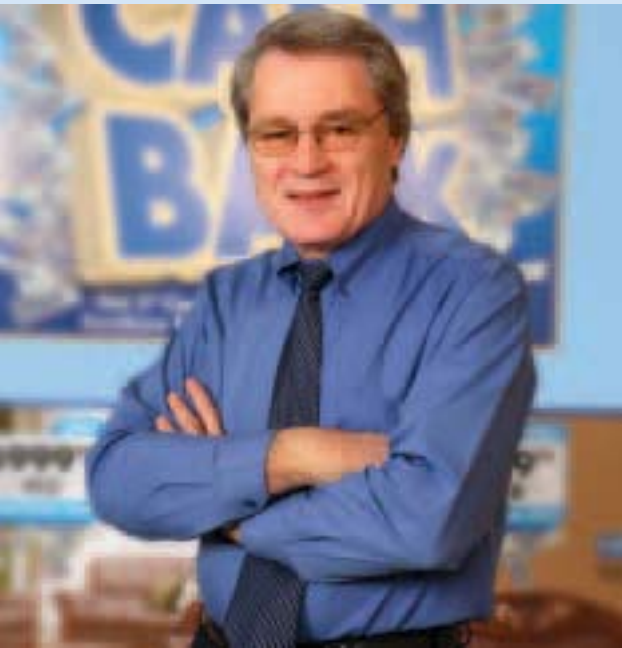




“To find the right product we talk to everybody, everywhere. We are tough negotiators, but value our relationships with our suppliers.”

Chris Heiberg (Merchandising and Marketing Executive)



merchandising and marketing

merchandising

Enhanced product sourcing has further differentiated the Lewis merchandise offering over the past year and this has contributed to increased turnover and higher margins for the group.

A core merchandising strategy at Lewis is the formation of strategic partnership relationships with suppliers which ensures unique design, exclusivity of high-quality products and potentially higher margins. The merchandise team works closely with local and international manufacturers to achieve these objectives.

Owing to the extensive range offered by Lewis, products are sourced from a diverse range of suppliers, with no single manufacturer producing more than 10% of the total purchases.

The merchandise strategy, which has been successful in the sourcing of local merchandise, has now been further extended to the group's import programme. A relationship was formed during the year with a Hong Kong supply chain specialist which will ensure Lewis's exclusive access to several large factories in the Far East. The group imports 13.7% of its total purchases directly.

As the largest furniture retail brand in South Africa, Lewis can guarantee large volume orders to suppliers which enhances price negotiations. Quality control is of paramount importance to the company. We take steps to ensure that a consistently high standard of merchandise is received in our stores.

Our customers are known to be extremely brand conscious. Exclusive electrical and audio-visual products have been sourced from leading brand manufacturers. Lewis and Best Electric's brand strategy in dealing with household electronic goods is to stock only well-known branded goods with extensive local service support. Consequently, the group does not subscribe to grey market or private label imports.



A benefit of being part of the group is that Lifestyle Living has been able to start sourcing product directly offshore, and with this has come innovation which appeals to the younger, more affluent customer base of the brand. The import programme has also improved margins.

There has been continued deflation in the electronic goods sector being driven mainly by improvements in technology. Sales of electronic goods increased by 20.6% in value and 29.4% in volume.

The Lewis distribution model is based on merchandise being delivered directly by suppliers to stores which both increases efficiency and limits the need for costly distribution centres and warehouses. Stores are responsible for their own deliveries to customers, with an estimated 90% of deliveries being made within 24 hours of the sale.

The merchandise team has been further strengthened through the recruitment of additional resources which will enable the brands to maintain a single-minded focus on merchandise offerings.

marketing

Marketing has a dual role in supporting the Lewis Group's business strategy: retaining the loyalty of the current customer base as a means of generating further business and creating brand awareness to attract new business to build market share.

Lewis enjoys a high level of loyalty from its customer base of over 680 000 and in the year under review more than half of the sales were generated from existing customers. A "re-serve" programme identifies the suitability of customers for further credit offers based on their payment behaviour and current debt obligations. Once the programme has assessed the creditworthiness and identified re-servable customers, marketing promotions are targeted at customers to stimulate further sales. The integration of these marketing promotions to the store systems ensures that there is follow through on the offers by sales staff.



Brochures continue to be the major form of advertising, with all current and recently-settled customers receiving a monthly brochure mailing. Brochures are distributed by “knock and drop” which continues to be the most used mechanism for distributing brochures. Brochures are also distributed through regional and local press as well as selected magazines.

The group has regular local promotions in store which take various forms and are directed at regaining settled and retaining existing customers.

Co-operative promotions with non-competing retail partners are specifically designed to attract new customers. These campaigns have proven to be successful and will be expanded in the coming year.

Television is used to build the brand and attract new customers. Brand recognition of Lewis's television advertising reached 72% for the year, substantially above prior year levels.

Overall brand awareness remains well above the industry norm after showing strong growth in recent years. Independent industry research by Adtrack shows that Lewis's brand awareness increased from 40% in 2001 to 75% in 2003, and has remained at this high level for the past two years.

Lewis maintained its second place in weighted brand awareness among furniture retailers in the 2005 Markinor report. Lewis was also ranked second in terms of brand relationship and customer loyalty.

Our in-house advertising studio has the expertise to plan, design and produce most aspects of the marketing media. The focus of our in-house advertising studio ensures the most flexible and cost-effective production and the fastest possible distribution of advertising material to the stores. A leading advertising agency has been engaged to assist the in-house studio with specialist communication services and creative input.

The Lewis Club

The Lewis Club is a customer loyalty programme in which membership is free and automatic to any customer taking any insurance product when purchasing merchandise at Lewis. The Lewis Club has a high level of acceptance.

Lewis Club members receive a monthly magazine, The Club, which includes special offers, discount coupons and regular competitions. The editorial content focuses on general interest and topical lifestyle issues relevant to the Lewis customer profile. Club members can also apply for educational bursaries worth R2 million and have free access to 24-hour legal, medical and HIV/AIDS advice lines. Members also participate in a monthly competition for prizes totalling R300 000.



“Lewis merchandise
has filled many homes and memories.
That’s why customers keep coming back.”

Johan Enslin (Operations Executive)



operations

The Lewis decentralised structure enables stores managers to be in control of all aspects of the customer interface. This results in Lewis stores being closer to our customers and ensures customer satisfaction.

The branch network of 490 stores across the Lewis, Best Electric and Lifestyle Living chains employs 5 879 people, including sales staff, administrative personnel, branch, regional and divisional management.

The Lewis and Best Electric structure includes 11 divisional general managers (DGM) who are responsible for all store operations and report to the operations director. A DGM has five or six regional controllers reporting in, while the regional controllers in turn have responsibility for six to eight stores each. The DGMs each have an average of 17 years' experience with the Lewis Group and the regional controllers each have an average of 10 years' experience.

Lifestyle Living's 16 stores are spread across three regions, with the regional managers reporting to the operations executive at head office.

The strong sales performance over the past year reflects the benefits of the multi-disciplinary approach, with the branch operations forming a close working

relationship with the merchandising, marketing, property development and information technology departments.

An important aspect of operations is the reactivation of settled customers and a promotional campaign has been successful in regaining in excess of 10 000 customers.

The group has created a store culture which is both empowering and entrepreneurial. Store managers are accountable for the entire operation of their branches, including sales and credit collection, and are empowered to make decisions which influence the performance of their stores.

Managers are remunerated in line with this philosophy, earning a basic salary and incentives based on their sales, credit collection and profit performance. Sales staff remuneration is largely commission-based with incentives for achieving performance targets. Credit collection staff also have collection performance incentives.

As more than 80% of the staff are employed in the branch operations, the human resources department is housed in the operations division. The training and recruitment functions are managed on a decentralised basis, with 11 divisional personnel managers providing a support service to operations.

Training and development remains a priority for the group. During 2006 1 827 staff members attended training courses, including 1 468 previously disadvantaged staff.

Lewis strives to be a leader in product knowledge training and has introduced a television broadcast system, Lewis Live, which is a weekly product knowledge training tool. Products are featured weekly and every salesperson throughout the country is required to write a test on these products.

We continually monitor our employee profile to reflect the demographics of the customer base and the communities in which Lewis trades. More than 75% of our staff are from black communities.

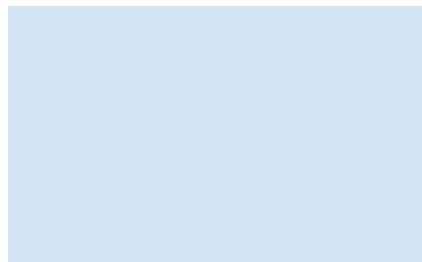


Lewis Stores

		2006	2005
Revenue, including insurance premiums written	Rm	2 485.0	2 225.5
Revenue growth	%	11.7	7.9
Merchandise sales	Rm	1 318.1	1 176.1
Merchandise sales growth	%	12.1	10.6
Comparable store merchandise sales growth	%	11.3	10.0
Number of stores		402	400
Total trading space	m ²	192 223	191 348
Increase in total trading space	%	0.5	0.3
Annual revenue per m ²	R'000	12.9	11.6
Credit sales	%	72.9	71.4

Lewis is South Africa's single largest furniture brand with 402 stores across the country, including 44 stores in the neighbouring states of Botswana, Lesotho, Namibia and Swaziland. Each store has a basic range of merchandise which is stocked in all stores. In addition to the basic range, there is an optional range which managers select from and which is appropriate to their individual markets and, thereby, catering for regional differences that exist in Southern Africa.

During the year Lewis opened six stores and closed four small under-performing stores. The brand has expanded into townships near major metropolitan areas with four of these new stores being opened in malls in Khayelitsha (Cape Town), KwaMashu (Durban), Lenasia (Johannesburg) and KaNyamazane (Nelspruit). A further eight stores are targeted for the forthcoming year.



Best Electric is a specialist electrical appliance and audio-visual retail chain with a similar customer profile to Lewis in the LSM 4 to 7 categories. The chain has grown rapidly since its formation in 1998 and operates out of 72 stores. The Best Electric concept is based on small stores situated in high traffic areas with high trading densities, with an average store size of approximately 150 m².

The model is based on popular branded merchandise fully supported by South African distributors. There is differentiation of product when compared to Lewis with Best Electric leveraging off the group's buying power. No "grey" unsupported merchandise is stocked by Best Electric.

Best Electric

		2006	2005
Revenue, including insurance premiums written	Rm	295.2	224.5
Revenue growth	%	31.5	26.5
Merchandise sales	Rm	164.3	125.0
Merchandise sales growth	%	31.4	26.2
Comparable store merchandise sales growth	%	10.8	11.5
Number of stores		72	58
Total trading space	m ²	10 929	9 263
Increase in total trading space	%	18.0	14.2
Annual revenue per m ²	R'000	27.0	24.2
Credit sales	%	66.1	69.1

Fourteen new stores were opened during the year and the store base has grown by close to 50% over the past two years. The chain will open approximately 12 new stores during 2007.

Lifestyle Living has been repositioned following its acquisition by the group in 2003 and the store location strategy reflects this revised business model. Three new stores were opened while four stores were closed in areas that were not appropriate for the new positioning of the chain. The new-format, mall-based stores opened during the year are performing well.

The Lifestyle chain has the potential to grow significantly in future. New stores are being planned for 2007 with several new sites being identified in areas where a higher level of credit is required.

Lifestyle Living

		2006	2005*
Revenue, including insurance premiums written	Rm	94.3	61.2
Revenue growth	%	54.1	n/a
Merchandise sales	Rm	85.4	50.8
Merchandise sales growth	%	68.1	n/a
Comparable store merchandise sales growth	%	58.4	n/a
Number of stores		16	17
Total trading space	m ²	7 049	6 984
Increase in total trading space	%	0.9	n/a
Annual revenue per m ²	R'000	13.4	8.8
Credit sales	%	35.5	35.6

* No comparatives were reported in 2005 as Lifestyle Living was acquired during the 2004 financial year.



insurance

Monarch Insurance Company ("Monarch") is a wholly-owned subsidiary of the group providing customer protection insurance products to credit customers who require insurance on the goods bought on credit for the contract period.

Monarch is governed by a board of directors which includes three executives of Lewis Stores, and two non-executive directors, Robert Shaw and Ray Sanger. The non-executive directors have extensive experience in the short-term insurance and reinsurance industries.

Monarch operates under a restricted short-term insurance licence and is registered with the Financial Services Board. The Short-Term Insurance Act requires Monarch to hold insurance reserves to meet future financial obligations and these funds may

only be invested in certain asset classes and within limits set out in the regulations promulgated under the Act.

As Monarch is licensed to operate in South Africa only, there are contracted third-party insurance partners in Botswana, Lesotho, Namibia and Swaziland to enable the group to offer customers in these countries similar insurance products on their credit purchases.

The basic insurance package covers the settlement of the outstanding balance in the event of the death, permanent disability or retrenchment of a customer. The insurance also covers the replacement of goods as a result of any form of accidental loss, such as fire, theft or natural disaster. A further feature of the insurance scheme is that customers automatically qualify for free membership of the Lewis Club.

Monarch utilises the group's existing operational infrastructure to sell insurance products, collect premiums and administer claims.

Monarch reinsures 40% of its insurance risk through Constantia Insurance Company. The investment of the insurance portfolio is outsourced to Sanlam Investment Management who determines the investment and asset allocation strategies in consultation with the Board of Monarch.



customer service

Delivery of superior customer service forms the foundation of the Lewis Group as evidenced in the company pledge. This function is relevant in ensuring that the group is meeting, and where possible exceeding, customer expectations.

While customer loyalty is reflected in the high level of repeat sales, a range of research techniques are applied to assess customer service standards across the group. Customer satisfaction levels averaged 93% in 2006, in line with the level in the previous year.

Mystery shoppers visit all stores across the three chains twice a year. This project is outsourced to an international client satisfaction research house to assess the professionalism of the customers' sales experience, the image of the store, the sales skills and product knowledge of store staff, merchandise presentation and pricing, and a general impression of the visit to the store.

Telephone calling is undertaken each year to all stores to assess the level of professionalism, product knowledge and telephonic sales skills of the staff.

Random courtesy surveys are conducted to evaluate the purchasing experience of new customers. These surveys are done at regular intervals over the account lifecycle to monitor ongoing satisfaction levels of customers.

All reports from the research company are given to the Operations Director for actioning.

Staff are recognised for their outstanding customer service through nomination to the Service Excellence Club. Qualification is based on feedback from customers, reports from mystery shopping research or nomination by senior management for consistently high customer service. Members of this club qualify for attractive incentives, including an annual draw for a motor car.

A toll-free facility which is advertised in stores and on customer statements encourages customers to contact a Customer Care department in the event of any service issue.

credit

The Credit division continually strives to improve the quality of the debtors book through maintaining industry-leading credit risk management techniques and collection processes. Credit-based sales accounted for 70.1% of sales in 2006 and one of the key focus areas is the granting and management of credit.

The credit granting and approval function is centralised, covering credit risk scoring, credit approval, underwriting, fraud prevention and customer account management. The credit collections process is, however, decentralised and stores are responsible for the cash collection and follow-up of their defaulting customers. The head office credit management team is supported by 11 divisional credit managers and 100 regional account managers based in regional offices around the country.

Credit risk management

Advanced technology-based credit scoring systems have been applied since 1998 to determine the credit risk of applicants. Credit application scorecards are constantly being refined and strengthened using the latest predictive indicators. A fourth generation credit application scorecard will be implemented in early June 2006.

The international expertise of Experian is utilised in the development of risk scorecards while the in-house team is

Summary of credit performance

		2006	2005
Gross debtors book	Rm	2 921.4	2 677.1
Increase in gross debtors book	%	9.1	1.8
Impairment provision	Rm	368.0	385.4
Percentage of gross debtors book	%	12.6	14.4
Bad debts written off and impairment provision	Rm	115.5	101.6
Percentage of gross debtors	%	4.0	3.8
Arrears percentage (full contractual)	%	22.0	25.7
Average length of book	Months	14.3	14.8
Credit application decline rate	%	22.4	20.5

responsible for the application, monitoring and maintenance of the credit management system.

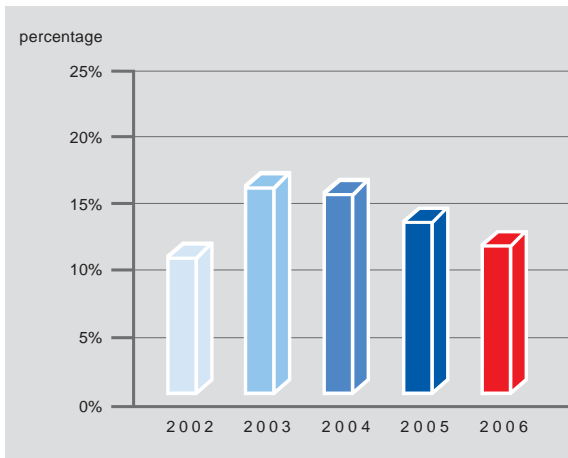
One of the features of the group's credit process which sets it apart in the retail sector is the speed at which credit is approved anywhere in South Africa. A credit decision is relayed back to the store on average nine seconds after submission of the credit application.

Applications are transmitted by the stores via the VSAT Satellite Network to the Transact SM credit application processing system. Transact interfaces with several databases, including the internal client payment history, the credit bureau, the national loans registry and the Hunter fraud database before passing the consolidated information to Strategy Manager, where the credit application scorecards and policy rules are applied.

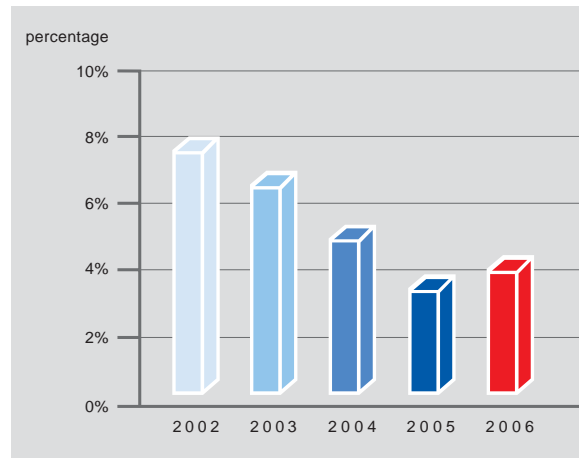
Following this process, a score is assigned to an applicant which is then used together with the applicant's income, and taking into account the applicant's total indebtedness, to calculate an initial credit limit for the new customer.

During the past year, an average of over 30 000 new credit applications were processed each month, with an annual acceptance rate of 77.6% (2005: 79.5%).

debtors impairment as a percentage of gross debtors



bad debt and impairment charge as a percentage of gross debtors



Note: 2003 includes the first time adoption of AC133/IAS39

As the relationship between a store manager and customer is critical to the credit-granting process, a scorecard recommendation to decline a credit application may be appealed to the credit referral department at head office, in consultation with divisional and regional staff.

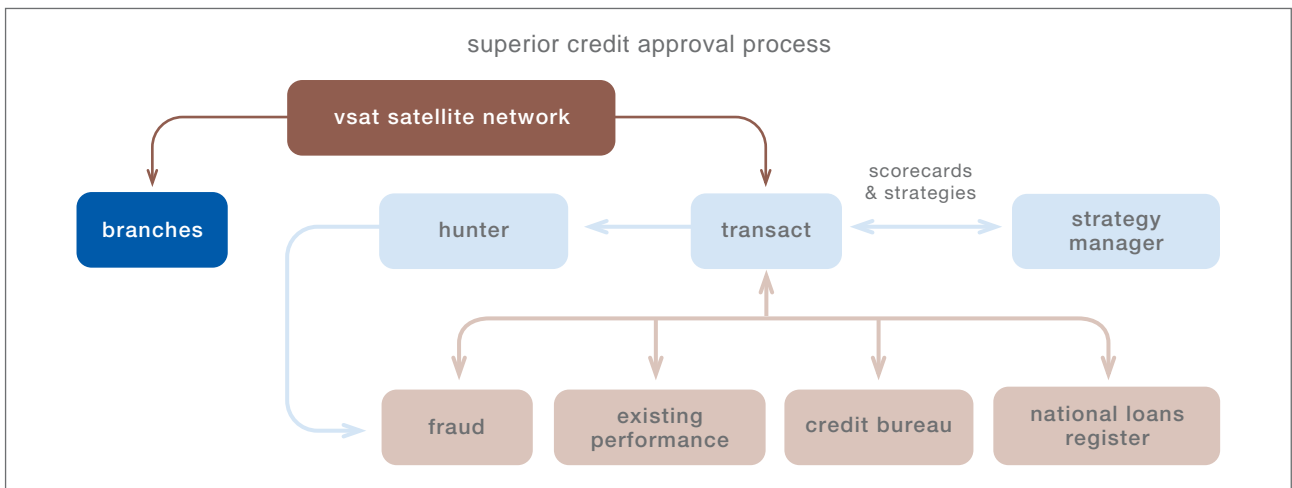
In order to manage existing customer credit levels, a behavioural scorecard, which assesses the risk of existing customers, has been fully integrated into customer account management strategies and processes. These scorecards not only take account of the credit extended by Lewis but also across the entire credit industry. This is a key element of credit risk management and will become increasingly important to meet the limit management and affordability

calculation requirements which will be introduced with the new credit legislation. Through the implementation of these scorecards and the subsequent improved segmentation, Lewis has realised both a reduction of credit risk levels and also an increase in the volume of re-servable business.

Credit collection

The continued tight management of credit collection processes and the growth in the debtors book of 9.1% has seen a marginal increase in bad debts during the year of 6.1% to R132.9 million (2005: R125.3 million). The impairment provision as a percentage of the receivables declined from 14.4% to 12.6% reflecting the improving quality of the debtors book. There was also a corresponding decline in arrears from 25.7% to 22.0%. While this improvement can be partially ascribed to the favourable economic environment, industry-leading credit granting systems and collection processes have played a major role in achieving this performance.

Our decentralised credit collection process has proved successful as the store personnel develop a relationship with their customers. Debtors clerks at the stores are incentivised to meet monthly and quarterly collection targets.





corporate services

group property and development

Store location strategy is key to trading performance. Lewis outlets are generally situated in main streets and town centres, with some presence in shopping centres. The Best Electric model is ideally suited for shopping areas with higher footfall, while Lifestyle Living stores are located in urban shopping malls.

The group property and development team is responsible for the administration of the property portfolio, negotiating lease agreements and renewals, sourcing new sites, managing store openings and refurbishments, co-ordinating store security and handling lease administration.

As the core business is furniture retailing and not property ownership, we have adopted a policy of leasing premises and currently occupy over 440 rented sites across the country.

Sourcing new locations is ongoing and the property team will continue to locate new sites and assist in managing the store expansions nationally.

	Lewis	Best Electric	Lifestyle Living	Total
Stores at 31/3/05:	400	58	17	475
– opened	6	14	3	23
– closed	4	–	4	8
Balance at 31/3/06	402	72	16	490

The group opened 23 new stores during the year, nine of which were in the Gauteng area.



information and communication technology

The information technology team is tasked with leveraging technology in the most cost-efficient manner to support the group's strategy. The main focus during the year was building further enhancements into the technology platform to improve service to branches, while creating infrastructure to ensure that all head office, branch and disaster recovery systems are resilient to external factors.

The Lewis Group has invested heavily since 1998 to create a technology platform that is up to date, stable, low cost and scalable. The key investment areas are detailed below:

Credit management technology

Transact, an automated credit application processing system, was introduced in 1998 to enable online bureau enquiries and facilitate the introduction of both the first application scorecard developed by Experian and the application of centralised credit policies. While the Lewis Group utilises the international expertise of Experian in the development and maintenance of risk scorecards and strategies where necessary, the Lewis Group also maintains the required experience and technical skills internally to maintain, adapt and improve the application of credit management systems.

Customer relationship management technology

In 2003, the Lewis Group introduced an Experian-developed customer management system called "Stratagem". The system is used for behavioural scoring, credit limit management, marketing and collections. Subsequent to the implementation of Stratagem, the first behavioural scorecard was adopted in mid-2003. Stratagem forms part of the monthly account management process and enables customers to be segmented at



multiple levels. It also allows for a combination of customer management strategies to be applied to each customer. The system is not a modular-based system and additional scoring modules and actions can easily be added into the workflow without requiring any additional systems development or costs.

Branch computer systems

The Lewis Group's in-store financial transactions operate on a transaction processing point-of-sale system. Most transactions are initiated in the store environment and the system automatically updates, on a daily basis via satellite, both the debtor and inventory databases that are located at both store and head office levels. The system also has strict change controls over finance charge rates, minimum deposit percentages, insurance and maintenance premiums. All changes have to be verified by the Lewis Group finance and IT executives and no changes can be made at branch level.

Intranet technology

The Lewis Communication System (LCS), an intranet-based system which links head office with the branch network, was expanded during the year. LCS provides an online product knowledge training and assessment facility in addition to enabling easy communication between branches and head office. It also facilitates several automated functions which eliminates administrative costs.

Outsourced services

While the group has an in-house management team, the maintenance of the software portfolio is outsourced to systems developers from Universal Computer Services (UCS). Maintenance of the branch network is outsourced to Unisys and open-source Linux software is used in stores.

Disaster recovery

The Lewis Group operates a distributed network that allows branches to operate independently of each other and head office. However, the credit vetting process for new applications requires real time connectivity to the credit bureau, which is achieved through Transact. To prevent downtime, an off-site disaster recovery server for the Transact system has been set up. This disaster recovery site connects to the branch satellite network infrastructure and the credit bureau independently of the live environment. The whole Transact system is replicated at the disaster recovery site on a daily basis and can be activated within minutes of a disaster. Furthermore, a diesel-powered generator has been installed at head office to ensure that key systems are not put at risk.