

Strategy implementation drivers

We use five drivers to achieve our strategic vision:

1. Growth in LFL at the main formats due to the introduction of a new value proposition
2. Sustaining our margin and ensuring investment in price leadership by enhancing operational efficiency at the store network and supply chain
3. Efficient growth in the store network
4. Expanding the customer's wallet share through a multi-format proposition linked to a unified loyalty program
5. Creating a platform for future growth through an omni-channel proposition

Growth in LFL in the main formats due to the introduction of a new value proposition

One of our Company's top priorities is to increase LFL within its main formats. In many regions, we are lagging behind our competitors in terms of sales density.

Closing this gap will significantly increase our revenue. To this end, we have launched a project to create a new customer value proposition (CVP) for our customers at locations tailored to the target audience and shopping missions.

The CVP determines all key aspects of the store's perception:

- Retail space and location
- Assortment, price, and promotions
- Atmosphere, experience, and communication

In 2018, we developed detailed CVPs for each of the main formats based on consumer research and an analysis of our competitors:

MAGNIT

The Company is focusing on its main format – convenience stores. This is the backbone format for Magnit and a rapidly growing segment in Russian retail. It's a convenient store for daily shopping that customers trust. The format offers a suitable range of products, prices that are always competitive, and the opportunity to experience the benefits of the Magnit family of stores. The main missions are routine top-up, food for tonight, or minor stock-up. The convenience store is a leader in terms of «favorable price» perception compared with its formatted competitors, has specific locations, and maintains its margins.

MAGNIT FAMILY

«Magnit Family» is a full-fledged supermarket for the whole family with an expanded product range and improved consumer experience, but which also has offerings for price-sensitive segments and is perceived as a value-for-money place to shop. This format has the ability to attract new target audiences for Magnit – comfort seekers and business people. Such customers are more demanding in terms of the quality of service and product range and less sensitive to prices. At the same time, we have retained our appeal to the three main segments – saving fans, goal-oriented customers, and enthusiasts. Target missions: routine top-up, major shopping, food for tonight, and eating out.

MAGNIT PHARMACY

The main competitive advantage of pharmacies is simple and easy navigation, a convenient open display, and friendly staff that is accessible to customers (not behind the glass wall) and willing to consult on the product. Large pharmacies offer additional services. The format enables customers to fix basic health issues and find preventive health care at an affordable price. The open display combined with the pharmacist's friendliness and expertise creates an atmosphere of simplicity, convenience, and trust. Basic issues can be solved with the guaranteed availability of the most in-demand drugs as well as medicines for acute/transient conditions. Preventive care includes specially designed «health baskets» and the purchase of drugs for chronic diseases.

MAGNIT COSMETIC

A store for women aged 30 to 55 years where they can enjoy regular shopping for personal care and household goods. This format is based on a basic approach to the customer experience: sophisticated and appropriate assortment, good prices, friendly staff alongside with the expertise in beauty products, and all other advantages of the Magnit family of stores.

Introducing the new CVP

We plan to start introducing the new CVP in 2019. To this end, we are carrying out a number of initiatives:

- The main components of the CVP involve comprehensively updating the product range, ensuring it meets customers' needs, and creates points of differentiation. The latter is particularly important for target categories – the ones in which our proposition will be much stronger than those of our competitors. We have already revised the basic principles for building our product range at the national level and over the course of 2019 we plan to highly localize the range through using district-based teams. In a number of large-format stores, we will also launch a reinforced proposition in the farm product, pet product, and baby product categories
- New pricing methods will help more clearly determine the competitive level of regular prices for each outlet. A new-look approach to promos will allow us to strategically manage promotional activities based on advanced analytics and make promos both more attractive to consumers and more profitable for us
- Optimizing the supply chain will improve the quality and freshness of the products on the shelf. Introducing modern retail technologies at the store level will enhance service standards (including displays, price tag matching, cleanliness, and queues) without any additional staff costs
- To support the CVP, we will continue the redesign program for retail outlets. In fact, the latest-generation redesigns have shown sales growth of more than +10% in all formats. As part of the redesign, we are conducting major repairs, refurbishing equipment, equipping the storefronts with stained glass, and updating the entrance space, exterior and interior decorations, and navigation. The new CVP will be introduced at stores redesigned under the previous concept as part of the light redesign program (with minimal capital expenditures)
- A new strategy for communications and the Magnit Store Family brand. Magnit will support the updated CVP. We will build a communications system with target customer segments based on the key emotional and practical themes for each format

Sustaining our margin and ensuring investment in price leadership by enhancing operational efficiency at the store network and supply chain

Optimizing processes and introducing technologies at the store network and supply chain will not only allow for implementing the CVP without additional transaction costs, but will create an opportunity for additional investments in price leadership.

Optimization of processes and technologies at the store network

Projects launched in 2018:

- Processes were updated at retail outlets. We optimized working hours at the retail outlet level, reduced the amount of administrative burden, launched staff rankings based on the quality of staff work, and optimized acceptance and display processes to reduce losses
- We added more cash registers and shopping carts to stores to increase throughput
- Store management at the district-level focused on store sales and mandatory visits to stores were introduced

The following projects will be implemented in the long term:

- Processes will be updated at stores, including trust-based acceptance and end-to-end digital workflow
- New equipment will be introduced (e.g. digital price tags and price checkers)
- The development of the supervisor system will be continued, and there will be greater availability of information on store KPIs

Optimization of processes and technologies in logistics

Projects launched in 2018:

- Improved planning and reduced logistic peaks
- Increased level of service from 78% to 82%
- 15% reduction in inventory at distribution centers
- Reduced workflow
- Launch of a supplier pooling project

Projects to be launched and completed by 2023:

- The transport structure will be revised and the proportion of contractors will be increased
- We will enhance quality control and freshness throughout the supply chain
- We will revise processes and tools, improve the quality of forecasts, and optimize the management structure
- In the future, we will enhance the level of service and further reduce inventory

Efficient growth in the store network

As the market continues to consolidate, the growth and development of the network is a matter of long-term survival. It is essential to ensure growth in the Company's market share in order to maintain a leading procurement position. The pace of development must also be maintained since the battle among retailers for locations closest to consumers has intensified amidst consolidation.

We plan to expand retail space using three sources of growth:

- The M&A of small modern retail networks that find themselves in a difficult situation as a result of price pressure from federal competitors
- Natural growth in locations with a low concentration of modern retail due to the displacement of traditional retail and regional networks
- Moving into retail space that emerges from the construction of new residential areas

We will ensure the efficiency of investment in the network's growth through a combination of geographical information systems and investment rules. To pre-determine the optimal locations, we will use an algorithm that takes into account the population in the coverage area, current traffic flows and points of interest as well as competition at a specific address. To make the final decisions, we have built a transparent process of financial approval for investments at the retail outlet level.

Expanding the customer's wallet share through a multi-format proposition linked to a unified loyalty program

In order to become the main retail platform of the Russian Federation and to fully meet the basic needs of our customers, we plan to launch a number of new formats and cubes.

Formats:

- Magnit Pharmacy is a simple, convenient, and reliable way to address all your basic health needs, including disease prevention, at an affordable price. The Pharmacy's success is driven by a high-quality customer proposition (recommendations and an open retail area) and unique multi-product offerings for the treatment and prevention of some of the most common health problems. We will build Pharmacies based on the traffic of the main formats and combine all the propositions with a unified loyalty program.
- Magnit Wholesale offers a format to meet the needs of a special shopping mission. The format will offer a range with a limited share of fresh products and large packages of dry goods.
- Magnit Post is an ultra-small format in collaboration with Russian Post to provide a basic product range in a wide range of locations throughout Russia without rent expenses and with minimal staff costs. With this format, we will be able to ensure our presence in the most remote corners of our country.

Cubes:

We are also planning to launch specialized cubes (a store-within-a-store) in large formats with the unique grocery offerings and additional customer experience. At present, we have already conducted a series of successful tests of farm product, of the potential of farm product, pet product, and baby product cubes.

In an effort to unite the whole Magnit Store Family, we plan to launch a loyalty program in the first quarter of 2019 that will become available throughout Magnit geographical presence by the end of 2019.

As the program kicks off, we will launch a cross-format loyalty card with a points system and three loyalty levels. Going forward, we plan to launch personalized promo and affiliate programs by the end of 2019. As part of the rollout of the loyalty program, we will also launch a new mobile app.

Creating a platform for future growth through an omni-channel proposition

To ensure long-term growth beyond the 2023 strategy, today we need to pilot and create an omni-channel eco-system that will ensure our presence in the fastest-growing market segment, enable us to meet the unfulfilled demand of our customers, and create an additional channel of communication with the consumer.

We plan to create an omni-channel eco-system that will offer:

- A high-quality product range and ease of choice (search, rating, and pricing)
- A convenient payment and delivery service (internal payment service, fast delivery, and friendly support)
- Trust and an understanding of demand and loyalty (mass personalization)

In 2019, we are planning to launch a pilot project to deliver our core hypermarket range offering to customers in Krasnodar in order to test demand for omni-channel offerings outside of Moscow and St. Petersburg.

Internal changes at Magnit

In order to successfully implement the five drivers and achieve our vision, Magnit will need to transform internally as well. We will revamp the organization and create a new corporate culture.

We are planning the following initiatives over the course of 2019:

- We will review the approach to the Company management. We need to update and merge outdated IT systems, create a unified policy for handling data and analytics, and build data-based decision-making processes
- We will build up our functional expertise. As one of the top priorities, we will focus on creating category management teams and CVP. We will also start developing expertise in analytics, big data, and digital marketing
- We will decentralize the organization based on multi-format districts to speed up the decision-making cycle and provide an understanding of the local consumer using functional teams at the local level. We will also launch a common service center and improve management efficiency.

In addition to organizational transformation, Magnit will need to convey its strategic goals to the entire organization and shift the focus from executing processes to the result in order to implement the strategy. Customer focus will become a part of Magnit's DNA.