P Mendo	–	75,410	–	–	75,410	–
Mr G Fallet	622,782	–	–	(622,782)	–	–

* Total KMP grants of 551,205 rights during the period over new issue shares were equal to 0.1% of common shares outstanding.

** Other changes represent performance rights that expired or were forfeited during the year.
At the end of the reporting period, no rights held by KMP have become vested but not exercisable.

DIRECTORS' REPORT

CONTINUED

MOVEMENTS IN SHARES

The movement during the year in the number of ordinary shares of the Company, held directly, indirectly or beneficially, by each KMP, including their personally related parties is as follows:

<i>In shares</i>	Held at 1 September 2016	Purchases/ issues	Sales	Held at 31 August 2017
Directors				
Mr P R Robinson	302,168	–	–	302,168
Ms E C Holley (ceased being a Director on 25 January 2017)	16,667	–	–	16,667
Mr R D Millner	1,605,620	150,000	–	1,755,620
Mr S P Roche (ceased being a Director on 15 February 2017)	676,667	268,007*	–	944,674
Ms L Ausburn	83,334	–	–	83,334
Mr G Masters	218,000	–	–	218,000
Mr K Gunderson-Briggs	–	10,000	–	10,000
Mr R Vincent (appointed a Director on 15 February 2017)	81,262	64,182*	–	145,444
Executives				
Mr P Mendo	–	–	–	–

* Issued in October 2016 pursuant to the STIP for the year ended 31 August 2015.

The movement during the previous year in the number of ordinary shares of the Company, held directly, indirectly or beneficially, by each KMP, including their personally related parties is as follows:

<i>In shares</i>	Held at 1 September 2015	Purchases	Sales	Held at 31 August 2016
Directors				
Mr P R Robinson	302,168	–	–	302,168
Ms E C Holley (ceased being a Director on 25 January 2017)	16,667	–	–	16,667
Mr R D Millner	1,455,001	150,619	–	1,605,620
Mr S P Roche (ceased being a Director on 15 February 2017)	676,667	–	–	676,667
Ms L Ausburn	83,334	–	–	83,334
Mr G Masters	218,000	–	–	218,000
Mr K Gunderson-Briggs	–	–	–	–
Executives				
Mr R Vincent (appointed a Director on 15 February 2017)	–	81,262*	–	81,262
Mr P Mendo	–	–	–	–

* Issued in November 2015 pursuant to the STIP for the year ended 31 August 2014.

DIRECTORS' REPORT

CONTINUED

Consequences of Performance on Shareholders' Wealth

In considering the performance of the consolidated entity and the benefits for shareholder wealth, the Remuneration Committee has regard for a range of indicators in respect of senior executive remuneration and linked these to the previously described short and long term incentives.

The following table presents these indicators over the past 5 financial years, taking into account dividend payments, share price changes and returns of capital during the financial years:

	31 August 2017	31 August 2016	31 August 2015	31 August 2014	31 August 2013
Net profit/(loss) after tax \$'000	52,371	51,670	43,126	(90,771)	24,292
Dividends declared in respect of the year ended – cents per share (franked)	7.0	6.0	4.5	3.5	3.3
Share price at	1.47	1.77	1.62	0.59	0.49

SECTION 3 OTHER MATTERS REQUIRED BY SECTION 300A CORPORATIONS ACT 2001

A. Comments on Remuneration Report at the most recent AGM of the Company

The Company's previous AGM was held on 25 January 2017. At this meeting:

- no comments were made on the Remuneration Report that was considered at this AGM;
- when the resolution that the Remuneration Report be adopted, at least 75% of the votes cast were in favour of adoption of that report.

B. Engagement of Remuneration Consultant

While the Remuneration Committee seeks external advice from advisers who are independent of management of remuneration matters, it did not require a remuneration recommendation as defined under Section 9B of the Corporations Act 2001 by an external remuneration adviser during the year ended 31 August 2017.

The Remuneration Report concludes at this point.

DIRECTORS' REPORT

CONTINUED

ENVIRONMENTAL REGULATION

The operations of the consolidated entity are subject to environmental regulation under Commonwealth, State and New Zealand Government legislation in relation to its manufacture of pharmaceutical products, retail stores and pharmaceutical distribution facilities. In respect of:

- Pharmaceutical and toiletries product manufacture – manufacturing plants operate under licence requirements relating to waste disposal, water and air pollution.
- Wholesale distribution – distribution facilities operate under licence requirements relating to waste disposal, water and air pollution.

The Board believes that the consolidated entity has adequate systems in place for the management of its environmental requirements and is not aware of any significant breach of the environmental requirements as applied to the consolidated entity.

CORPORATE SOCIAL RESPONSIBILITY

The consolidated entity has continued its involvement with the Priceline Sisterhood and has supported the establishment of The Priceline Sisterhood Foundation as a public ancillary fund registered with the Australian Charities and Not-for Profits Commission and registered with the ATO as a deductible gift recipient. The Sisterhood Foundation Board has a majority of independent Directors who are responsible for deciding the strategic direction of the Foundation as well as determining appropriate policies dealing with fund raising and distribution of funds to chosen diverse charities.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

There were no significant changes in the nature of the activities of the consolidated entity during the year.

DIVIDENDS

A dividend was paid during the year ended 31 August 2017 in respect of the year ended 31 August 2016. The dividend was at the rate of 3.5 cents per share, fully franked. The dividend totalled \$17.143 million and was paid on 4 December 2016.

An interim dividend of 3.5 cents per share amounting to \$17.143 million, fully franked in respect of half year ended 28 February 2017 was paid out of Profits Reserves on 2 June 2017.

EVENTS SUBSEQUENT TO REPORTING DATE

On 18 October 2017, a final dividend of 3.5 cents per share, fully franked to be paid out of the Profits Reserve on 8 December 2017, amounting to \$17.431 million was declared.

Other than above, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the Directors of the Company, to affect significantly the operations of the consolidated entity, the results of those operations or the state of affairs of the consolidated entity in future years.

LIKELY DEVELOPMENTS

The consolidated entity will continue to pursue its policy of improving the profitability and market share of each of its major operating businesses during the next financial year.

Further information regarding the business strategies of the consolidated entity and the expected results of those operations in future financial years have not been included in this report as disclosure of this information would likely result in unreasonable prejudice to the consolidated entity.

DIRECTORS' REPORT

CONTINUED

DIRECTORS' INTERESTS

The relevant direct and indirect and beneficial interest of each Director, in the share capital of the Company, as notified by the Directors to the Australian Securities Exchange in accordance with section 205G(1) of the Corporations Act 2001 at the date of this report is as follows:

	Ordinary Shares	Performance Rights over Ordinary Shares
Mr P R Robinson	302,168	–
Ms E C Holley (ceased being a Director on 25 January 2017)	16,667	–
Mr R D Millner	1,755,620	–
Mr S P Roche (ceased being a Director on 15 February 2017)	944,674	1,535,551
Ms L Ausburn	83,334	–
Mr G J Masters	218,000	–
Mr K Gunderson-Briggs	10,000	–
Mr R Vincent (appointed a Director on 15 February 2017)	145,444	663,465

PERFORMANCE RIGHTS GRANTED TO DIRECTORS AND OFFICERS OF THE COMPANY

Details of the performance rights granted to Directors and officers of the Company are set out in the Remuneration Report.

INSURANCE AND INDEMNIFICATION OF DIRECTORS AND OFFICERS

During the year the Company paid a premium in respect of a contract insuring the Directors and officers against all liabilities to another person (other than the Company or a related body corporate) that may arise from their position, except where the liability arises out of conduct involving a lack of good faith. The contract covers any past, present or future Director, Secretary, Executive Officer or employee of the Company and its controlled entities. Further details have not been disclosed due to confidentiality provisions of the contract of insurance. The Directors are each parties to a Director's Access and Insurance Deed. This Deed includes an indemnity by the Company (subject to and to the fullest extent permitted by applicable law) summarised as follows:

- a. for any liability incurred by the Director as an officer of the Company;
- b. for legal costs incurred by the Director in defending proceedings for a liability incurred as an officer of the Company, or in seeking relief from that liability under applicable law; and
- c. for any liability for legal costs incurred by the Director in connection with legal proceedings of a Government or Regulatory authority which is brought against the Director because of their present or former capacity as an officer of the Company.

DIRECTORS' REPORT

CONTINUED

NON-AUDIT SERVICES

During the year KPMG, auditors of the Company, have performed certain other services in addition to their statutory duties.

The Board has considered the non-audit services provided during the year by the auditor and in accordance with written advice provided by resolution of the Audit and Risk Committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the Corporations Act 2001 for the following reasons:

- All non-audit services were subject to the corporate governance procedures adopted by the Company and have been reviewed by the Audit and Risk Committee to ensure they do not impact the integrity and objectivity of the auditor; and
- The non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 Code of Ethics for Professional Accountants, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision making capacity for the Company, acting as an advocate for the Company, or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Company, KPMG, and its related practices for audit and non-audit services provided during the year are set out in Note 28 to the financial statements.

Lead Auditor's Independence Declaration

The Lead Auditor's Independence Declaration is set out on page 32 and forms part of the Directors' report for the financial year ended 31 August 2017.

Rounding off of Amounts

The Company is of a kind referred to in ASIC Corporations Instrument 2016/191 dated 24 March 2016 and in accordance with that Class Order, amounts in the consolidated financial report and Directors' Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

Dated at Sydney, 18 October 2017

Signed in accordance with a resolution of the Directors:



Peter R. Robinson
Director

LEAD AUDITOR'S INDEPENDENCE DECLARATION



Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To: the Directors of Australian Pharmaceutical Industries Limited

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 31 August 2017 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the audit.

A handwritten signature in black ink that reads 'M. Bisetto'.

KPMG

A handwritten signature in black ink that reads 'M. Bisetto'.

Maurice Bisetto

Partner

Melbourne

18 October 2017

KPMG, an Australian partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. Liability limited by a scheme approved under Professional Standards Legislation.

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31 AUGUST 2017

<i>In thousands of AUD</i>	Note	Year ended 31 August 2017	Year ended 31 August 2016
Revenue	4	4,061,200	3,839,987
Cost of sales		(3,567,817)	(3,362,053)
Gross profit		493,383	477,934
Other income and expense	4	5,961	5,621
Warehousing and distribution expenses		(135,152)	(134,050)
Marketing and sales expenses		(187,895)	(178,263)
Administration and general expenses		(87,021)	(84,111)
Result from operating activities		89,276	87,131
Financial income		309	1,237
Financial expenses		(13,173)	(17,022)
Net financing costs	6	(12,864)	(15,785)
Loss from investment in associates		–	(2,437)
Profit before tax		76,412	68,909
Income tax expense	7	(24,041)	(17,239)
Profit for the year		52,371	51,670
The profit for the year is attributable to equity holders of the parent company.			
Earnings per share for profit attributable to the ordinary shareholders of the Company (cents):			
Basic earnings per share	8	10.7	10.6
Diluted earnings per share	8	10.6	10.5

Notes to the Consolidated Income Statement are annexed.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 AUGUST 2017

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Profit after income tax for the year	52,371	51,670
Items that will not be reclassified subsequently to the income statement		
Remeasurements of defined benefit liability, net of tax	(22)	33
	(22)	33
Items that may be reclassified subsequently to the income statement		
Exchange fluctuations on translation of foreign operations, net of tax	(1,804)	1,990
Effective portion of changes in fair value of cash flow hedges, net of tax	149	240
	(1,655)	2,230
Other comprehensive (loss)/income for the year, net of income tax	(1,677)	2,263
Total comprehensive income for the year attributable to equity holders of the parent company	50,694	53,933

Notes to the Consolidated Statement of Comprehensive Income are annexed.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 AUGUST 2017

<i>In thousands of AUD</i>	Note	As at 31 August 2017	As at 31 August 2016
Assets			
Cash and cash equivalents	26	39,776	25,489
Trade and other receivables	9	681,620	689,695
Inventories	10	399,344	413,782
Total current assets		1,120,740	1,128,966
Trade and other receivables	9	21,187	10,882
Deferred tax assets	13	20,210	19,757
Property, plant and equipment	14	95,280	100,129
Intangible assets	15	193,659	189,975
Total non-current assets		330,336	320,743
Total assets		1,451,076	1,449,709
Liabilities			
Trade and other payables	16	804,473	799,237
Loans and borrowings	17	2,765	2,978
Employee benefits	18	18,989	22,402
Provisions	19	7,907	7,656
Income tax payable	12	16,899	13,359
Total current liabilities		851,033	845,632
Trade and other payables	16	7,903	8,436
Deferred tax liability	13	364	534
Loans and borrowings	17	29,834	48,420
Employee benefits	18	3,834	5,339
Provisions	19	3,862	4,653
Total non-current liabilities		45,797	67,382
Total liabilities		896,830	913,014
Net assets		554,246	536,695
Equity			
Share capital		566,461	566,461
Reserves		92,449	74,898
Accumulated losses		(104,664)	(104,664)
Total equity		554,246	536,695

Notes to the Consolidated Statement of Financial Position are annexed.

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 AUGUST 2017

<i>In thousands of AUD</i>	Note	Year ended 31 August 2017	Year ended 31 August 2016
Cash flows from operating activities			
Cash receipts from customers (inclusive of GST)		4,445,196	4,140,016
Cash payments to suppliers and employees (inclusive of GST)		(4,315,384)	(4,043,355)
Cash generated from operations		129,812	96,661
Interest received		309	1,237
Financing costs paid		(13,610)	(16,954)
Income taxes (paid)/refund		(21,029)	1,913
Net cash from operating activities	26	95,482	82,857
Cash flows from investing activities			
Proceeds from sale of stores, property, plant and equipment		513	2,115
Acquisition of property, plant and equipment		(12,130)	(14,417)
Proceeds from divestment of associates		–	4,361
Payment for intangibles		(16,160)	(5,128)
Net cash used in investing activities		(27,777)	(13,069)
Cash flows from financing activities			
Proceeds from borrowings		1,598,000	1,327,196
Repayment of borrowings		(1,615,198)	(1,374,147)
Payment of finance lease liabilities		(1,601)	(1,455)
Dividends paid		(34,286)	(24,430)
Net cash used in financing activities		(53,085)	(72,836)
Net increase/(decrease) in cash and cash equivalents		14,620	(3,048)
Cash and cash equivalents at the beginning of the year		25,489	28,047
Effect of exchange rate fluctuations on cash held		(333)	490
Cash and cash equivalents at the end of the year	26	39,776	25,489

Notes to the Consolidated Statement of Cash Flows are annexed.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 AUGUST 2017

<i>In thousands of AUD</i>	Share Capital	Accumulated Losses	Profits* Reserve	Translation Reserve	Hedging Reserve	Equity Reserve	Total Equity
Balance at 1 September 2016	566,461	(104,664)	68,092	1,615	(353)	5,544	536,695
Total comprehensive income for the year							
Profit after tax	–	–	52,371	–	–	–	52,371
Total other comprehensive income/(loss)	–	–	(22)	(1,804)	149	–	(1,677)
Total comprehensive income for the year	–	–	52,349	(1,804)	149	–	50,694
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Purchase of treasury shares**	(493)	–	–	–	–	–	(493)
Shares vested under the STIP	493	–	–	–	–	(493)	–
Dividends to equity holders	–	–	(34,286)	–	–	–	(34,286)
Share based payment transactions	–	–	–	–	–	1,636	1,636
Total contributions by and distributions to owners	–	–	(34,286)	–	–	1,143	(33,143)
Balance at 31 August 2017	566,461	(104,664)	86,155	(189)	(204)	6,687	554,246

<i>In thousands of AUD</i>	Share Capital	Accumulated Losses	Profits* Reserve	Translation Reserve	Hedging Reserve	Equity Reserve	Total Equity
Balance at 1 September 2015	566,461	(104,664)	40,819	(375)	(593)	3,754	505,402
Total comprehensive income for the year							
Profit after tax	–	–	51,670	–	–	–	51,670
Total other comprehensive income/(loss)	–	–	33	1,990	240	–	2,263
Total comprehensive income for the year	–	–	51,703	1,990	240	–	53,933
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Dividends to equity holders	–	–	(24,430)	–	–	–	(24,430)
Share based payment transactions	–	–	–	–	–	1,790	1,790
Total contributions by and (distributions) to owners	–	–	(24,430)	–	–	1,790	(22,640)
Balance at 31 August 2016	566,461	(104,664)	68,092	1,615	(353)	5,544	536,695

Notes to the Consolidated Statement of Changes in Equity are annexed.

(*) The profits reserve represents current year profits transferred to a reserve to preserve the characteristic as a profit and not appropriate those profits against prior year accumulated losses. Such profits will be available to enable payment of franked dividends in the future.

(**) Shares were purchased on market and issued to the previous Managing Director for the vesting of the 2014 STIP. These are treated as treasury shares bought on market.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 AUGUST 2017

1. BASIS OF PREPARATION

a. Reporting Entity

Australian Pharmaceutical Industries Limited (the 'Company') is a Company limited by shares incorporated and domiciled in Australia, operating in Australia and New Zealand whose shares are publicly traded on the Australian Stock Exchange under the ASX code API. The summarised information of the Parent Company is included in Note 11.

The Company is a for profit entity for the purpose of preparing the consolidated financial report (the 'financial report'). The financial report of the Company included herein comprises the Company and its subsidiaries (together referred to as the 'consolidated entity' or the 'Group'). The financial report was authorised for issue by the Directors on 18 October 2017.

b. Statement of Compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards ('AASBs') adopted by the Australian Accounting Standards Board ('AASB') – including Australian Interpretations and the Corporations Act 2001.

Compliance with IFRS

The financial report of the consolidated entity also complies with International Financial Reporting Standards (IFRS) and interpretations adopted by the International Accounting Standards Board.

c. Basis of Measurement

The financial report is presented in Australian dollars, which is the functional currency of the Company and the consolidated entity.

The financial report is prepared on the historical cost basis except for derivative financial instruments and employee defined benefit plan which are stated at their fair value.

The consolidated entity is of a kind referred to in ASIC Corporations Instrument 2016/191 (Rounding in Financial/Directors' Reports) dated 24 March 2016 and in accordance with that Class Order, amounts in the consolidated financial statements and Directors' Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

d. Accounting estimates and judgements

The preparation of a financial report in conformity with Australian Accounting Standards requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an

ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in future periods.

In particular, information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements include:

Carrying value of goodwill and brand names

Management judgement is applied to identify the Cash Generating Units ("CGUs") and determine the recoverable amounts using a "value in use" calculation. These judgements include establishing forecasts of future financial performance, as well as the assessment of earnings growth rates, discount rates and terminal growth rates based on past experience and expectations for the future. The cash flow projections are based on a maximum of five-year Board approved budgets and strategic plan. The forecasts use management estimates to determine revenue, expenses, working capital movements, capital expenditure and associated cash flows for each CGU.

Carrying value of trade debtors

Management judgement is applied to assess the recoverability of trade debtors regularly and at each reporting period. Trade debtors are considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows.

Objective evidence that trade debtors may not be recoverable can include default or delinquency by a debtor, restructuring of an amount due on terms that the consolidated entity would not consider otherwise, and indications that a debtor or issuer will enter some form of administration or bankruptcy.

Where the likelihood of recovery of trade debtors is remote, the amount receivable is fully provided for and recognised against profit. In instances where there is a reasonable prospect of recovery, management has made their best estimate based on all available information, on the most likely outcome as at the reporting period. Any provision for impairment for trade debtors is recognised against profit during the reporting period.

In determining the appropriate provision for impairment of pharmacy receivables, consideration is given to financial guarantees provided to individual debtors and debtor groups which are recorded as current liabilities where it is considered probable that the guarantees will be called. In assessing collective impairment management considers historical trends of the probability of default, timing of recoveries and the amount of loss incurred, and current economic and credit conditions.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

Carrying value of inventory

Management judgement is applied to assess the recording of inventory at the lower of cost and net realisable value and ensure that appropriate provision is made for all obsolete or slow moving stock is at each reporting date. These judgements involve assumptions, estimates and calculations around specific inventories and to the best of management's knowledge inventories have been correctly and fairly recorded as at 31 August 2017.

Estimation of useful lives of assets

The estimation of the useful lives of assets has been based on historical and industry experience and lease terms (for leased equipment). Adjustments to useful life are made when considered necessary.

Lease make good provision

Management judgement is applied to assess the provision for rehabilitation ("dismantling provisions") under its lease agreements on distribution centres, support offices and stores at each reporting date. Estimates and assumptions are made in determining the provision as there are numerous factors that will affect the ultimate liability payable. These factors include estimates of the extent and costs of rehabilitation activities, cost increases and changes in discount rates. Those uncertainties may result in future actual expenditure differing from the amounts currently provided. The provision at reporting date represents the best estimate by management of the present value of the future make good costs required.

Share based payments

The Company measures the cost of equity settled securities allocated to employees by reference to the fair value of the equity instruments at the date at which the equity instruments are granted.

For the executive long term incentive plans (LTIP's), the fair value of the performance share rights is determined using the Black Scholes pricing model.

e. Going concern basis of accounting

The Directors have prepared the financial report on a going concern basis having considered the continuity of business operations, realisation of assets and settlement of liabilities in the ordinary course of business.

f. New accounting standards and interpretations

In the current year, the consolidated entity has adopted all of the following new and revised standards and interpretations issued by the Australian Accounting Standards Board (the AASB) that are relevant to its operations and effective for the current annual reporting period:

- i. *AASB 2014-4 Amendments to Australian Accounting Standards – Clarification of Acceptable Methods of Depreciation and Amortisation;*
- ii. *AASB 2015-1 Amendments to Australian Accounting Standards – Annual Improvements to Australian Accounting Standards 2012-2014 Cycle; and*
- iii. *AASB 2015-2 Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 101.*

The adoption of these new and revised standards and interpretations did not have any significant financial impact on the amounts recognised and the disclosures presented in the financial statements.

Standards issued but not yet adopted

A number of new standards and amendments to standards are effective for annual periods beginning after 1 September 2017. The consolidated entity has not applied the following new or amended standards in preparing the consolidated financial statements for this reporting period:

AASB 9 Financial Instruments (2014) – initially expected to be applied in the financial year beginning 1 September 2018

AASB 9, approved in December 2014, replaces the existing guidance in AASB 139 Financial Instruments: Recognition and Measurement. AASB 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from AASB 139. AASB 9 is effective for annual reporting periods beginning on or after 1 January 2018 with early adoption permitted. The Company currently plans to apply AASB 9 for the financial year ending 31 August 2019.

The actual impact of adopting AASB 9 on the consolidated financial statements of the Company in 2019 is not known and cannot be reliably estimated because it will be dependent on the financial instruments that the Company holds and economic conditions at that time as well as accounting elections and judgements that it will make in the future. The new standard will require the Company to revise its accounting processes and internal controls related to reporting financial instruments, and these changes are not yet complete. However, the Company has performed a preliminary assessment of the potential impact of adoption of AASB 9 based on its positions as at 31 August 2017 and hedging relationships designated during 2017 under AASB 139.

NOTES TO THE FINANCIAL STATEMENTS

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1. BASIS OF PREPARATION (continued)

i. Classification – Non-derivative Financial Assets

AASB 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics.

AASB 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL).

As at 31 August 2017, the non-derivative financial assets on the balance sheet of the Company are: trade receivables, and cash & cash equivalents.

Based on its preliminary assessment, the Company does not believe that the new classification requirements, if applied at 31 August 2017, would have a significant impact on its classification of trade receivables that are managed on an amortised cost basis.

ii. Impairment – Financial Assets

AASB 9 replaces the incurred loss model in AASB 139 with a forward-looking expected credit loss (ECL) model. This will require judgement as to how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. The new impairment model will apply to the trade receivables of the Company.

Under AASB 9, loss allowances will be measured on either of the following basis:

- 12-month ECLs: These are ECLs that result from possible default events within the 12 months after the reporting date; and
- Lifetime ECLs: These are ECLs that result from all possible default events over the expected life of a financial instrument.

Under AASB 9, for trade receivables with a duration of one year or less or those that do not contain a significant financing component, a simplified approach is available in which a provision is recognised initially based on the Lifetime ECLs. The Company currently plans to apply the simplified approach in applying the ECL impairment model to trade receivables.

The lifetime ECL will be calculated by applying historical observed default rates over the expected life of the receivables adjusted for forward-looking estimates such as economic, regulatory or customer base external market indicators impacts. The Company has assessed that the current level of provisioning would be adequate to cover the provision required if AASB 9 were applied at 31 August 2017.

iii. Classification – Non-derivative Financial Liabilities

The non-derivative financial liabilities of the Company comprise interest bearing liabilities, trade payables and financial guarantees. AASB 9 largely retains the existing requirements in AASB 139 for the classification of financial liabilities with interest bearing liabilities and trade payables measured at amortised cost and financial guarantees measured at the maximum potential obligation. The Company's preliminary assessment did not indicate any significant impact if AASB 9 were applied at 31 August 2017.

iv. Hedge Accounting

AASB 9 will require the Company to ensure that hedge accounting relationships are aligned with the Company's risk management objectives and strategies and to apply a more qualitative and forward-looking approach to assessing hedge effectiveness. The Company will be required to provide additional levels of disclosure pertaining to its risk management objectives and strategies.

The type of hedging arrangements that the Company currently implements will continue to qualify for hedge accounting under the new standard.

The current accounting treatment applied by the Company regarding effective cash-flow hedges is consistent with the requirements of AASB 9.

v. Disclosures

AASB 9 will require new disclosures regarding hedge accounting, credit risk and expected credit losses. The preliminary assessment by the Company included an analysis to identify data gaps against current processes and the Company plans to implement the system and controls changes that the Company believes will be necessary to capture the required data.

AASB 15 Revenue from Contracts with Customers – initially expected to be applied in the financial year beginning 1 September 2018

AASB 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including AASB 118 Revenue, and AASB Interpretation 13 Customer Loyalty Programmes. The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

Expected impact

The key revenue streams of the Company are:

- Sales of goods and Sister Club loyalty points through Company-owned stores;
- Sales of goods and Sister Club loyalty points to Franchise stores;
- Franchise fees from Franchise partners;
- Sales of goods and membership fees to Wholesale customers; and
- Community service obligation (CSO) income from Government.

The Company has completed an initial assessment of the potential impact of the adoption of AASB 15 on the consolidated financial statements and has identified the following areas that may be affected:

i. Allocation of revenue to performance obligations

AASB 15 requires the distinct performance obligations in a contract with a customer to be identified. The transaction price is allocated to each performance obligation and revenue is recognised as each performance obligation is satisfied. This affects the accounting for the following revenue streams of the Company as follows:

- Franchise fees: The Company receives various types of franchise fees and membership fees from its franchisees and wholesale customers. These include 'start-up' fees received at the start of a franchise arrangement, which are currently recognised as revenue upon signing of the franchise agreement. The Company has assessed that there is no distinct performance obligation that is satisfied at the start of a franchise arrangement, therefore AASB 15 requires these fees to be deferred and recognised over the life of the franchise agreement. The amount of deferral is not expected to be significant.
- Sister Club points: AASB 15 requires the total consideration received from customers to be allocated between the goods sold and Sister Club points awarded to the customer, based on relative stand-alone selling prices of the goods and the points. The Company has assessed that its current accounting policy is materially consistent with the requirements of AASB 15 in this respect.

ii. Variable consideration

AASB 15 introduces new requirements for the recognition of variable consideration, which is to be recognised as part of the transaction price only when it is highly probable that there will be no reversal of revenue when the variability is resolved.

This affects the revenue streams of the Company as follows:

- Rebates payable to franchisees for compliance with the brand and operational standards of Priceline: These rebates represent variable consideration. The Company has assessed that its current accounting policy for these rebates is materially consistent with the requirements of AASB 15.
- Rebates and discounts payable to franchisees and wholesale customers on the sale of goods: These rebates and discounts are mostly either fixed discounts or discounts connected with specific promotional campaigns, and are applied at the time of sale. The Company has assessed that its current accounting policy for these rebates and discounts is materially consistent with the requirements of AASB 15.
- Return of Goods: The treatment of variable consideration under AASB 15 extends to goods returns from wholesale customers, with an estimate of probable returns to be factored into the transaction price. The Company has a right to return such goods to suppliers. This required change in treatment is expected to be insignificant to the results of the Company.

iii. Community service obligation (CSO) income

The CSO is a Government grant and is accounted for under AASB 120 Accounting for Government Grants and Disclosure of Government Assistance, which has not changed. Adoption of AASB 15 will not affect the accounting for the CSO by the Company.

Transition

AASB 15 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. The Company plans to adopt the new standard in its consolidated financial statements for the year ending 31 August 2019, using the retrospective approach. As a result, the Company will apply the requirements of AASB 15 to each comparative period presented.

The Company plans to use the practical expedients for completed contracts. This means that completed contracts that began and ended in the same comparative reporting period, as well as contracts that are completed contracts at the beginning of the earliest period presented, are not restated.

The Company is undertaking a detailed assessment of the impact resulting from the application of AASB 15 and the systems and operational changes required in this regard, and expects to disclose additional qualitative information before it adopts the new standard.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

1. BASIS OF PREPARATION (continued)

AASB 16 Leases – initially expected to be applied in the financial year beginning 1 September 2019

AASB 16 introduces a single, on-balance sheet accounting model for lessees. A lessee recognises a right-of-use asset representing the lessee right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting remains unchanged by the current standard with lessors continuing to classify leases as finance leases or operating leases.

AASB 16 replaces existing leases guidance including AASB 117 Leases, AASB Interpretation 4 Determining whether an Arrangement contains a Lease, AASB Interpretation 115 Operating Leases – Incentives and AASB Interpretation 127 Evaluating the Substance of Transactions involving the Legal form of a Lease.

The standard is effective for annual periods beginning on or after 1 January 2019. While early adoption is permitted in certain circumstances, the Company currently intends to adopt AASB 16 for the financial year ending 31 August 2020.

The Company has started an initial assessment of the potential impact on the consolidated financial statements. The most significant impact identified is that the Company will recognise new assets and liabilities for the operating leases of the warehouse and distribution facilities as well as the store network of the Company. In addition, the nature of expenses related to those leases will change as AASB 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense in respect of the lease liabilities.

No significant impact is expected in respect of the finance leases of the Company.

Transition

As a lessee, the Company can either apply the fully retrospective approach, or the simplified transition method with optional practical expedients. Under the fully retrospective approach the Company adopts the standard as if it has always applied, whereas under the simplified transition method the Company adopts the standard as if each lease that exists on transition is a new lease on the transition date (1 September 2019). The Company is yet to determine which transition approach to apply.

The Company is yet to quantify the impact on the reported assets and liabilities of the Company on adoption of AASB 16. The quantitative effect will depend on, inter alia, the transition method chosen, the extent to which the Company uses the practical expedients and recognition exemptions, and any additional leases into which the Company enters. The Company will disclose the transition approach and quantitative information before adoption.

The Company has commenced discussions with the financiers of the Company on the impact that adoption of AASB 16 will have on the reported assets and liabilities of the Company and ensuring that the impacts will be appropriately reflected in revised loan covenants.

2. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in financial report unless otherwise stated.

a. Basis of Consolidation

i. Subsidiaries

Subsidiaries are all entities over which the Group has control. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from the activities of the entity. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The subsidiaries are fully consolidated from the date that control commences until the date that control ceases.

Investments in subsidiaries are carried at their cost, less any impairment, in the financial statements.

ii. Transactions Eliminated on Consolidation

Intra-group balances, income and expenses and unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Unrealised losses are also eliminated, but only to the extent that there is no evidence of impairment.

Accounting policies of the Company and all subsidiaries in the Group are consistent.

b. Foreign Currency

i. Foreign Currency Transactions

Transactions in foreign currencies are initially translated into Australian currency at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into Australian currency at the exchange rate ruling at that date.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

Foreign exchange gains and losses arising on translation are recognised in the income statement in other income and expense. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Australian dollars at foreign exchange rates ruling at the dates the fair value was determined.

ii. Foreign Operations

The assets and liabilities of foreign controlled subsidiaries, including goodwill and fair value adjustments arising on consolidation, are translated to Australian currency at foreign exchange rates current at the balance sheet date, while revenues and expenses are translated at rates approximating to the foreign exchange rates ruling at the dates of the transactions.

Foreign exchange differences arising on translation are recognised in other comprehensive income, and taken to the foreign currency translation reserve in equity.

c. Financial Instruments

i. Non-derivative Financial Instruments

Non-derivative financial instruments comprise debt securities, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

Financial instruments subject to material deferred settlement terms are recognised at their present value discounted using an interest rate that reflects the credit risk applicable to the counterparty equivalent to the extent of any underlying security. The unwinding of discounting is recognised in net finance costs.

Receivables

The majority of trade debtors are settled within 40-120 days of the invoice date and are carried at amounts due less provision for impairment. Trade debtors are presented as current assets unless collection is not expected for more than 12 months after the reporting date.

When receivables are considered to be impaired, the carrying amount of the asset is reduced, by applying through the use of a provision for impairment with the amount of the impairment recognised against profit.

When a trade receivable is uncollectible due to remote likelihood of payment, it is written off against the provision for impairment account for trade receivables. Subsequent recoveries of amounts previously written off are credited to profit.

Trade payables

Liabilities are recognised for amounts to be paid in the future for goods or services received or provided prior to the end of the reporting period. Trade accounts payable are normally settled within 30-60 days of the invoice date.

Interest bearing liabilities

Interest bearing liabilities are classified as current liabilities unless there is an unconditional right to defer settlement of the liability for at least 12 months after reporting date.

Interest-bearing loans and borrowings are recognised initially at fair value less attributable transaction costs.

Cash and cash equivalents

These comprise of cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the cash management for the consolidated entity are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

ii. Derivative Financial Instruments

The consolidated entity may from time to time hold derivative financial instruments to hedge interest rate and foreign currency risk exposures.

Derivatives are recognised initially at fair value. Attributable transaction costs are recognised against profit when incurred. Subsequently derivatives are measured at fair value. The accounting for changes in fair value is dependant on the instrument meeting the criteria as a cash flow hedge.

Cash Flow Hedges

Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognised directly in other comprehensive income to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in profit or loss.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in other comprehensive income remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in equity is transferred to the carrying amount of the asset when it is recognised. In other cases the amount recognised in other comprehensive income is transferred to profit or loss in the same period that the hedged item affects profit or loss.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

iii. Ordinary Shares

Issued and paid up capital is recognised at the fair value of the consideration received by the Company. Incremental costs directly attributable to the issue of new shares are recognised as a reduction from equity, net of any related tax benefit.

Dividends

Dividends are recognised as a liability when an obligation to pay a dividend arises. The obligation arises following declaration of the dividend by the Board.

iv. Financial guarantees

Financial guarantee contracts are recognised as a financial liability when it becomes probable that guarantees would be called upon in the foreseeable future, for the maximum potential obligation that the consolidated entity has an obligation to meet. The liability is not discounted.

v. Securitised receivables

Securitised receivables are recognised on the statement of financial position as the consolidated entity assumes the risks and rewards of the receivables collection performance.

d. Property, Plant and Equipment

i. Recognition and Measurement

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Purchased software that is integral to the functionality of the equipment is capitalised as part of that equipment.

Subsequent expenditure is added to the carrying value of the asset when it is probable that future economic benefits, in excess of the original assessed standard of performance of the existing asset, will flow to the consolidated entity. All other subsequent expenditure is expensed in the period in which it is incurred.

ii. Disposal and de-recognition of property, plant and equipment

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on de-recognition of the asset is included in the income statement in the period the item is derecognised.

iii. Depreciation

Property, plant and equipment, other than freehold land, are depreciated or amortised on a straight-line basis at various rates dependent upon the estimated average useful life for that asset. The estimated useful lives of each class of asset are as follows:

– buildings	40 years
– plant and equipment	3-15 years
– fixtures and fittings	10 years

The residual value, the useful life and the depreciation method applied to an asset are reassessed at least annually.

e. Intangible Assets and Goodwill

Intangibles are carried at cost less accumulated amortisation and impairment losses where applicable. Intangible assets acquired separately are capitalised at cost or, if arising from a business combination, at fair value as at the date of acquisition.

i. Goodwill

All business combinations are accounted for by applying the purchase method. Goodwill represents the excess of the cost of the acquisition over the fair value of the net identifiable assets acquired. Acquisition-related costs are recognised in the income statement as incurred.

Goodwill is stated at cost less any accumulated impairment losses. An impairment loss recognised for goodwill is not reversed in subsequent periods.

In respect of associates, the carrying amount of goodwill is included in the carrying amount of the investment in the associate. Negative goodwill arising on an acquisition is recognised directly against profit.

ii. Brand Names

Brand names acquired are included in the financial statements at cost less accumulated impairment losses.

Brand names are not amortised as at this point of time the useful lives of these assets are indefinite. The brand names have an unlimited legal life and based on industry experience it is rare for leading brand names to disappear or become commercially or technically obsolete. If an event occurs which results in an impairment of the value of a brand name then the difference between recoverable amount and carrying value is charged against profit in the year in which the event occurred.

Independent valuations of brand names are obtained during the year of acquisition. Expenditure incurred in developing, maintaining and enhancing brand names is charged against profit in the year in which the expenditure is incurred.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

iii. Research and Development

Expenditure on research activities, undertaken with the prospect of gaining new technical knowledge and understanding, is recognised in the income statement as an expense as incurred.

Expenditure on development activities, whereby research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised if the product or process is technically and commercially feasible and the consolidated entity has sufficient resources to complete development. The expenditure capitalised includes the cost of materials, direct labour and appropriate proportion of overheads. Other development expenditure is recognised against profit as an expense as incurred. Capitalised development expenditure is initially recorded at cost and amortised on a straight line basis over the estimated useful lives but not greater than a period of 4 years.

iv. Software

Capitalised software are initially recorded at cost and amortised on a straight line basis over the estimated useful lives but not greater than a period of 7 years.

v. Subsequent Expenditure

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

f. Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The cost of inventories is generally determined on a weighted average basis and includes expenditure incurred in acquiring the inventories and bringing inventories to the existing location and condition net of any rebates or trade discounts received or receivable. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads based on normal operating capacity.

g. Impairment

Financial Assets

Refer to the accounting policy included in Note 1(d).

Non-Financial Assets

The carrying amounts of tangible assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the recoverable amount of the asset or its CGU is estimated.

An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of goodwill allocated to the cash generating unit and then to reduce the carrying amount of the other assets including tangible assets in the unit or group of units on a pro-rata basis.

Calculation of recoverable amount

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate, risk adjusted to a post-tax discount, that reflects current market assessments of the time value of money and the risks specific to the asset.

For goodwill and intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated annually and whenever there is an impairment indicator.

Reversals of impairment

An impairment loss in respect of goodwill is not reversed.

In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the carrying amount of the asset does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

h. Leases

Leases in terms of which the consolidated entity assumes substantially all the risks and rewards of ownership are classified as finance leases. Other leases are classified as operating leases. Assets, subject to finance leases, are capitalised. The initial amount of the lease asset is the lower of fair value and the present value of the minimum lease payments. The corresponding liability represents the future rental obligations net of finance charges. The leased assets are amortised on a straight-line basis over the life of the relevant lease.

Lease liabilities are reduced by repayments of principal. The interest components of lease payments are charged against profit.

Operating leases are not capitalised. Operating lease payments are charged to profit as incurred on a straight-line basis. Lease incentives received are recognised as an integral part of the total lease expense and spread over lease term.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

i. Employee Benefits

i. Wages, Salaries, Annual Leave and Non-monetary Benefits

Liabilities for employee benefits for wages, salaries, annual leave and sick leave that are expected to be settled within 12 months of the reporting date represent present obligations resulting from the services of employees provided to reporting date, are calculated as undiscounted amounts based on remuneration wage and salary rates that are expected to be paid as at reporting date including related on-costs, such as workers compensation insurance and payroll tax. Benefits expected to be settled after 12 months from the reporting date are measured at the present value of the estimated future cash outflows to be made in respect of services provided by employees up to the reporting date. Non-accumulating non-monetary benefits, such as cars and free or subsidised goods and services, are expensed as the benefits are taken by the employees based on the net marginal cost.

ii. Long Service leave

The provision for long service leave represents the present value of the estimated future cash outflows to be made resulting from employees services provided up to the reporting date. The provision is calculated using expected future increases in wage and salary rates including related on-costs and expected settlement dates, and is discounted using corporate bonds rates at the reporting date which most closely match the terms of maturity of the related liabilities. The unwinding of the discount is treated as long service leave expenses.

iii. Defined Contribution Plans

Obligations for contributions to defined contribution superannuation funds are recognised as an expense against profit.

iv. Defined Benefit Plans

The net obligation in respect of defined benefit pension plans is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is discounted to determine its present value, and the fair value of any plan assets is deducted.

The discount rate is the yield at the reporting date on corporate bonds that have maturity dates approximating the terms of the obligations of the consolidated entity. The calculation is performed by a qualified actuary using the projected unit credit method.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the income statement on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately against profit.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, and the return on plan assets (excluding interest), are recognised immediately in other comprehensive income. The consolidated entity determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual reporting period to the then net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognised against profit.

Past service cost is the increase in the present value of the defined benefit obligation for employee services in prior periods, resulting in the current period from the introduction of, or changes to, post-employment benefits or other long-term employee benefits. Past service costs may either be positive (where benefits are introduced or improved) or negative (where existing benefits are reduced).

v. Share-based Payment Transactions

Share Performance Rights granted to employees are recorded at fair value and recognised as an expense with a corresponding increase in equity. At the end of each reporting period, the consolidated entity revises the estimate of the number of equity instruments expected to vest. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the options/performance rights reserve. The fair value is initially measured at grant date and spread over the period during which the employees become unconditionally entitled to payment. The fair value of the share performance rights is measured based on the Black-Scholes Option Pricing model for the ROE performance hurdle, taking into account the terms and conditions upon which the instruments were granted.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

j Provisions

A provision is recognised when the consolidated entity has a present legal or constructive obligation and can be reliably measured as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation, the timing or amount of which is uncertain. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

i. Provision for Sister Club

The provision for Sister Club points which can be converted quarterly by customers in the form of gift vouchers is based upon the expected cost to the consolidated entity on redemption of Sister Club vouchers. A redemption rate is applied based on historical experience and is updated quarterly.

k. Revenue

i. Sale of goods

Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer, usually when goods are delivered to manufacturing and wholesale customers or the point of sale for retail customers.

No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, the costs incurred or to be incurred cannot be measured reliably, there is a risk of return of goods, or there is continuing management involvement with the goods. Revenue is recognised net of returns, allowances, trade discounts and volume rebates.

ii. Community Service Obligation ("CSO")

A Community Service Obligation is an arrangement whereby the Government provides a pool of funding which is available to qualifying wholesalers to provide services that would not otherwise be provided by that organisation in the pursuit of its other objectives. In the case of the consolidated entity this requirement is around minimum delivery obligations throughout Australia. The Government provides income to the consolidated entity to compensate for the higher expenditure incurred to meet these minimum delivery obligations.

Revenue from CSO is recognised when the consolidated entity has complied with the conditions attached to the obligation and has reasonable assurance that the income will be received.

iii. Other revenue

Membership and brand fees

The Priceline, Soul Pattinson and Pharmacist Advice banner stores pay fees to the consolidated entity. These fees entitle the stores to access certain discounts (specifically applicable to banner members) and other benefits including participation in catalogue advertising. This revenue is recognised over the period of the year which matches the period over which the services are rendered.

Franchise service charges

This category primarily covers fees billed to franchisees for various operational services including stores development, lease negotiation, human resource and information technology assistance. This revenue is recognised once the delivery service has been performed.

Marketing services and promotional income

This category relates to income received from suppliers relating to promotional services rendered. This revenue is recognised once the service obligations have been performed.

Loyalty Card (Sister Club formerly known as Clubcard)

A provision for loyalty card deferred revenue is recognised as a reduction in sales revenue when the underlying products or services are sold. The deferred revenue is based on historical loyalty card data and a weighting of all possible outcomes against their associated probabilities. Revenue is earned when loyalty card awards are redeemed.

iv. Interest on overdue accounts

Interest revenue is recognised on financial assets on an accrual basis when it is considered probable of being recovered. Interest fee revenue includes interest earned on loans to customers and late fee charges on overdue debtors.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

l. Net Financing Costs

Finance costs are recognised as expenses in the period as incurred, unless directly attributable to the acquisition of, or production of, a qualifying asset which are capitalised as part of the cost of that asset using the weighted average cost of borrowings. Finance costs include:

- interest on bank overdrafts, short-term and long-term borrowings;
- interest payable on trade debtors' securitisation programs;
- finance lease charges; and
- amortisation of ancillary costs incurred in connection with the arrangement of borrowings.

Interest income is recognised in the income statement as it accrues, using the effective interest method. Dividend income is recognised in the income statement on the date when the right to receive payments is established.

m. Income Tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not recognised:

- initial recognition of goodwill;
- the initial recognition of assets or liabilities that arises in a transaction that is not a business combination and affects neither accounting nor taxable profit at the time of the transaction; and
- differences relating to investments in subsidiaries to the extent that the differences will probably not reverse in the foreseeable future.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. The carrying amount of deferred income tax assets is reviewed at each reporting period and reduced to the extent that it is no longer probable that the sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilised.

n. Operating Segment

An operating segment is a component of the consolidated entity that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to the transactions with any of the other segments. The operating results of all operating segments are regularly reviewed by the consolidated Chief Executive Officer (CEO) to make decisions about the allocation of resources to the segment and assess the performance of the segment for which discrete financial information is available.

Segment results that are reported to the CEO include items directly attributable to a segment to the level of reportable segment profit.

o. Comparatives

Where applicable, comparative periods have been adjusted to disclose comparatives on the same basis as the current year.

3. OPERATING SEGMENTS

AASB 8 Operating Segments requires a management approach under which segment information is presented on the same basis as that used for internal reporting provided to the Chief Operating Decision Maker (CODM) of the Group. The CODM has been identified as the CEO.

Segment information is presented to the CEO comprising two segments: Australia and New Zealand.

NOTES TO THE FINANCIAL STATEMENTS

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Australia

Segment activities: Distribution of pharmaceutical, medical, health, beauty and lifestyle products to pharmacies, the purchase and sale of health, beauty and lifestyle products within the retail industry and provider of retail services to pharmacies.

The consolidated entity predominantly operates within Australia. Monthly management reports provided to the CEO report Australian reportable segment profit.

New Zealand

Segment activities: Manufacturer and owner of rights of pharmaceutical medicines and consumer toiletries.

<i>In thousands of AUD</i>	Australia		New Zealand		Eliminations		Consolidated	
	Aug 17	Aug 16	Aug 17	Aug 16	Aug 17	Aug 16	Aug 17	Aug 16
Revenue								
External revenue	3,863,605	3,653,903	45,204	45,213	–	–	3,908,809	3,699,116
External services	152,391	140,871	–	–	–	–	152,391	140,871
Inter-segment revenue*	–	–	5,442	8,294	(5,442)	(8,294)	–	–
Total segment revenue	4,015,996	3,794,774	50,646	53,507	(5,442)	(8,294)	4,061,200	3,839,987
Reportable segment gross profit	471,342	454,291	22,041	23,643	–	–	493,383	477,934
Reportable segment profit	88,576	84,826	700	2,305	–	–	89,276	87,131
Unallocated amounts								
Net financing costs							(12,864)	(15,785)
Loss from investment in associates							–	(2,437)
Consolidated profit before tax							76,412	68,909

* All inter-segment sales are on an arm's length basis.

4. REVENUE, OTHER INCOME AND EXPENSE

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Revenue		
Sales revenue	3,908,809	3,699,116
Service revenue	152,391	140,871
	4,061,200	3,839,987
Other income and expense		
Gain on disposal of stores, property, plant and equipment	50	1,305
Interest fee income	5,978	4,685
Net foreign exchange loss	(67)	(369)
	5,961	5,621

NOTES TO THE FINANCIAL STATEMENTS

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5. PERSONNEL EXPENSES

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Wages and salaries	180,407	177,260
Other associated personnel expenses	18,442	18,143
Contributions to defined contribution superannuation funds	13,882	13,084
Expenses related to defined benefit superannuation funds	13	43
Equity settled share based payment transactions	1,636	1,790
	214,380	210,320

6. FINANCE INCOME AND COSTS

Recognised in Profit and Loss

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Interest income on bank deposits	309	666
Other interest income	–	571
Finance income	309	1,237
Interest expense	(6,243)	(8,942)
Borrowing costs	(1,814)	(2,446)
API Rewards	(4,871)	(5,339)
Finance charges – leased assets	(245)	(295)
Finance costs	(13,173)	(17,022)
Net finance costs	(12,864)	(15,785)

Interest fee income on overdue debts is presented in other income in Note 4 rather than in net finance costs.

NOTES TO THE FINANCIAL STATEMENTS

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7. INCOME TAX EXPENSE

Numerical reconciliation between tax expense and pre-tax net profit

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Profit before tax	76,412	68,909
Income tax using the domestic corporation tax rate of 30% (2016: 30%)	22,924	20,673
Increase in income tax expense due to:		
Non-deductible expenses		
– Share based payment transactions	341	531
– Entertainment and other sundry items	279	286
– Dismantling costs	135	95
Other		
– Capital loss on sale of shares in associate	–	731
Decrease in income tax expense due to:		
Bad debt write-offs	–	(4,138)
Capital gain/(loss) on sales of business	128	(290)
Expenses paid in foreign jurisdictions	255	–
Effect of tax rate in foreign jurisdictions	4	(24)
Research and development benefit	(139)	(500)
	23,927	17,364
Adjustment for prior years		
Research and development benefit	221	–
Other	(107)	(125)
Income tax expense on pre-tax net profit	24,041	17,239

Recognised in the Income Statement

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Current tax expense		
Current year	25,279	13,553
Adjustments for prior years	(678)	404
	24,601	13,957
Deferred tax expense		
Current year-origination and reversal of temporary differences	(1,352)	3,811
Adjustment for prior years	792	(529)
	(560)	3,282
Total income tax expense in income statement	24,041	17,239

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

7. INCOME TAX EXPENSE (continued)

Deferred tax recognised in equity

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Relating to		
Derivatives	(64)	103
Defined benefit superannuation fund	10	14
Unrealised foreign exchange gains	90	100
	36	217

8. EARNINGS PER SHARE

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Profit attributable to ordinary shareholders	52,371	51,670
In thousands of shares		
Basic weighted average number of ordinary shares for the year	489,704	488,911
Effect of potential ordinary shares on issue	4,935	5,057
Diluted weighted average number of ordinary shares for the year	494,639	493,968
In cents		
Basic earnings per share	10.7	10.6
In cents		
Diluted earnings per share	10.6	10.5

9. TRADE AND OTHER RECEIVABLES

<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Current		
Trade receivables	685,630	678,959
Provision for impairment	(26,835)	(18,688)
	658,795	660,271
Other receivables and prepayments	22,825	29,424
	681,620	689,695
Non-current		
Trade receivables, non-current	20,486	10,136
Pension asset	701	746
	21,187	10,882

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

10. INVENTORIES

<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Raw materials and consumables	5,746	4,726
Work in progress	–	241
Finished goods	395,594	410,549
Provision for obsolescence and shrinkage	(1,996)	(1,734)
	399,344	413,782

During the year, inventories were reduced by \$1,500,000 (2016: \$1,221,000) as a result of the write-down to net realisable value. The write-downs were recognised as an expense during 2017.

11. SUMMARISED PARENT ENTITY FINANCIALS

<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Current assets	367,814	477,611
Total assets	1,046,048	923,256
Current liabilities	568,003	453,234
Total liabilities	598,856	500,359
Net assets	447,192	422,897
Equity		
Share capital	566,461	566,461
Reserves	6,484	5,191
Accumulated Losses	(190,383)	(190,383)
Profits reserve	64,630	41,628
Total equity	447,192	422,897
Profit after tax	57,310	20,725
Other comprehensive (loss)/ income	(22)	33
Total comprehensive income	57,288	20,758
Capital commitments of the parent entity at year end	95	635

Details of any guarantees and contingencies of the parent entity are included in Note 23.

12. CURRENT TAX ASSETS AND LIABILITIES

The current tax liability for the consolidated entity of \$16,899,000 (31 August 2016: \$13,359,000 current tax liability) represents the amount of income taxes payable in respect of current and prior financial years. In accordance with the Australian tax consolidation legislation, the Company as the head entity of the Australian tax consolidated group has assumed the current tax asset/liability initially recognised by the members in the Australian consolidated tax group.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

13. DEFERRED TAX ASSETS AND LIABILITIES

Recognised Deferred Tax Assets and Liabilities

Deferred tax assets and liabilities are attributable to the following:

Consolidated	Assets		Liabilities		Net	
	31 August 2017	31 August 2016	31 August 2017	31 August 2016	31 August 2017	31 August 2016
<i>In thousands of AUD</i>						
Property, plant and equipment	–	–	(7,150)	(7,279)	(7,150)	(7,279)
Unrealised foreign exchange losses	–	–	(26)	(93)	(26)	(93)
Employee benefits	6,726	8,272	–	(14)	6,726	8,258
Provisions	13,731	12,095	–	–	13,731	12,095
Derivatives	87	152	–	–	87	152
Other items	6,478	6,090	–	–	6,478	6,090
Tax assets/(liabilities)	27,022	26,609	(7,176)	(7,386)	19,846	19,223

Comprised of:

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Australia – net deferred tax asset	20,210	19,757
New Zealand - net deferred tax liability	(364)	(534)
	19,846	19,223

Movement in Deferred Tax

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Balance at 1 September	19,223	22,722
Recognised in income statement	560	(3,282)
Employee benefits transferred from store acquisitions	27	–
Recognised directly in equity	36	(217)
Balance as at 31 August	19,846	19,223

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

14. PROPERTY, PLANT AND EQUIPMENT

<i>In thousands of AUD</i>	Land and Buildings	Plant and Equipment	Leased Plant and Equipment	Capital Works in Progress	Total
Year ended 31 August 2017					
Opening net book value	5,210	88,232	3,889	2,798	100,129
Additions	–	2,121	–	24,374	26,495
Disposals	–	(2,513)	(210)	–	(2,723)
Depreciation charge for the year	(273)	(14,885)	(1,883)	–	(17,041)
Impairment reversal*	–	1,163	–	–	1,163
Reclassification of assets	57	10,081	–	(10,138)	–
Transfer of assets to intangibles	–	–	–	(12,244)	(12,244)
Effect of movement in foreign exchange	(199)	(207)	–	(93)	(499)
Closing net book amount	4,795	83,992	1,796	4,697	95,280
Comprised of:					
Cost	10,318	207,294	8,065	4,697	230,374
Accumulated depreciation	(5,523)	(123,302)	(6,269)	–	(135,094)

* As part of the annual impairment assessment of the property, plant and equipment, the Company determined that some previously impaired Priceline stores were no longer impaired due to improved trading results. Following this review, the excess impairment provision no longer required was reversed.

<i>In thousands of AUD</i>	Land and Buildings	Plant and Equipment	Leased Plant and Equipment	Capital Works in Progress	Total
Year ended 31 August 2016					
Opening net book value	5,239	88,906	4,801	3,000	101,946
Additions	–	88	–	20,579	20,667
Disposals	–	(1,775)	(62)	–	(1,837)
Depreciation charge for the year	(270)	(14,432)	(1,884)	–	(16,586)
Impairment gain	–	498	–	–	498
Reclassification of assets	–	14,689	1,034	(15,723)	–
Transfer of assets to intangibles	–	–	–	(5,128)	(5,128)
Effect of movement in foreign exchange	241	258	–	70	569
Closing net book amount	5,210	88,232	3,889	2,798	100,129
Comprised of:					
Cost	10,711	206,060	8,511	2,798	228,080
Accumulated depreciation	(5,501)	(117,828)	(4,622)	–	(127,951)

Financing costs are expensed in the income statement unless directly attributable to the acquisition of, or production of, a qualifying asset which are capitalised as part of the cost of that asset using the weighted average cost of borrowings.

NOTES TO THE FINANCIAL STATEMENTS

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15. INTANGIBLE ASSETS

<i>In thousands of AUD</i>	Goodwill	Brand Names	Software	Development Costs	Total
Year ended 31 August 2017					
Opening net book value	46,973	96,360	46,266	376	189,975
Transfer from property, plant and equipment	–	–	12,202	42	12,244
Other acquisitions*	3,917	–	–	–	3,917
Disposals	–	–	(3)	–	(3)
Amortisation for the year	–	–	(11,464)	(119)	(11,583)
Effect of movements in foreign exchange	(871)	–	(72)	52	(891)
Closing net book amount	50,019	96,360	46,929	351	193,659
Comprised of:					
Cost	106,379	99,000	112,759	1,225	319,363
Accumulated Amortisation	(56,360)	(2,640)	(65,830)	(874)	(125,704)

<i>In thousands of AUD</i>	Goodwill	Brand Names	Software	Development Costs	Total
Year ended 31 August 2016					
Opening net book value	45,979	96,360	51,104	250	193,693
Transfer from property, plant and equipment	–	–	4,920	208	5,128
Disposals	–	–	(3)	–	(3)
Amortisation for the year	–	–	(9,755)	(102)	(9,857)
Effect of movements in foreign exchange	994	–	–	20	1,014
Closing net book amount	46,973	96,360	46,266	376	189,975
Comprised of:					
Cost	103,333	99,000	101,724	1,175	305,232
Accumulated Amortisation	(56,360)	(2,640)	(55,458)	(799)	(115,257)

* Consists of goodwill arising upon acquisition of Priceline stores during the year.

Amortisation and Impairment Charge

The amortisation charge is recognised in administration and general expenses in the income statement.

Impairment tests for Cash Generating Units (CGU) containing Goodwill and Brand Names

The following cash generating units have goodwill and brand names with indefinite useful lives:

Goodwill

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Australia	33,673	29,757
New Zealand	16,346	17,216
	50,019	46,973

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

Brand names

<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Australia		
– Soul Pattinson brand name	37,500	37,500
– Priceline brand name	58,860	58,860
	96,360	96,360

The recoverable amount of each asset and CGU is determined based on a "value in use" calculation which uses cash flow projections based on earnings (i.e. EBITDA) covering a five-year period. Cashflow projections have been based on Board approved budgets and the Board endorsed five-year strategic plan. These forecasts use management estimates to determine income, expenses, working capital movements, capital expenditure and cashflows for each CGU. The projected cashflows for each CGU are discounted using an appropriate discount rate. The discount rate represents the pre-tax discount rate, risk adjusted to the post-tax weighted average cost of capital (WACC) applied to the cash flow projections and reflects the specific risks relating to the CGU. Cash flows beyond that five-year period have been extrapolated using long-term growth rate. The long-term growth rate is based on the Group's expectation of the CGUs' long-term performance in its market.

During the year, the Company reviewed the carrying value of the Australian and NZ CGU's. The recoverable amount for both CGU's continues to exceed the carrying value. Set out below are the key assumptions included in the review.

AUSTRALIA CGU

Assumption	Description
Budgeted EBITDA growth rate (average of next 5 years)	<p>The Budgeted EBITDA growth includes:</p> <ul style="list-style-type: none"> – Pharmaceutical distribution business growth reflects the Board approved financial plan and is based on recent history. – New store rollout estimates derived from the analysis by management of the likely net annual increase in stores in the five-year forecast period, based on recent past history, applications from prospective franchisees currently under consideration and the potential pool of new franchisees, after adjusting for the risks associated with execution of the strategic plan and the potential for loss of existing franchisees. The cash flow contribution from new stores is based on the estimates by management of net contribution from individual stores, including working capital, marketing and supply chain costs. – Comparable stores sales growth is based on management estimates and recent history of 3% for the period in FY18 to FY22.
Discount Rate	The discount rate of 14.4% represents the pre-tax discount rate applied to the cash flow projections, based on a market-determined, risk adjusted post-tax discount rate of 10.1%.
Terminal Growth rate	The terminal growth rate of 2.5% represents the growth rate applied to extrapolate cash flows beyond the five year forecast period. The terminal growth rate is based on management expectations of the CGU's long term performance after considering current conditions and available external market data.

NOTES TO THE FINANCIAL STATEMENTS

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15. INTANGIBLE ASSETS (continued)

NZ CGU

Assumption	Description
Budgeted annual sales and EBITDA growth rate (average of next 5 years)	The budgeted EBITDA growth rate includes: <ul style="list-style-type: none"> – Contracts entered into with new local and international customers, that will provide annual sales increases. – Leveraging and increasing synergies with the Australian business to achieve growth within the supply business.
Discount Rate	The discount rate of 15.7% represents the pre-tax discount rate applied to the cash flow projections, based on a market-determined, risk adjusted post-tax discount of 11.0%.
Terminal Growth rate	The terminal growth rate of 2.5% represents the growth rate applied to extrapolate cash flows beyond the five year forecast period. The growth rate is based on expectations of the CGU's long term performance.

Reasonably possible change

The impairment assessment for both CGUs, including sensitivity analysis on the key assumptions, did not result in any impairment being recognised. The recoverable amount of the NZ CGU assumes the achievement of annual sales growth targets in the period from FY18 to FY22. Holding all other assumptions constant, if actual annual sales growth was below targets by greater than 10%, this may result in an impairment of goodwill for the NZ CGU. A reasonably possible change in the discount rate, holding all other assumptions constant, would not result in an impairment for the NZ CGU.

16. TRADE AND OTHER PAYABLES

<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Current		
Trade payables	751,500	748,749
Accrued expenses and other payables	52,973	50,488
	804,473	799,237
Non-current		
Lease payable	7,903	8,436

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

17. LOANS AND BORROWINGS

This note provides information about the contractual terms of the interest-bearing loans and borrowings of the consolidated entity.

<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Current liabilities		
Insurance premium funding	1,608	1,457
Finance lease liabilities	1,157	1,521
	2,765	2,978
Non-current liabilities		
Finance lease liabilities	1,192	2,428
Securitisation of trade receivables	25,000	40,237
Cash advance facilities - secured	3,642	5,755
	29,834	48,420
Financing Facilities		
Bank overdraft - secured	8,732	8,877
Standby letters of credit	–	500
Cash advance facilities - secured	33,463	33,756
Securitisation of trade receivables	275,000	295,000
	317,195	338,133
Facilities utilised at reporting date¹		
Cash advance facilities - secured	3,642	5,755
Securitisation of trade receivables	25,000	40,237
	28,642	45,992
Facilities not utilised at reporting date²		
Bank overdraft - secured	8,732	8,877
Standby letters of credit	–	500
Cash advance facilities - secured	29,821	28,001
Securitisation of trade receivables	250,000	254,763
	288,553	292,141

1. Average used facilities during the year was \$171,509,399 (2016: \$ 205,041,989).

2. Average unused facilities during the year was \$146,155,209 (2016: \$ 169,554,786).

NOTES TO THE FINANCIAL STATEMENTS

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17. LOANS AND BORROWINGS (continued)

Bank Overdraft

The Company is a guarantor to a bank facility agreement which provides a total overdraft facility of \$8,732,000 (31 August 2016: \$8,877,000) to entities within the Group. The facility is subject to set off arrangements between companies within the consolidated entity. Interest on bank overdrafts is charged at prevailing market rates. The bank overdraft is repayable on demand and subject to annual review.

Finance Lease Facility

The lease liabilities of the consolidated entity are secured by the leased assets. In the event of default, the assets revert to the lessor.

Cash Advances

The consolidated cash advance facilities of \$33,463,000 (31 August 2016: \$33,756,058) are secured by way of fixed and floating charge over the assets of the consolidated entity. Interest is based on the bank-bill reference rate plus a margin charged by the lender.

Securitisation

Refer Note 21.

Classification of facilities

As at 31 August 2017, API has no intention to repay the securitisation facilities prior to the termination date on the facilities of 1 May 2020. As such, in accordance with accounting standards, the debt drawn on API's securitisation facilities have been classified entirely as non-current liabilities.

Finance Lease Liabilities

Finance lease liabilities of the consolidated entity are payable as follows:

<i>In thousands of AUD</i>	Minimum Lease Payments 31 August 2017	Interest 31 August 2017	Principal 31 August 2017	Minimum Lease Payments 31 August 2016	Interest 31 August 2016	Principal 31 August 2016
Less than one year	1,266	109	1,157	1,730	209	1,521
Between one and five years	1,252	60	1,192	2,618	190	2,428
	2,518	169	2,349	4,348	399	3,949

The consolidated entity leases plant and equipment under finance leases expiring within five years. At the end of the lease term the consolidated entity has the option to purchase the leased equipment.

Under the terms of the lease agreements no contingent rents are payable.

18. EMPLOYEE BENEFITS

Current

<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Short-term incentive payments	438	4,050
Liability for long service leave	7,247	7,142
Liability for annual leave	11,304	11,210
	18,989	22,402
Non-current		
Liability for long service leave	3,834	5,339

NOTES TO THE FINANCIAL STATEMENTS

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a. Defined Benefit Plan

The consolidated entity makes contributions to a defined benefit superannuation fund that provides defined benefit amounts for employees upon retirement.

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Fair value of fund assets - funded	1,629	1,506
Present value of funded obligations	(928)	(760)
Present value of net fund assets	701	746

Movements in the net asset for defined benefit obligations recognised in the balance sheet

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Net defined benefit asset at beginning of the year	746	742
Contributions received	52	18
Gains allocated to Other Comprehensive Income	(32)	47
Expense recognised in the income statement	(65)	(61)
Net defined benefit asset at end of the year	701	746

b. Defined Contribution Superannuation Funds

In addition to the contributions to the defined benefit plan outlined above, the consolidated entity makes contributions to various defined contribution superannuation funds. The amount recognised as an expense was \$13,882,000 for the year ended 31 August 2017 (31 August 2016: \$13,084,000).

c. Share Based Payments

Share performance rights

The consolidated entity granted equity settled performance rights that entitle key management personnel and senior employees to receive shares in the Company if defined performance conditions are achieved.

On 16 December 2014, performance rights (the 2014 grant) were granted with a performance period commencing 1 September 2014 and ending 31 August 2017. Vesting was subject to an aggregate Return on Equity (ROE) hurdle and an Earnings Per Share (EPS) Compound Annual Growth Rate (CAGR). The performance conditions were tested and audited with the following outcomes:

- actual aggregate ROE for the performance period was 28.26% for an achievement of 61.22% of half the grant; and
- actual CAGR EPS was 36.96% for an achievement of 100% of the other half of the grant.

The combined achievement of the 2014 LTIP for performance measured over a 3 year period resulted in 80.6% of the total grant vesting.

On 13 January 2016, performance rights (the 2015 grant) were granted with a performance period commencing 1 September 2015 and ending 31 August 2018. The performance conditions, being ROE and EPS for the exercise of performance rights will be assessed by the Remuneration Committee and the Board following the 31 August 2018 year end.

On 1 February 2017, performance rights (the 2016 grant) were granted with a performance period commencing 1 September 2016 and ending 31 August 2019. The performance conditions, being ROE and EPS for the exercise of performance rights will be assessed by the Remuneration Committee and the Board following the 31 August 2019 year end.

Performance conditions will be tested once only, and any performance rights that do not meet the performance conditions will lapse and will not be re-tested.

NOTES TO THE FINANCIAL STATEMENTS

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18. EMPLOYEE BENEFITS (continued)

The terms and conditions of the grants at 31 August 2017 are as follows. All performance rights are settled by physical delivery of shares:

Grant date/ employee entitled	Number of instruments	Vesting conditions	Contractual life of Performance Rights
Performance rights to key management personnel and senior employees - Performance period to Aug 2017	2,970,348	Three years of service. Cumulative ROE with a minimum of 21.38% achievement permitting exercise of 20% of the rights subject to the ROE Performance Condition and 34.74% achievement to exercise 100% of the rights subject to the ROE Performance Condition and proportionate between these two levels. Compound Annual Growth Rate (CAGR) of EPS with a minimum of 7.5% achievement permitting exercise of 20% of the rights subject to the EPS Performance Condition and 10.0% achievement to exercise 100% of the rights subject to the EPS Performance Condition and proportionate between these two levels.	3 years
Performance rights to key management personnel and senior employees - Performance period to Aug 2018	1,103,290	Three years of service. Cumulative ROE with a minimum of 25.07% achievement permitting exercise of 20% of the rights subject to the ROE Performance Condition and 40.74% achievement to exercise 100% of the rights subject to the ROE Performance Condition and proportionate between these two levels. Compound Annual Growth Rate (CAGR) of EPS with a minimum of 7.5% achievement permitting exercise of 20% of the rights subject to the EPS Performance Condition and 10.0% achievement to exercise 100% of the rights subject to the EPS Performance Condition and proportionate between these two levels.	3 years
Performance rights to key management personnel and senior employees - Performance period to Aug 2019	924,512	Three years of service. Cumulative ROE with a minimum of 26.96% achievement permitting exercise of 20% of the rights subject to the ROE Performance Condition and 43.81% achievement to exercise 100% of the rights subject to the ROE Performance Condition and proportionate between these two levels. Compound Annual Growth Rate (CAGR) of EPS with a minimum of 7.5% achievement permitting exercise of 20% of the rights subject to the EPS Performance Condition and 10.0% achievement to exercise 100% of the rights subject to the EPS Performance Condition and proportionate between these two levels.	3 years
4,998,150			

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

The number of performance rights outstanding in the year is as follows:

<i>In thousands of Performance Rights</i>	Number of Performance Rights 31 August 2017	Number of Performance Rights 31 August 2016
Outstanding at the beginning of the year	4,074	6,196
Forfeited/lapsed during the year	–	(3,225)
Exercised during the year	–	–
Granted during the year	924	1,103
Outstanding at the end of the year	4,998	4,074
Exercisable at the end of the year	–	–

Fair value of performance rights and assumptions	Key Management Personnel and Senior Managers 31 August 2017	
Performance period commences and performance conditions	1 Sept 2016 EPS/ROE	1 Sept 2015 EPS/ROE
Grant date	1 Feb 17	13 Jan 16
Fair value at measurement date	\$1.68	\$1.82
Share price	\$1.87	\$1.98
Expected volatility (expressed as weighted average)	35%	40%
Performance Rights life (expressed as weighted average life)	3yrs	3yrs
Expected dividends	4.0%	3.0%
Risk-free interest rate (based on Federal Government bonds)	1.93%	1.98%

The expected volatility is based on the historic volatility (calculated based on the weighted average expected life of the share performance rights), adjusted for any expected changes to future volatility due to publicly available information.

Share performance rights are granted under a service condition and, for grants to key management personnel and Executives market and non-market performance conditions apply. Non-market performance conditions are not taken into account in the grant date fair value measurement of the services received.

Executive Short Term Incentive Plan

The short term incentive plan (STIP) for Executives of the Group is designed to drive key performance measures aligned to strategy and financial objectives. For STIP performance scorecard measures established after 1 September 2012, 50% of any resulting STIP payment is converted from cash to rights to acquire API shares and is deferred for 12 months to encourage employee retention. It is also designed to manage risk by ensuring that decisions taken in the previous reporting period have resulted in sustainable benefit for the consolidated entity. Further details of the STIP are set out in the Remuneration Report.

NOTES TO THE FINANCIAL STATEMENTS

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18. EMPLOYEE BENEFITS (continued)

Set out below is a summary of the performance rights granted under the STIP:

Grant Date	Value at Grant Date	Balance at start of the year	Granted during the year	Exercised during the year	Forfeited during the year	Balance at end of the year	Vested at end of the year
2015							
21 Oct 15	\$1.83	983,725	–	(971,477)	(12,248)	–	971,477
2016							
7 Nov 16	\$1.90	–	512,718	–	–	512,718	–

Performance rights are valued on a volume weighted average closing price of API shares on the ASX in the 10-day period after announcement of full year results. The vesting period for 2014 grant of performance rights commenced on 1 September 2013, the vesting period for the 2015 grant of performance rights commenced on 1 September 2014 and the vesting period for the 2016 grant of performance rights commenced on 1 September 2015.

Employee Expenses

Total expenses arising from share-based payment transactions attributable to employees recognised during the period as part of total share-based payment expenses are as follows:

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Performance rights granted in 2013 – equity settled	–	(918)*
Performance rights granted in 2014 – equity settled	231	659
Performance rights granted in 2015 – equity settled	399	661
Performance rights granted in 2016 – equity settled	518	–
Deferred component 2014 – STIP program	–	–
Deferred component 2015 – STIP program	–	900
Deferred component 2016 – STIP program	488	488
Total expense recognised as employee costs	1,636	1,790

* Reflects the reversal of expenses previously recognised for performance rights forfeited.

19. PROVISIONS

<i>In thousands of AUD</i>	Directors' retirement scheme	Provision for dismantling	Provision for onerous leases	Provision for Loyalty Programs	Total
Balance at 1 September 2016	351	5,082	68	6,808	12,309
Provisions made during the year	–	2,793	–	24,672	27,465
Provisions used during the year	–	(116)	(68)	(21,627)	(21,811)
Provision reversed during the year	–	(3,519)	–	(2,829)	(6,348)
Unwind of discount	–	154	–	–	154
Balance at 31 August 2017	351	4,394	–	7,024	11,769
Current	–	883	–	7,024	7,907
Non-current	351	3,511	–	–	3,862
	351	4,394	–	7,024	11,769

NOTES TO THE FINANCIAL STATEMENTS

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Directors' Retirement Scheme

Retirement benefits for non-executive Directors are included on an accrual basis. The benefits are to be paid on a pro-rata basis up to 10 years service to a maximum of three times the average annual remuneration in the three years preceding retirement. The retirement benefit is capped at \$220,000 per Director and applies only to Directors appointed prior to 9 September 2003. On 31 August 2009 the Directors agreed to freeze this benefit.

Dismantling

The consolidated entity provides for the estimated costs to cover its obligations to lessors to restore premises to the condition that existed when leases of real property were entered.

Loyalty Programs

Consists of the provision for Sister Club points which can be converted quarterly by customers in the form of gift vouchers. The provision is based upon the expected cost to the consolidated entity on redemption of Sister Club vouchers. A redemption rate is applied based on historical experience and is updated quarterly.

20. CAPITAL AND RESERVES

Share capital

<i>In thousands of shares</i>	Ordinary shares	
	31 August 2017	31 August 2016
Shares on issue at the beginning of the year - fully paid	489,097	488,116
Shares issued as a consequence of the Company's 2015 Short Term Incentive Plan (31 August 2016: 2014 Short Term Incentive Plan)	703	981
Shares on issue at the end of the year - fully paid	489,800	489,097

Ordinary shares

The Company does not have authorised capital or par value in respect of its issued shares. All issued shares are fully paid. Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders meetings. In the event of a winding up of the Company, ordinary shareholders rank after all other creditors and are fully entitled to any proceeds of liquidation.

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations where their functional currency is different to the presentation currency of the reporting entity.

Equity reserve

The equity reserve relates to share-based payment transactions measured at fair value.

Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments relating to hedged transactions that have not yet occurred.

Dividends

During the year the Company recognised the following dividends:

On 9 December 2016 a final dividend of \$17,143,023 in respect of the year ended 31 August 2016 was paid out of the Profits Reserve. It was at the rate of 3.5 cents per share, fully franked.

An interim dividend (paid out of the Profits Reserve) in respect of the half year ended 28 February 2017 amounting to \$17,143,023 paid on 2 June 2017. It was at the rate of 3.5 cents per share, fully franked.

On 18 October 2017 a final dividend of 3.5 cents per share (payable out of the Profits Reserve), fully franked to be paid on 8 December 2017, amounting to \$17,143,023 was declared.

NOTES TO THE FINANCIAL STATEMENTS

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20. CAPITAL AND RESERVES (continued)

Dividend Franking Account

<i>In thousands of AUD</i>	The Company	
	31 August 2017	31 August 2016
Franking credits available at 30 percent to shareholders of the Company for subsequent financial years	52,943	42,960

The above available amounts are based on the balance of the dividend franking account at year-end adjusted for the following:

- Franking credits that will arise from the payment of the current tax liabilities;
- Franking debits that will arise from the payment of dividends recognised as a liability at the year end;
- Franking credits that will arise from the receipt of dividends recognised as receivables by the tax consolidated group at the year end;
- Franking credits that the entity may be prevented from distributing in subsequent years; and
- Franking debits that will arise from receipt of the current income tax receivable.

The ability to utilise the franking credits is dependent upon there being sufficient available profits to declare dividends. The future reduction in the dividend franking account of dividends proposed after the balance sheet date but not recognised as a liability at year end is \$7,347,006 (31 August 2016: \$6,861,590).

21. FINANCIAL INSTRUMENTS

Financial Risk Management

Overview

The consolidated entity has exposure to the following risks from its use of financial instruments:

- Credit risk;
- Liquidity risk; and
- Market risk.

The Board has overall responsibility for the establishment and oversight of the risk management framework of the consolidated entity. The Board has established the Audit and Risk Committee ("Committee"), a sub-committee of the Board, which is responsible for developing and monitoring the risk management policies. The Committee reports regularly to the Board on its activities.

The risk management policies are established to identify and analyse the risks faced by the consolidated entity, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the activities of the consolidated entity.

The Committee oversees the monitoring of compliance with the risk management policies and procedures by management and reviews the adequacy of the risk management framework in relation to the risks. The Committee is assisted in its oversight by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Committee.

Credit risk

Credit risk is the risk of financial loss to the consolidated entity if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the receivables from customers and financial guarantees.

Trade and other receivables

The exposure to credit risk is mainly influenced by the individual characteristics of each customer.

The consolidated entity has established a credit policy under which new customers are analysed individually for credit worthiness including using external ratings, where available. Purchase limits are established for each customer, which represents the maximum open amount available and limits are reviewed on an "as needs" basis. Customers that fail to meet the benchmark credit worthiness may transact with the consolidated entity on a prepayment basis.

NOTES TO THE FINANCIAL STATEMENTS

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In monitoring customer credit risk, customers are grouped by state and reviewed monthly. "High risk" customers are placed on "credit hold", with orders manually released as appropriate.

Goods sold under some customer arrangements are subject to retention of title clauses, so that in the event of non-payment the consolidated entity may have a secured claim in respect of the goods sold.

The consolidated entity establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables and investments. The main component of this allowance is a specific loss component that relates to individually significant exposures (after consideration of any collateral or security held).

Guarantees

Financial guarantees are initially recognised at fair value. The fair value is amortised as an expense through the income statement over the life of the guarantee. Subsequent to initial measurement, the guarantee is measured at the higher of the amortised balance of the guarantee or the value of the guarantee determined in accordance with AASB 137 Provisions, Contingent Liabilities and Contingent Assets.

Liquidity risk

Liquidity risk is the risk that the consolidated entity will not be able to meet its financial obligations as they fall due. The approach to managing liquidity is to ensure, as far as possible, that there will always be sufficient liquidity to meet liabilities when due, under both normal and stressed conditions.

The consolidated entity has varying borrowing levels based on seasonal requirements of the business. Any obligations can be met by the unused facilities.

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates, will affect the income of the consolidated entity or the value the financial instruments held by the consolidated entity. The objective of market risk management is to manage and monitor market risk exposures within acceptable parameters, whilst optimising the return on risk.

Currency risk

The consolidated entity had no material exposure to foreign currency risk on sales and purchases that are denominated in a currency other than the respective functional currencies of the consolidated entity companies.

Interest rate risk

The consolidated entity is exposed to interest rate risk as a consequence of its financing facilities. The consolidated entity adopts a policy that up to 85% of its exposure to the changes in interest rates on its long term variable rate borrowings relating to the securitised trade receivables may be hedged on a fixed rate basis. At 31 August 2017, the consolidated entity had interest rate swaps with a notional contract amount of \$25,000,000, with a maturity date of December 2017 and fixed rate of 2.65%.

The consolidated entity classifies interest rate swaps as cash flow hedges. The notional contracted interest cash flows are consistent with highly probable forecast interest cash flows to December 2017 based on the forecast of used facilities for the securitised trade receivables.

Capital Management

The policy of the Board is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business.

The Board seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position.

There were no changes in the approach of the consolidated entity to capital management during the year.

Securitisation

The consolidated entity has access to funds as a result of the securitisation of current trade receivables provided the receivables meet certain criteria. The \$275 million facility is allocated into an overdraft facility of \$100 million available to repay and redraw on a daily basis and a term facility of \$175 million. As part of the program, the program provider charges a monthly variable interest rate plus margin based on the drawn down portion of the program. As at 31 August 2017 the weighted average rate was 3.51% (31 August 2016: 3.98%).

The funds able to be drawn down under securitisation facility are limited to the existence of qualifying trade receivables at the time of drawdown which may be less than the unutilised amount otherwise available under the facility (set out in Note 17). The trade receivables are collateralised in full against amounts drawn down.

The facility imposes rights and obligations on the consolidated entity with respect to the quality and maintenance of the receivables, collection of receivables, settlement and reporting to the financier. The consolidated entity has complied with its obligations under the facility throughout the financial year.

At 31 August 2017, \$25,000,000 was drawn down on the program by the consolidated entity (31 August 2016: \$40,237,064). The trade receivables and loans and borrowings relating to these transactions are recognised in the statement of financial position.

NOTES TO THE FINANCIAL STATEMENTS

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21. FINANCIAL INSTRUMENTS (continued)

Credit Risk

Exposure to credit risk

The exposure to credit risk of the consolidated entity as at the reporting date was in relation to the carrying amounts of current and non-current trade receivables (Note 9), other receivables (Note 9), and cash deposits.

Concentrations of credit risk

Concentrations of credit risk arise from customers that have similar characteristics and are affected in a similar manner when there are changes in economic, regulatory, or other conditions. In this regard, the economic entity has a significant concentration of credit risk associated with the pharmacy and retail industries in Australia.

Trade Receivables

Details of the ageing of Trade Receivables and the impairment losses at the reporting date are set out below:

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Not past due	594,649	624,507
Past due 0-30 days	32,468	26,736
Past due 31+ days	58,513	27,716
Sub-total	685,630	678,959
Impairment	(26,835)	(18,688)
	658,795	660,271

The movement in the provision for impairment losses in respect of Trade Receivables was as follows:

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Balance at start of year	18,688	13,482
Amounts provided during the year	10,716	9,709
Amounts written off during the year	(2,569)	(4,503)
Balance at end of year	26,835	18,688

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

Liquidity Risk

The following are the contractual maturities of financial liabilities, including interest payments and excluding the impact of netting arrangements.

<i>In thousands of AUD</i>	Carrying Amount	Contract Cash Flows	1 year or less	1–2 years	2–5 years	More than 5 years
31 August 2017						
Non-derivative financial liabilities						
Finance lease liabilities	2,349	2,518	1,266	1,212	40	–
Insurance premium funding	1,608	1,608	1,608	–	–	–
Trade and other payables	812,376	812,376	804,473	646	3,357	3,900
Cash Advance facility	3,642	3,642	–	3,642	–	–
	819,975	820,144	807,347	5,500	3,397	3,900
31 August 2016						
Non-derivative financial liabilities						
Finance lease liabilities	3,949	4,348	1,730	1,240	1,378	–
Insurance premium funding	1,457	1,457	1,457	–	–	–
Trade and other payables	807,673	807,673	799,237	1,284	3,641	3,511
Cash Advance facility	5,755	5,755	–	–	5,755	–
	818,834	819,233	802,424	2,524	10,774	3,511

Cash Flow Hedges

The only financial assets or financial liabilities carried at fair value are derivative financial instruments designated as cash flow hedges. The Company considers the derivatives to be Level 2 financial instruments because, unlike Level 1 financial instruments, their measurement is derived from inputs other than quoted prices that are observable for the assets or liabilities, either directly (as prices) or indirectly (derived from prices). There have been no transfers between levels 1, 2 and 3 for recurring fair value measurements during the year. The derivative fair values have been obtained from third party valuations derived from forward interest rates at the reporting date.

The fair value of the derivatives designated as cash flow hedges at 31 August 2017 was a net liability of \$291,803 (31 August 2016: liability of \$504,090).

The following table indicates the periods in which the cash flows and profit and loss impact associated with derivatives that were designated as cash flow hedges existing as at balance date are expected to occur.

<i>In thousands of AUD</i>	31 August 2017						
	Carrying Amount	Expected Cash Flows	6 months or less	6–12 months	1–2 years	2–5 years	More than 5 years
Consolidated and the Company							
Interest Rate Swap-Liability	(130)	(130)	(83)	–	(47)	–	–
Foreign Exchange Forward-Asset	(162)	(162)	(162)	–	–	–	–
31 August 2016							
Consolidated and the Company	Carrying Amount	Expected Cash Flows	6 months or less	6–12 months	1–2 years	2–5 years	More than 5 years
Interest Rate Swap-Liability	(519)	(519)	(382)	–	(137)	–	–
Foreign Exchange Forward-Asset	15	15	15	–	–	–	–

NOTES TO THE FINANCIAL STATEMENTS

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21. FINANCIAL INSTRUMENTS (continued)

Interest Rate Risk

Effective Interest Rates and Repricing Analysis

In respect of income-earning financial assets and interest-bearing financial liabilities, the following table indicates their effective interest rates for each at reporting date and the periods in which each of the assets and liabilities reprice.

Consolidated		31 August 2017						31 August 2016					
In thousands of AUD	Note	Effective interest rate	Total	1 year or less	1-2 years	2-5 years	More than 5 years	Effective interest rate	Total	1 year or less	1-2 years	2-5 years	More than 5 years
Cash and cash equivalents	26	0.98%	39,776	39,776	-	-	-	1.03%	25,489	25,489	-	-	-
Restricted cash (Aspire cash reserve)	9	-	-	-	-	-	-	1.60%	4,895	4,895	-	-	-
Trade receivables, non current*	9	9.28%	20,241	-	14,244	5,997	-	12.0%	9,991	7,730	2,261	-	-
Securitised trade receivables	17	3.51%	(25,000)	-	-	(25,000)	-	3.98%	(40,237)	-	-	(40,237)	-
Finance lease liabilities*	17	7.57%	(2,349)	(1,157)	(1,152)	(40)	-	6.66%	(3,949)	(1,521)	(1,126)	(1,302)	-
Bank overdrafts and cash advance facility	17	4.29%	(3,642)	-	(3,642)	-	-	5.66%	(5,755)	-	-	(5,755)	-
Insurance premium funding*	17	3.51%	(1,608)	(1,608)	-	-	-	3.98%	(1,457)	(1,457)	-	-	-
			27,418	37,011	9,450	(19,043)	-		(11,023)	35,136	1,135	(47,294)	-

* Fixed rate income earning financial assets and interest bearing financial liabilities. Remaining balances are variable rates.

Fair value sensitivity analysis for fixed rate instruments

The consolidated entity does not account for any fixed rate financial assets and liabilities at fair value through profit and loss, and the consolidated entity does not designate derivatives (interest rate swaps) as hedging instruments under a fair value hedge accounting model. Therefore a change in interest rates at reporting date would not affect profit and loss unless any hedges became ineffective.

NOTES TO THE FINANCIAL STATEMENTS

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Cash flow sensitivity analysis for variable rate instruments

A strengthening by 100 basis points in interest rates at the reporting date would have increased (or in the event of a commensurate weakening, decreased) profit or loss and equity (pre-tax) at the end of the reporting period by the amounts shown below. This analysis assumes that all other variables remain constant.

<i>In thousands of AUD</i>	Profit/(loss)		Equity	
	100bp increase	100bp decrease	100bp increase	100bp decrease
31 August 2017				
Interest rate swap	–	–	79	(79)
Cash flow sensitivity (net)	–	–	79	(79)
31 August 2016				
Interest rate swap	–	–	455	(455)
Cash flow sensitivity (net)	–	–	455	(455)

Fair values

The fair values of financial assets and liabilities are not materially different from the carrying amounts shown in the balance sheet.

Estimation of Fair Values

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the table.

Loans and Borrowings

Fair value is calculated based on discounted expected future principal and interest cash flows.

Finance Lease Liabilities

The fair value is estimated as the present value of future cash flows, discounted at market interest rates for homogeneous lease agreements. The estimated fair values reflect change in interest rates.

Trade and other Receivables/Payables

For receivables/payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value. All other receivables/payables are discounted to determine the fair value.

Interest rates used for determining fair value

The entity uses the Government yield curve at the end of the reporting period, plus an adequate constant credit spread, to discount financial instruments. The interest rates used are as follows:

	31 August 2017	31 August 2016
Loans and borrowings	3.5%–4.5%	4.0%–6.0%
Leases	7%–8%	6.0%–7.0%
Receivables	Nil	Nil

NOTES TO THE FINANCIAL STATEMENTS

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22. COMMITMENTS

Operating Leases – Leases as Lessee

Non-cancellable operating lease rentals are payable as follows:

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Less than one year	42,301	47,828
Between one and five years	97,033	103,345
More than five years	36,417	26,251
	175,751	177,424

The consolidated entity leases property and plant under non-cancellable operating leases expiring from two to fifteen years. Leases generally provide the consolidated entity with a right of renewal at which time all terms are renegotiated. During the year ended 31 August 2017, \$67,231,409 was recognised by the consolidated entity as an expense in the profit and loss in respect of operating leases and other related occupancy costs (31 August 2016: \$64,345,429).

Certain leases are subject to contingent rental clauses calculated as a percentage of revenue earned in excess of pre-determined thresholds set out in the lease agreements. The consolidated entity recognises these amounts as an expense in the period where it is anticipated these thresholds will be reached.

With certain franchise arrangements, the consolidated entity continues to hold the head lease and recharges the franchisee the rental charge at arm's length. For those leases, the franchisee is invoiced in advance and offset against the rental charge from the landlord.

Capital Expenditure Commitments

<i>In thousands of AUD</i>	31 August 2017	31 August 2016
Contracted but not provided for or payable:	446	1,636

23. CONTINGENT LIABILITIES

Contingent liabilities

The Directors are of the opinion that provisions are not required in respect of these matters, as it is not probable that a future sacrifice of economic benefits will be required or the amount is not capable of reliable measurement.

<i>In thousands of AUD</i>		Consolidated		The Company	
		31 August 2017	31 August 2016	31 August 2017	31 August 2016
Guarantee of bank facilities to controlled entities	(i)	–	–	–	8,632
Financial guarantees to pharmacists	(i)	10,459	19,243	10,459	19,243

(i) Guarantees relate to the parent entity.

The parent entity has entered into a deed of cross guarantee with the effect that Australian Pharmaceuticals Industries Limited guarantees debts in respect of its subsidiaries.

Further detail of the Deed of Cross Guarantee and the nominated subsidiaries subject to the deed are disclosed in Note 25. Financial guarantees of \$10,459,000 (2016: \$19,243,000) have been provided to financial institutions of individual debtors and debtor groups. The consolidated entity has strict controls over the approval of guarantees of pharmacy customers and takes security over the assets of the relevant pharmacy. The Directors are of the opinion that provisions are not required in respect of these guarantees, as it is not probable that the exposure is greater than the value of the security over the assets of the relevant pharmacy.

NOTES TO THE FINANCIAL STATEMENTS

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24. CONSOLIDATED ENTITIES

	Note	Ownership interest	
		31 August 2017	31 August 2016
Parent Entity			
Australian Pharmaceutical Industries Limited			
Subsidiaries			
API Services Australia Pty Ltd		100	100
Australian Pharmaceutical Industries (Queensland) Pty Limited	(ii)	100	100
API Victoria Pty Limited	(ii)	100	100
Soul Pattinson (Manufacturing) Pty Limited		100	100
API Financial Services Australia Pty Limited	(ii)	100	100
Pharma-Pack Pty Limited		100	100
API (Canberra) Pty Limited		100	100
Canberra Pharmaceutical Supplies Trust		100	100
Stevens KMS Equities Limited	(i)	100	100
API Healthcare Holdings (NZ) Limited	(i)	100	100
Priceline (NZ) Pty Ltd	(i)	100	100
PAF (New Zealand) Ltd	(i)	100	100
The Medicine Shoppe Limited	(i)	100	100
PSM Healthcare Limited	(i)	100	100
Pharmaceutical Sales and Marketing Ltd	(i)	100	100
Garrett Investments Limited	(i)	100	100
Healthcare Manufacturing Group Limited	(i)	100	100
Synapse Finance Pty Ltd	(ii)	100	100
New Price Retail Finance Pty Ltd	(ii)	100	100
New Price Retail Pty Ltd		100	100
New Price Retail Services Pty Ltd		100	100
Priceline Proprietary Limited	(ii)	100	100
Priceline Unit Trust		100	100
Second Priceline Unit Trust		100	100
Making Life Easy – Mobility and Independent Living Superstores Pty Ltd		100	100
MLE Unit Trust		100	100

(i) These controlled entities are incorporated in New Zealand and carry on business predominantly in New Zealand. All other controlled entities are incorporated and carry on business predominantly in Australia.

(ii) These controlled entities have each entered into a Deed of Cross Guarantee with Australian Pharmaceuticals Industries Limited in respect of relief granted from specific accounting and financial reporting requirements in accordance with ASIC Corporations (Wholly owned Companies) Instrument 2016/785.

All subsidiaries have a balance date equivalent to the parent entity.

NOTES TO THE FINANCIAL STATEMENTS

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25. DEED OF CROSS GUARANTEE

Pursuant to ASIC Corporations (Wholly owned Companies) Instrument 2016/785, the wholly-owned subsidiaries listed below are relieved from the Corporations Act 2001 requirements for preparation, audit and lodgement of financial reports, and Directors reports.

It is a condition of the Class Order that the Company and each of the controlled entities (the "Closed Group") enter into a Deed of Cross Guarantee. The effect of the Deed is that the Company guarantees to each creditor payment in full of any debt in the event of winding up of any of the subsidiaries under certain provisions of the Corporations Act 2001. If a winding up occurs under other provisions of the Act, the Company will only be liable in the event that after six months any creditor has not been paid in full. The controlled entities have also given similar guarantees in the event that the Company is wound up.

The controlled entities subject to the Deed are:

- API Financial Services Australia Pty Ltd;
- API Victoria Pty Ltd;
- Australian Pharmaceutical Industries (Queensland) Pty Ltd;
- New Price Retail Finance Pty Ltd;
- Priceline Pty Ltd; and
- Synapse Finance Pty Ltd

The Statement of comprehensive income, retained profits and reserve and the Statement of financial position of the Closed Group, after eliminating all transactions between members of the Closed Group, at 31 August 2017 is set out as follows:

Summarised Statement of Comprehensive Income, Retained Profits and Reserves

<i>In thousands of AUD</i>	Closed Group	
	Year ended 31 August 2017	Year ended 31 August 2016
Profit before tax	76,519	37,854
Income tax expense	(17,143)	(6,794)
Profit after tax	59,376	31,060
Other comprehensive income	149	240
Total comprehensive income for the year	59,525	31,300
Accumulated losses at beginning of the year	(120,516)	(120,516)
Profit after tax	-	-
Accumulated losses at end of the year attributable to equity holders	(120,516)	(120,516)
Reserves at beginning of the year	15,184	6,491
Profits reserve	59,376	31,060
Dividend paid out of profits reserve	(34,286)	(24,430)
Other comprehensive income	149	240
Remeasurements of Defined Benefit Liability, net of tax	(22)	33
Share based payment transactions	1,143	1,790
Reserves at the end of the year attributable to equity holders	41,544	15,184

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

Summarised Statement of Financial Position

<i>In thousands of AUD</i>	Closed Group	
	As at 31 August 2017	As at 31 August 2016
Assets		
Cash and cash equivalents	32,878	13,705
Trade and other receivables	677,181	605,148
Inventories	296,083	316,120
Total current assets	1,006,142	934,973
Trade and other receivables	48,150	37,342
Investments	133,530	134,757
Deferred tax assets	1,300	3,359
Property, plant and equipment	48,980	51,884
Intangible assets	111,241	109,289
Total non-current assets	343,201	336,631
Total assets	1,349,343	1,271,604
Liabilities		
Trade and other payables	794,962	725,920
Loans and borrowings	1,978	2,408
Employee benefits	11,380	14,830
Provisions	90	68
Income tax payable	16,807	13,445
Total current liabilities	825,217	756,671
Trade and other payables	5,466	5,795
Loans and borrowings	25,365	40,862
Employee benefits	2,353	3,018
Provisions	3,453	4,129
Total non-current liabilities	36,637	53,804
Total liabilities	861,854	810,475
Net assets	487,489	461,129
Equity		
Share capital	566,461	566,461
Reserves	6,482	5,190
Profit reserves	35,062	9,994
Accumulated losses	(120,516)	(120,516)
Total equity	487,489	461,129

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

26. RECONCILIATION OF CASH FLOWS FROM OPERATING ACTIVITIES

<i>In thousands of AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Cash Flows from Operating Activities		
Profit for the year	52,371	51,670
<i>Adjustments for:</i>		
Depreciation	17,041	16,586
Amortisation	11,583	9,857
Reversal of impairment loss on property, plant and equipment	(1,163)	(498)
Foreign exchange loss	67	369
Loss in divestment of associates	–	2,437
Net (gain)/loss on sale of stores, property, plant and equipment	615	(292)
Equity-settled share-based payment expenses	1,636	1,790
Net finance cost	12,864	15,785
Income tax expense	24,041	17,239
Operating profit before changes in working capital and provisions	119,055	114,943
Increase in trade and other receivables	(2,315)	(77,946)
Decrease/(increase) in inventories	14,438	(49,576)
Increase in trade and other payables	4,655	133,008
Decrease in provisions and employee benefits	(6,021)	(23,768)
	129,812	96,661
Net interest paid	(13,301)	(15,717)
Income taxes refunded/(paid)	(21,029)	1,913
Net Cash from Operating Activities	95,482	82,857
<i>In thousands of AUD</i>	As at 31 August 2017	As at 31 August 2016
Cash at bank	39,776	25,489
Cash and cash equivalents in the statement of cash flows	39,776	25,489

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

27. RELATED PARTIES

Key management personnel compensation

The key management personnel compensation included in 'Personnel Expenses' is as follows:

<i>In AUD</i>	Year ended 31 August 2017	Year ended 31 August 2016
Short-term employee benefits	2,385,786	3,214,233
Other long term employee benefits	248,685	157,201
Final payouts	986,988	–
Share based payments	904,026	914,055
	4,525,485	4,285,489

Individual Directors and Executives compensation disclosures

Information regarding individual Directors and Executives' compensation and some equity instruments disclosures as required by Corporations Act S300A and Corporations Regulations 2M.3.03 are provided in the Remuneration Report section of the Directors' Report.

Apart from the details disclosed in this note, no Director has entered into a material contract with the Company or the consolidated entity since the end of the previous financial year and there were no material contracts involving Directors' interests existing at year-end.

Other Key Management Personnel transactions with the Company or its Controlled Entities

Certain Directors of the Company are directors of companies that have entered into transactions with the Company and its controlled entities during the financial year. These transactions may include purchasing of inventories from the Company or its controlled entities. All transactions with the Directors and the companies they represent are on the same terms and conditions as those entered into by other entities, employees or customers and are trivial or domestic in nature.

No shares were granted during the period to Directors.

Mr R D Millner is a Director of Washington H Soul Pattinson and Company Limited. Washington H Soul Pattinson and Company Limited holds 95,068,472 shares (31 August 2016: 120,214,969 shares) in the Company at year end 31 August 2017.

During the year, further performance rights were issued by the Company to key management personnel and certain Executives. Share rights forfeited by and issued to key management personnel have been disclosed in the Remuneration Report contained within the Directors' Report of this report.

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

28. AUDITORS' REMUNERATION

<i>In AUD</i>	Consolidated	
	Year ended 31 August 2017	Year ended 31 August 2016
Audit services		
Auditors of the Company		
<i>KPMG Australia:</i>		
Audit and review of financial reports	475,000	525,000
<i>Overseas KPMG firms:</i>		
Audit and review of financial reports	36,000	45,800
	511,000	570,800
Other services		
Auditors of the Company		
<i>KPMG Australia:</i>		
Due diligence services	585,000	–
Other assurance services	61,314	81,250
Taxation services	41,205	180,820
<i>Overseas KPMG firms:</i>		
Taxation services	22,916	11,100
	1,221,435	843,970

29. SUBSEQUENT EVENTS

Details of the final dividend declared since balance date is set out in Note 20.

The Directors have not become aware of any other significant matter or circumstance that has arisen since 31 August 2017, that has affected or may affect the operations of the Group, the results of those operations, or the state of affairs of the Group in subsequent years, which has not been covered in this report.

DIRECTORS' DECLARATION

1. In the opinion of the Directors of Australian Pharmaceutical Industries Limited ('API'):
 - a. the consolidated financial statements and notes set out on pages 33 to 78, and the Remuneration Report set out on pages 15 to 28 in the Directors' Report, are in accordance with the Corporations Act 2001, including:
 - (i) giving a true and fair view of the financial position of the consolidated entity as at 31 August 2017 and of its performance, for the financial year ended on that date; and
 - (ii) complying with Australian Accounting Standards and the Corporations Regulations 2001;
 - b. the consolidated financial report also complies with International Financial Accounting Standards as disclosed in Note 1(b); and
 - c. there are reasonable grounds to believe that API will be able to pay its debts as and when they become due and payable.

There are reasonable grounds to believe that API and the controlled entities identified in Note 24 will be able to meet any obligations or liabilities to which they are or may become subject to by virtue of the Deed of Cross Guarantee between the Company and those controlled entities pursuant to ASIC Corporations (Wholly owned Companies) Instrument 2016/785.

2. The Directors have been given the declarations by the Chief Executive Officer and Chief Financial Officer for the financial year ended 31 August 2017 pursuant to Section 295A of the Corporations Act 2001.

Dated at Sydney, 18 October 2017

Signed in accordance with a resolution of the Directors:



Peter R. Robinson
Director

INDEPENDENT AUDITOR'S REPORT

FOR THE YEAR ENDED 31 AUGUST 2017



To the shareholders of Australian Pharmaceutical Industries Limited

Report on the audit of the Financial Report

Opinion

We have audited the Financial Report of Australian Pharmaceutical Industries Limited (the Company).

In our opinion, the accompanying **Financial Report** of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the **Group's** financial position as at 31 August 2017 and of its financial performance for the year ended on that date; and
- complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

The **Financial Report** comprises:

- Consolidated statement of financial position as at 31 August 2017;
- Consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity, and consolidated statement of cash flows for the year then ended;
- Notes including a summary of significant accounting policies; and
- Directors' Declaration.

The **Group** consists of the Company and the entities it controlled at the year end and from time to time during the financial year.

Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Group in accordance with the *Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

The **Key Audit Matters** we identified are:

- Asset valuation; and
- Valuation of receivables (including financial guarantee assessment).

Key Audit Matters are those matters that, in our professional judgment, were of most significance in our audit of the Financial Report of the current period.

These matters were addressed in the context of our audit of the Financial Report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

INDEPENDENT AUDITOR'S REPORT

CONTINUED



Asset valuation (Carrying value of goodwill and brand names of \$130.0m for Australia and carrying value of goodwill of \$16.3m for New Zealand)

Refer to Note 15 to the Financial Report

The key audit matter	How the matter was addressed in our audit
<p>Asset valuation of the Group's indefinite useful life assets is a key audit matter due to the significant forward-looking assumptions the Group applied in its value in use models being inherently difficult to determine with precision. We focussed on the following significant assumptions:</p> <ul style="list-style-type: none"> ● Market-related assumptions such as macro-economic factors contributing to variability in pharmacy and retail sales, impacting EBIT growth rates and terminal growth rates; ● Non-market related assumptions detailed in the Group's Strategic Plan including EBIT growth rates driven by increased like-for-like store sales and net franchise store growth; ● The Group's model is sensitive to changes in EBIT growth rates, discount rates and terminal growth rates which are key assumptions. This drives additional audit effort specific to the feasibility and consistency of application to the Group's strategy. Reasonably possible changes to key assumptions increases the possibility of non-current assets being impaired, plus the risk of inaccurate forecasts or a wider range of possible outcomes for us to consider; and ● Discount rates which are inherently subjective and vary according to the conditions and environment the specific cash generating unit (CGU) is subject to from time to time and the impairment model's approach to incorporating risks into the cash flows or discount rates. <p>The Group uses a valuation model to perform its impairment assessment which includes a range of internally and externally sourced inputs. The Group's New Zealand business has not met prior year forecasts, raising our concern for the reliability of current forecasts. Valuation models, particularly those containing judgemental allocations of corporate costs to CGUs, and forward-looking assumptions tend to be prone to greater risk for potential bias, error and inconsistent application. These conditions necessitate additional scrutiny by us, in particular to address the objectivity of sources used for assumptions, and their consistent application.</p> <p>Given the inherent complexity of this key audit matter, we chose to involve valuation specialists to supplement our senior audit team members.</p>	<ul style="list-style-type: none"> ● We evaluated the appropriateness of the value in use method applied by the Group to perform impairment testing against the requirements of the accounting standards; ● We assessed the integrity of the value in use model used, including the mathematical accuracy of the underlying calculation formulas; ● We assessed the Group's underlying methodology and documentation for the allocation of corporate costs to the forecast cash flows contained in the value in use model, for consistency with our understanding of the business and the criteria in the accounting standards; ● We compared the forecast cash flows contained in the value in use model to the Strategic Plan approved by the Board; ● We assessed the accuracy of previous Group forecasts to inform our evaluation of forecasts incorporated in the models. We noted previous trends of variability in pharmacy and retail sales for use in further testing. We applied additional focus to forecasts in the areas where previous forecasts were not achieved; ● We compared key market-related assumptions such as forecast EBIT growth rates to published industry growth rates and independent industry market research reports, and terminal growth rates to independent economic outlook reports; ● We considered the sensitivity of the model by varying key assumptions, such as EBIT growth rates, discount rates and terminal growth rates within a reasonably possible range, to identify those CGUs at higher risk of impairment and to focus our further procedures; ● We assessed the Group's prior accuracy in forecasting EBIT growth rates driven by net franchise store growth and like-for-like store sales growth by comparing historical forecasts detailed in Group Strategic Plans to actual results to inform our evaluation of forecasts incorporated in the models; ● Working with our valuation specialists we independently developed a discount rate range using publicly available market data for comparable entities, adjusted by risk factors specific to the Group, such as variability in pharmacy and retail sales and the uncertain outcome of government reforms to the Pharmaceutical Benefits Scheme; ● We assessed the disclosures in the financial report using our understanding of the issue obtained from our testing and against the requirements of the accounting standards.

INDEPENDENT AUDITOR'S REPORT

CONTINUED



Valuation of receivables ((including financial guarantee assessment of \$10.5m) (\$702.1 million))

Refer to Notes 9 and 23 to the Financial Report

The key audit matter	How the matter was addressed in our audit
<p>The Group is exposed to credit risk in relation to overdue trade receivables and long term loans provided as financial assistance to certain pharmacy customers.</p> <p>The recoverable value of these receivables from customers was a key audit matter due to the audit effort to address multiple and varying credit conditions across a large pool of customers. We focused on:</p> <ul style="list-style-type: none"> ● Amendments to standard terms of trade with certain customers, such as long term funding arrangements; ● The value of security held by the Group over the customers' assets and its impact to the Group's credit risk exposure. In particular, the value of the retention of title on inventory held by the customers, the value of the formal charges over customer's assets used as collateral, and the ranking of the Group's debt compared to other creditors; and ● Assessing the Group's subjective judgements related to the customers' ability to repay amounts and the timing of these repayments. The specific trading situations of those customers was critical to our assessment. 	<p>We assessed the Group's valuation of receivables methodology against the requirements of relevant accounting standards.</p> <p>We identified customers with receivables balances which were at greater risk of non-recovery by reading the Group's credit committee reports and inspecting aged debtors ledgers. For those customers at greater risk of non-recovery, our audit procedures included:</p> <ul style="list-style-type: none"> ● We assessed amendments to standard terms of trade with customers against signed long term funding arrangements. We also assessed patterns of customer's repayments since the amendments for consistency. We followed up unusual or inconsistent patterns; ● We assessed the value of the security held by the Group over the customer's pharmacy assets by comparing the Group's analysis of value to conclusions of independent valuation reports obtained by the Group in relation to similar pharmacy businesses; ● We evaluated the objectivity, competence and scope of work undertaken by the independent valuation expert appointed by the Group; ● We assessed the Group's analysis of the value for other security held by the Group such as retention of title of inventory, formal charges over customer's assets and the ranking of the Group's debt compared to other creditors. This involved comparing the Group's estimates to customer inventory records, property mortgage documents and other information; ● We challenged assumptions made about the ability of customers to repay amounts due and the associated timing of repayments. This included assessing the customer's current trading status, payment history, payments made subsequent to year end for its effect in reducing the balance outstanding at year end, and evaluating the actions taken by the Group to recover overdue amounts.

INDEPENDENT AUDITOR'S REPORT

CONTINUED



Other Information

Other Information is financial and non-financial information in Australian Pharmaceutical Industries Limited's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon, with the exception of the Remuneration Report.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*;
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error; and
- assessing the Group and Company's ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Group and Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this Financial Report.

A further description of our responsibilities for the Audit of the Financial Report is located at the Auditing and Assurance Standards Board website at: http://www.auasb.gov.au/auditors_files/ar2.pdf. This description forms part of our Auditor's Report.

INDEPENDENT AUDITOR'S REPORT

CONTINUED



Report on the Remuneration Report

Opinion

In our opinion, the Remuneration Report of Australian Pharmaceutical Industries Limited for the year ended 31 August 2017, complies with Section 300A of the Corporations Act 2001.

Directors' responsibilities

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with Section 300A of the Corporations Act 2001.

Our responsibilities

We have audited the Remuneration Report included in the Directors' report for the year ended 31 August 2017.

Our responsibility is to express an opinion on the Remuneration Report, based on our Audit conducted in accordance with Australian Auditing Standards.

KPMG

Maurice Bisetto
Partner
Melbourne
18 October 2017

SHAREHOLDER INFORMATION

FOR THE YEAR ENDED 31 AUGUST 2017

ASX ADDITIONAL INFORMATION

Additional information required by the ASX Listing Rules and not disclosed elsewhere in this report is set out below.

Shareholdings as at 17 October 2017

Substantial shareholders

The number of shares held by substantial shareholders and their associates as notified to the ASX are set out below:

Washington H Soul Pattinson and Company Limited	95,068,472	ordinary shares
UBS Group AG	24,523,392	ordinary shares

Voting rights

The voting rights attaching to the ordinary shares, as set out in clause 16.2 of the Company's Constitution, are:

- a. on a show of hands:
 - (i) if a member has appointed two proxies, neither of those proxies may vote;
 - (ii) a member who is present and entitled to vote and is also a proxy, attorney or representative of another member has one vote; and
 - (iii) subject to paragraphs (a)(i) and (a)(ii), every individual present who is a member, or a proxy, attorney or representative of a member, entitled to vote has one vote.
- b. on a poll every member entitled to vote who is present in person or by proxy, attorney or representative:
 - (i) has one vote for every fully paid share held; and
 - (ii) subject to paragraph (c), in respect of each partly paid share held has a fraction of a vote equal to the proportion which the amount paid bears to the total issue price of the share;
- c. unless:
 - (i) permitted under the Listing Rules; and
 - (ii) otherwise provided in the terms on which shares are issued, in calculating the fraction of a vote which the holder of a partly paid share has, the Company must not count an amount:
 - (iii) paid in advance of a call; or
 - (iv) credited on a partly paid share without payment in money or money's worth being made to the Company.

On-market share buy-back

There is no current on-market share buy-back.

Distribution of shareholders as at 17 October 2017

Category

Ordinary Shares	Number of shareholders
1 – 1,000	2,978
1,001 – 5,000	4,253
5,001 – 10,000	1,750
10,001 – 100,000	2,060
100,001 and over	216
	11,257

The number of shareholders holding less than a marketable parcel at 17 October 2017 was 760 (20 October 2016: 528).

Stock Exchange

The Company is listed on the Australian Securities Exchange. The Home Exchange is Melbourne.

Other Information

Australian Pharmaceutical Industries Limited, incorporated and domiciled in Australia, is a publicly listed company limited by shares.

SHAREHOLDER INFORMATION

CONTINUED

Twenty largest Shareholders as at 17 October 2017*

Name	Number of Ordinary shares held	Percentage of Capital held
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	100,220,161	20.46
WASHINGTON H SOUL PATTINSON AND COMPANY LIMITED	95,068,472	19.41
J P MORGAN NOMINEES AUSTRALIA LIMITED	61,761,993	12.61
CITICORP NOMINEES PTY LIMITED	54,052,020	11.04
NATIONAL NOMINEES LIMITED	21,346,117	4.36
PRUDENTIAL NOMINEES PTY LTD	8,000,000	1.63
BNP PARIBAS NOMS PTY LTD	6,664,463	1.36
BNP PARIBAS NOMINEES PTY LTD	4,737,330	0.97
JUM PTY LIMITED	1,567,286	0.32
MR FREDERICK BENJAMIN WARMBRAND	1,500,000	0.31
MR RAYMOND FRANCIS FREW & MRS GILLIAN MARGARET FREW	1,325,000	0.27
UBS NOMINEES PTY LTD	1,098,434	0.22
AMP LIFE LIMITED	1,058,855	0.22
MR STEPHEN PATRICK ROCHE	944,674	0.19
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED – GSCO ECA	887,056	0.18
CITICORP NOMINEES PTY LIMITED	881,002	0.18
MERRILL LYNCH (AUSTRALIA) NOMINEES PTY LTD	818,297	0.17
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED - A/C 2	814,290	0.17
MR JOHN JOSEPH MURPHY	681,879	0.14
MRS PATRICIA JUNE MURPHY	681,371	0.14
	364,108,700	74.35

* As shown on the register, beneficial holdings may differ.

Shareholder Communications

Enquiries or notifications by shareholders regarding their shareholdings or dividend should be directed to API's share registry:

Boardroom Pty Limited
Grosvenor Place
Level 12
225 George Street
Sydney NSW 2000

GPO Box 3993
Sydney NSW 2001

Telephone 1300 737 760
International +61 2 9290 9600
Facsimile 1300 653 459

Shareholders can also send queries to the share registry via email: enquiries@boardroomlimited.com.au

You can access information about your API shareholding and download forms via the internet by visiting: www.boardroomlimited.com.au

SHAREHOLDER INFORMATION

CONTINUED

Dividends

If you wish your dividends to be paid directly to a bank, building society or credit union account in Australia contact the share registry or visit the website of Boardroom at www.boardroomlimited.com.au for an application form. The payments are electronically credited on the dividend payment date and confirmed by payment advices sent through the mail to the shareholder's registered address. All instructions received remain in force until amended or cancelled in writing.

Tax File Number (TFN), Australia Business Number (ABN or exemption)

You are strongly advised to lodge your TFN, ABN or exemption with the share registry. If you choose not to lodge these details, then API is obliged to deduct tax at the highest marginal rate (plus the Medicare levy) from the unfranked portion of any dividend. Certain pensioners are exempt from supplying their TFN's. You can confirm whether you have lodged your TFN, ABN or exemption via the Boardroom website.

Uncertificated Forms of Shareholdings

Two forms of uncertificated holdings are available to API shareholders:

Issuer Sponsored Holdings:

This type of holding is sponsored by API and provides shareholders with the advantages of uncertificated holdings without the need to be sponsored by any particular stockbroker.

Broker Sponsored Holdings ('CHESS'):

Shareholders may arrange to be sponsored by a stockbroker (or certain other financial institutions) and are required to sign a sponsorship agreement appointing the sponsor as their 'controlling participant' for the purposes of CHESS. This type of holding is likely to attract regular stock market traders or those shareholders who have their share portfolio managed by a stockbroker.

Shareholders communicating with the share registry should have their Security Holder Reference Number (SRN) at hand or Holder Identification Number (HIN) as it appears on the Issuer Sponsored/ CHESS statements or dividend advices. For security reason, shareholders should keep their Security Holder Reference Numbers confidential.

Annual Report Mailing List

Shareholders (whether Issuer or Broker Sponsored) wishing to receive the Annual Report should advise Boardroom in writing so that their names can be added to the mailing list. Shareholders are able to update their preference via the Boardroom website. Shareholders can also elect to receive the Annual report by e-mail or by accessing the Company website.

Change of Address

Shareholders who are Issuer Sponsored should notify any change of address to the share registry promptly in writing quoting their Security Holder Reference Number, previous address and new address. Application forms for Change of Address are also available for download via the Boardroom website. Broker Sponsored (CHESS) holders must advise their sponsoring broker of the change.

Share Trading and Price

API shares are traded on the Australian Securities Exchange. The stock code under which they are traded is 'API' and the details of trading activity are published in most daily newspapers under that abbreviation.

Off-Market Share Transfers

Stamp duty on transfer of listed shares was abolished on 1 July 2001.

Information on API

API has an internet site featuring news items, announcements, corporate information and a wide range of product and service information. API's internet address is www.api.net.au

The Annual Report is the main source of information for shareholders. Other sources of information include:

- Interim results;
- Annual results;
- The Annual General Meeting (the Chairman and the Managing Director address the meeting); and
- ASX announcements.

Financial Calendar*

Half year end	28 February 2018
Half year profit announcement	19 April 2018
Year end	31 August 2018
Full year profit announcement	18 October 2018
Annual General Meeting	24 January 2019

* Timing of events is subject to change

Requests for publications and other enquiries about API's affairs should be communicated to:

Company Secretary
 Australian Pharmaceutical Industries Limited
 Level 5
 250 Camberwell Road
 Camberwell, Vic 3124

CORPORATE DIRECTORY

Offices and Officers

Company Secretary

Mr Peter Sanguinetti B.Juris, LLB, GAICD

Registered Office

Australian Pharmaceutical Industries Limited
Level 5
250 Camberwell Road
Camberwell Vic 3124

Locked Bag 3002
Hawthorn BC
Vic 3122

Telephone: (03) 8855 3000
International: +61 3 8855 3000
Facsimile: +61 3 8855 3406
Email: legal@api.net.au

Location of Share Registry

Boardroom Pty Limited

Grosvenor Place
Level 12
225 George Street
Sydney NSW 2000

GPO Box 3993
Sydney NSW 2001

Telephone: 1300 737 760
International: +61 2 9290 9600
Facsimile: 1300 653 459
E-mail: enquiries@boardroomlimited.com.au



api

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