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# Reports to Shareholders

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The Massmart Executive Committee meets at the Sunninghill head office for monthly reviews of operational performance.

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# Chairman's report

**In this environment and time, it is easy to be diverted from the primary purpose of a large business in a transforming society. The demands on the time, attention and resources of South African business are legion, with every constituency making claims founded frequently on interests that are diametrically opposed to the development of industry and commerce. We cannot be distracted by this.**

With the average lifespan of a company still far from that of a human being, we at Massmart regard survival as our primary objective, reflected most obviously in the preservation and growth of your capital. The fact that we have been able to exceed this minimum requirement over the past year with a 53% return on average shareholders' equity and a 73% return on capital employed, is attributable to four things: strategic clarity; leadership; a quest for excellence in every aspect of our endeavour; and a proven commitment to satisfying the legitimate needs of all stakeholders. In addition to its fiduciary obligations as defined by the law and good governance practice, the Board of Massmart applies its collective competence to these issues.

## Strategic clarity

We are clear that the sole objective of our strategic thought and action is the achievement of competitive advantage. For many years we have done this through the continual improvement of a high-volume, low-margin, low-expense business model that has enabled us to provide exceptionally low prices on an extensive range of products, to a broad spectrum of society in 14 sub-Saharan countries.

Over the past year we increased sales per store, per employee and per square metre, we reduced gross margins at the product level and we decreased operating expenses as a percentage of sales. Customer response to the consequent lower prices was evident in real comparable store sales growth in all Divisions – the ultimate vindication of a retail trading strategy. Concurrently, and notwithstanding our mass market position as one of Africa's largest distributors of consumer goods, we have mitigated risk by being selective in our choice of markets, sites, categories, products and payment methods. Finally, by virtue of productivity improvements, we have again grown profits ahead of sales to establish an 18-year compounded annual growth rate of 56,0% in sales, 75,8% in profit before tax and 26,7% in net asset value since the Group's founding in 1990.

Massmart's annual three-year strategic review ensures that there is continuity and coherence in the Group's strategic thinking, and this year the Board was delighted by the prospects for revenue and profit growth arising from the new initiatives tabled in Vision 2011, covered in detail in the Chief Executive Officer's review.

An important development since year-end has been the formation of the Strategy and Investment Committee of the Board. Although the Group's high cash generation will further reduce its low gearing over the coming year, it is likely that the number and size of opportunities facing the Group will require capital rationing decisions unlike those we have previously faced. The Strategy and Investment Committee was formed to enhance the quality of such decisions by facilitating a robust analysis and evaluation of options by the Board and executive management.



**“We are clear that the sole objective of our strategic thought and action is the achievement of competitive advantage.”**

**MARK J LAMBERTI** CHAIRMAN OF THE BOARD

## Leadership

For many years Massmart has adopted an innovative and oftentimes unconventional approach to human capital development in general, and leadership in particular. Nowhere was this more evident than in the CEO succession process. The ease with which all Massmart stakeholders have adapted to and embraced Grant's leadership is both a vindication of the process that the Board adopted and a tribute to his technical ability, business acumen and leadership stature.

The Executive Committee, the most senior executive decision-making body in Massmart, and their direct reports, constitute a young leadership cadre with the necessary formal education, retail and wholesale experience, and tenure to sustain performance and growth. The enhancement of their skills and those of the next generation of managers is carefully monitored and addressed in career and succession plans, which inculcate a developmental and performance ethos, while striving without compromising competence, for defined racial and gender targets throughout the Group. We can think of no greater insult than telling someone in Massmart that they hold their positions because of their race or gender.

The skills shortage in our country is no longer a matter of opinion. South Africa has too few competent managers, leaders, professionals and technicians of every race, gender and creed to meet our need. This need is being fuelled not just by South African factors such as transformation, rapid economic growth, the continued emigration of young graduates seeking international experience, and by some escaping the high crime rate. It is also being fuelled by the worldwide exit from the workplace of my generation – the baby boomers, by a decline, other than in India and South East Asia, of graduates in the quantitative disciplines, and by the fact that the market for top-level executives has become one of the world's few truly global markets.

Massmart's response to this has been to increase investment in education, training and to fast-track executive development programmes which accelerate individuals' competence and confidence to take the hard commercial decisions associated with accountability and responsibility for profits, assets and people. We intend to redouble these efforts.

## The quest for excellence

Every business is particularly good at something. Great businesses are good at many things. The reasons are obvious. As people imbibe the processes, practices and focus that lead to success in one aspect of an organisation's endeavour, lower standards of performance are exposed elsewhere and the motivation to address these is increased. Over time the quest for excellence becomes a way of life.

David Susman, the founder of Woolworths and one of South Africa's greatest retailers, described this as "divine dissatisfaction", a state of being pleased with progress, but never satisfied. This philosophy is deeply ingrained in the leadership of Massmart and evidence of continual learning is abundant.

While the achievement of excellence is reward in itself, we were humbled by the public recognition of our accomplishments over the past year.

The following were the most notable of these:

- First in the Financial Mail Top Companies Survey
- Top of the JSE retail sector in the Financial Mail/Empowerdex 2008 Top Empowerment Companies Survey
- The only company to achieve Top Performer Status in the 2007 JSE SRI-Index medium environmental impact category
- Massmart's 2007 Annual Report was ranked fourth in the Ernst & Young Excellence in Corporate Reporting Awards
- Massmart's 2007 Sustainability Report was ranked Best Sustainability Report, Non-Extractive Industries in the Association of Chartered Certified Accountants (ACCA) 2008 Sustainability Awards.

These awards are a tribute to every employee of Massmart and in my mind are almost equal in the quest for excellence, to the letters I receive from customers acknowledging a particularly satisfying shopping experience.

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**“While the achievement of excellence is reward in itself, we are humbled by the public recognition of our accomplishments over the past year.”**

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## Satisfying stakeholders

The Massmart Vision lays out our objectives in our relationship with stakeholders.

We believe that our commitment to you as one of Massmart's 10 817 owners are fulfilled only by ensuring enduring, productive relationships with other stakeholders and by establishing a reputation as a trusted, patriotic corporation in touch with the evolving needs and aspirations of our unique society. To this end we invest time, effort and money in canvassing and responding to the needs of our current and prospective stakeholders.

Whenever possible, we interact proactively with consumer bodies, industry forums, organised labour, non-governmental organisations, political parties, thought leaders and law makers on matters of importance to the performance and future of our business and industry.

We are committed to playing a constructive practical role in the normalisation of our society and we see no better way to do this than through collaborative and influential relationships with stakeholders.

Finally, and possibly most importantly, we recognise the importance of our stewardship of the planet. We have measured our carbon footprint and are determined to reduce it.

## Governance

Our compliance with the letter and spirit of good governance practice is reported on fully elsewhere, compromised only by the Board's decision to appoint me non-executive Chairman. My independence – as defined in the governance literature – is negated by my tenure and prior role as CEO. Both I and the Board are mindful of this, and Chris Seabrooke's role as non-executive Deputy Chairman and Lead Independent Director is one taken seriously and utilised when necessary by all. We encourage shareholders to do the same.

Notwithstanding the above, the skills and diversity of the Board are well matched to your Company's needs, and the allocation of committee responsibilities ideally aligned to the qualifications and experience of the Chairpersons and members involved. The Board's independence is assured by 11 of its 14 members being independent non-executive directors, as are the Chairs of the Audit, Remuneration and Nominations, Risk, and Sustainability Committees.

## Appreciation

Massmart is a large, complex organisation that in the past year handled billions of transactions, millions of customers and over two hundred thousand line items through 242 large stores in 14 countries.

The relative ease with which this happens belies the risks associated with this scale and complexity and it would not be possible without the wisdom of a diligent Board, the leadership of a talented CEO, whose performance in his first year has been flawless, the creativity and energy of an extraordinary executive and managerial group, the loyalty and competence of our 24 308 employees, and the support of our suppliers, bankers and professional advisers. On behalf of the Board I thank them all.

On a personal note, I record my appreciation for the support and counsel of my Board colleagues throughout the year and their presentation of a 20-year service award at the August 2008 Board meeting. That scroll meant more to me than any of you can imagine.

## Looking forward

Economic cycles are a business reality. Massmart's superior relative performance over the past year reinforces your Board's conviction that the assets, resources, capabilities, controls and leadership of Massmart have been configured to withstand the less-than-favourable trading conditions that will prevail in the short term, and to prosper in the better times that will inevitably follow.

### Further reading

Vision and mission can be found at the beginning of the report	3
<b>MASSMART AT A GLANCE</b>	

*“We are committed to playing a constructive practical role in the normalisation of our society and we see no better way to do this than through collaborative and influential relationships with stakeholders.”*

Presidential transitions are a democratic reality. Your Board is concerned that ours is proving to be as divisive as it is. In contrast to the past, and despite despicable but thankfully isolated racial incidents, the basis of division in South Africa today is not race, but political allegiance. Were it not coloured by attacks on the constitution, the judiciary and the rule of law, the reckless public rhetoric surrounding this could be dismissed as electioneering. It is not, and the unashamed assault on the pillars of our democracy cannot be tolerated under any guise of national interest.

In difficult times, criticism of capitalism is a social reality. Business must respond. Confronted with critique that seeks to vilify all businesses based on the behaviour of very few, and legislators who place votes above efficiency, the South African business community must stand proud as the unapologetic bastion of free market economic activity and growth, the major creator of employment (unionised or not), and the originator of a corporate and personal tax base that funds our institutions of democracy, pays our politicians and civil servants, and creates a social safety net for the most disadvantaged.

Ours is a region of extraordinary opportunity and challenge. The opportunity is in the abundance of our natural resource, the challenge is in the underdevelopment of our human resource. Business has a central role to play in redressing the latter by investing time, effort and resources to enhance education and training, accelerate the acquisition of skills and experience, develop competent leaders, and more broadly share power and profits at all levels of our organisations. Finally we must engage and collaborate more generously with government and civil society to address all matters of national concern, very few of which will be solved without the innovation, creativity and focus resident in business.

Massmart stands ready to play its part.



**Mark J Lamberti**  
Chairman of the Board

1 October 2008

# Chief Executive Officer's review

**It is a pleasure to present my report on my first year as CEO of Massmart. Even though it was a challenging year, we managed to deliver a strong overall performance thanks to a balanced contribution from the four Divisions. The economic cycle was clearly gaining downward momentum, but we proved that the Group is able to ride through the troughs.**

The year began with my taking on the role of CEO after a three-year succession process and ten years with the Group. The process ensured that I have been able to take on the role well prepared for the challenges of managing the Group. My thanks are due to Mark Lamberti, who left the CEO position to become Chairman, the rest of the Board and the Executive Committee for their support and confidence. I remain inspired by the calibre of the team at Massmart.

## Environment

Many challenges tested the country over the past year, some fuelled globally and some locally. The political temperature rose as the ruling party elected new leadership, shifting the balance of power. Crime remained a serious issue, though some victories were scored in bringing it under control. Maintaining and growing the country's infrastructure came under close scrutiny as a result of load-shedding by Eskom.

Food and energy inflation continued to drive general inflation, forcing interest rates higher and putting the middle-income consumer under pressure. It also put low-income consumers, who are living hand to mouth and struggling daily to feed their families, under even greater pressure. This has challenged both government and ourselves to redouble efforts to provide support to those who cannot support themselves.

## Financial performance

The economic environment was reflected in the trading patterns across the Group. Food and liquor sales grew 17,1%, general merchandise sales growth was steady at 11,2%, while home improvement sales grew 14,4%, although this growth slowed during the year.

For the 53 weeks to 29 June 2008, total sales grew 14,3%. Comparable store sales – which measures sales in stores that were open for the full financial year and the year before – grew at 13,1%. Operating profit increased 24,6% and profit before tax increased at a slightly slower rate of 24,1%. The difference was largely due to increased interest costs because of higher interest rates and a slightly worse working capital position during the year. A lower net tax rate and fewer shares in issue boosted headline earnings per share by 23,8% before accounting for our Thuthukani empowerment scheme.

Analysis of the financial results is complicated by the 53-week period, which is compared to the 52-week period the year before. To better understand the operating performance relative to the prior year, we need to review the results for the 52 weeks to 23 June 2008. For that period, total sales grew 11,9% and comparable store sales grew 10,8%. Operating profit increased 17,7% and profit before tax increased 20,7%.

A further consideration is the impact of foreign exchange gains on these financial results. Because of the accounting treatment of various items on the income statement and the balance sheet, the movement of the Rand exchange rate can cause large (mostly unrealised) losses or profits. For the period, translation gains amounted to R62,5 million, or 3,7% of the growth in operating profit. Therefore, a truer reflection of performance is that operating profits grew 12,5%, maintaining operating margin from the previous year.

The Chief Financial Officer's review provides a detailed financial analysis.



**“We are pleased with the performance of the Group across all areas, although we still see much room for improvement in our pursuit of world-class standards.”**

**GRANT PATTISON** CHIEF EXECUTIVE OFFICER

## Operating performance

For the 52-week period, Masswarehouse and Masscash produced strong profit growth while Massdiscounters and Massbuild did well to grow profits at or near their rate of sales growth. The Divisional figures below represent the growth for the comparable 52-week period. A fuller discussion of each Division's performance is in the Operational Review.

### Massdiscounters

Massdiscounters consists of the 83-store General Merchandise retail discounter Game and the six-store hi-tech retailer Dion Wired. Game trades in South Africa, Namibia, Botswana, Zambia, Uganda, Mozambique, Mauritius, Malawi, Tanzania, Nigeria and Ghana.

Massdiscounters had a challenging year although much progress was made in implementing various initiatives that will pay off in years to come. Sales increased 7,5% (7,6% on a comparable store basis) and profit before tax by 9,5%. In South Africa, comparable sales grew throughout the year thanks to investment in trading aggression and a shift in focus towards value. African sales and profits performed at substantially higher levels than in South Africa. Locally, the National Credit Act reduced the Division's trading profit by an estimated R30 million.

However, future growth is on track thanks to investment in several areas. African expansion gained momentum with at least ten new potential sites identified, two of which were recently approved. The debtors book was sold and outsourced the day after the financial year-end. The original Dion brand was finally removed through store closures and conversions, while a new regional distribution centre was recently commissioned in Cape Town. The Dion Wired format was also successfully established as a profitable national brand focused on the high-tech consumer market, and three new stores were opened. Four new Game stores were opened and two Dion stores converted to the Game format. Two other Dion stores were closed and five Game stores closed.

The team is in good shape with a new Financial Director and HR Director settled in.

### Masswarehouse

Masswarehouse consists of the 13-store Makro warehouse club, trading in food, general merchandise and liquor in South Africa. A further two Zimbabwean stores are not consolidated in the results.

Masswarehouse had a good operating year. Sales increased 14,7% (10,5% on a comparable store basis) and profit before tax 34,4%. Margins, cost and stock remain under tight control. Its unique formula demonstrated its resilience in the tightening economic environment while management responded to trading opportunities faster than competitors.

The new Silver Lakes Makro store had a record opening and subsequent trading has been pleasing, although the performance of food is below expectations. Cannibalisation has been within forecast levels.

A major upgrade to the SAP ERP system was also implemented faultlessly.

We believe that there is potential for at least four more Makro stores to be opened in South Africa. The challenge, however, is to identify new properties that are well situated at appropriate prices. We continue to pursue opportunities.

### Massbuild

Massbuild consists of 68 outlets trading in DIY, home improvement and builders' hardware, under the Builders Warehouse, Builders Express and Builders Trade Depot brands in South Africa.

Sales increased 12,4% (9,0% on a comparable store basis) and profit before tax by 7,8%. Trade Depot had a particularly good year with sales up 12,6% and profit before tax up 27,4%.

Activities during the year were focused on stabilising the structure of the business, processes and control following the previous year's rapid consolidation of brands and systems. During the year the Massbuild head office was removed and Builders Express was consolidated within Builders Warehouse. A number of processes and systems were upgraded and improved, including those handling imports, supply chains and stock management. One new Builders Warehouse store and three new Builders Express stores were opened.

The teams at both Warehouse and Trade Depot are now complete and performing well.

### Further reading

More detail on the Divisions can be found in the Operational Review 55

OPERATIONAL REVIEW

“...Massdiscounters and Massbuild did well to grow profits at or near their rate of sales growth.”

**Masscash**

Masscash consists of 71 Cash and Carry stores trading in South Africa, Lesotho, Namibia and Botswana, and Shield, a voluntary buying association.

The Division had an exceptional year. Sales increased 13,2% (14,3% on a comparable store basis) and profit before tax by 38,5%. The performance was driven by high food inflation of 13,3% for the year and by benefits extracted from the merger of CBW, Jumbo, Shield and Cell-Shack the previous year. Food inflation fed into sales and trading margin, while the merger successfully eliminated costs.

There were two main strategic thrusts for the year: to test the rollout of a new in-store system and to implement the hybrid strategy. The system rollout test was successful and final approval for the rollout has been given. By the end of this financial year we should have all the Cash & Carry stores on one system with one stock master file – a major achievement.

The hybrid strategy aims to develop a store format that includes both retail and wholesale food. This gained momentum with the acquisition of ten stores with combined R1,0 billion in annual turnover that are awaiting competition authority approval and a further five stores that are still being negotiated.

The Masscash team is in good shape. During the period Operations Director Fred Cresswell moved to the Trade Depot business. This resulted in a reshuffle in which Neville Dunn moved from Financial Director to Operations Director and Dino Holmes from Financial Manager to Financial Director. We are in the process of appointing a new Financial Manager.

**Progress on vision 2011**

Vision 2011 covers our focus on leadership and transformation, supply chain, private label, financial services, organic growth, new formats and sustainability, all of which represent the headlines of our three-year rolling strategic plans.

Emigration and the general skills shortage is seen as a priority risk in the Group, so we are focusing on building our skills base internally. The year saw 42 executives and senior managers participate in Massmart University programmes and the participation of all senior management across the Group in a diversity management programme. Another ten executives participated in a Walton College of Business programme during the year. In total, 17 black graduates completed our in-house programme and were appointed to roles across the Group, while a further 17 are already in the pipeline. We have planned to increase the intake to 25 per year. Our annual Black Economic Empowerment scorecard saw an improvement by 13 percentage points in our self-assessed rating to 49%, making Massmart a level 6 contributor.

The completion of the regional distribution centre in Cape Town marks a new era of logistics for Massmart, but we still have much to learn. We have also learnt a lot in space planning by examining best practice overseas and a trial is under way of a new methodology. We have also established automatic replenishment systems in all retail divisions.

A complete rework was undertaken of some of the Group’s private label brands – those brands which are exclusive to Massmart – and the foundation has been set to improve the quantity and quality of our participation in some of the biggest consumer brands in Africa. We now have the ambition to become one of the leading owners of consumer goods brands in South Africa.

On the financial services front, we completed the sale of the Massdiscounters book just after year-end and will look for leverage opportunities across the Group in future.

Our organic growth has continued, and will continue to ensure we have an up to date, optimally structured portfolio. The latest review of our store opening opportunities shows potential for unweighted space growth of 5,1%, 6,0% and 3,5% in 2009, 2010 and 2011 respectively. That suggests a net 25 new stores across the Group, including 147 698m<sup>2</sup> and R3,66 billion in annualised turnover. That scenario excludes any acquisitions. However, our efforts to deliver on that opportunity have been frustrated by bureaucracy and unrealistic price expectations for land, resulting in slower store opening progress than the potential suggests.

Our greenfield formats have done well – Dion Wired has now established six stores and is profitable. We have identified further sites and are talking to landlords.

“...Masswarehouse and Masscash produced strong profit growth...”

“The completion of the regional distribution centre in Cape Town marks a new era of logistics for Massmart...”

<b>Further reading</b>	□
For detail on new stores target and new trading space target refer to the 'Looking forward' section	6
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<b>MASSMART AT A GLANCE</b>	

We also continue to look for more growth in Africa. During the year we found a number of fantastic sites on the continent and we are working on further store openings. We have also established a New Formats division and have made exciting progress with preparations to enter new categories with new formats.

We also continue to look out for acquisitions that comply with our strategic objectives. We have identified targets and continue to evaluate opportunities as they arise.

Sustainability is the final area in our vision for 2011. We have made good progress in improving our BEE scoring and we now rank as the most empowered listed retailer. We received a number of plaudits for our Sustainability Report. We have also now calculated the carbon footprint in the Group and are working on ways to improve it, including a pilot e-waste recycling project begun during the financial year. We also continue to build environmental awareness in our procurement processes and are bringing suppliers on board to improve overall energy consumption, packaging use, food sourcing and water consumption.

## Prospects

Trading in the new financial year has been good. The resilience of Massmart through previous economic cycles gives us confidence that we will continue to perform well relative to our competitors trading in similar categories. This short-term cycle presents both opportunities and threats as consumers adjust their purchasing behaviour to accommodate higher food, energy and interest costs. Parts of the Group will benefit as consumers 'trade down' to take advantage of our value proposition relative to other retailers. Other parts of the Group will have to adjust to the new environment. We are closely monitoring the effects of the interest rate cycle on our relatively new home improvement business.

We are confident in the medium- to long-term scenario for the South African consumer economy. It will continue to benefit from a growing middle class, a general shortage of housing, the social spending programme and the downstream economic benefits from the country's infrastructure investments.

Africa also continues to provide opportunities as its economies respond to improved governance and higher commodities prices.

We are pleased with the performance of the Group across all areas, although we still see much room for improvement in our pursuit of world-class standards.

Given the current economic environment, we are cautious about the year ahead but are confident that our business model will prove its resilience. We remain excited about the opportunities that are available to ensure medium- to longer-term growth.

## Appreciation

In my first year as CEO I have benefited from the support of the Executives and Board and thank them for their contribution to the CEO hand-over process. I am very grateful for their ongoing commitment to the Group and their exceptional contribution to our success.

I am well aware that financial success is a lagging indicator of human performance. Every one of our 24 308 employees has contributed to the Group's performance, evident particularly during a time of tightening retail conditions. Thank you.



**Grant Pattison**  
Chief Executive Officer

1 October 2008

**“In the 13 weeks to 28 September 2008, total sales increased 13,1% and comparable sales increased by 11,8%.”**

# Chief Financial Officer's review

We continually strive to improve the quality and relevance of Massmart's public financial reporting. It is also necessary to ensure that our technical disclosure is of the highest standard, while keeping the details and explanations clear and simple even as the accounting standards become increasingly complex and technical. We believe these efforts were recognised earlier this year when the Massmart 2007 Annual Report was judged fourth overall and awarded an Excellent rating, the second consecutive such rating, in the Ernst & Young 2008 Excellence in Corporate Reporting Awards.

## Financial targets

The Group has clearly stated medium-term financial targets or measures that we believe represent optimal performance levels within the income statement, balance sheet, or the combination of both. Certain of these targets are 'stretch targets' that will only be achieved in the medium term and are 'through-the-cycle' targets meaning that during a strongly negative or positive economic environment, we may under- or over-perform against those targets.

These target ratios are shown below.

Medium-term target ratios	Definition
ROS > 5,5%	Return on sales (ROS) is the ratio of operating profit before tax to sales
ROE > 35%	Return on equity (ROE) is the ratio of headline earnings to average ordinary shareholders' equity
Gearing < 30%	Gearing is the ratio of average long-term interest-bearing debt to average ordinary shareholders' equity
Dividend cover of x 1,7	Dividend cover represents the ratio of headline earnings to dividends paid to ordinary shareholders

### Return on sales (ROS)

This ratio combines all the key income statement elements, being sales, gross margin, supplier income, expenses (including depreciation and amortisation), and net interest. Every important financial aspect of the retail or wholesale business model is therefore captured in this ratio. In addition, the largest asset investment in the Divisions is net working capital (being inventory and trade receivables), less the associated funding liability (in trade payables). The relative success of management's impact on net working capital will therefore be reflected in changed net finance charges or receipts from one year to the next.

The Divisional ROS targets can be found in the 'Looking forward' section on page 6 and the Operational Review on pages 60 to 83. As a Division reaches new levels of trading or operating efficiency that we believe are permanent, then that Division's target ROS is increased. The Group's target ROS is derived by applying each Division's target ROS to its actual sales.

In the 'Looking forward' section we refer to trading ROS. The difference between trading profit before tax and EBITA is the corporate net interest of R293,6 million (2007: R185,9 million) and the IFRS 2 charge of R67,1 million (2007: R54,3 million) relating to the BEE transaction.



“...the Massmart 2007 Annual Report was judged fourth overall and awarded an Excellent rating...”

GUY HAYWARD CHIEF FINANCIAL OFFICER

Progress to date – Massmart’s current ROS is 5,3% (prior year 4,9%). Massmart has grown its ROS every year since 2000 and we believe that the target of 5,5% remains achievable in the medium term.

### Return on equity

Massmart is committed to delivering superior returns to shareholders. The Group’s medium-term targets are to exceed a 35% return on average ordinary shareholders’ equity.

Progress to date – Massmart’s current return on average shareholders’ equity is 53,0% (2007: 52,3%).

The Divisions are responsible for delivering *operational* returns, being the returns to net working capital and non-current assets excluding goodwill and trademarks. In addition to these operational returns, Massmart, through the Board and Executive Committee, is responsible for delivering *investment* returns that will also include the book value of intangibles (raised on acquisitions or otherwise), as well as setting the Group’s gearing levels that will influence returns to shareholders and the overall risk profile.

As part of this, the Divisions are recapitalised annually by Massmart with non-interest-bearing shareholders’ funds that are equivalent to the book value of long-term assets in each Division. Each therefore must fund its net working capital position through cash or interest-bearing debt, depending upon the characteristics of that business model. This process enables divisional returns to be evaluated and compared on a consistent basis across the Group, and from one year to the next. This policy has not yet been rigidly applied in CBW owing to minority shareholders in that business.

Depending upon the purchase price, retail and wholesale acquisitions tend to generate significant accounting goodwill owing to the relatively low net asset values of those business models. Adjusting for goodwill and trademarks previously written off in 2001 (ie reversing accounting write-offs previously allowed under GAAP), the Group’s return on average shareholders’ equity is 41%.

### Gearing

Given the Group’s high cash generation and our preference for leasing rather than owning most stores, it is difficult to permanently and meaningfully gear (ie maintain a net interest-bearing debt position) the Group over the long term. Massmart prefers some level of gearing, up to a maximum of 30%, in order to leverage the return on shareholders’ equity but without introducing excessive financial risk to the Group. It should be noted that our stores’ lease obligations represent a significant form of permanent gearing (these lease obligations currently represent a discounted present value of approximately R3,2 billion). As regards financing any acquisitions, depending on that company’s cash profile and cash generation ability, this gearing ratio may be increased, but probably to no higher than 50%.

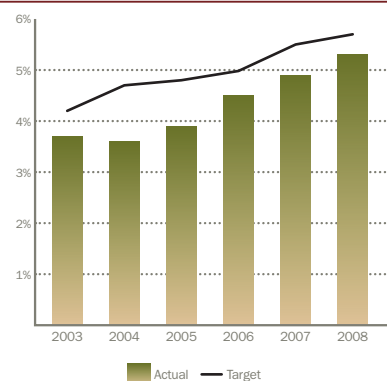
As the period-end balance sheet tends to be unrepresentative of the Group’s average net cash or debt position during the year (showing higher cash balances as monthly creditors are paid after month-end), the Group’s gearing levels can be calculated using the net interest paid (or received) for the period as a proxy.

Progress to date – the Group’s gearing was 9,8% (2007: 18,0%) for the financial year.

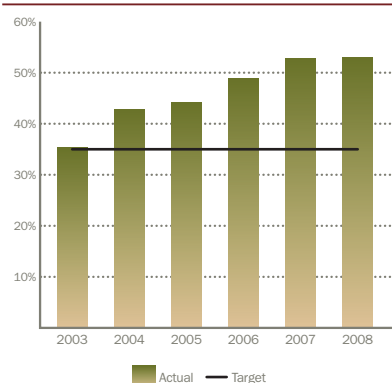
### Dividend cover

Massmart’s current dividend policy is to pay total annual cash distributions representing a x 1,7 dividend cover ratio, unless circumstances dictate otherwise. The reference point for the calculation is headline earnings, which includes the effect of the Thuthukani IFRS 2 change and associated dividend. This ratio is not a target – because it is already being achieved – but is disclosed to give shareholders clarity on future dividend levels. The Board believes that this dividend cover ratio is appropriate given the Group’s current and forecast cash generation, planned capital expenditure and gearing levels.

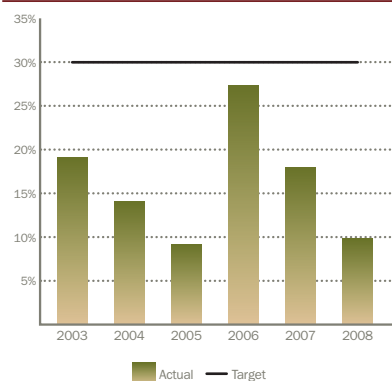
### Return on sales



### Return on equity



### Gearing



The Board has no desire to build up a cash reserve and so will, where practical, reduce dividend covers and/or may execute a share buyback – depending upon the current share price and our view of its valuation – in order to return surplus cash to shareholders.

Historical dividend cover ratios:

	2008	2007	2006	2005	2004	2003
Dividend cover	x 1,7	x 1,7	x 2,0	x 2,0	x 2,0	x 2,5

## Acquisitions

There were no major acquisitions concluded during the financial year.

## Disposals

With effect from the day immediately following the close of the 2008 financial year, the Massdiscounters’ consumer credit business and associated debtors book was sold for cash of R174 million. This disposal therefore has no effect on the 2008 financial figures, apart from the net asset position associated with that business being reflected as ‘Assets held for sale.’ For 2009 this disposal will have no effect on the Group’s financial performance but thereafter should contribute positively to Massdiscounters’ profit.

## Accounting policies

There were no significant changes in accounting policies during the year.

Since 2007, the results for Makro Zimbabwe have been deconsolidated as Massmart can no longer be said to be controlling the day-to-day management of that business following legislative changes in that country. Control is defined as “the power to govern the financial and operating policies of the entity so as to obtain benefits from its activities”. The financial effect is minimal.

For more details, see note 6 in the annual financial statements on page 123.

## Black Economic Empowerment staff equity issue

Massmart’s Black Economic Empowerment (BEE) staff equity issue was effective from October 2006 and so its financial impact had not yet fully annualised in the 2008 financial year.

Full details on this BEE staff equity issue were published in the June 2006 shareholders’ circular but the main financial points are repeated below:

- Equity representing 10% of the Massmart ordinary issued shares, pre-dilution, or 9,1% post-dilution, was issued.
- There were two categories of participant, being the General Staff and Scarce Skills, and separate trusts were formed for both.
- Although the underlying instrument is effectively an option with a strike price of R49,98, the actual legal instruments are two classes of preference shares. The reason preference shares were used was to give the participants voting rights and, in one case, a right to dividends as explained below.
- The first category, ‘A’ preference shares, was a once-off issue to the General Staff trust, called the Thuthukani Trust, for the benefit of all 14 500 permanent employees in the Group at that time. These shares have voting rights equal to those of ordinary shares and have a right to dividends on the following basis: 25% of the ordinary dividend in year 1 (being 2007), 50% of the ordinary dividend in year 2 (2008), 75% of the ordinary dividend in year 3 (2009), and 100% of the ordinary dividend in year 4 (2010). These ‘A’ preference shares are converted into Massmart ordinary shares, for the direct use or benefit of each beneficiary, in three equal annual tranches commencing on 1 October 2010.
- The second category, ‘B’ preference shares, was issued to the Scarce Skills Trust for the benefit of current and future black managers in the Group – and so there will be ongoing issues from this Trust. These shares have voting rights but do not attract dividends. These shares can convert into Massmart ordinary shares, for the direct use or benefit of each beneficiary, in four equal annual tranches commencing from the end of the second year of the issue date.

“...immediately following the close of the 2008 financial year, the Massdiscounters’ consumer credit business... was sold for cash...”

### Further reading

The accounting policies can be found in the Group Financial Statements 113

GROUP FINANCIAL STATEMENTS

At the effective date, the total IFRS 2 *Share-based Payment* charge arising from this BEE staff issue was R373 million. In terms of IFRS 2, this amount must be amortised over the life of the scheme, being six years, commencing from 1 October 2006. The current year's charge was R67 million (2007: R54 million, for a nine-month period) and the charge for 2009 is anticipated to be R75 million. Current South African tax legislation does not allow any tax deduction associated with this non-cash charge.

Using the total IFRS 2 charge of R373 million relative to the Group's market capitalisation at the same date suggests that the total likely dilution to ordinary shareholders of this transaction will be 3,3%. This total, however, does not take into account forfeitures by employees which will reduce the dilution effect. In terms of IFRS 2, the BEE transaction is not yet dilutive, owing to the adjusted strike price, including the IFRS 2 charge, being higher than the average share price over the year.

## Impact of the 53rd week

Like most major international retailers, Massmart runs its internal accounting and administrative timetable using the retail calendar which treats each financial year as an exact 52-week period. This has the effect of a day per year being 'lost' which is then caught up every seventh year by including a 53rd week in the financial calendar. This is not an 'artificial' week – the Group's earnings and cash are higher as a result of trading during this week.

This additional week includes sales, the associated gross margin and a limited amount of variable expenses. The estimated impact of the 53rd week is shown below.

- Sales were R826 million. Total sales growth for the 52-week period was therefore 11,9%.
- Profit before taxation of R86 million. Growth in profit before taxation for the 52-week period was therefore 18,7%.
- Headline earnings of R56 million. Growth in headline earnings for the 52-week period was therefore 16,5% and growth in headline earnings per share 17,3%.
- During the 53rd week the Group's monthly supplier payment cycles commenced, which had the effect of reducing the amount of creditor funding in our working capital.

The 53rd week has two other major consequences, namely that the final dividend declared in this second half is higher than would usually be the case, and that growth in the second half of the 2009 financial year will appear relatively muted compared to this 27-week period.

All figures shown in this report are for the 53-week period, unless noted otherwise.

## Income statement

This review covers the consolidated income statement and the related notes.

### Sales

The Group's average product inflation rate for the 2008 financial year was 7,5%. Our General Merchandise prices for the financial year, using the Group's sales mix, averaged inflation of 1,1%. Food inflation remained high, particularly in commodities where price inflation was as high as 20% in certain categories. Combined product inflation for the Group's Food and Liquor was 12,5%, while Home Improvement reported inflation of 7,5%.

Although there is some pressure on product prices from South African core inflation rising, this is expected to abate slightly from the first quarter of calendar 2009 owing to the base-effect. We are expecting average Group inflation to be 7% for the 2009 financial year.

Total sales of R39 784 million increased by 14,3% over 2007. Comparable stores' sales growth for the 52-week period was 10,8%, non-comparable stores added 1,5% and the 53rd week added another 2,0%.

**“All figures in this report are for the 53-week period, unless noted otherwise.”**

Further reading	
The consolidated income statement and related notes can be found in the Group Financial Statements	109
<b>GROUP FINANCIAL STATEMENTS</b>	
Detailed commentary on Divisional-specific issues can be found in the Operational Review	55
<b>OPERATIONAL REVIEW</b>	

During the financial year the Group opened 12 new stores and closed eight stores, thereby increasing its trading area by an unweighted 1,9% to 1 012 784m<sup>2</sup> (unweighted meaning that the new space has not been proportionately adjusted if only open for part of the financial year). Although 7,3% new space was opened, the closure of the original Dion format stores resulted in significantly lower growth in net space.

Details of stores changes are:

- In Massdiscounters, one Game store was opened in Gauteng, one in KwaZulu-Natal, one in North West and one in the Eastern Cape.
- Also in Massdiscounters, four new-format Dion Wired stores were opened: three in Johannesburg and one in Durban.
- Makro opened a new store, for the first time in three years, in Silver Lakes, to the east of Pretoria.
- In Masscash, the Jumbo store in Nelspruit was closed.
- In Massbuild, Builders Warehouse opened a store in Nelspruit and Builders Express opened three stores in the Johannesburg area.

**Gross profit**

Gross profit of R7 302,2 million reflects an 18,35% gross margin that is just higher than the prior year’s 18,31%. Two factors influenced this: lower gross margins in Massdiscounters as we invested in product pricing to improve our price perception, and slightly higher gross margins in CBW owing to food inflation in that business.

The Group’s gross margin will always be dependent upon the sales mix across the Divisions and the required trading aggression occasioned by competitor activity, but is expected to improve marginally over time owing to the increased contribution from the faster growing Massbuild division. Gross profit includes rebates and other forms of income earned from suppliers as well as ongoing revenue from sales of cellular products and airtime.

**Other income**

Other income of R161,2 million (2007: R157,1 million) comprises royalties and franchise fees from in-store third parties, property rentals, investment income excluding interest, finance charges from Massdiscounters’ consumer credit book, and sundry management and administration fees.

**Expenses**

Total net expenses of R5 378,3 million (2007: R4 855,7 million) represent 13,5% of sales, an improvement on the prior year’s 14,0% of sales. Included in ‘Other operating costs’, however, is a net unrealised gain on foreign exchange transactions and translations of R62,5 million (2007: R41,4 million loss). Adjusting for these amounts changes the expense ratios to 13,68% for 2008 and 13,83% for 2007, still reflecting better expense management performance. There are other large items included in total expenses that are discussed in more detail below.

Owing to ongoing store refurbishments and new stores, the depreciation and amortisation charge of R302,5 million (2007: R267,2 million) increased ahead of sales growth, and will continue to increase as it reflects the higher capital costs of this expansion. Makro, Game and Builders Warehouse have been refurbishing their stores, resulting in higher depreciation charges, compounded by the new Makro store with new capital expenditure of R61 million.

As a result of the annualisation of depreciation arising from the capital expenditure on new stores in 2007/08, and that arising from the new store expenditure scheduled for 2009, the Group’s depreciation charge for 2009 will grow by more than the rate of sales growth.

Employment costs, the Group’s single largest cost category, of R2 736,2 million (2007: R2 449,8 million) are 11,7% higher than the prior year. Included in these figures are IFRS 2 *Share-based Payment* charges totalling R109,1 million (2007: R73,3 million) which are significantly higher owing to the annualising of the IFRS 2 charges associated with the Thuthukani BEE Staff Scheme. Excluding this IFRS 2 charge, total employment costs are 10,5% higher than the prior year and, at 6,6% of sales, an improvement on last year’s equivalent figure of 6,8%. The Group employed 0,5% fewer employees (on a full-time equivalent basis) compared to 2007, despite several new stores, as IT-driven in-store labour scheduling improved the use and rotation of our employees during their working days. Most of this reduction occurred in the fourth quarter of the financial year.

“During the financial year the Group opened 12 new stores and closed eight...”

<b>Further reading</b>	□
Other income is shown in more detail in note 3 in the Group Financial Statements	
	121
GROUP FINANCIAL STATEMENTS	

For the forthcoming financial year the Group's salary increases are between 8% and 10% and the wage increases, which have all been finalised, are in a similar range.

Occupancy costs, the Group's second biggest operating cost, increased by 13,8% to R962,7 million (2007: R846 million). As a percentage of sales, this figure, at 2,42%, is very similar to the prior year equivalent of 2,43%. Total net trading space increased by 1,9%. The lease-smoothing accounting policy applicable to operating leases (thereby affecting store leases) has the effect of keeping comparable-store lease charges broadly equal from one year to the next, and so any increase between the years would be from new stores. Another effect of this accounting policy is that annual lease escalations no longer increase the Group's lease charge. Adjusting for the non-cash lease-smoothing adjustment in both years shows that annual cash occupancy costs increased by 12,8%.

The three major cost categories described above represent almost 74% of the Group's total expenses.

#### Other significant items

As noted above, included in operating profit is a net unrealised gain on foreign exchange transactions and translations of R62,5 million (2007: R41,4 million loss). In the current year this entire amount is equivalent to the realised and unrealised exchange differences from Massdiscounters' African stores (2007: R18 million loss). A further net translation loss of R23 million (2007: R7 million loss) arose during the year primarily from IAS 39 *Financial Instruments: Recognition and Measurement* adjustments relating to forward-exchange contracts held at Massmart, but this was offset by an unrealised gain of R23 million (2007: R16 million loss) that arose on translation of offshore assets held at Massmart Corporate.

When a new store is opened, a large amount of once-off or exceptional operating costs can be incurred in preparing the store (including temporary staff, marketing initiatives, special promotions, signage, amongst others). These costs are referred to as store pre-opening costs and in 2008 amounted to R51 million (2007: R48 million), of which R12 million related to the opening of the new Makro store.

#### Operating profit

Group operating profit of R2 085,1 million (2007: R1 673,3 million) is 24,6% ahead of the prior year and improved from 4,8% to 5,2% of sales. On a 52-week basis, Group operating profit would have been R1 992 million, a 19,1% increase over the prior year and representing 5,0% of the 52-week sales.

This improvement arose from different actions across the Divisions but can broadly be summarised as: sales growth exceeding cost growth; good cost control in Massdiscounters, Makro and CBW; slightly increased gross margins in CBW and slightly lower gross margins in Massdiscounters. Given the anticipated cost increases described above and the expected lower level of sales volumes in 2009, cost control and efficiency remain key imperatives for the Group.

#### Net finance costs

Net interest paid of R64,1 million (2007: R44,4 million) increased owing to higher commercial interest rates and higher levels of inventory carried for most of the financial year. Although significant funds were expended on capital expenditure and share buybacks in 2008, these did not exceed the expenditure on similar items in the prior year. The lower dividend cover implemented in February 2007 has reduced the Group's net cash position by R160 million, compared to the position had the previous higher dividend cover been maintained.

Included in 2007 was a once-off R18,1 million interest charge relating to a settlement reached between Massmart, a major financial institution and the South African Revenue Service (SARS).

Taking into account anticipated capital expenditure and excluding any unforeseen developments or new initiatives, the Group will remain net geared for two years. Using long-term interest-bearing debt, the Group was 9,8% geared (2007: 18,0%).

**“For the forthcoming financial year...wage increases...have all been finalised...”**

#### Further reading

More detail on net finance costs can be found in note 7 in the Group Financial Statements	123
<b>GROUP FINANCIAL STATEMENTS</b>	

**Taxation**

The total tax charge of R662,9 million (2007: R554,8 million) represents an overall tax rate of 32,8% (2007: 34,1%). For several years two factors have caused the Group's tax rate to be higher than the standard South African corporate rate, the first is the charge from the Secondary Tax on Companies (STC), payable on net dividends paid, and the second is the effect of significant non-deductible expenses, specifically the IFRS 2 charge. In the current year, STC added 3,4% (2007: 3,6%) to the tax rate while the non-deductible IFRS 2 charge had a further adverse effect of 1,7% (2007: 1,5%).

Excluding the impact of STC and IFRS 2, Massmart expects its future effective tax rate to be at or near the South African corporate rate of 28%, although higher tax rates in certain foreign jurisdictions may marginally increase this.

Massmart is not concerned about any specific element of historical tax risk in the Group, but there is the uncertainty that material adjustments arising from potentially unfavourable tax assessments from the past tax returns, some of which have not yet been assessed by SARS, could impact future after-tax earnings. In addition, SARS can re-open any tax assessments within three years of issuing such assessment.

**Headline earnings**

Headline earnings of R1 319,4 million (2007: R1 083,3 million) are 21,8% greater than the prior year. Adjusting for the IFRS 2 charge arising from the Thuthukani BEE scheme, which has not yet annualised but will do so from the 2009 financial year, increases revised headline earnings to R1 409 million (2007: R1 146 million) representing growth of 22,9%.

Headline earnings per share (HEPS) of 663,0 cents is 22,7% higher than the 2007 HEPS of 540,4 cents. Following the share buyback during the year, the weighted-average number of shares is below last year and so the growth in headline earnings per share (HEPS) at 22,7% was higher than the growth in headline earnings. After adjusting for the potential future conversion of 4,9 million share options, the diluted HEPS is 647,2 cents.

It should be noted that under IFRS 2 the approximately 20 million 'A' and 'B' preference shares issued under the Thuthukani BEE scheme are not yet included in the diluted headline earnings calculation. In terms of the IFRS 2 rules, the approximately 17,9 million Thuthukani preference shares currently in issue are only included in the diluted earnings per share calculation when Massmart's average share price in any given financial year exceeds R79,66 per share. As noted earlier, however, the total dilution to ordinary shareholders expected from this BEE transaction is 3,3%.

**Balance sheet**

This review covers the consolidated balance sheet and the related notes.

**Non-current assets**

Property, plant and equipment of R1 392,9 million (2007: R1 123,8 million) and goodwill of R1 362,3 million (2007: R1 346,8 million) together represent the greatest proportion of the Group's non-current assets.

Over the past few years Massmart has been refurbishing and building new stores and during this year expenditure of R508,0 million (2007: R391,3 million) was spent on property, plant and equipment. Of this, R243 million (2007: R124 million) was replacement capital expenditure, while the balance of R265 million (2007: R268 million) was invested in new capital assets, including new stores.

Goodwill increased by R15,5 million, reflecting the goodwill from the acquisition of certain of the CBW store managers' minority interests. Under IFRS all goodwill must be tested annually against the value of the business units with which it is associated and, if overstated, that goodwill must be impaired.

<b>Further reading</b>		□
More detail on the Group's taxation charge is in note 8 in the Group		
Financial Statements	124	
.....		
<b>GROUP FINANCIAL STATEMENTS</b>		

<b>Further reading</b>		□
More details on the headline earnings reconciliation and the weighted-average number of share workings are in note 10 in the		
Group Financial Statements	125	
.....		
<b>GROUP FINANCIAL STATEMENTS</b>		

<b>Further reading</b>		□
The consolidated balance sheet and related notes can be found in		
the Group Financial Statements	110	
.....		
<b>GROUP FINANCIAL STATEMENTS</b>		

The figure of R132,0 million (2007: R130,2 million) in 'Other intangibles' primarily represents computer software that IFRS requires to be disclosed in this category. In terms of IFRS the 'depreciation charge' arising from this asset category is classified as an amortisation charge.

Capital expenditure for 2009 is budgeted to be R627 million and, *inter alia*, reflects the investment in eight new stores that are scheduled to be opened during the 2009 financial year, representing new space growth of 5,1%. As can be seen in the graph, despite the growth of the Group and the acceleration in new stores and refurbishments, capital expenditure since 2003 has generally represented 1,0% to 1,5% of Group sales.

### Investments and other financial assets

Investments of R311,3 million (2007: R241,2 million) comprise mainly a R243,2 million (2007: R168,2 million) investment in an international treasury, shipping and trading business unit, revalued to reflect the foreign-denominated net assets within that module. The R45 million shown as a bare dominium revaluation represents the Group's proportionate share of the market value of the bare dominiums in certain Makro stores.

The held-to-maturity investment of R560,7 million and the associated liability represents a ten-year investment structure that terminates in February 2009.

Other financial assets include executive and employee loans of R226,7 million (2007: R173,4 million), that being primarily of loans totalling R174,4 million (2007: R127,1 million) attracting zero percent interest and owed by participants in the Massmart employee share purchase trust. This loan amount reduces as employees sell their shares and repay the associated loans, and increases where executives elect to own Massmart shares, funded with these loans, rather than options issued by the trust. The finance lease deposit of R45 million is related to the financing of the Makro Strubens Valley store.

### Deferred tax

The deferred tax asset of R415,2 million (2007: R432,8 million) arises primarily from numerous temporary differences, including tax deductions on trademarks, the operating lease liability arising from the lease-smoothing accounting policy, and unutilised assessed losses. This net asset will reduce over time as the associated tax benefits are utilised.

One of the consequences of the reduction in the South African corporate tax rate during 2008 was that the proportionate release of the net deferred tax asset reduced the net benefit to the Group's tax charge for this financial year.

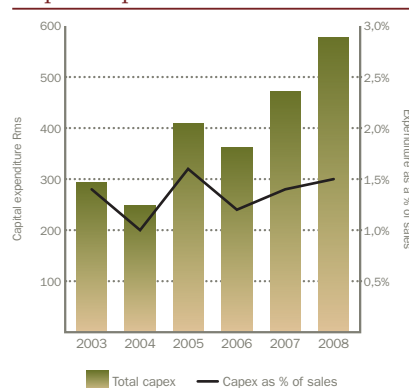
### Current assets

Net inventories of R4 758,6 million (2007: R4 027,3 million) represent approximately 53 days' sales (using the historic basis), just higher than the prior year's figure of 52 days. Inventory levels were deliberately increased in two Divisions. In response to the supply constraints currently being experienced by major South African food suppliers, both Masscash and Makro are carrying more food inventory to avoid out-of-stock situations. Makro was also carrying slightly higher inventory at year-end in anticipation of a potential IT information 'black-out' during the SAP upgrade that went live on 29 and 30 June 2008. The combined effect of these issues is that year-end inventory levels were higher by about R230 million, representing 2,5 days of sales.

In general, Massdiscounters, being a retail discounter with 90 stores, has the highest inventory levels and its sales days in inventory are almost double those for Massmart's wholesale businesses (Makro and Masscash). Builders Warehouse also has higher inventory days given the broader and deeper merchandise range in those stores. As a result of good in-store planning and buying disciplines, Builders Warehouse's year-end inventory was lower than that of the prior year.

The net inventory of General Merchandise at R2 183,7 million (2007: R1 987,3 million) represents almost half of total Group inventory. This is to be expected given the higher inventory days in that category.

### Capital expenditure



### Further reading

The following sections can be found in the Group Financial Statements:

Property, plant and equipment (note 11)	126
Goodwill (note 12)	128
Other intangible assets (note 13)	129
Investments (note 14)	130
Other financial assets (note 15)	132
Deferred taxation (note 16)	133
Inventory (note 17)	134
Trade receivables with additional IFRS 7 disclosure (note 18)	135
Asset held for sale (note 19)	135

GROUP FINANCIAL STATEMENTS

Total trade receivables and prepayments, net of provisions, is R1 764,2 million (2007: R1 876,5 million) and is 6,0% lower than the prior year's figure. Included here are net trade accounts receivable of R1 074,7 million (2007: R980,8 million), which increased by only 9,6%, well below the rate of sales growth. This reduction is the result of improved debtors collection at Shield (in Masscash). Although trade credit is offered to certain customers in all Massbuild businesses and in Masscash, it is well controlled, often insured with a credit risk insurer, and kept within the Group's parameters, and does not affect the Group's working capital. The improved situation is also reflected in lower allowances for doubtful debts at year-end, which reduced from 9% of total trade receivables to 5,3% at year-end.

In the current year the total consumer accounts receivable is Rnil (2007: R283,4 million). This consumer credit, being hire-purchase and revolving credit, is found only in Massdiscounters and was sold to the independent financial services provider, RCS, immediately after the close of the 2008 financial year-end. For this reason, in the current year this balance has been shown as an 'Asset held for sale.' For more detail, refer also to the commentary on credit risk in the Financial risks section on page 159.

### Non-current liabilities

This total category comprises medium-term bank loans, capitalised finance leases, income received in advance relating to extended warranties, the operating lease liability arising from the lease-smoothing adjustment, deferred tax and long-term provisions.

Non-current interest-bearing liabilities are R267,7million (2007: R402,7 million) and are medium-term bank loans. This balance reduced during the financial year owing to the amortising payment profile on the two R250 million five-year loans. These loans were raised during the 2006 financial year to finance the Massbuild acquisitions and interest on both loans is fixed at 8,8% and 8,7% respectively.

Capitalised finance lease balances are R82,0 million (2007: R89,2 million).

Non-current non-interest-bearing liabilities are R557,2 million, which is coincidentally the same figure in the prior year. The main balance is the operating lease liability of R462,0 million (2007: R475,0 million) arising from the lease-smoothing accounting policy and which will be released over the remaining period of the Group's operating leases.

Included in non-current liabilities (non-current provisions) is the long-term provision of R47,7 million (2007: R45,0 million) arising from the actuarial valuation of the Group's potential liability arising from post-retirement medical aid contributions owed to current and future retirees. This liability is unfunded. With effect from 1999, post-retirement medical aid benefits were no longer offered to new employees joining the Group.

The deferred tax liability of R141,9 million (2007: R115,5 million) arises primarily from prepayments and property, plant and equipment.

### Current liabilities

Included in the total trade and other payables figures of R7 380,0 million are trade payables of R5 928,1 million (2007: R5 285,8 million) representing approximately 58 days of cost of sales (using the historic basis), which is lower than the prior year's figure of 60 days. As noted earlier, owing to payments to creditors being made shortly after each month-end, the Group trade payables balances at year-end are not representative of the average during the remaining period. The amount by which the year-end trade payables is overstated in comparison to the average cannot be accurately calculated but is approximately R1 billion.

The current taxation liability of R543,1 million (2007: R534,4 million) reflects the Group's liability for provisional corporate tax payments that are generally payable within a few days of the financial year-end.

### Further reading

The following sections can be found in the Group Financial Statements:

Deferred taxation (note 16)	133
Non-current liabilities (note 23)	140
Non-current provisions (note 24)	141
Trade and other payables (note 25)	141

GROUP FINANCIAL STATEMENTS

## Cash flow statement

Operating cash before working capital movements of R2 394,9 million (2007: R1 926,4 million) is 24,3% higher than the prior year and closely approximates this year's operating profit before depreciation, amortisation and impairment of R2 387,6 million, demonstrating the fundamental cash underpin of Massmart's earnings.

Cash taxation paid of R668,1 million (2007: R531,6 million) increased owing to the growth in taxable income.

The 25,6% increase in the total dividend paid in cash of R709,9 million approximates the Group's profit growth.

Total capital expenditure (replacement and expansion) was R577,9 million, an increase on the prior year's total of R470,8 million.

Included in the R325,5 million under 'Other investing activities' is the R281 million invested in this year's share buyback programme. A total of 3,3 shares were purchased at an average price of R83,10 per share.

## Financial risks

### Liquidity risk

Liquidity risk is considered low owing to the Group's conservative funding structure and its high cash generation. Massmart's liquidity requirements are continually assessed through the Group's cash management and treasury function.

The Group has total banking facilities, incorporating overnight, short- and medium-term borrowings, letters of credit, forward exchange contracts and electronic fund transfers, of R2 951 million (2007: R3 492 million). As at June 2008, total interest-bearing debt amounted to R535 million (2007: R568 million).

As the Group begins to build inventory levels for the festive season, net interest-bearing debt will increase up to a maximum of approximately R1,0 billion in November, but will reduce rapidly as year-end trading accelerates with higher cash proceeds.

### Interest risk

Interest rate exposure is actively monitored owing to the Group's significant intra-month cash movements and the seasonal changes in its net funding profile during the financial year. As noted above, interest rates on the two medium-term bank loans are fixed at 8,8% and 8,7% respectively.

Of the Group's total financial liabilities of R6,3 billion, 93% or R5,9 billion of this is represented by non-interest-bearing accounts payable funding.

### Credit risk

Credit is available to wholesale customers at Makro, Massbuild and Masscash, and is adequately controlled by using appropriately trained personnel, applying credit granting criteria, continual monitoring and the use of software tools. A portion of the trade debtors book in Shield is insured with an international insurance company and a further portion is secured through general notarial bonds, pledges and other forms of security. Similarly, the trade debtors books in Builders Warehouse and Trade Depot are also insured with an international insurance company.

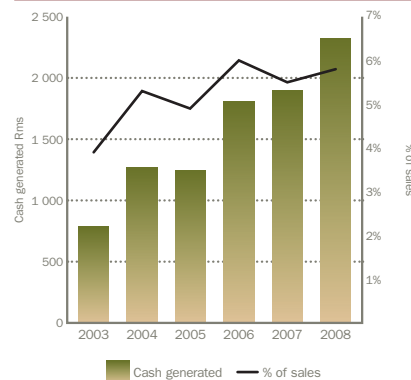
Massmart was only exposed to consumer debt through its hire-purchase and revolving-credit debtors books in Massdiscounters, and, as noted above, this book was sold immediately after the financial year-end.

### Further reading

The consolidated cash flow statement can be found in the Group Financial Statements 111

GROUP FINANCIAL STATEMENTS

### Cash generated by operations



### Further reading

More detail on liquidity risk, interest risk, credit risk and currency risk can be found in note 37 in the Group Financial Statements 156

GROUP FINANCIAL STATEMENTS

**Currency risk**

Where possible and practical, currency risk in the Group is actively managed. All foreign-denominated trading liabilities are covered by matching forward-exchange contracts. At financial year-end, there were open forward exchange contracts totalling R462 million (2007: R433 million) of which 95% were US Dollar liabilities.

The sensitivity of the Group to this exposure is shown in note 37 on page 160. In brief, if the Rand strengthened by 5% from the year-end rate of R7,96/US Dollar, there would be a R33 million charge, while a 5% weakening would raise a R12 million gain.

Foreign-denominated assets are not covered by forward exchange contracts, as these are permanent assets held for the long term.

**Technical review**

The Board reports that the appropriate accounting policies, supported by sound and prudent management judgement and estimates, have been consistently applied.

The Group's accounting policies are governed by IFRS and the AC 500 series as issued by the Accounting Practices Board. Guidance has been obtained from IFRICs and circulars effective on 1 October 2008. Owing to the nature and volatility of Exposure Drafts (EDs), no review has been provided.

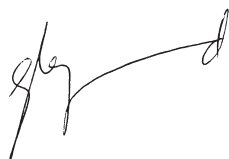
The Group maintains the view that accounting standards set the minimum requirement for financial reporting. The financial statements in this annual report have been prepared with the aim of exposing the reader to a very detailed view of the numbers, using a simplified approach, in the hope of facilitating a deeper and informed understanding of the business.

**Going-concern assertion**

The Board has formally considered the going-concern assertion for Massmart and its subsidiaries and believes that it is appropriate for the forthcoming financial year. See page 108 for more detail.

**Appreciation**

As always, I would like to acknowledge and pay tribute to the high-quality performance and significant effort invested by my financial colleagues and their teams at all the Massmart Divisions and at the Massmart corporate office.



**Guy Hayward**  
Chief Financial Officer

1 October 2008

<b>Further reading</b>	□
A detailed technical review can be found in note 2 in the	
Group Financial Statements	118
.....	
<b>GROUP FINANCIAL STATEMENTS</b>	

“Given the current economic environment, we are cautious about the year ahead but are confident that our business model will prove its resilience.”

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GRANT PATTISON CHIEF EXECUTIVE OFFICER