

Case Study:

My Price Discounter Stores

- Underpenetrated market segment in Russia compared to developed markets
- Fast growing channel targeting price-sensitive consumers
- Rolling out discounter stores after success of pilot project
- Enabling expansion into new regional and remote locations
- Limited assortment in lower-price segments

Expanding Magnit's offering into formats that are complementary to the core business to better satisfy consumer needs is central to our corporate strategy. We regularly pilot new store formats to cover the maximum number of relevant shopping missions and attract customer segments.

Magnit started piloting discounter stores in July 2020 in response to the fast-changing economic environment. As at 31 December 2021 the Company had 190 operating My Price discounters compared to 15 stores a year ago. During 2021 Magnit opened 175 stores. Today we have over 200 discounters in operation delivering encouraging results.

The discounter concept is aimed at price-sensitive consumers who frequently make minor purchases of traditional goods or stock up on products.

Market background

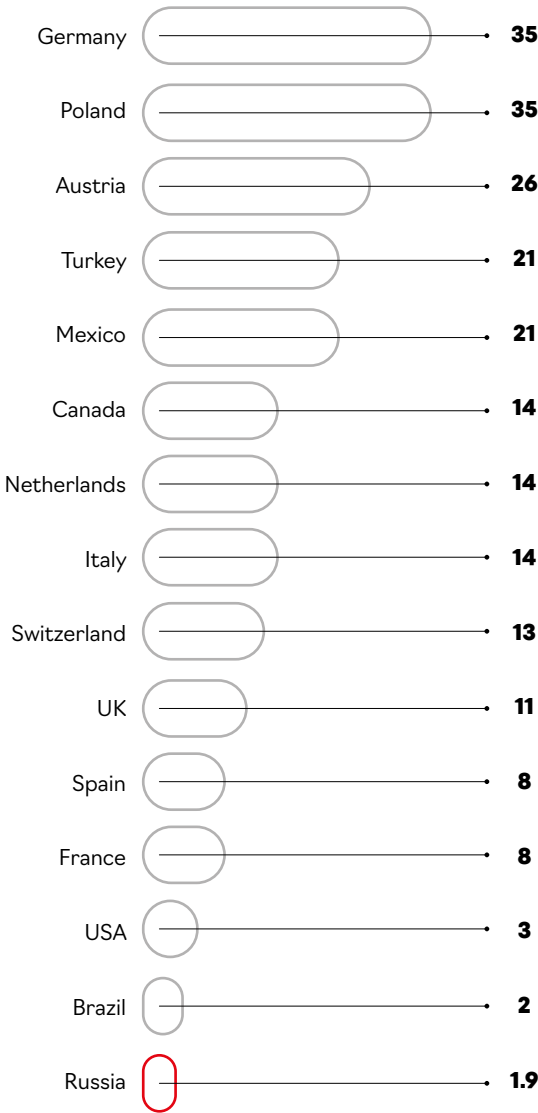
The hard discounter segment is underpenetrated in Russia compared to other developed markets where they are often seen as market disruptors, providing considerable room for growth.

The macro environment is also supportive for developing the discounter format, as real disposable income has been declining since 2012.

Hard discounters currently have 1.9% penetration in Russia, and this is expected to grow to around 5% by 2025.¹

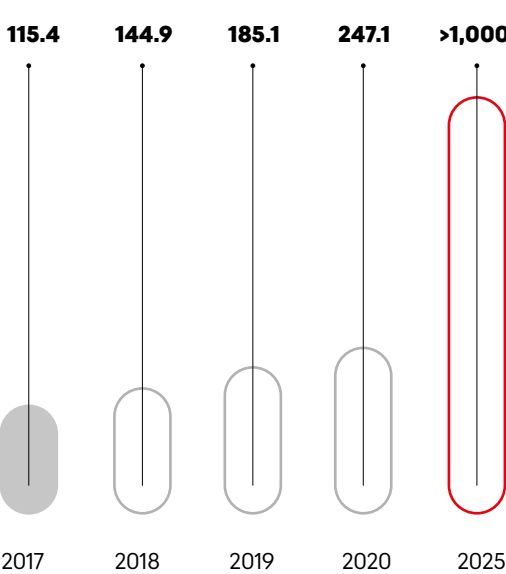
¹GOLDMAN SACHS, RUSSIA RETAIL, DECEMBER 2021

Discounters market shares in grocery retail , %



SOURCE: EUROMONITOR

Russian discounter market size, RUB bln



SOURCE: EUROMONITOR, INFOLINE

Store format

My Price discounters have selling space below 250 sq. m and offer a regular limited assortment of around 2,000 high-demand SKUs with a high rotation. 65% of total assortment is in lower-price segments, and the share of Private Label is currently around 23% of total sales.

Discounters offer a variety of value packs in the following categories: fruits, vegetables, dry foods, dairy, confections, baby food, drinks, pet food, household chemicals, and others. Most of the assortment is dry food with a limited share of fresh and ultra-fresh. Fruit and vegetable availability is designed to cover basic needs.

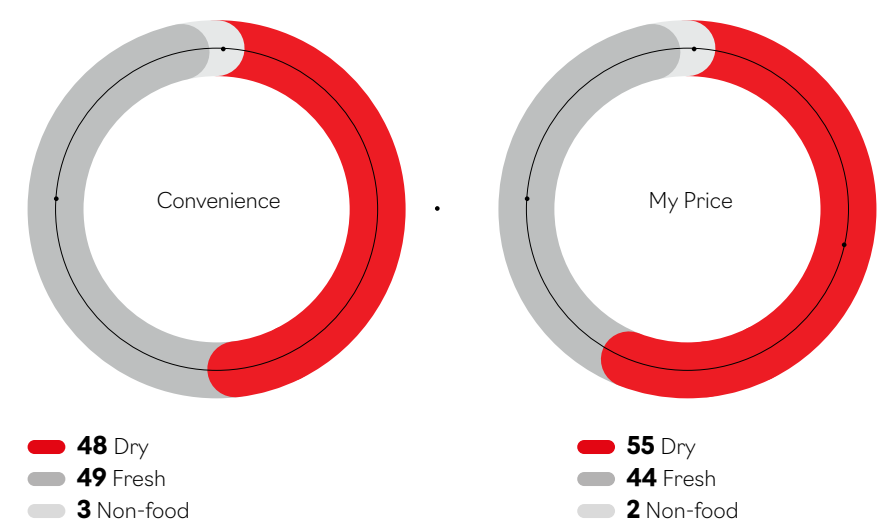
The format follows Magnit's EDLP (everyday low price) pricing policy where regular prices are already low without any promotions. The stores are designed to attract customers from other chains rather than from our own convenience stores. Pricing is set at 0.85 of the consumer price index, or 15% lower than prices elsewhere. The objective is to have the best customer attractiveness within a particular catchment area in terms of value for money.



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(continued)

Product mix differences, %



The layout of the store is simple and aimed at maximum efficiency, e.g. fresh fruit and vegetables are located next to the open refrigerated displays to save on additional equipment; products are displayed in show boxes and less often on a pallet.

The concept implies an optimised staffing level compared to convenience stores – 5 FTE vs 11 in convenience stores on average – though customer service levels remain high. In discounters that generate sales comparable to a convenience store there are still 2 FTE less vs convenience format. Discounters require significantly less capital expenditure for opening, including investments in repairs and refurbishment.

In September 2021, we launched a new design that was created specifically for our discounter format. It emphasises the low-price concept while creating a positive ambiance and providing a comfortable shopping space. Previously, our discounters used visual elements of our convenience stores.

The results of these stores are encouraging, sometimes exceeding our expectations and fully prove the concept.

2021 Performance

The results from My Price stores in 2021 were encouraging, at times exceeding our expectations and fully prove the long-term potential of the concept:

- LFL sales growth of 30 % in reformatted stores mainly driven by footfall
- The lower average transaction value compared to a convenience store is due to a narrower assortment, shift to lower price segments and lower prices
- Optimised operating model resulting in higher sales productivity despite the limited number of grocery and general merchandise SKUs across a narrow range of categories with a focus on entry-level prices
- Higher share of Private Labels at lower prices vs convenience stores enables better merchandise margin
- Assortment mix, EDLP model and sharply priced commodity goods leading to lower gross profit margin despite improved shrinkage
- Limited fixturing, low rent, and labour costs help reduce SG&A expenses, with savings potentially reinvested back into price to help drive volume
- Discounters converted from convenience stores generate higher profitability vs their performance as convenience stores driven by higher sales density and lower SG&A
- Pilot stores operate with positive EBITDA and Net Income after the ramp-up phase
- The share of highly rotated items on the shelves leads to higher inventory turnover – by 30–40% – allowing for higher profitability
- CAPEX is about 40% lower than for the same size convenience store implying very attractive returns.

My Price potential

We see significant potential in this concept for a number of reasons:

Decline in real disposable income	Real disposable income has been declining since 2012 and price-conscious customers are sensitive to ongoing economic uncertainty and rising food prices.
High growth potential not limited by Moscow and St. Petersburg markets	The fastest-growing market segments now are specialist stores, hard discounters and online. However, hard discounters have much greater growth potential, have proven success in developed markets, and are not limited by geographies like Moscow and St. Petersburg. The niche can become sizeable when roll-out brings efficiencies.
Everyday low prices are part of Magnit's DNA	The EDLP model is part of Magnit's DNA. Our production capacities across Russia have increased substantially supporting the development of the Private Label offering.
High availability of locations < 250 sq. m	Since the COVID-19 pandemic an increasing number of locations below 250 sq. m have become available at attractive rental rates.
Fits certain locations which would not support a regular convenience store	Customers are willing to travel further to visit My Price due to the affordable price points, giving greater flexibility on where stores can be located.
Production growth in Russia supports Private Label expansion	Production capacities across Russia have increased substantially supporting the development of Private Label offering through hard discounters.
Lower CAPEX and strict OPEX control lead to attractive returns	Low CAPEX and strict OPEX control allow us to derive returns that fit our internal requirements and achieve better sales densities.
Magnit's purchasing power, own production and direct import operations	Magnit's own production facilities, direct import operations and high purchasing power make our offer attractive for customers in that we can offer a regular assortment of products, differentiating us from our competitors.

Future development

We see an opportunity to open 300–500 My Price discounters in 2022 including reformatting some convenience stores, potentially including Dixy stores, making Magnit the largest discounter operator amongst Russian retailers.

We see significant potential for expanding this format in specific regions and areas. Discounters fit well in locations such as small and remote locations, where opening a convenience store may be inefficient, and where consumer incomes are lower than average.

Meanwhile we are continuing to develop the concept, including giving discounters their own unique design to make the format uniquely recognisable. We are developing our product range to increase the proportion of Private Label and are expanding our product mix so that there are more non-food items and seasonal offers. We are also engaging with suppliers to develop shelf-ready packaging and layout.

To support our growth in this area, we have appointed a dedicated operational director for discounters and are building a dedicated team to manage Magnit's discounter infrastructure including analytics, operations, and expansion teams.

Given our competitive strengths, including own production capabilities, Magnit is exceptionally well positioned to take advantage of the growing customer demand for discounters and basic fast-moving consumer goods.