

# Chief Executive's statement

**Since we started in 1995, Howdens has grown to become the leading supplier of kitchens in the UK. When we began with our first fourteen depots, selling directly to the builder wasn't as obvious as it seems today.**

I am pleased to report that Howdens has seen another successful year, ending 2016 with 642 depots, more than 450,000 customer accounts and 8,900 employees. We continue to expand and are laying down the foundations for the next phase of growth, providing further opportunities for our people, their families as well as the business.

## OUR MODEL

Since we started in 1995, Howdens has grown to become the leading supplier of kitchens in the UK. When we began with our first fourteen depots, selling directly to the builder wasn't as obvious as it seems today.

From the outset, our business model has been to make the builder the centre of what we do. We supply kitchens directly to them from local depots,

run by managers who understand their needs and can make decisions on the spot. Importantly, we ensure that our depot managers have no worries about the price, quality, or style of the kitchens we supply to them.

It remains crucial to me that the business should be also worthwhile for all concerned – for the people who work for Howdens, buy from Howdens, who supply Howdens, as well as our local communities. By doing so, I believe we can create a virtuous circle, securing a long-term sustainable future for the Group.

## Local supply

The key to our trade-only business model is our local depots, who supply small builder customers, with more than fifty kitchen ranges in stock, together with sinks and taps, appliances, flooring and hardware. Our depots also have a range of joinery including internal and external doors, skirting and stair parts.

Importantly, we do not tell the depot manager how to run their depot. Each manager is empowered to make the key decisions – set discounts for individual account holders, develop new accounts, market their products, and set stock and staffing levels. Our managers are authorised to swap items, take decisions and give advice. Every day, they balance the needs of builders, end-users, staff and everyone in their local area who has an interest in the success of their depot. No two geographic areas are the same and this allows managers to create a business that is tailored to the local builder.

## Local incentives

So that managers run their depot as if it were their own business, all the people in the depot receive a monthly bonus based on profitability measures, which can represent a significant percentage of their total compensation. This means that they are focussed on serving their builder customers and growing their business. And I am pleased to note that at the end of 2016, we had more than 450,000 customer accounts, up from 430,000 the previous year.

## Local service for builders

Our aim is simple. It is to make a builder's life as easy as we can, so they can attract customers, secure work and run a profitable business.

When a builder comes into one of our depots for the first time, we open a nett monthly account for them, enabling the management of cash flow, so they can complete the job before paying Howdens. The local depot manager is authorised to give each builder a personal, confidential discount, giving builders the freedom to manage their own margin.

Once the builder has been contacted regarding installing a new kitchen, a designer will go to the prospective customer's property. The designer will create an expert, accurate plan, ensuring that everything will look good and fit properly. This saves the builder time, which helps their profitability. Both builder and their customer can come into the local depot and see the kitchen displayed on a large screen via our bespoke computer aided display software, enabling any final changes to be made before signing off on the job.

## Saving time for the builder

Once the kitchen and price have been agreed on, importantly, a Howdens depot is always in stock and is a normally a short drive away. There's no waiting for items to be ordered, or replaced, or swapped, or brought back. This allows the builder to plan and start the job when they are ready to do so, ensuring there are no delays. In turn, this allows us to collect payments efficiently, as all of the builder's requirements can be fully supplied and signed off by our depots.

We also save time by selling pre-assembled cabinets, increasingly with pre-fitted elements, which saves builders time on site. Our cabinets are built to high standards of consistency, are rigorously tested and do not break, ensuring that the builder does not have to go back to the depot, again saving time and ensuring that the building job does not get delayed.

## Changing tastes and new demands

It is important for the builder when they show Howdens' kitchens to their customer, that our kitchens look good. Kitchen technology and design do not stand still, and there should be no worries at the depot about the suitability of our product lines. We recognise that kitchens are an area in which taste and fashion are moving faster than before.

We ensure that our range of kitchens and appliances are regularly refreshed to meet the builders' and their customer's expectations for price, look and feel. A number of new products were introduced during the year across all categories.

Notable amongst these were three new Burford ranges with a textured wood grain finish, as a lower priced option to the Tewkesbury family. We also introduced three new grey kitchens in our Greenwich and Clerkenwell families, and an ivory Greenwich Shaker door, following the growth of this colourway. We have seen positive developments with our range of granite worktops.

We have also successfully tested pre-finished doors to make the builders' life easier, which will be rolled out to all depots during 2017.

Given the increasing demand for new kitchen designs, during 2017, we will accelerate product introductions, bringing to market around twenty new kitchen ranges, an upgraded cabinet platform, a refreshed design for our Lamona range of appliances, as well as a new collection of sinks, taps, worktops and joinery.

## Our suppliers and supply chain

We have our own warehouses and distribution operations, and our trucks deliver our product only to Howdens depots. During the peak autumn trading period in 2016 (period 11), our supply division made 9,500 deliveries to our depots, and of the 7.4 million items received, all were correctly delivered. This is only possible if there is a shared understanding of what is expected, ensuring a smooth operation of our supply chain and the support functions on which the depots depend.

We were able to have 100% availability of products to our depots during period 11, demonstrating the strength of our supply chain. Achieving this level of service demonstrates to me our shared values and positive personal relationships, both within Howdens and with our suppliers of bought-in product and raw materials.

## Our manufacturing

We have two manufacturing facilities, one in Howden, Yorkshire and one in Runcorn, Cheshire, which are configured to meet our exact requirements. Our site in Runcorn specialises in standard cabinet boxes, while the site in Howden also deals with shorter-run products.

Both only serve one customer – Howdens – and so their working practices and scheduling exactly match the requirements of our depots. Within our factories, the machinery is bespoke to us and work is done to our specifications. The result is an efficient system with no unnecessary waste, whether of time, space, or product. We believe that our cabinets cost much less than we could source externally, providing Howdens with a significant cost advantage.



# Chief Executive's statement continued

## Support systems

In order to meet current and future requirements, we continue to invest in robust, stable and scalable systems. These include manufacturing, warehouse management, transport monitoring, depot stock and sales reporting, payment processing, cyber-security and management information, as well as industry-leading design tools for kitchen planning.

## Depots and costs

Howdens has chosen to serve trade-only, and as such, does not have to bear the costs associated with kitchen retailers, such as high-street showrooms, installation services and national advertising campaigns. A typical Howdens depot occupies around 10,000 square feet on an industrial estate and costs a fraction of high-street retail properties.

On average, a depot costs approximately £300,000 to fit out and breaks even once it has achieved annual sales of £650,000. This is typically two years after we first open the depot. In general, a depot reaches maturity after approximately seven years of trading.

## Working capital

We extend a significant amount of working capital to builders who have a trade account with Howdens, which in 2016 during period 11 peaked at around £220m. At the same time, we have a highly efficient collection operation and the total cost of credit control, including bad debts, remains less than 1% of Group revenue.

## Market conditions

We saw a number of developments in the market during 2016. In April 2016, there were changes to UK Stamp Duty on house purchases, which brought forward market activity to the first half of the year. In the second half of the year, we saw a shift in both the foreign exchange markets and consumer confidence.

While we saw positive volume growth for the market in the first half of the year, we saw negative volume growth in the second half. In the second half, we also saw a decline in the pound against the US dollar and the Euro. Howdens sells a mixture of its own manufactured product and bought-in goods, much from international manufacturers and the direct impact of the decline in the pound during 2016 will result in extra costs going forward.

This, as well as increases in costs in areas such as salaries, will require Howdens to increase prices at greater pace than in the previous few years. We have already acted on this and implemented a range of price increases - earlier than our usual annual pattern - at the end of 2016.

## OUR MARKET

In Great Britain, there are around 26m households, of which approximately two-thirds are owner-occupied and one-third is rented. Regardless of ownership, all of these properties are likely to need a new kitchen at some time.

Every home has a kitchen and this is the centre of the home. As our way of life and expectations change, so does the kitchen, which is becoming more complex and has greater functionality. As a result, the types of kitchens demanded by today's lifestyle means that DIY is not a reasonable option for most people. The level of skill required to fit today's kitchens, due to the types of cabinets, finishes, appliances and interior work within the cabinet, is beyond many of us, and we simply don't have the time to do the work involved.

## The connected home

One change we see impacting the kitchen, are more and more devices connected together in the home, such as heating, lighting, and security. These are being controlled from a mobile or tablet and as the home gets more screen-led, this means that a kitchen will steadily become a much more complex product than before. At Howdens, we are actively investigating how customers use their screens to interact with the devices in their kitchen.

The growth in complexity of the kitchen means that builders want sound advice to meet increased customer expectations. This is why we ensure that our depot staff are trained to the highest standards and are increasing our focus on apprenticeships. And as kitchens become more complex, we are also increasing our investment in people with specific skills, such as designers, salespeople and managers.

## More for the builder

The products we sell have to meet the requirements of an increasingly demanding regulatory environment. Builders need to know that they comply in areas such as safety, data security, energy use, sustainability, and waste management. We discuss how we address regulations and expectations in the Corporate Social Responsibility Report beginning on page 27.

## OUR STRATEGY

Our strategy has been to do things well - first time. For a builder, this means that they can open an account quickly and simply with us, start doing business, receive the support they need to help win customers, while knowing the product they want will be in stock and of the right quality.

As Howdens continues to expand, this brings both opportunities and challenges to the business. In order to meet the potential for growth, we continue to invest in areas including people, new depots, systems, manufacturing and distribution capabilities. We believe that the additional expenditure programme is crucial to provide the platform for the continued sustainable expansion of Howdens.

## Depot expansion

We believe that there is some way to go before we have saturated the UK market and continue to see significant opportunities to grow our business. We expect to open around 30 new depots during 2017.

While we take account of market conditions in planning our roll-out of new depots, we continue to see untapped requirement by builders for a local and convenient service in much of the country. This need is shown by the fact that when we add a new depot near to an existing one, we see overall sales increase in the area within a short time.

## Manufacturing investment

In order to deliver the potential we see in our market and ensure supply as we expand, we are undertaking significant investment in our supply chain. This involves replacing aging machinery, increasing production capacity where necessary and ensuring adequate disaster recovery capability.

## Distribution

We currently have a one million square feet warehouse in Northampton which is nearly forty years old. In order to migrate from this older facility and meet our future requirements for warehousing capacity, we are looking to expand into two new warehouses, both of which will be more efficient than Northampton due to their roof height and ability to stack product.

This first warehouse comprises 650,000 square feet of distribution capabilities in Raunds, Northampton, which is to the east of our existing national distribution centre in Northampton. The warehouse was handed over to us in July, fit-out has been completed and IT systems integration is underway.

## International expansion

We continue to investigate the opportunities for Howdens in Europe. At the end of 2016, we had twenty four depots outside the UK: twenty in France, two in Belgium, one in the Netherlands and one in Germany. We have been in mainland Europe for eleven years and continue to learn. We intend to thoroughly understand these markets before any decision is made to expand in them.

## Aftercare

The key to our business is service. In an increasingly digital world, Howdens provides an alternative way of working, with local people providing our products mostly via face-to-face communication. It is vital, as we move towards an increasingly complex and connected kitchen that we expand our aftercare service, so that builders and their customers can call us to explain and sort out any issues with their kitchen.

In order to do that, we continue to recruit good people who understand our values and culture, and we support our staff with increased levels of training, targeted incentives, better systems and improved planning tools.

## People and service

The home is becoming more complex and digital technology is becoming more pervasive. In order to reflect the changes to the market and our increasing focus on aftercare, we have expanded our mission statement, which now reads:

"To supply from local stock nationwide the small builder's ever-changing, routine, integrated kitchen and joinery requirements, assuring best local price, no-call-back quality and confidential trade terms, and to provide the builder's customer with enough choice, advice and aftersales to make a home to be proud of."

I believe that including service directly into our mission statement will enable Howdens to continue to stand out from the crowd.

## Worthwhile for all

It is worth reiterating that the key aim of Howdens is to create a business that is worthwhile for all concerned - customers, prospective customers, homeowners, tenants, local communities, our suppliers, investors, staff and their families, and our apprentices.

Since 1995, we have grown in a balanced way, investing in sensible things and being prepared for all market conditions. Underlying our success has been the lowest cost and a flexible approach to our production, a low break-even point for our depots and an entrepreneurial spirit.

I look forward to the next phase of our growth with confidence.

**Matthew Ingle**  
Chief Executive Officer

22 February 2017