

## CHIEF EXECUTIVE OFFICER'S REPORT

### GENERAL

Verimark's proud and successful history of nearly three decades led to a listing on the JSE Limited in 2005. The business continued its success by delivering impressive results in its first year as a listed entity, but sadly thereafter ran into a particularly tough and lengthy phase of adverse performance.

We are pleased to report that the long-awaited turnaround in the Group's trading activities has firmly materialised during the year under review, resulting in a profit before tax of R20.2 million versus a loss of R4.2 million in the previous year. To fully comprehend the timing and magnitude of the turnaround, it is important to point out that trading during the year was made up of two halves with diametrically opposed outcomes:

- the downward trend of the previous three years continued during the first half of the year, resulting in a loss of R11.1 million – the worst ever in the history of the Group; and
- trading in the second half of the year resulted in a profit before tax of R31.2 million – the best six month period in the Group's entire history!

Although it took a lot longer than initially anticipated to effect a successful turnaround; the quantum thereof affirms that the entrepreneurial spirit that took this start-up business from humble beginnings to one of South Africa's most trusted and recognised brands; is very much alive and growing. Verimark's performance, especially over the last few months, is proof that the Group is ready to continue its proud and successful history, built over the previous 33 years.



**Michael J van Straaten**  
Chief Executive Officer

### FINANCIAL PERFORMANCE

#### Highlights

The critical performance indicators for the year under review were as follows:

- Sales increased from R252.5 million to R347.5 million (38%)
- Operating profit of R28.3 million vs. a loss of R2.8million
- Profit before taxation of R20.2 million vs. a loss of R4.2 million
- Headline earnings of R13.6 million vs. a loss of R3.7 million
- Headline earnings per share of 12.4 cents vs. a loss of 3.4 cents
- Dividend per Share of 6,0 cents vs. nil
- Cash inflows from operating activities of R38.5 million vs. cash outflows from operating activities of R5.8 million.

Given the successful turnaround and significant improvement in profitability and cash flow of the Group, the Board has decided to declare a dividend of 50% of profit attributable to shareholders in terms of a new dividend policy moving forward.

The main reasons for the significant improvement in profitability were:

#### Increase in Sales and Gross Profits

The single most important contributor of the successful turnaround was the substantial increase in sales and resultant gross profit. The factors that contributed to this improvement are detailed in the Operational Review.

#### Expenses, Operational Gearing and Finance Costs

Although reduction and control of expenses is very important in every business, it unfortunately shows limited benefits during periods when sales decrease; as has happened to Verimark

## CHIEF EXECUTIVE OFFICER'S REPORT

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### FINANCIAL PERFORMANCE (continued)

#### Expenses, Operational Gearing and Finance Costs (continued)

during the recent difficult phase. The real benefits however become much more prevalent when the sales trend changes from negative to positive, as experienced by the Group during the year under review.

Expenses did increase but at a far lesser rate than sales. The focus placed on cost control in the past, finally did show the expected benefits during the year.

Finance costs were much higher due to foreign exchange net losses on hedge contracts (R3.3 million in current year vs. a profit of R3.1 million in the previous year). Interest on the preference share liability (R1.2 million) relating to the Verimark Employment Empowerment Trust was in line with that of the previous year.

Where the high operational gearing nature of the business turned negative in the recent past, it has now again turned positive and benefited the Group, during the latter part of the year under review.

### OPERATIONAL REVIEW

The improved financial performance is a result of improved operational efficiencies and the re-ignition of Verimark entrepreneurial spirit, brought about by a complete change in top management.

To understand the uncertainties and challenges faced during the successful turnaround of the business, a basic understanding of the Verimark business model is necessary.

The key areas are:

#### a) Sourcing, development and selection of products

- Products are sourced by visiting trade fairs, retail stores and through a network of business partners and manufacturers, from across the globe.
- The selection criteria are: uniqueness, quality, demonstrability and the widest possible demographic demand.
- Our product range covers the following categories:
  - Cook- and kitchenware – Bauer, Bastille, Twista.
  - Home cleaning – Genesis, Big Green Extreme, Floorwiz.
  - Health and Fitness – Maxxus, V-ssage.
  - DIY and Automotive – Diamond Guard, Prolong, Gorilla.
  - Educational and Fun Toys – I-Play.
- Some of the products introduced during the year to complement our existing, established range were:

**Twista:** Ultima (manual food processor),  
Chop-N-Go (manual food processor).

**Shogun:** Peeler Set

**Iron Gym:** Home Exerciser

**Orbitrek:** Home Elliptical Trainer

**Biggi Bubble:** Fun Toy

**Stunt Racer:** Remote Control Toy

- The downward trend in sales experienced over the previous three years, was triggered by a slowdown in new product introductions in the beginning of that period. To consistently identify "home runs" (products that generate exceptional sales value) forms a critical component of our business model and will never be an exact science. However, through the necessary management changes and major refocus, new product introductions have reached record levels in the year under review. This, in conjunction with further product introductions scheduled for first six months, bodes well for continued growth in the year ahead.

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### OPERATIONAL REVIEW (continued)

#### b) Conceptualising and production of Direct Response Television (DRTV) commercials and other marketing materials

- Verimark pioneered DRTV advertising in South Africa nearly two decades ago. This long form (1 to 28 minutes) of advertising has proven to be hugely effective as a sales medium, given that virtually all innovative products initially require a longer form of TV commercial to properly explain the unique selling points (USP) of the product and to generate sales. DRTV commercials direct the television viewer to a call centre or website where the sale is generated. We have refined this advertising format to also allow for brand building (sometimes referred to as "brand-response advertising") and to accommodate retail distribution.
- Still today, every product selected for introduction requires a TV commercial. If products are sourced via another DRTV company, we would use theirs; otherwise Verimark would produce its own TV commercials as well as the necessary marketing materials.
- Innovative thinking and creativity are paramount when producing a TV commercial. Verimark's experience and skill in this area, built up over two decades, ensures that each commercial is produced in a way that best demonstrates and sells that product – giving it the best chance of success.

#### c) TV Advertising and promotional activities

- Each new product (and TV commercial) goes through a sales test to ensure an acceptable consumer response. Only after a product passes this test, do we commit to big purchase volumes (Roll Out). Our "success rate" averages around 70%, whereas the international norm is less than 7%.
- All products marketed will continuously be aggressively TV advertised to maximise demand and sales. During the year under review, our television and other advertising spend increased substantially. In a recent AC Nielsen survey, Verimark was rated the 4th largest TV advertiser in South Africa!
- Other key components of Verimark's promotion strategy include: print advertising, the internet (via our website), in-store demonstrations and the use of TV playback units at virtually all of our retail selling points.

#### d) Distribution and Sale of products

- After pioneering DRTV in South Africa, Verimark again pioneered the distribution of DRTV products through retail. Today the Group's products are sold through most of the large retailers, in most cases in a dedicated Verimark area (Shop-Within-a-Shop). We have also over the last ten years invested in setting up our own Verimark Direct Stores (company owned and franchised).

This integrated business model has taken DRTV marketing to a level not seen anywhere in the world and resulted in Verimark being recognised internationally as the benchmark.

- The sell-through at our retail training partners and Verimark Direct Stores was disappointingly flat during the first few months of the year, but progressively increased thereafter, ending with the last three months sell-through being 60% up on the previous year (some retailers were more than 100% up!).

To achieve this level of growth in a depressed economy with official retail statistics reflecting negative growth, confirms not only the successful turnaround of the business, but more so the sustainability of the Verimark business model.



## CHIEF EXECUTIVE OFFICER'S REPORT

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## OPERATIONAL REVIEW (continued)

## d) Distribution and Sale of products (continued)

This impressive growth in sales was due to:

- The number of new product introductions that complemented the existing product range.
- The increased prominence and space utilisation in most retail stores – credit is due to our retail partners who saw the high growth potential Verimark offered, given our product range, TV exposure and ability to promote in-store.
- The management changes effected in this part of the business were key in the turnaround and the growth achieved.

## People

In the previous two years' CEO Reports, the challenge was put to the new management team to prove their (our) ability to turn the business around. Given the current year's results, they and every member of the Verimark staff, must be congratulated on their efforts. I would like to thank everyone that contributed for their unrelenting efforts.

When our entire management team (excluding myself) changed and in most cases were new in their respective positions, the challenges and uncertainties were huge, especially in a business dependent on entrepreneurial flair, creativity and innovation. Verimark has grown well beyond the point where a single individual can control its fate. We are pleased that good progress has been made in building a team that does have the capabilities to continue the business success.

## TWISTA CHOP-N-GO

When it comes to kitchen essentials, every household needs a Twista. The latest addition to this leading brand is the Twista Chop-N-Go. Now you can chop, slice, mince and dice all your fruits, vegetables, nuts and more - in seconds. With every push on the soft rubber plunger the ultra-hardened Stainless Steel blade cuts and rotates for the quickest and easiest food preparation. Unlike other cheap imitations, the Twista opens up completely for easy cleaning. In true Verimark style, we have included a Power Grater in the set – absolutely Free! Now you can grate cheese, nuts, even chocolate; and the handy cover allows you to store what you don't use. Twista Chop-N-Go is a true kitchen essential for every home.



## CHIEF EXECUTIVE OFFICER'S REPORT

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### OPERATIONAL REVIEW (continued)

#### Delisting application in the beginning of 2009

The recent tough phase that stretched over three years was undoubtedly the most challenging period of Verimark's history. Sales and profits over the period continuously declined, ending with a loss at the end of February 2009.

Given the risks and uncertainties around the new management team's ability to affect a turnaround in the business, and the further worsening of the financial position of the Group, it was decided at the beginning of 2009 that it would be in the best interests of all stakeholders for Verimark to apply for a delisting.

However, the delisting proposals were not sanctioned by the Court and Verimark continued as a listed company.

Hindsight is an exact science and if we knew then what we know now (that we would be capable of turning the business around within 12 months of taking the decision to delist), we would not have considered a possible delisting. Looking back and given the recent successful turnaround, we are pleased that the delisting was not sanctioned. It gives Verimark the opportunity to prove to the market that it can continue its successes of the past as an entrepreneurially-spirited, listed entity.

#### Business Environment

The negative trend in consumer spending that resulted from the global financial crisis continued during the current year with virtually all retailers and consumer-focused businesses being negatively affected.

Verimark's financial results for the current year prove that we were not really affected by this tough economic environment, to the extent that other retailers were. This anomaly substantiates Verimark's well known assertion that its business model is different from general retail companies. Macro economic cycles that impact on consumer spend in the broad retail environment, will have less of an impact on our business, with our innovations and marketing strategies based on a "recession resistant" direct sales model being far more important.

#### Prospects

As pleased as we are about the successful turnaround of the business, we are equally excited about the future. The increased level of sales experienced over the last few months leading up to the financial year end, is continuing into the new financial year. Given the recent impressive growth recorded through our retail partners, some have indicated that they believe that Verimark is still under trading in their businesses and have committed to a bigger presence in their stores. This in conjunction with the expansion plans of our own Verimark Direct store concept bodes well for the future growth of our business.

The difficult phase experienced after the public listing was clearly just another challenge that Verimark as an entrepreneurial business had to face and overcome – as it has successfully done with many other challenges in its 33 year history. Although there will be new challenges in the future, we are ready to continue the Verimark success record.



**MJ Van Straaten**

*Chief Executive Officer*

7 May 2010