

ADAIRES LIMITED
ABN 50 147 375 451

ANNUAL FINANCIAL REPORT
FOR THE
52 WEEKS ENDING
2 July 2017

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CORPORATE INFORMATION

ABN 50 147 375 451

Directors

Michael Butler
Mark Ronan (appointed 18 November 2016)
David Maclean
Michael Cherubino
Trent Peterson
Kate Spargo
David Briskin

Company Secretary

Mandy Drake (appointed 3 November 2016)

Registered office

2 International Court
Scoresby
Victoria, 3179
Australia

Principal place of business

2 International Court
Scoresby
Victoria, 3179
Australia
Phone: 1800 990 475

Share register

Link Market Services
Locked Bag A14
Sydney South NSW 1235
Phone: 1300 554 474

Auditors

Ernst & Young

Solicitors

Herbert Smith Freehills

Bankers

Commonwealth Bank of Australia

DIRECTORS' REPORT

Your directors submit their report on the consolidated entity (referred to hereafter as "Adairs", "the Group" or "the Company") for the 52 weeks ended 2 July 2017 ("FY2017" or "FY17").

Adairs operates on a retail accounting calendar which consists of four quarters of 13 weeks, equating to an annual 52 week reporting period of 364 days in most years, with a 53 week reporting period (i.e. 371 days) every five to six years. In FY2016, there was a 53 week reporting period with an additional week of operations occurring. The implication of this is that in FY2017 Adairs has 364 financial year days versus 371 financial year days in FY2016. The directors include in our commentary below a comparison of EBIT between FY17 and FY16, including an adjustment to normalise FY16 EBIT to a comparable 52 week period.

DIRECTORS

The following persons were directors of Adairs Limited during the period and up to the date of this report unless otherwise stated.

Michael Butler
Mark Ronan (appointed 18 November 2016)
David MacLean
Michael Cherubino
Trent Peterson
Kate Spargo
David Briskin

Information on qualifications and experience of directors is included on pages 10 to 12 of this report.

Principal Activities

During the period, the principal continuing activities of the Company consisted of the retailing of homewares and home furnishings in Australia and New Zealand.

Dividends

In respect of the financial year ended 2 July 2017, an interim dividend of 3.5 cents per share was paid to the holders of fully paid ordinary shares on 26 April 2017 and the directors have declared the payment of a final dividend of 4.5 cents per share, to be paid to the holders of fully paid ordinary shares on 28 September 2017. Both dividends are franked to 100% at the 30% corporate income tax rate. The total dividend for the full year of 8 cents per share represents a payout ratio of 63.1% of the full year earnings in line with Adairs dividend policy.

2017 Operating and Financial Review

The profit from ordinary activities after income tax for FY2017 amounted to \$21.017m (2016: \$27.172m).

The Directors' Report includes references to pro-forma results to exclude the FY2016 impact of the 53rd week of trade. It also includes references to non-IFRS financial measures such as Earnings Before Interest and Tax ("EBIT"), EBIT margin, EBITDA (EBIT excluding depreciation and amortisation), like-for-like sales growth ("LFL"), Pro-forma EBIT and related Pro-forma adjustments.

The EBIT of the Group for FY2017 was \$30.8m (2016: EBIT \$40.7m).

Continuing Operations

	2017 \$'000	2016 \$'000
Statutory profit after income tax for continuing operations	21,017	27,172
Add back:		
Finance expenses	1,946	2,006
Interest income	(55)	(81)
Income tax (benefit)/expense	7,904	11,651
EBIT⁽¹⁾	30,812	40,748

⁽¹⁾ Earnings Before Interest and Tax (EBIT) is used as a measure of financial performance by excluding certain variables that affect operating profits but which may not be directly related to all financial aspects of the operations of the group. EBIT is not a measure of operating income, operating performance or liquidity under IFRS. Other companies may calculate EBIT in a different manner to us. The above EBIT reconciliation has not been audited.

DIRECTORS' REPORT (continued)

The table below reconciles the statutory result to the pro-forma result for FY17 and FY16 showing the full year results from continuing operations on a comparative 52 week basis.

Continuing Operations	Note	2017 \$'000	2016 \$'000
Statutory EBIT from continuing operations		30,812	40,748
<i>Add back:</i>			
53rd Week EBIT	1	-	(1,618)
Transaction costs	2	-	101
Pro-forma EBIT from continuing operations (52 weeks)		30,812	39,231

Notes on pro-forma adjustments:

1. 53rd Week EBIT - reflects the EBIT earned in the week commencing 27th June 2016.
2. Transaction Costs - Includes costs relating to the IPO and the related corporate restructure.

The table below sets out the operating results for FY2017 compared to the pro-forma operating results for FY2016. The pro forma consolidated statement of profit or loss adjusts the statutory results for FY2017 and FY2016 for the pro forma adjustments as set out in the table above.

Continuing Operations	2017 \$'000	Pro-forma 2016 \$'000	Change %
Revenue	264,964	247,426	7.1%
Gross Profit	156,801	151,015	3.8%
Gross Margin	59.2%	61.0%	-1.8%
EBIT	30,812	39,231	-21.5%
EBIT Margin	11.6%	15.9%	-4.3%

Results Summary

The Company had a disappointing year with a significant decline in EBIT notwithstanding achieving growth in total revenue. The total revenue growth achieved came from the opening of 13 stores with 4 of these in New Zealand, the annualised sales of stores opened in FY16 and the continued growth in our online channel.

The poor EBIT result was largely due to unsatisfactory sales results in the period of late September 2016 through to March 2017. Underlying this was a primary issue that our range did not meet our customers' expectations, particularly in the key bed linen category. Execution errors in our efforts to interpret current fashion trends well and develop and deliver product that appealed to our fashion oriented customer played a significant role in our poor performance. However, we believe our product range issues in FY17 are best described as Adairs offering a range that 'lacked balance'. In essence, with our range biased to a relatively narrow number of fashion looks, at the expense of delivering a product offering that appropriately spanned both on-trend and traditionally popular looks. This led to missed opportunities as we did not deliver a range of looks appropriate to the different styles of homes our customers have across Australia.

These issues resulted in negative like for like sales in the second (-6.8%) and third quarters (-2.4%) that led to a significant reduction in EBIT. The earnings impact was pronounced as we missed sales during key trading periods. Encouragingly, as we rebalanced the range we saw positive like for like sales growth achieved in the fourth quarter (+3.8%), as the product range improvements delivered better results across a number of important product categories including bed linen.

The overall negative like for like sales result for the year was observed across most parts of the business, but was less so in Homemaker stores due to the stronger performance of some of our other product categories including home decoration and soft furnishings. Adairs ongoing strategy of product differentiation, category range extension and growth in fashion and decorator product categories also helped support the performance of homemaker stores in FY17. In contrast, due to the more limited range offered in our smaller shopping centre stores, our regular store format was more heavily impacted by the unsatisfactory sales performance in some of our core product categories.

The emerging store formats of Adairs Kids and Urban Home Republic also had a difficult trading year with both store formats reporting negative like for like sales growth. As the Urban Home Republic store format has a heavier reliance on the fashion and design elements of the product range, our issues in this product area, as discussed above, impacted our ability to drive like for like sales growth. In the Adairs Kids store format, our sales were impacted by missed opportunities in key product ranges, designs which lacked compelling differentiation and customer appeal, and more intense competition. The Adairs Kids business remains more susceptible to changes in consumer and retail sentiment due to its premium position in the market. We continue to work on the product mix within this format and improving its performance and attractiveness.

DIRECTORS' REPORT (continued)

Whilst our store sales were down like for like, the online business continued to grow achieving 20.8% like for like sales growth, representing approximately 9% of total group sales in FY17. We enjoyed particularly strong LFL sales growth online in H2, with sales growth of +41%, which we expect to continue to build upon in FY18. Our online channel sales totalled \$23.7 million in FY17, and is now material to both our total sales (and sales growth), and is a strong contributor to our profitability.

At the gross margin level the Company was down 180 basis points on the prior year. While the lower effective Australian dollar buying rate over the first half (relative to prior year) played a role in reducing our gross margin rate, the more significant issue was the impact of increased discounting and promotional activity related to surplus and underperforming inventory at lower margins to ensure an appropriate inventory position at year end. The Company looked to offset these issues by continuing to pursue cost price reductions and taking advantage of the reduced import duty rates on certain textile products.

The relative stability of the Australian Dollar (vs pcg) and the improved product offering in the last quarter sees the Company move into FY18 in a good position to improve upon the gross margin rate achieved in FY17. Our objective remains to deliver a gross margin rate in a "sustainable margin range" of 59% to 61%.

During the year the business incurred additional costs (approximately \$720,000) associated with the roll out of the new point of sale, the re-platforming of the website, and the setup of the New Zealand operations. In addition, Adairs incurred an operating loss in New Zealand of approximately \$800k, being slightly better than our forecast loss of \$1m.

The group EBIT margin of 11.6% fell (430 bps from FY16) as a result of the declining like for like sales, reduced gross margin rate and the operating leverage within the business. After adjusting for the impact of the additional costs and the NZ operations the EBIT margin of the business was 12.3% (2016 15.9%). The majority of this decline in EBIT margin was suffered in the first half of FY16, and we saw greater stability emerge in our gross margin and EBIT margin levels as H2 progressed.

The decline in the EBIT in FY17 flowed through to the Net Profit After Tax (NPAT) and Earnings per Share (EPS) results.

Capital Management

There was no significant change in the capital structure of Adairs through FY2017. During the year the business renegotiated its debt facility. The overall debt facility remains at \$50m in aggregate and represents a \$42m revolving cash advance term facility (fully drawn) and a further \$6.75m cash advance term facility which remains undrawn at year end. The multi option revolving working capital facility has been reduced from \$8m to \$1.25m.

The leverage ratio as at June 2017 was 1.1x actual EBITDA (EBITDA is calculated from EBIT, as mentioned above, plus depreciation and amortisation). Net debt is \$27.6m. The company's debt facility maintained the three key financial covenants, the debt to capital ratio, fixed cover charge ratio and the leverage ratio with significant headroom existing within all of the financial covenants as at June 2017. We have no current plans to materially increase or decrease our debt levels and believe they are appropriate.

Adairs Strategic Update

Our strategy is aimed at delivering profitable growth with the strategies reflecting the continued evolution of the business' existing proven strategies which have contributed materially to the earnings growth achieved by the business in recent years.

Product, Product and Product

Our FY17 result has highlighted the importance of strong execution of our product and range differentiation strategy to growing revenue and profitability. We understand the importance of our product, and within this maintaining a balanced range to meet the needs of our customers. One of the key drivers of our like for like sales growth over the coming years will be the two key components of our product strategy:

- **Product differentiation:** Offer customers a range of on trend products at value-for-money prices that are designed by and exclusive to Adairs.
- **Category range expansion:** Offer customers an increasingly broader range of co-ordinated decorator products relative to our competitors. Adairs will continue to expand its range to cover new product areas based on management's assessment of customer demand, balanced with the physical floor space availability in our stores. Recent examples include the adding of wall art, mirrors, home fragrances, floor rugs, bedroom chairs, bedside tables and lamps to Adairs' product range. A critical aspect of this strategy is to ensure that any range extension is complementary to the existing product categories and range and has similar attributes such as value, quality, styling and fashionability. This helps customers develop a co-ordinated look across product categories and enables store teams to deliver superior service. Our objective is to furnish more of our customers living, entertaining and functional spaces in their homes.

More inspiring, larger size and bigger store network

Adairs will continue its' store roll-out in Australia, with the business looking to open 6-8 net new stores per year over the next 3 years. This reflects the current store profile of the business and the work Adairs does on identifying new profitable store opportunities. Given the current retail environment Adairs expects the majority of these stores to be Adairs core formats of Adairs and Adairs Homemaker stores, with the expansion into Adairs Kids and Urban Home Republic to be slowed whilst we review and refine these formats.

With the ongoing work on product and range differentiation and expansion, Adairs will also continue to up-size selected existing Adairs Regular and Adairs Homemaker stores (i.e. our core store formats), with 24 stores identified for potential up-sizing over the next 5 years. Adairs believes there is significant opportunity in providing our customers an enhanced shopping experience and wider range of product via these larger store formats, and our current experience with this strategy indicates an attractive incremental ROCE. Over the past year Adairs upsized 4 stores which have delivered improved results and an attractive ROCE, supporting the continuation of this strategy subject to negotiating suitable rental terms.

Consistent with the above upsizing strategy for existing stores, Adairs also has a strategy of seeking to selectively open moderately larger stores (in square metres) in new locations in our core stores formats. Our experience to date is that these larger stores give us a better opportunity to merchandise a wider range, and deliver the customer a superior shopping experience. We note for completeness that ultimately the size of each store is determined on a site by site basis and is a function of a range of commercial and practical factors.

After opening 4 Adairs Kids stores in FY2016 Adairs is not opening new standalone Adairs Kids sites in FY18 whilst we review the operating model to deliver an improved return on these new stores. The business continues to make incremental changes to the operating model to improve the relative position of the brand in the market to ensure any future store roll out delivers strong ROCE.

Best in class omni retain capabilities

Growing and investing in Adairs online and loyalty program ('Linen Lovers') is core to our operations and the centre piece of our customer engagement activities. Adairs strategy of operating both physical store locations and delivering a strong online customer experience remains a focus to ensure we deliver a seamless and flexible customer experience.

The Online sales drivers include:

- Broader product range availability
- Improved product information available online
- Click and collect offering
- Enhanced site user experience
- Faster, more flexible delivery options
- Growing international territories
- Marketplace opportunities
- Delivering flexible payment options

The above key strategic priorities are expected to grow online sales to greater than 12% of our total sales by 2019.

International expansion

Adairs successfully opened 4 stores in New Zealand in FY2017 supported by a New Zealand website. The initial results from these stores highlight the opportunity that exists in the New Zealand market for Adairs. Our initial stores have allowed us to gain more insights into the New Zealand market and better understand the opportunity for Adairs therein.

In FY2018 Adairs expects to open a further 2 stores in New Zealand with one of these stores scheduled to be opened in October. Adairs sees the New Zealand market as having the potential to initially support up to 12 -18 stores across Adairs existing core store formats, subject to the ongoing success of the initial stores.

Similar to our store roll out strategy in Australia, Adairs has a preference to open more Adairs Homemaker format stores in New Zealand (relative to other store formats). Adairs Homemaker stores provide the New Zealand customer with an enhanced shopping experience and wider product range via these larger store formats.

Adairs expects the international expansion strategy into New Zealand to breakeven in the FY2018 year before being profitable in the FY2019 year and beyond.

DIRECTORS' REPORT (continued)

The international expansion strategy will be further complemented over the coming years with the roll out of an international website to enable Adairs to sell online into a variety of new countries, and assess the underlying demand from selected other countries.

Material Business Risks

There are a number of risk factors both specific to Adairs and of a general nature which may impact the future operating and financial performance of the Company. The performance of the Company is influenced by a variety of general economic and business conditions, including levels of consumer spending, inflation, interest and exchange rates, access to debt and capital markets and government policies.

The specific material business risks that are likely to have an effect on the financial prospects of Adairs include:

- **Customers buying habits or seasonal trading patterns may change**
Many of Adairs' products are considered to be discretionary goods, particularly products in Adairs' fashion item lines where consumer preferences and tastes can change quickly. Consumer demand for these products is sensitive to Adairs' fashion and design selections and product range. A broad-based or series of significant misjudgements in interpreting product and fashion trends and over estimation of the quantum of demand for these products could adversely affect Adairs' financial performance.
- **The retail environment and general economic conditions may worsen**
Consumers may consider many of Adairs' products to be discretionary goods, and sales levels are sensitive to consumer and retail sentiment as a result. If consumer and retail sentiment were to decline, this may reduce the demand for Adairs' products, thereby reducing product sales. This would have a flow on affect with regard to like for like sales and have a materially adverse effect on Adairs' financial performance.
- **Competition may increase and change**
The competitive environment in which Adairs operates in is relatively stable, however there is a risk that Adairs may lose market share to new or existing competitors. Adairs' competitive position may deteriorate as a result of increased competition, and Adairs customers may choose to purchase products from its competitors rather than from Adairs and could lead to downward pressure on margins and subsequently have an adverse impact on Adairs' financial performance.
- **Management may be unable to achieve its growth objectives**
Adairs' management has developed a number of growth strategies for the business. The success of growth strategies is key to Adairs' future financial performance, however there is a risk that Adairs' growth strategies are ineffective or are not executed effectively.
- **Adairs may be unable to retain or secure suitable store sites**
Adairs' store footprint and lease portfolio is frequently assessed and revised in order to optimise financial and operational performance. Adairs' financial performance and future growth is dependent on its ability to both retain existing store sites and secure new store sites in suitable locations and on acceptable terms. Adairs' ability to achieve this may be impacted by a range of factors including availability of new store sites, profitability of new sites, landlord disputes, potential cannibalisation of existing stores by new store openings as examples.
- **Adairs may make material execution errors in its operations or in the implementation of its strategy**
Our ongoing operations and the successful implementation of our strategy is highly reliant on the skills and judgements of our management team and the teams of marketers, product designers and inventory planners in Adairs. While there is an intrinsic and normal level of mistakes or errors that are made in development and delivery of a product range, there is also a risk that the error rate or severity and scale of the mistakes exceeds normal levels, and this can adversely affect the appeal of our range to our customers and therefore materially impact sales and margins.
- **International expansion may not be successful**
The introduction of international business operations into the group adds complexity and requires management to consider additional factors impacting a different economy and varied regulatory requirements. Adairs have mitigated this risk by seeking advice and expertise from people who have previously operated in the market and have specific expertise related to the market. Despite this Adairs strategies in relation to international expansion may be ineffective or not executed effectively adversely impacting the future financial performance.

Outlook

After a disappointing year in FY17, Adairs expects to again grow the business by regaining the market share lost for a range of the reasons discussed above. The ongoing execution of our strategy and the changes made over the 2H FY17 are forecast to deliver sales in FY2018 in the range of \$285m to \$300m.

DIRECTORS' REPORT (continued)

We are pleased to report that we have started FY18 well building on the momentum that re-started in Q4 2017. These early results give us increasing confidence that the changes we have made to address the issues we had in Q2 and Q3 of FY17 have been effective and so we are increasingly confident that we will deliver better results in FY18 than in FY17.

Adairs expects to continue to grow its store network both in Australia and New Zealand through the continued roll out of the Adairs and Adairs Homemaker formats.

Adairs also expects to see online revenue growth through continuing to focus on our omni channel strategy of building great customer experience both in store and online.

Significant changes in the state of affairs

There have been no significant changes in the state of affairs of Adairs during the financial year ended 2 July 2017.

Matters subsequent to the end of the financial year

On 28 August 2017, the directors of Adairs Limited declared a final dividend on ordinary shares in respect of the 2017 financial year. The total amount of the dividend is \$7.46m which represents a fully franked final dividend of 4.5 cents per share. The dividend has not been provided for in the 2 July 2017 financial statements.

Other than the matter noted above, no matters or circumstances have arisen since the reporting date which significantly affected or may significantly affect the operations of the Group, the results of those operations, or the state of affairs of the Group.

Environmental regulation

The Company's operations are not subject to any significant environmental obligations or regulations. No environmental breaches have been notified to the Company during the 52 weeks ended 2 July 2017.

DIRECTORS' REPORT (continued)

Directors and Directors' Interests

The directors of Adairs Limited in office at the date of this report are listed below together with details of their relevant interest in the securities of the Company at that date.

Michael Butler *Independent Chair Non-Executive.*

Michael has extensive experience in finance and investments in both executive and board roles. He has over 20 years' experience as a non-executive director of ASX listed companies across a broad range of industries including financial services, tourism, logistics, property, resources, and retailing.

Other Current Directorships

Non-executive director of Total Tools Holdings Pty Ltd

Former Listed Directorships in the last 3 years

Non-executive director of Metcash Limited

Special Responsibilities

Chair of the Board

Chair of the Nomination Committee

Member of the Audit and Risk Committee

Member of the Remuneration Committee

Interest in Shares and options

238,656 ordinary shares in Adairs Limited

Mark Ronan *Managing Director and Chief Executive Officer.*

Mark was appointed Chief Executive Officer and Managing Director in November 2016, following roles at Adairs in Finance, Merchandise Planning, Store Operations and as Chief Operating Officer. Mark is a Chartered Accountant with prior experience in operating businesses, funds management and Deloitte.

Other Current Directorships

None

Former Listed Directorships in the last 3 years

None

Special Responsibilities

Managing Director and Chief Executive Officer

Interest in Shares and options

681,668 ordinary shares in Adairs Limited

651,000 options in Adairs Limited

David MacLean *Non-Executive Director*

During the year David resigned as Chief Executive Officer and Managing Director and was invited to remain on the Board in a non-executive director capacity. David worked for Adairs for the past 27 years and was Adairs Chief Executive Officer and Managing Director for 15 years.

Other Current Directorships

Non-executive director of dusk Retail Holdings Group Pty Ltd

Former Listed Directorships in the last 3 years

Managing Director of Adairs Limited

Special Responsibilities

Member of the Nomination Committee

Interest in Shares and options

4,318,273 ordinary shares in Adairs Limited

DIRECTORS' REPORT (continued)

Trent Peterson *Non-Executive Director*

Trent has over 20 years investment and private equity experience, focused primarily on businesses operating in consumer, retail and media sectors. Trent is Managing Director of Catalyst Investment Managers and the founder and Managing Director of both Catalyst Direct Capital Management and IPMB Capital Partners. Trent was Non-executive Chairman of the Board of the Company from 2010 until the IPO in 2015, being the period of Catalyst's majority ownership.

Other Current Directorships

Chair and Non-executive director of dusk Retail Holdings Group Pty Ltd
Chair and Non-executive director of Cirrus Media
Chair and Non-executive director of AATS (trading as SkyBus)
Non-executive director of Max Fashions
Non-executive director of Power Farming Group
Non-executive director of The Shaver Shop Limited
Non-executive director of Australian Pure Health (trading as Mr Vitamins)

Former Listed Directorships in the last 3 years

None

Special Responsibilities

Chair of the Remuneration Committee
Member of the Audit and Risk Committee
Member of the Nomination Committee

Interest in Shares and options

595,334 ordinary shares in Adairs Limited

Trent also has an indirect interest in approximately 747,204 shares as a result of his minority interests in funds managed or advised by Catalyst Investment Managers. Trent also has a further indirect economic interest in all Adairs shares held by the Catalyst funds subject to certain conditions including the performance of those funds taken as a whole.

David Briskin *Non-Executive Director*

David has extensive experience in the fashion and retail sector as a former shareholder and Managing Director of Mimco and a former shareholder and Chief Executive Officer of sass & bide. David began his professional career as a commercial lawyer at Corrs Chambers Westgarth.

Other Current Directorships

Non-executive director of Virgin Australia Melbourne Fashion Festival
Director of MJ Bale Pty Ltd

Former Listed Directorships in the last 3 years

None

Special Responsibilities

Member of the Remuneration Committee
Member of the Nomination Committee

Interest in Shares and options

208,334 ordinary shares in Adairs Limited

Kate Spargo *Non-Executive Director*

Kate has broad commercial and organisational experience, as well as a focus on risk, audit and governance, supported by her legal background in both government law and private practice. Kate has been an independent Company director for 20 years, covering listed and unlisted companies in a variety of sectors including infrastructure, construction and engineering, energy, financial services, building product manufacture and distribution, and health services.

Other Current Directorships

Non-executive director of Sonic Healthcare Ltd
Non-executive director of CoInvest Ltd
Non-executive director of Fletcher Building Ltd
Non-executive director of SMEC Ltd
Non-executive director of Sigma Pharmaceuticals Ltd
Non-executive director of Geelong Football Club
Non-executive director of Xenith IP Ltd

DIRECTORS' REPORT (continued)

Former Listed Directorships in the last 3 years
Chair of UGL Ltd

Special Responsibilities

Chair of the Audit and Risk Committee
Member of the Remuneration Committee
Member of the Nomination Committee

Interest in Shares and options

41,667 ordinary shares in Adairs Limited

Michael Cherubino *Property and Business Development Director*

Michael has over 19 years' experience in the retail sector. Michael's previous roles were with National Australia Bank and Bankwest.

Other Current Directorships

None

Former Listed Directorships in the last 3 years

None

Special Responsibilities

Member of the Nomination Committee

Interest in Shares and options

2,158,135 ordinary shares in Adairs Limited

372,000 options in Adairs Limited

Company Secretary

The Company Secretary is Mandy Drake. Mandy is also Chief Financial Officer. Mandy commenced with Adairs as the Chief Financial Officer and was appointed Company Secretary in November 2016.

Meetings of Directors

The following table sets out the number of meetings of the Company's Board of Directors and each Board Committee held during the 2017 financial year and the number of meetings attended by the members of the Board or the relevant Committee.

	Board		Meetings of Committees					
			Audit		Nomination		Remuneration	
Director	Held	Attended	Held	Attended	Held	Attended	Held	Attended
M Butler	9	9	3	3	1	1	3	3
D MacLean	9	9	n/a	n/a	1	1	n/a	n/a
T Peterson	9	9	3	3	1	1	3	3
M Cherubino	9	9	n/a	n/a	1	1	n/a	n/a
K Spargo	9	9	3	3	1	1	3	3
D Briskin	9	9	n/a	n/a	1	1	3	3
M Ronan	5	5	n/a	n/a	n/a	n/a	n/a	n/a

Held: number of meetings held while a Director was a member

Attended: number of meetings attended

Non-Audit Services

The Company may decide to employ the auditor on assignments additional to their statutory audit duties where the auditors' expertise and experience with the Company are important.

Details of the amount paid to the auditor Ernst & Young Australia for audit and non-audit services provided during the year are set out in Note 25 of the financial statements.

The directors are satisfied that the provision of non-audit services is compatible with the general standards of independence for auditors imposed by the *Corporations Act 2001*. The directors are satisfied that the services provided

DIRECTORS' REPORT (continued)

did not compromise the external auditor independence for the following reasons:

- all non-audit services are reviewed and approved by the Audit and Risk Committee prior to commencement to ensure that they do not impact the integrity and objectivity of the auditor; and
- the nature of the services provided does not compromise the general principles relating to auditor independence as set out in APES110 - Code of Ethics for Professional Accountants.

Auditors Independence Declaration

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 33.

Proceedings on behalf of the Company

There are currently no proceedings on behalf of the Company.

Indemnification and insurance of officers

The Group has agreed to indemnify all the directors and executive officers against loss, cost, damage, expense or other liability suffered or incurred by the directors as officers of the Group. The indemnity does not extend to indemnify the director:

- (a) in bringing or prosecuting any claim, unless the claim is a claim in the nature of a cross-claim or third-party claim for contribution or indemnity in, and results directly from, any proceedings in respect of which the directors have made a claim under the indemnity;
- (b) in connection with any proceedings between the directors and the director's appointee or any related body corporate of the appointer (within the meaning of section 50 of the *Corporations Act 2001*) or their respective insurers; or
- (c) to the extent that the amount of the claim under the indemnity is increased as a result of failure of the director to comply with their obligations under the indemnity agreement.

During or since the financial year, the Company has paid premiums in respect of a contract insuring all the directors of Adairs Limited against legal costs incurred in defending proceedings for conduct other than:

- (a) A wilful breach of duty
- (b) A contravention of sections 182 or 183 of the *Corporations Act 2001*, as permitted by section 199B of the *Corporations Act 2001*

Under the terms of the policy, the total amount of insurance contract premiums paid cannot be disclosed.

Indemnification of Auditors

To the extent permitted by law, the Company has agreed to indemnify its auditors, Ernst & Young Australia, as part of the terms of its audit engagement agreement against claims by third parties arising from the audit (for an unspecified amount). No payment has been made to indemnify Ernst & Young during or since the financial year.

Rounding

The amounts contained in the Directors' Report and in the financial report have been rounded to the nearest \$1,000 (where rounding is applicable) where noted (\$000) under the option available to the Company under ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191. The Company is an entity to which this legislative instrument applies.

REMUNERATION REPORT

The directors of Adairs Limited present the Remuneration Report for the Company for the 52 week period of 4 July 2016 to 2 July 2017. This Remuneration Report forms part of the Directors' Report and has been audited in accordance with the *Corporations Act 2001*.

This Report sets out the remuneration arrangements for Adairs' key management personnel (KMP) (listed in the table below) who have been KMP during the reporting period. For the remainder of this Remuneration Report, the KMP are referred to as either Non-executive directors or Senior Executives.

All Non-executive directors and Senior Executives have held their positions for the entire duration of the reporting period unless indicated otherwise.

Name	Position
Non-executive Directors	
Michael Butler	Independent, Non-executive Chairman
David Briskin	Independent, Non-executive Director
Trent Peterson	Non-executive Director
Kate Spargo	Independent, Non-executive Director
David MacLean	Non-executive Director (from 18 November 2016)
Senior Executives	
David MacLean	Former Chief Executive Officer (CEO) and Executive Director (until 18 November 2016)
Mark Ronan	Chief Executive Officer (CEO) and Executive Director (from 18 November 2016) Former Chief Operating Officer (until 18 November 2016) and Company Secretary (until 3 November 2016)
Michael Cherubino	Executive Director Property and Business Development (from 17 October 2017) Former Chief Financial Officer (until 17 October 2017)
Mandy Drake	Chief Financial Officer (CFO) (from 17 October 2016) and Company Secretary (from 3 November 2016)

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REMUNERATION REPORT (continued)

Section 1: Remuneration overview

FY2017 has been a challenging year for the Company. The Board continues to focus on building and delivering value to shareholders, progress its growth plans and selectively pursue opportunities which we believe will add value in a manner which is appropriate having regard to the associated risks. Having a robust remuneration and reward framework that supports and encourages sustainable growth, risk management, and retains our people, is critical to the successful execution of our strategy.

The remuneration outcomes outlined in this Remuneration Report reflect the Company's approach to rewarding executives for delivering strong performance and holding executive team members accountable to ensure value for shareholders. For FY2017, no short term incentive (STI) cash bonuses were paid to Senior Executive. The Company's STI scheme for Senior Executives is based on achieving pre-determined performance criteria and targets. The primary performance condition of the FY2017 STI was the EBIT of the business. In FY2017, the Company's financial performance was disappointing and as a result the STI did not meet all of its performance conditions and no STI was awarded. The Board believes the FY2017 STI outcomes were fair and appropriate, and reflect the alignment between shareholders' interests and the Company's remuneration policies and practices.

During FY2017, the Company implemented a long term incentive (LTI) plan whereby Senior Executives of the Group were offered options over the ordinary shares of Adairs Limited. The options, issued for nil consideration, are subject to the satisfaction of both performance and service conditions, with the performance conditions ending on 30 June 2019 and the service condition ending 30 June 2020. Key details of the LTI plan are summarised in section 5. Shareholder approval for the LTI grants of options to both Mark Ronan and Michael Cherubino was obtained at the Annual General Meeting on 18 November 2016.

The Company's remuneration structure is intended to remain the same for FY2018. However, as announced to the ASX Mark Ronan was appointed Managing Director & CEO on 18 November 2016 and to reflect the change in his role and increased responsibilities Mark Ronan's fixed remuneration increased from \$425,000 to \$500,000 per annum. His STI opportunity for FY2018 remains at 50% of his fixed remuneration, which is \$250,000 as a result of his increase in fixed remuneration.

Section 2: Remuneration strategy and policy

A core belief of the Adairs Board is that the attraction, development, engagement and retention of skilled and culturally aligned leaders and team members provides a competitive advantage which is fundamental to the long term success of the Company. The maintenance and development of our leaders and fostering a workplace culture that supports this belief are priorities for the Company.

Adairs is committed to creating a focused and high performance culture. A summary of our philosophy is to provide simple and competitive market based total remuneration arrangements that also are linked in material part to measures of financial performance that we believe best represent the outcomes relevant to the value creation strategy of the Company.

Remuneration can include a number of different elements such as fixed pay, superannuation, short term incentives, long term incentives and other benefits such as tools of trade, study and relocation assistance and car lease arrangements. The elements of the total remuneration package may vary according to the job role, team members experience and performance. The Remuneration Committee also has regard for the equity ownership position of the KMPs when setting remuneration packages.

In considering the remuneration arrangements of KMP, the Remuneration Committee makes recommendations based on 7 important concepts;

1. **Simplicity:** We seek to ensure remuneration arrangements are simple, and can be easily understood by both the KMP and other key stakeholders.
2. **Alignment:** We seek to ensure material components of the KMP's remuneration arrangements (including their shareholding as appropriate) contribute to alignment of the interests of the KMP with those of the shareholders.
3. **Sustainability:** We seek to ensure the material aspects of an employee's remuneration arrangements are sustainable and could withstand tests of precedent and transparency within the organisation and market place.
4. **Competitive:** We seek to ensure our KMP are remunerated such that (when taken as a whole, and having regard to their particular circumstances, including any risks and opportunities) their individual remuneration arrangements are competitive with relevant comparable positions.
5. **Risk Aware:** In considering remuneration arrangements, the Company seeks to manage certain key risk exposures, including the risk of loss of an individual, retention of intellectual property and skills, issues associated with replacement of the individuals, risk of poaching, and the presence and quality of our succession planning.

REMUNERATION REPORT (continued)

6. **Company First:** The Company develops systems, policies, processes and team depth to manage its reliance on any given individual within its leadership team. This extends to remuneration, where we seek to ensure the remuneration architecture and individual arrangements are orderly and considered. Finally, we seek to respond to changes in an individual's circumstance or market conditions in a measured and sustainable manner.
7. **Reward for outcomes and performance:** We back ourselves to identify the outcomes that drive sustainable value creation (or value protection), and seek to reward executives who influence those outcomes most significantly and directly.

Section 3: Role of the Remuneration Committee and external advisers

The primary objective of the Remuneration Committee is to assist the Board to fulfil its corporate governance and oversight responsibilities in relation to the Company's people strategy including remuneration components, performance measurements and accountability frameworks, recruitment, engagement, retention, talent management and succession planning.

The Committee also works with the CEO in considering specific situations pertaining to employment terms for individuals, or groups of individuals as needed.

The Committee undertakes an annual review of the Company's remuneration strategy and remuneration policy to facilitate understanding of the overall approach to remuneration and to confirm alignment with the Company's business strategy, high standards of governance and compliance with regulatory standards.

The Committee reviews and recommends to the Board for approval, remuneration arrangements for the CEO and other Senior Executives. The Committee also establishes the policy for the remuneration arrangements for non-executive directors. The Committee reviews KMP arrangements on an annual basis against the remuneration policy, external remuneration practices, market expectations and regulatory standards. The Committee also reviews relevant individual's remuneration arrangements in the event that significant circumstances change (e.g. a role or company restructure or change of role). The Committee obtains independent external remuneration advice where appropriate.

The Remuneration Committee exercises caution in interpreting remuneration surveys. While we seek independent data from time to time, we believe benchmarking of salaries requires an intimate knowledge of the details and role and circumstances of the components of reference data set, and this is rarely possible, complex and prone to error. We therefore regard such information as only one component of the balanced consideration of base salaries and other remuneration terms and do not have a stated position regarding a target benchmark. Market information is sourced from internal and external sources.

No remuneration consultants or external advisers provided a remuneration recommendation during the 52 weeks ended 2 July 2017.

Section 4: Company Performance – relationship between financial performance and remuneration

The Company's executive remuneration is directly linked to the performance of the Company. The FY2017 STI is subject to the Company's EBIT result (as detailed above and shown below) and the FY2017 LTI is subject to the Company's earnings per share growth rate. The following table shows the Company's financial performance for FY2015 to FY2017. Comparative numbers for the previous 2 financial years are shown as this is only the Company's third Remuneration Report as a listed entity following listing on ASX on 17 June 2015.

The measures of profitability set out below reflects the Pro-forma ⁽¹⁾ result for the Company, calculated applying a methodology consistent with that set out in the Prospectus. The primary differences between the Statutory and Pro-forma results relate to the exclusion of the contribution of the dusk business, and exclusion of costs associated with the Listing.

DIRECTORS' REPORT (continued)

REMUNERATION REPORT (continued)

Continuing Operations	Pro-forma ⁽¹⁾		
	FY17 Performance	FY16 Performance	FY15 Performance
Sales (\$'000)	\$264,964	\$247,426	\$210,878
EBIT (\$'000) ⁽¹⁾	\$30,812	\$39,231	\$33,137
Net profit before tax (\$'000)	\$28,921	\$37,353	\$31,409
Net profit after tax (\$'000)	\$21,017	\$26,143	21,986
Share price at end of year	\$0.86	\$2.49	\$2.78 ⁽²⁾
Dividends paid per shares	8 cents	11.5 cents	N/A
Earnings per share	13 cents	16 cents	15 cents

(1) Pro-forma and EBIT results are non-IFRS financial measures contained within this report and are not subject to audit or review.

(2) The opening share price on 17 June 2015 was \$2.65.

Section 5: Senior Executive remuneration structure

Senior Executives are remunerated under a Total Reward structure which currently consists of three elements:

- fixed remuneration comprising base salary package (inclusive of superannuation contributions, car allowances and other benefits);
- short term incentives (STI); and
- long term incentives (LTI).

The mix of remuneration between fixed and variable (i.e. at risk) components for a Senior Executive is determined having regard to the seniority of the role, the responsibilities of the role for driving business performance and responsibilities for developing and implementing business strategy.

The mix of fixed and at risk components for each of the Senior Executives as a percentage of total target remuneration for FY2017 was as follows:

Figure 1:

Senior Executive	% of total target remuneration for FY2017		
	Fixed remuneration	At risk remuneration STI maximum opportunity	At risk remuneration LTI maximum opportunity ⁽¹⁾
David MacLean ⁽²⁾	100%	Nil	Nil
Mark Ronan	55%	25%	20%
Michael Cherubino	60%	25%	15%
Mandy Drake	100%	Nil	Nil

(1) LTI Options are eligible to vest on 30 June 2020.

(2) David MacLean retired as an Executive Director and CEO on 18 November 2016. As a result he was not eligible for at risk remuneration (STI and LTI).

Fixed remuneration

The remuneration for Senior Executives includes a fixed component comprised of base salary and employer superannuation contributions that are in line with statutory obligations.

The remuneration policy provides Senior Executives a base salary package that reflects the base salary for a comparable, role in similarly sized companies operating in the retail industry, having regard to the experience and expertise of the Senior Executive, their performance and history with the Company, and other relevant factors. Senior Executives and the Board acknowledge that this requires both quantitative and subjective assessment.

Fixed remuneration is reviewed annually by the Remuneration Committee and recommendations are made to the Board. Any change is usually effective from the commencement of the new financial year. There is no guaranteed salary increase in any Senior Executive's service contract.

REMUNERATION REPORT (continued)**STI arrangements for FY2017**

Set out below is a summary of the terms and conditions of the FY2017 STI.

What is the Adairs Management Incentive Scheme (STI Scheme)?	An annual incentive scheme under which Adairs Senior Executives are eligible to receive an annual cash award based on the achievement of performance conditions.																												
Why does the Board consider the STI Scheme an appropriate incentive?	The STI scheme aligns Senior Executive reward with the achievement of performance targets that are aligned to delivering and protecting sustainable value to shareholders.																												
What is the performance period?	12 months from 4 July 2016 to 2 July 2017																												
What are the performance conditions?	<p>The STI scheme has the following performance conditions:</p> <ul style="list-style-type: none">• Minimum stock turn target• Company EBIT measures• Continuing service condition <p>Stock turn target: for a Senior Executive to be eligible to earn any part or all of their STI in FY2017, the Company’s stock turn target must be met. If the Company’s stock turn target is not met, no STI will be awarded.</p> <p>Company EBIT: the STI scheme is primarily based upon the Company’s EBIT result for the financial year. Each year the Board will determine the EBIT benchmarks with reference to the annual forecast and prior year results. On achievement of the EBIT benchmark, the Senior Executive will be entitled to an initial incentive and will share in any amount achieved in excess of the EBIT benchmark. For FY2017, the EBIT benchmarks and corresponding bonus amounts payable were:</p> <table><tr><th></th><th>EBIT</th><th>M Cherubino</th><th>M Ronan</th></tr><tr><td>Below benchmark</td><td>less than \$41.16m</td><td>nil</td><td>Nil</td></tr><tr><td>Benchmark</td><td>\$41.16m</td><td>\$35,000</td><td>\$50,000</td></tr><tr><td>Level 2</td><td>\$42.14m</td><td>\$70,000</td><td>\$100,000</td></tr><tr><td>Level 3</td><td>\$43.12m</td><td>\$105,000</td><td>\$150,000</td></tr><tr><td>Level 4</td><td>\$44.10m</td><td>\$140,000</td><td>\$200,000</td></tr><tr><td>Level 5</td><td>\$45.08m</td><td>\$175,000</td><td>\$250,000</td></tr></table> <p>Service condition: there is an additional requirement that on the STI payment date (anticipated to be in September each year), the Senior Executive must be employed by Adairs (and not have given notice or be suspended from employment) otherwise no STI will be paid subject to director’s discretion.</p>		EBIT	M Cherubino	M Ronan	Below benchmark	less than \$41.16m	nil	Nil	Benchmark	\$41.16m	\$35,000	\$50,000	Level 2	\$42.14m	\$70,000	\$100,000	Level 3	\$43.12m	\$105,000	\$150,000	Level 4	\$44.10m	\$140,000	\$200,000	Level 5	\$45.08m	\$175,000	\$250,000
	EBIT	M Cherubino	M Ronan																										
Below benchmark	less than \$41.16m	nil	Nil																										
Benchmark	\$41.16m	\$35,000	\$50,000																										
Level 2	\$42.14m	\$70,000	\$100,000																										
Level 3	\$43.12m	\$105,000	\$150,000																										
Level 4	\$44.10m	\$140,000	\$200,000																										
Level 5	\$45.08m	\$175,000	\$250,000																										
Why were the performance conditions chosen?	<p>EBIT and stock turn levels were chosen as performance conditions to ensure that the STIs are linked to the achievement of key financial objectives and business drivers that we believe are well understood by stakeholders and balanced indicators of success of the individual’s contribution to performance.</p> <p>The Board believes that stock turn is an important measure to support the underlying quality and sustainability of the EBIT result, and ensure underlying cash generation and productivity of the business is also improving.</p> <p>The Remuneration Committee recommends to the Board annual EBIT targets in consultation with the CEO. In setting these targets, the Committee considers the EBIT projections set out in the Company’s approved business plan, and performance (growth) relative to prior year, and other factors specific to the upcoming year. The Board believes that achieving acceptable levels of growth</p>																												

REMUNERATION REPORT (continued)

	year on year, and meeting targets set out in the Company's annual business plan are both important.
How are the performance conditions measured and why were these methods chosen?	<p>The Remuneration Committee has ultimate responsibility for assessing whether performance conditions are achieved and for approving STI payments.</p> <p>Following the end of the financial year, the Remuneration Committee assesses achievement against performance targets, and determines the STI awards to be made to Senior Executives (if any).</p> <p>Individual stock turn target: the stock turn level is set using Adairs' internal measure of stock turns which is calculated by dividing the total cost of goods sold (excluding distribution costs) by the average month end level of inventory held by the business through the financial year. Adairs uses this methodology as it ensures that the inventory is better managed throughout the year rather than using opening and closing balances.</p> <p>Company EBIT: for the purpose of determining the Company's achievement of the EBIT benchmark, financial results are extracted by reference to the Company's audited financial statements. The use of financial statements ensures the integrity of the measure and alignment with the true financial performance of the Company.</p> <p>One off adjustments will only be considered by the Committee in exceptional circumstances and where they occur as a result of matters that are materially outside the control of management and could not have reasonably been contemplated at the time of setting the targets. The Board expects such events to be rare.</p> <p>The Board may determine a discretionary amount of STI award beyond the award that is achieved based on the criteria above.</p> <p>The Board rarely exercises this discretion, and only does so in exceptional circumstances. No additional discretionary cash bonuses have been awarded to KMP's in relation to FY2017.</p>

Figure 2: Percentage of FY2017 STI paid and forfeited for Senior Executives

The FY2017 STI was tested following completion of the performance period on 2 July 2017. No FY2017 STI was awarded.

Senior Executives	Target STI (\$)	Actual STI awarded (\$)	Actual STI awarded as % of maximum STI	% of maximum STI award forfeited
Mark Ronan	250,000	Nil	0%	100%
Michael Cherubino	175,000	Nil	0%	100%

REMUNERATION REPORT (continued)**STI arrangements for FY2018**

Set out in Figure 3 (below) is the maximum STI opportunity for each Senior Executive for FY2018. The maximum STI opportunity as a percentage of fixed remuneration remains unchanged for Mark Ronan and Michael Cherubino. FY2018 will be the first year Mandy Drake is eligible to receive a STI.

The FY2018 STI will be on the same terms as the FY2017 STI (as set out above). The Board has reviewed and reset the EBIT targets for FY2018. Details of the FY2018 STI and any amount awarded to Senior Executives will be disclosed in the FY2018 Remuneration Report.

Figure 3: FY2018 remuneration opportunities

Senior Executive	Fixed remuneration (at 2 July 2017)	Maximum STI opportunity for FY2018 ⁽¹⁾	% of fixed remuneration available as base STI
Mark Ronan	\$500,000	\$250,000	50.0%
Michael Cherubino	\$433,000	\$175,000	40.4%
Mandy Drake	\$340,000	\$175,000	51.5%

(1) This is based on the maximum STI opportunity. The actual reward is dependent on the achievement of performance conditions in FY2018.

LTI arrangements for FY2017

The Remuneration Committee introduced a LTI plan during FY2017 to assist in the motivation, retention and reward of Senior Executives. The Board believe that equity ownership is an important component of aligning the interests of KMP with shareholders.

In FY2017, Mark Ronan and Michael Cherubino received grants of options as their FY2017 LTI award. Each option entitles the Senior Executive to acquire an ordinary share in the Company subject to meeting specific performance and service conditions (set out below) and payment of an exercise price (**LTI Options**). The LTI Options were granted at no cost to the Senior Executives as they form part of the Senior Executive's remuneration for FY2017.

The performance period for the FY2017 LTI Option grant is 4 years from 4 July 2016 to 30 June 2020. The LTI Options will vest and become exercisable if the relevant performance and service conditions have been met. The Senior Executive may then exercise any vested LTI Options until 18 November 2022, being 6 years from the LTI Options grant date. After 18 November 2022, any unexercised LTI Options will lapse. On vesting, an exercise price of \$2.00 will be payable by the Senior Executive to receive their share allocation. LTI Options do not carry any voting or dividend entitlements prior to exercise.

Performance criteria

The LTI Options are subject to two performance conditions:

- **EPS performance condition** – 60% of the LTI Options are subject to an earnings per share (EPS) performance condition. This is based on the compound annual growth rate (CAGR) of the Company's EPS over a 3 year period ending 30 June 2019.

The percentage of LTI Options that vest against the EPS performance condition will be determined in accordance with the following vesting schedule:

EPS CAGR	% of EPS LTI Options vest
Less than or equal to 5% per annum	0%
Between 5% and 20% per annum	pro-rata between 0% and 100%
Greater than 20% per annum	100%

The EPS performance condition was selected because of its correlation with long term shareholder return and its lower susceptibility to short term share price volatility. This measure also provides a greater 'line of sight' between Senior Executives' actions and the way in which their performance is measured. Consequently, this component was more heavily weighted in order to drive performance and provide an appropriate retention incentive.

For the purpose of testing the achievement of the EPS performance condition, financial results are extracted by reference to the Company's audited financial statements. The use of financial statements ensures the integrity of the measure and alignment with the true financial performance of the Company.

DIRECTORS' REPORT (continued)

REMUNERATION REPORT (continued)

EPS is calculated using earnings on a pre-significant items (i.e. any unusual or material one-off items in the result) basis adjusted for the related income tax (benefit)/expense, and using the number of ordinary shares on issue at the effective date of grant and the number of ordinary shares on issue at the end of the relevant measurement period to calculate EPS.

Assessment of achievement of the EPS performance condition will be determined by the Board.

- **Sales performance condition** – 40% of the LTI Options are subject to a like-for-like sales growth performance condition.

The percentage of LTI Options that vest against the Sales performance condition will be determined in accordance with the following vesting schedule:

Like for like sales growth	% of sales growth LTI Options that vest
Less than or equal to 2.5% per annum	0%
Between 2.5% and 12.5% per annum	pro-rata between 0% and 100%
Greater than 12.5% per annum	100%

Like-for-like sales growth measures growth in sales in one year compared to the previous year, taking into consideration only like-for-like sales.

Like for like sales growth measures the sales generated from stores (including online) in a relevant period compared to the total aggregated sales from the same set of stores in the relevant corresponding period. For the purposes of the calculation the like for like sales result will be the compounded annual growth rate achieved over the period. Like for like sales growth was selected as a performance measure as the Board believe it is well understood fair measure of the long term health of the businesses customer proposition.

Service criteria

The LTI Options are also subject to a service condition where participants must remain employed on a full time basis by, and must not have given notice of resignation from, the Group at the vesting date (being 30 June 2020).

Treatment on cessation of employment

Where a Senior Executive ceases employment for cause or due to resignation, all unvested LTI Options lapse. In all other circumstances, a pro rata portion (based on the portion of the performance period that has elapsed) of a Senior Executive's unvested LTI Options will remain on foot and subject to the original performance conditions, as if the participant had not ceased employment.

Where a Senior Executive ceases employment with the Group for cause or due to resignation, all vested but unexercised LTI Options will lapse. In all other circumstances, vested but unexercised LTI Options will remain on foot and exercisable for a period of 3 months after which time they will lapse (if not exercised).

However, pursuant to the Plan Rules, the Board retains absolute discretion to determine, vest or lapse some or all LTI Options in all circumstances.

Treatment on change of control

Where there is likely to be a change of control, the Board has the discretion to accelerate vesting of some or all of the LTI Options. If an actual change of control occurs before the Board exercises its discretion, a pro-rata portion of the Options (equal to the portion of the relevant performance period that has elapsed up to the change of control) will vest. The Board retains a discretion to determine whether the remaining unvested LTI Options will vest and become exercisable or lapse.

On a change of control, vested LTI Options will remain exercisable for a period of 3 months after the actual change of control and will lapse after the end of that period (if not exercised).

Service Agreements

Adairs Holding Australia Pty Ltd (ACN 128 275 838) (a wholly owned subsidiary of the Company) (**Adairs Holding**) has entered into service agreements with David MacLean (ceased on 18 November 2016), Michael Cherubino, Mark Ronan and Mandy Drake to formalise the remuneration and terms of their employment with Adairs. Each of these agreements provides for the provision of fixed remuneration, performance related cash bonuses and other benefits.

DIRECTORS' REPORT (continued)

REMUNERATION REPORT (continued)

The term of the service agreements with the Senior Executives are ongoing until terminated by either Adairs Holding or the relevant Senior Executive. The service agreements with the Senior Executives may be terminated early by either party with six months' notice. In either event, Adairs Holding may make payment in lieu of notice. In the event of serious misconduct or other circumstances warranting summary dismissal, Adairs Holding may terminate the Senior Executive's employment contract immediately without notice.

The Corporations Act restricts the termination benefits that can be provided to KMP on cessation of their employment, unless shareholder approval is obtained. The shareholders of the Company and Adairs Holding approved termination arrangements for David MacLean and Michael Cherubino at a general meeting of the Company on 1 June 2015.

After cessation of employment for any reason, for a period of 6 months, the Senior Executive must not compete with the Company (including direct or indirect involvement as a principal, agent, partner, employee, shareholder, unit holder, director, trustee, beneficiary, manager, contractor, adviser or financier), without first obtaining the consent of the Company in writing, subject to certain carve outs and exemptions.

In addition, in the case of Mark Ronan and Michael Cherubino, where the Senior Executive has resigned from the Company, the Board may elect to extend this restraint period for further period of up to 6 months by notifying the employee and paying the employee a further amount for each month (up to a maximum of 6 months) on a monthly basis.

No contracted retirement benefits are in place with any of the Company's Senior Executives.

Section 6: Non-Executive Directors Remuneration Structure

Overview

The Company's remuneration strategy is designed to attract and retain experienced, qualified non-executive directors and to remunerate appropriately to reflect the demands which are made on them and the responsibilities of the position.

The level of fees are reviewed annually by the Remuneration Committee, and are based on the fees paid for comparative Non-executive director roles in similarly sized publicly listed companies operating in the retail industry.

Non-executive directors' fees

Non-executive director fees are determined within an aggregate directors' fee pool approved by shareholders. The current approved fee pool of up to \$450,000 per annum was approved by shareholders at a general meeting of the Company on 1 June 2015.

Currently, annual base non-executive directors' fees are \$136,875 for the Chairman and \$70,000 for each other non-executive director. All non-executive director fees include superannuation. No additional fees are paid to the chairs and members of the Audit and Risk Committee, and the Remuneration Committees. The director fees for Trent Peterson are paid to Catalyst Investment Managers Pty Ltd.

Directors may also be reimbursed for travel and other expenses incurred in attending to the Company's affairs. Directors may be paid additional or special remuneration where a director performs services outside the ordinary duties of a non-executive director. There are no retirement benefit schemes for non-executive directors other than statutory superannuation contributions, and non-executive directors do not currently receive shares, performance rights or options as part of their remuneration.

Section 7: KMP Disclosures

Material Contracts with the Company

No director or other KMP (including their related parties) has entered into a material contract with the Company or a subsidiary during the reporting period.

Loans with the Company

No director or other KMP (including their related parties) has entered into a loan made, guaranteed or secured, directly or indirectly, by the Company or a subsidiary during the reporting period.

DIRECTORS' REPORT (continued)

REMUNERATION REPORT (continued)

Section 8: Statutory Remuneration Details and Other Statutory Disclosures

Remuneration – statutory disclosures

Details of the remuneration for KMP of the Company paid in the financial year are as follows:

2017	Short term employee benefits			Post-employment benefits		Other long term benefits	Termination benefits	Share-based payments	Total
	Cash salary and fees	Short Term Incentive Cash bonuses	Non-monetary benefits	Superannuation	Other				
Non-Executive Directors									
Michael Butler	\$125,000	-	-	\$11,875	-	-	-	-	\$136,875
Trent Peterson ⁽¹⁾	\$70,000	-	-	-	-	-	-	-	\$70,000
Kate Spargo	\$63,927	-	-	\$6,073	-	-	-	-	\$70,000
David Briskin	\$63,927	-	-	\$6,073	-	-	-	-	\$70,000
David MacLean ⁽²⁾	\$39,503	-	-	\$3,753	-	-	-	-	\$43,256
Total non-executive Directors	\$362,357	-	-	\$27,774	-	-	-	-	\$390,131
Executive Directors									
David MacLean ⁽²⁾	\$236,250	-	-	\$14,135	-	-	\$387,945	-	\$638,330
Mark Ronan ⁽³⁾	\$448,749	-	-	\$19,616	-	-	-	\$20,126	\$488,491
Michael Cherubino ⁽⁴⁾	\$407,550	-	-	\$25,000	-	-	-	\$11,501	\$444,051
Other Senior Executives									
Mandy Drake ⁽⁵⁾	\$215,576	-	-	\$19,809	-	-	-	-	\$235,385
Total executive	\$1,308,125	-	-	\$78,560	-	-	\$387,945	\$31,627	\$1,806,257
Total 2017	\$1,670,482	-	-	\$106,334	-	-	\$387,945	\$31,627	\$2,196,388

(1) The Director fees for Trent Peterson are paid to Catalyst Investment Managers Pty Ltd.

(2) David MacLean ceased on 18 November 2016 as Chief Executive Officer and Executive Director and commenced as Non-Executive Director. The termination benefits represent accrued untaken leave entitlements on cessation.

(3) Mark Ronan ceased on 18 November 2016 as Chief Operating Officer and Company Secretary and commenced as Chief Executive Officer and Executive Director.

(4) Michael Cherubino ceased on 17 October 2016 as Chief Financial Officer and commenced as Property and Business Development Director.

(5) Mandy Drake commenced on 17 October 2016 as Chief Financial Officer and on the 3 November 2016 as Company Secretary.

DIRECTORS' REPORT (continued)

REMUNERATION REPORT (continued)

2016	Short term Employee Benefits			Post-employment benefits		Other long term benefits	Termination benefits	Share-based payments	Total
In AUD	Cash Salary and Fees	Short Term Incentive Cash Bonuses	Non-monetary benefits	Superannuation	Other			Long Term Incentive Options	
Michael Butler	\$125,989	-	-	\$11,969	-	-	-	-	\$137,958
Trent Peterson ⁽¹⁾	\$70,000	-	-	-	-	-	-	-	\$70,000
Kate Spargo	\$63,927	-	-	\$6,073	-	-	-	-	\$70,000
David Briskin	\$63,927	-	-	\$6,073	-	-	-	-	\$70,000
Total non-executive Directors	\$323,843	-	-	\$24,115	-	-	-	-	\$347,958
David MacLean	\$515,000	\$280,000	-	\$35,000	-	-	-	-	\$830,000
Michael Cherubino	\$395,000	\$200,000	-	\$25,000	-	-	-	-	\$620,000
Mark Ronan	\$355,692	\$175,000	-	\$19,308	-	-	-	-	\$550,000
Total executives	\$1,265,692	\$655,000	-	\$79,308	-	-	-	-	\$2,000,000
Total 2017	\$1,589,535	\$655,000	-	\$103,423	-	-	-	-	\$2,347,958

(1) The Director fees for Trent Peterson are paid to Catalyst Investment Managers Pty Ltd.

DIRECTORS' REPORT (continued)

REMUNERATION REPORT (continued)

Shareholdings of Key Management Personnel

The following table details the ordinary shareholdings and the movements in the shareholdings of KMP (including their personally related entities) for FY2017.

No. of Shares	Balance at 4 July 2016	Granted as Remuneration	Received on exercise of options	Other net change ⁽²⁾	Held at 2 July 2017
Non-executive Directors					
Michael Butler	62,500	-	-	176,156	238,656
Trent Peterson ⁽¹⁾	1,092,538	-	-	250,000	1,342,538
Kate Spargo	41,667	-	-	-	41,667
David Briskin	208,334	-	-	-	208,334
David MacLean	4,152,273	-	-	166,000	4,318,273
Executive Directors					
Mark Ronan	631,668	-	-	50,000	681,668
Michael Cherubino	2,076,135	-	-	82,000	2,158,135
Other Senior Executives					
Mandy Drake	-	-	-	-	-

(1) This excludes the economic interest held by Trent Peterson in shares held by Catalyst Funds as a result of his role at Catalyst Investment Managers Pty Ltd. Trent Peterson has an economic interest in all Adairs Limited shares held by Catalyst Funds subject to certain conditions including the performance of those funds taken as a whole.

(2) Reflects on market share purchases made by KMP over the course of FY2017.

Option holdings of Key Management Personnel

The following table details the option holdings and the movements in the options of KMP (including their personally related entities) for FY2017. This was the first year options were granted to Senior Executives as LTI remuneration. Accordingly, no options were vested, exercised, lapsed or forfeited during the reporting period and no options are presently capable of being exercised.

No. of Options	Balance at 4 July 2016	Granted as Remuneration	Vested/ Exercisable	Exercised	Balance at 2 July 2017	Exercisable / Vested as at 2 July 2017
Non-executive Directors						
Michael Butler	-	-	-	-	-	-
Trent Peterson	-	-	-	-	-	-
Kate Spargo	-	-	-	-	-	-
David Briskin	-	-	-	-	-	-
David MacLean	-	-	-	-	-	-
Executive Directors						
Mark Ronan	-	651,000	-	-	651,000	-
Michael Cherubino	-	372,000	-	-	372,000	-
Other Senior Executives						
Mandy Drake	-	-	-	-	-	-

During the reporting period, 651,000 options with a fair value of \$175,770 (\$0.27 per option) were granted to Mark Ronan with a grant date of 18 November 2016. The options vest upon the satisfaction of the service condition on 30 June 2020 and satisfaction of the performance conditions outlined under the LTI arrangements in section 5 above.

During the reporting period, 372,000 options with a fair value of \$100,440 (\$0.27 per option) were granted to Michael Cherubino with a grant date of 18 November 2016. The options vest upon the satisfaction of the service condition on 30 June 2020 and satisfaction of the performance conditions outlined under the LTI arrangements in section 5 above.

DIRECTORS' REPORT (continued)

REMUNERATION REPORT (continued)

Signed in accordance with a resolution of the directors.

On behalf of the Board

A stylized, handwritten signature in blue ink, consisting of a single, continuous, sweeping line that forms a large, open 'M' shape.

Michael Butler
Independent Chairman
Non-Executive Director

A handwritten signature in blue ink, featuring a series of loops and flourishes, with the name 'Mark Ronan' being clearly legible.

Mark Ronan
Chief Executive Officer and Managing Director

Melbourne
28 August 2017

Independent Auditor's Report to the Members of Adairs Limited

Report on the Audit of the Financial Report

Opinion

We have audited the financial report of Adairs Limited (the Company) and its subsidiaries (collectively the Group), which comprises the consolidated statement of financial position as at 2 July 2017, the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the 52 weeks then ended, notes to the financial statements, including a summary of significant accounting policies, and the directors declaration.

In our opinion, the accompanying financial report of the Group is in accordance with the *Corporations Act 2001*, including:

- a) giving a true and fair view of the consolidated financial position of the Group as at 2 July 2017 and of its consolidated financial performance for the 52 weeks ended on that date; and
- b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial report of the current year. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial report. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial report.

1. Inventory valuation

Why significant

As at 2 July 2017, the Group held \$33.0 million (or 18% of total assets) in inventories which is a material balance for the Group.

As detailed in Note 2(m) and Note 7 to the financial report, inventories are valued at the lower of cost and net realisable value. There is judgment in determining an appropriate costing basis and assessing the net realisable value.

In capturing the cost of inventories, the Group estimates an absorption cost for distribution centre costs. The Group capitalises part of its cost to operate the warehouse, as well as freight, duty and insurance costs incurred at the distribution centre into inventories as these are costs incurred in order to ready the inventory for sale.

The Group sells homeware and home furnishing products and is subject to changing consumer demands and fashion trends, increasing the level of judgment involved in estimating inventory provisions. Judgment is required to assess the appropriate level of provisioning for items which may be ultimately sold below cost as a result of a reduction in consumer demand. Such judgments include expectations for future sales and inventory liquidation plans.

How our audit addressed the key audit matter

Our audit procedures assessed the valuation of inventories and the related disclosures. In performing our assessment, we:

- ▶ Assessed the application of inventory valuation methodologies and whether this was consistent with Australian Accounting Standards.
- ▶ Assessed and tested the design and operating effectiveness of relevant controls in relation to the standard costing process and assessed the accuracy of the Group's inventory valuation model including costs capitalised into inventories, on a sample basis.
- ▶ Assessed the basis for inventory provisions recorded by the Group, including the rationale for recording specific provisions. In doing so, we examined the aging profile of inventories, the process for identifying specific slow-moving inventories and historical inventory turnover.
- ▶ Considered the completeness of inventory provisions by identifying promotional sales at or subsequent to 2 July 2017, and compared the sale prices against the value of inventories.

2. Carrying value of intangible assets

Why significant

As at 2 July 2017, the Group held \$111.2 million (or 58% of total assets) in goodwill and indefinite-life brand names recognised from historical business combinations.

As explained in Note 2(q) and Note 9 to the financial report, the goodwill and brand names are tested by the Group for impairment annually.

The recoverable amount has been determined based on a value-in-use model referencing discounted cash flows of the Adairs cash generating unit (CGU). This model contains estimates and significant judgments regarding future projections and the achievement of those forecasts which are critical to the assessment of impairment, particularly planned growth rates and gross margins.

The Group has disclosed in Note 9 the assessment method, including the key underlying assumptions, the results of the assessment as well as the impact of applying sensitivities.

How our audit addressed the key audit matter

Our audit procedures assessed the carrying value of intangible assets and the related disclosures. In performing our assessment, we involved our valuation specialists and:

- ▶ Assessed the application of valuation methodologies.
- ▶ Assessed the key inputs and assumptions, including forecasted cash flows, gross margins, discount rates and growth rates adopted in the valuation. We agreed the cash flows to the Board approved FY2018 budget.
- ▶ Compared the data used in the value-in-use model to the actual and budgeted financial performance of the underlying CGU.
- ▶ Performed sensitivity analysis on key inputs, assumptions and budgeted financial performance to determine whether any reasonably possible change could result in impairment.
- ▶ Compared earnings multiples derived from the Group's value-in-use model to those observable from external market data of comparable listed entities.
- ▶ Assessed the adequacy of the disclosures made in the financial report.

Information Other than the Financial Report and Auditor's Report Thereon

The directors are responsible for the other information. The other information comprises the information included in the Group's 2017 Annual Report other than the financial report and our auditor's report thereon. We obtained the directors' report that is to be included in the Annual Report, prior to the date of this auditor's report, and we expect to obtain the remaining sections of the Annual Report after the date of this auditor's report.

Our opinion on the financial report does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated to the directors, we determine those matters that were of most significance in the audit of the financial report of the current year and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on the Audit of the Remuneration Report

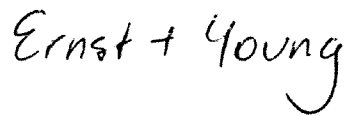
Opinion on the Remuneration Report

We have audited the Remuneration Report included in pages 14 to 26 of the directors' report for the 52 weeks ended 2 July 2017.

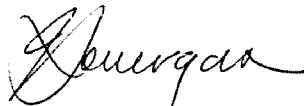
In our opinion, the Remuneration Report of Adairs Limited for the 52 weeks ended 2 July 2017, complies with section 300A of the *Corporations Act 2001*.

Responsibilities

The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.



Ernst & Young



Joanne Lonergan
Partner
Melbourne

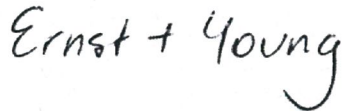
28 August 2017

Auditor's Independence Declaration to the Directors of Adairs Limited

As lead auditor for the audit of Adairs Limited for the 52 weeks ended 2 July 2017, I declare to the best of my knowledge and belief, there have been:

- a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the review; and
- b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Adairs Limited and the entities it controlled during the financial period.



Ernst & Young



Joanne Lonergan
Partner

28 August 2017

DIRECTORS' DECLARATION

In accordance with a resolution of the directors of Adairs Limited, we state that:

1. In the opinion of the directors:

(a) the financial statements and notes of Adairs Limited for the 52 weeks ended 2 July 2017 are in accordance with the *Corporations Act 2001*, including:

(i) giving a true and fair view of the consolidated entity's financial position as at 2 July 2017 and of its performance for the 52 weeks ended on that date; and

(ii) complying with Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*;

(b) the financial statements and notes also comply with International Financial Reporting Standards as disclosed in Note 2; and

(c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

2. This declaration has been made after receiving the declarations required to be made to the directors by the chief executive officer and chief financial officer in accordance with *section 295A of the Corporations Act 2001* for the financial year ended 2 July 2017.

On behalf of the board



Michael Butler
Independent Chairman
Non-Executive Director

Melbourne
28 August 2017



Mark Ronan
Managing Director and Chief Executive Officer

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

FOR THE 52 WEEKS ENDING 2 July 2017

	Note	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
Revenues from sale of goods	3(a)	264,964	253,182
Cost of sales		(108,163)	(98,863)
Gross profit		156,801	154,319
Other income	3(a)	245	487
Depreciation and amortisation expenses	3(b)	(5,877)	(5,266)
Finance expenses	3(c)	(1,946)	(2,006)
Salaries and employee benefits expense	3(d)	(62,094)	(58,813)
Asset, property and maintenance expenses		(982)	(515)
Occupancy expenses		(36,854)	(32,007)
Advertising expenses		(6,419)	(5,467)
Other expenses from ordinary activities	3(e)	(13,953)	(11,808)
Transaction expenses		-	(101)
Profit before income tax		28,921	38,823
Income tax expense	4	(7,904)	(11,651)
Profit for the period		21,017	27,172
Earnings per share attributable to ordinary equity holders of the Parent			
Basic earnings per share	20	12.7 cents	16.4 cents
Diluted earnings per share	20	12.7 cents	16.4 cents

This Consolidated Statement of Profit and Loss should be read in conjunction with the notes to the financial statements.

CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME

FOR THE 52 WEEKS ENDING 2 July 2017

	Note	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
Profit for the period		21,017	27,172
Other comprehensive income			
<i>Items that may be reclassified subsequently to profit or loss</i>			
Net movement of cash flow hedges		346	(1,771)
Income tax relating to the components of other comprehensive income	4	(104)	531
Exchange differences on translation of foreign operations		(7)	-
Other comprehensive income for the period, net of tax		235	(1,240)
Total comprehensive income for the period		21,252	25,932

This Consolidated Statement of Other Comprehensive Income should be read in conjunction with the notes to the financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 2 July 2017

		As at 2 July 2017	As at 3 July 2016 Restated*
	Note	\$'000	\$'000
ASSETS			
CURRENT ASSETS			
Cash and cash equivalents	5	14,313	14,676
Trade and other receivables	6	4,488	6,599
Inventories	7	32,992	26,272
TOTAL CURRENT ASSETS		51,793	47,547
NON CURRENT ASSETS			
Property, plant and equipment	8	20,188	16,007
Intangibles	9	114,671	113,399
Deferred tax assets	4	6,029	6,725
TOTAL NON CURRENT ASSETS		140,888	136,131
TOTAL ASSETS		192,681	183,678
LIABILITIES			
CURRENT LIABILITIES			
Trade and other payables	10	26,393	15,391
Interest bearing liabilities	11	(44)	(121)
Current tax liabilities		849	8,794
Provisions	12	4,167	3,496
Derivative financial instruments	15	657	1,015
TOTAL CURRENT LIABILITIES		32,022	28,575
NON CURRENT LIABILITIES			
Deferred tax liabilities	4	12,559	12,453
Interest bearing liabilities	11	41,955	41,921
Provisions	12	5,818	5,136
Derivative financial instruments	15	15	3
TOTAL NON CURRENT LIABILITIES		60,347	59,513
TOTAL LIABILITIES		92,369	88,088
NET ASSETS		100,312	95,590
EQUITY			
Contributed equity		68,349	68,349
Share based payment reserve	13(b)	58	-
Foreign currency translation reserve	13(c)	(7)	-
Cash flow hedge reserve	13(d)	(471)	(713)
Retained earnings	13(e)	32,383	27,954
TOTAL EQUITY		100,312	95,590

* Refer to Note 2 (c)(ii) for restatement disclosure.

This Consolidated Statement of Financial Position should be read in conjunction with the notes to the financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE 52 WEEKS ENDING 2 July 2017

Note	Ordinary shares \$'000	Share based payment reserve \$'000	Foreign currency translation reserve \$'000	Cash flow hedge reserve \$'000	Retained earnings \$'000	Total \$'000
At 3 July 2016	68,349	-	-	(713)	27,954	95,590
Profit for the period	-	-	-	-	21,017	21,017
Other comprehensive income for the period	-	-	(7)	242	-	235
Total comprehensive income for the period	-	-	(7)	242	21,017	21,252
Transactions with owners in their capacity as owners:						
Dividend payment	22	-	-	-	(16,588)	(16,588)
Share-based payments	23	-	58	-	-	58
At 2 July 2017	68,349	58	(7)	(471)	32,383	100,312

	Ordinary shares \$'000	Share based payment reserve \$'000	Foreign currency translation reserve \$'000	Cash flow hedge reserve \$'000	Retained earnings \$'000	Total \$'000
At 28 June 2015	68,349	-	-	527	9,076	77,952
Profit for the period	-	-	-	-	27,172	27,172
Other comprehensive income for the period	-	-	-	(1,240)	-	(1,240)
Total comprehensive income for the period	-	-	-	(1,240)	27,172	25,932
Transactions with owners in their capacity as owners:						
Dividend payment	-	-	-	-	(8,294)	(8,294)
Share-based payments	-	-	-	-	-	-
At 3 July 2016	68,349	-	-	(713)	27,954	95,590

This Consolidated Statement of Changes in Equity should be read in conjunction with the notes to the financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE 52 WEEKS ENDING 2 July 2017

	Note	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from customers (inclusive of GST)		293,022	277,047
Payments to suppliers and employees (inclusive of GST)		(248,550)	(235,447)
Interest received		55	81
Income tax paid		(15,152)	(8,659)
Interest paid		(1,731)	(1,936)
IPO transaction costs paid		-	(7,229)
Net cash flows from operating activities	5	27,644	23,857
CASH FLOWS FROM INVESTING ACTIVITIES			
Acquisition of property, plant, equipment and intangibles		(11,330)	(10,324)
Net cash flows used in investing activities		(11,330)	(10,324)
CASH FLOWS FROM FINANCING ACTIVITIES			
Borrowings costs paid		(89)	-
Dividends paid	22	(16,588)	(8,294)
Net cash flows used in financing activities		(16,677)	(8,294)
Net increase in cash and cash equivalents		(363)	5,239
Cash and cash equivalents at beginning of the period		14,676	9,437
CASH AND CASH EQUIVALENTS AT END OF PERIOD	5	14,313	14,676

This Consolidated Statement of Cash Flows should be read in conjunction with the notes to the financial statements .

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTES TO THE FINANCIAL STATEMENTS

FOR THE 52 WEEKS ENDING 2 July 2017

NOTE 1. CORPORATE INFORMATION

The consolidated financial statements of Adairs Limited and its subsidiaries (collectively, the Group) for the 52 weeks ending 2 July 2017 were authorised for issue in accordance with a resolution of the directors on 28 August 2017.

Adairs operates on a retail accounting calendar which consists of four 13 weeks quarters based on weekly financial and operating performance, equating to an annual 52 week reporting period with a 53 week reporting period every five to six years. In FY2017, there was a 52 week reporting period. This was in comparison to FY2016 which was a 53 week reporting period. The implication of this is FY2016 has 371 financial year days versus 364 financial year days in FY2017.

Adairs Limited (the Company or the parent) is a for profit company limited by shares incorporated in Australia whose shares are publicly traded on the Australian Securities Exchange.

The Group is principally engaged in retail operations in the Manchester, Homewares and Home Décor market segments within Australia and New Zealand. The Group's principal place of business is International Court, Scoresby, Australia. Further information on the nature of the operations and principal activities of the Group is provided in the Directors' Report. The Group's structure consists of a two operational entities and information on other related party relationships is provided in Note 19.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Preparation

The financial report is a general purpose financial report, which has been prepared in accordance with the requirements of the *Corporations Act 2001*, Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board. The financial report has also been prepared on a historical cost basis, except for derivative financial instruments and share based payments which have been measured at fair value.

The carrying values of recognised assets and liabilities that are designated as hedged items in fair value hedges that would otherwise be carried at amortised cost are adjusted to record changes in the fair values attributable to the risks that are being hedged in effective hedge relationships.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars (\$000) unless otherwise stated.

The consolidated financial statements provide comparative information in respect of the previous period where there is a retrospective application of an accounting policy, a retrospective restatement, or a reclassification of items in financial statements as presented in Note 2 (c).

The financial report has been prepared on the basis of accounting practices applicable to a going concern. This basis presumes that funds will be available to finance future operations and the realisation of assets and settlement of liabilities will occur in the ordinary course of business.

(b) Compliance with International Financial Reporting Standards (IFRS)

The financial report also complies with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

(c) Changes in accounting policy, accounting standards and interpretations

The accounting policies adopted in the preparation of the consolidated financial statements are consistent with those followed in the preparation of the Group's annual financial statements for the 53 weeks ended 3 July 2016, except as follows:

(i) New and amended standards and interpretations

The Group has adopted all the new and amended Australian Accounting Standards and AASB Interpretations that apply for the first time from 4 July 2016, as noted below:

(a) *AASB 2013-9 - Amendments to Australian Accounting Standards – Conceptual Framework, Materiality and Financial Instruments*

The Standard contains three main parts and makes amendments to a number of Standards and Interpretations.

Part A of AASB 2013-9 makes consequential amendments arising from the issuance of AASB CF 2013-1.

Part B makes amendments to particular Australian Accounting Standards to delete references to AASB 1031 and also makes minor editorial amendments to various other standards.

Part C makes amendments to a number of Australian Accounting Standards, including incorporating Chapter 6 Hedge Accounting into AASB 9 *Financial Instruments*.

The adoption of this amendment had no material impact on the financial position or performance of the Group.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

- (b) *AASB 2015-3 - Amendments to Australian Accounting Standards arising from the Withdrawal of AASB 1031 Materiality*. The Standard completes the AASB's project to remove Australian guidance on materiality from Australian Accounting Standards.

The adoption of this amendment had no material impact on the financial position or performance of the Group.

(ii) Changes in accounting policies

At the time of the business combination, the Group applied a common accounting policy for the determination of deferred taxes on indefinite life intangibles considering them to be non-depreciable and, accordingly, a related deferred tax liability was not recognised on the basis that the deferred tax could be calculated on the assumption of sale rather than use.

On identification of divergent practice, the IFRS interpretation Committee (IFRIC) clarified that indefinite life assets are subject to consumption by an entity, however the entity may not be able to reliably predict the time period over which the asset will be consumed. The IFRIC therefore concluded that the assumption of sale could not be presumed in calculating the deferred tax on indefinite life intangibles.

As a result of this clarification, the Group has amended its accounting policy to recognise a deferred tax liability on indefinite life intangibles acquired as part of a business combination. The change in accounting policy has been applied retrospectively and results in a restatement of the consolidated Statement of Financial Position. The impact on the financial statements of prior periods is noted below:

Impact on Consolidated Statement of Financial Position, increase / (decrease):

	As at 3 July 2016 \$'000	As at 29 June 2015 \$'000
Non-current assets		
Intangibles	12,395	12,395
Total assets	12,395	12,395
Non-current liabilities		
Deferred tax liabilities	12,395	12,395
Total liabilities	12,395	12,395
Net impact on equity	-	-

(iii) Accounting Standards and Interpretations issued but not yet effective

Certain new Accounting Standards and Interpretations have been published that are not mandatory for the 2 July 2017 reporting period. The Group has not early adopted any standard, interpretation or amendment that have been issued but not yet effective.

- (a) *AASB 9 - AASB 9* (December 2014) is a new standard which replaces *AASB 139* and includes a model for classification and measurement, a single, forward-looking 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. *AASB 9* is effective for annual periods beginning on or after 1 January 2018.

Hedge accounting

Amendments to *AASB 9* (December 2009 & 2010 editions and *AASB 2013-9*) issued in December 2013 included the new hedge accounting requirements, including changes to hedge effectiveness testing, treatment of hedging costs, risk components that can be hedged and disclosures.

The Group is currently continuing to assess the impact of the changes, however does not anticipate a material impact.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

- (b) *AASB 15 - AASB 15 Revenue from Contracts with Customers* replaces the existing revenue recognition standards, *AASB 118 Revenue* and related Interpretations (Interpretation 13 Customer Loyalty Programmes).

The core principle of AASB 15 is that an entity recognises revenue in accordance with the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

An entity recognises revenue in accordance with that core principle by applying the following steps:

- Step 1: Identify the contract(s) with a customer
- Step 2: Identify the performance obligations in the contract
- Step 3: Determine the transaction price
- Step 4: Allocate the transaction price to the performance obligations in the contract
- Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation.

The Group is currently in the process of determining the potential impact of adopting AASB 15 and management cannot at this stage reasonably estimate the impact in the period of initial application. Work to date has focused on identifying key areas of the business that may have potential risk of impact and may require a greater level of work effort to quantify the financial impact of AASB 15. This includes identifying changes to accounting policies, reporting requirements, business processes and associated internal controls with the objective of quantifying the expected first time adoption impacts as well as supporting ongoing compliance with the new accounting requirements. The Group will continue to assess the impact of the standard to establish the transition approach and ensure readiness for the implementation of the new standard in advance of its effective date.

- (c) *AASB 16 – Leases*

The key features of *AASB 16* are as follows:

Lessee accounting

- Lessees are required to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value.
- A lessee measures right-of-use assets similarly to other non-financial assets and lease liabilities similarly to other financial liabilities.
- Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments (including inflation-linked payments), and also includes payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease.
- *AASB 16* contains disclosure requirements for lessees.

AASB 16 supersedes:

- (a) *AASB 117 Leases*
- (b) Interpretation 4 Determining whether an Arrangement contains a Leases
- (c) *SIC – 15 Operating Leases – Incentives*
- (d) *SIC – 27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease*

The new standard will be effective for annual periods beginning on or after 1 January 2019. Early application is permitted, provided the new revenue standard, *AASB 15 Revenue from Contracts with Customers*, has been applied, or is applied at the same date as *AASB 16*.

The Group is currently continuing to assess the impact of the change in standard which it expects to be material. The new standard is expected to result in an increase in assets and liabilities, change in the timing in which lease expenses are recognised, a classification shift in earnings categories from operating expense to depreciation and interest expense, and an increase in gearing levels.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(d) Segment reporting

For management purposes, the Group is organised into business units based on its various store formats, however is aggregated as one reportable segment, being home furnishings.

Operating segments are identified on the basis of internal reports to Senior Management about components of the company that are regularly reviewed by the directors and senior management who have been identified as the chief operating decision makers, in order to allocate resources to the segment and to assess its performance and for which discrete financial information is available.

Information reported to the directors and senior management for the purposes of resource allocation and assessment of performance is specifically focused on core products and services offered in specific store formats, which when aggregated, forms one reportable operating segment.

The Group's store formats exhibit similar long-term financial performance and economic characteristics, which include:

- (a) The nature of the products and services - all store formats provide home furnishings to its customer base;
- (b) The nature of the production processes - all store formats utilise common design processes and source from the same or similar suppliers;
- (c) The type or class of customer for their products and services - all store formats possess an interchangeable customer base;
- (d) The methods used to distribute their products or provide their services - all store formats have product fulfilled from the same two DCs; and
- (e) No store format has different regulatory or consumer legislation requirements from another.

On this basis the Group deems there to be one operating segment.

Group financing (including finance costs and finance income) and income taxes are managed on a Group basis and are not allocated to store formats.

The company operated in one geographical segment for the 52 weeks ended 2 July 2017 being Australia and New Zealand.

(e) Current versus non-current classification

The Group presents assets and liabilities in the Statement of Financial Position based on current and non-current classification. An asset is current when it is:

- Expected to be realised or intended to be sold or consumed in the Group's normal operating cycle
- Held primarily for the purpose of trading;
- Expected to be realised within twelve months after the reporting period; or
- Cash or a cash equivalent unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

The Group classifies all other assets as non-current.

A liability is current when:

- It is expected to be settled in the Group's normal operating cycle;
- It is held primarily for the purpose of trading;
- It is due to be settled within twelve months after the reporting period ; or
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Group classifies all other liabilities as non-current.

Deferred tax assets and liabilities are classified as non-current assets and liabilities.

(f) Trade and other receivables

Other receivables and prepayments make up the majority of trade receivables. Trade and other receivables are initially recognised at fair value and subsequently measured at amortised cost less an allowance for any cancellable amounts.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(g) Basis of consolidation

The consolidated financial statements comprise the financial statements of the Group and its subsidiaries as at 2 July 2017. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if and only if the Group has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee)
- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect its returns

The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions have been eliminated in full. Unrealised losses are eliminated unless costs cannot be recovered.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group.

Investments in subsidiaries held by the Group are accounted for at cost in the separate financial statements of the parent entity.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method of accounting involves allocating the cost of the business combination to the fair value of the assets acquired and the liabilities and contingent liabilities assumed at the date of acquisition (see note (h) below).

(h) Goodwill

Goodwill on acquisition is initially measured at cost, being the excess of the consideration for the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances dictate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management
- is not larger than a segment based on the Group's primary reporting format determined in accordance with AASB 8 *Operating Segments*.

Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. When the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised.

When goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation.

Goodwill disposed of in this circumstance is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Impairment losses recognised for goodwill are not subsequently reversed.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(i) Income tax

Current tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities based on the current period's taxable income. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date.

Deferred income tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences except:

- when the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- when taxable temporary differences are associated with investments in subsidiaries, associates or interests in joint ventures, and the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax credits and unused tax losses can be utilised, except:

- when the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- when the deductible temporary difference associated with investments in subsidiaries, associates and interests in joint ventures, in which case deferred tax asset is only recognised to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax relating to items recognised outside profit or loss is recognised outside profit or loss. Deferred tax items are recognised in correlation to the underlying transaction either in OCI or directly in equity.

Deferred tax assets and deferred tax liabilities are offset only if a legally enforceable right exists to offset current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to the same taxable entity and the same taxation authority.

Tax consolidation legislation

Adairs Limited and its wholly-owned Australian controlled entities implemented the tax consolidation legislation as of 1 November 2010.

The head entity, Adairs Limited and the controlled entities in the tax consolidated group continue to account for their own current and deferred tax amounts. The Group has applied the Group allocation approach in determining the appropriate amount of current taxes and deferred taxes to allocate to members of the tax consolidated group.

In addition to its own current and deferred tax amounts, the legal entity also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from controlled entities in the tax consolidated group.

Assets or liabilities arising under tax funding agreements with the tax consolidated entities are recognised as amounts receivable from or payable to other entities in the Group.

Any difference between the amounts assumed and amounts receivable or payable under the tax funding agreement are recognised as a contribution to (or distribution from) wholly-owned tax consolidated entities.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(j) Other Taxes

Revenues, expenses and assets are recognised net of the amount of GST except:

- when the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item
- receivables and payables, which are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the Statement of Financial Position. Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

Cash flows are included in the Statement of Cash Flows on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority, are classified as operating cash flows.

(k) Foreign currencies

The Group's consolidated financial statements are presented in Australian dollars, which is also the parent company's functional currency. For each entity, the Group determines the functional currency and items included in the financial statements of each entity are measured using that functional currency. The Group uses the direct method of consolidation and on disposal of a foreign operation, the gain or loss that is reclassified to profit or loss reflects the amount that arises from using this method.

(i) Transactions and balances

Transactions in foreign currencies are initially recorded by the Group's entities at their respective functional currency spot rates at the date the transaction first qualifies for recognition.

Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date.

Differences arising on settlement or translation of monetary items are recognised in profit or loss.

(ii) Group companies

On consolidation, the assets and liabilities of foreign operations are translated into Australian dollars at the rate of exchange prevailing at the reporting date and their statements of profit or loss are translated at exchange rates prevailing at the dates of the transactions. The exchange differences arising on translation for consolidation are recognised in OCI. On disposal of a foreign operation, the component of OCI relating to that particular foreign operation is reclassified to profit or loss.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operation and translated at the spot rate of exchange at the reporting date.

(l) Leases

The determination of whether an arrangement is (or contains) a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are recognised as an expense in the profit and loss.

Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Operating lease payments are recognised as an expense in the profit and loss on a straight-line basis over the lease term.

Operating lease incentives are recognised as a liability when received and subsequently reduced by allocating lease payments between rental expense and reduction of the liability.

Lease incentives are capitalised when received and credited to revenue over the term of the store lease to which they relate.

Operating lease expenses are recognised on a straight-line basis over the lease term, which includes the impact of annual fixed rate percentage increases.

(m) Inventories

Inventories are valued at the lower of cost and net realisable value.

- Finished goods - purchase cost plus a proportion of the freight, handling and warehouse costs incurred to deliver the goods to the point of sale.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated direct costs necessary to make the sale.

At the 52 week period end of 2 July 2017, inventories held by the Group were finished goods.

(n) Cash dividend and non-cash distribution to equity holders of the parent

The Company recognises a liability to pay cash or make non-cash distributions to equity holders of the parent when the distribution is authorised and the distribution is no longer at the discretion of the Company. A corresponding amount is recognised directly in equity.

Non-cash distributions are measured at the fair value of the assets to be distributed with fair value re-measurement recognised directly in equity.

Upon distribution of non-cash assets, any difference between the carrying amount of the liability and the carrying amount of the assets distributed is recognised in the Statement of Profit or Loss.

(o) Property, plant and equipment

Plant and equipment is stated at historical cost less accumulated depreciation and any accumulated impairment losses. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

Class	Method	Period
• Computer Hardware	Straight Line	2 - 3 years
• Plant & other Equipment	Straight Line	5 years
• Leasehold Improvements	Straight Line	5 years
• Shop Fixtures & Fittings	Straight Line	Over initial lease term

The assets' residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each reporting date.

(i) Derecognition and disposal

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from its use or disposal.

Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the Statement of Profit or Loss in the year the asset is derecognised.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(p) Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses. Internally generated intangibles, excluding capitalised development costs, are not capitalised and the related expenditure is reflected in profit or loss in the period in which the expenditure is incurred.

The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the Statement of Profit or Loss as the expense category that is consistent with the function of the intangible assets.

Intangible assets with indefinite useful lives are not amortised, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the Statement of Profit or Loss when the asset is derecognised.

(i) Computer Software

The Group record direct costs associated with the development of computer software for external direct costs of materials and services consumed. Computer software has been determined to have a finite life, and is amortised on a straight line basis over its useful life.

(ii) Brand Names

Brand Names have been determined to have an indefinite life, are not amortised, are acquired and are subject to impairment testing annually or where an indicator of impairment exists. The indefinite-useful life reflects management's intention to continue to operate these brands to generate net cash inflows into the foreseeable future.

At each reporting date or where an indicator of impairment exists, the Group makes a formal estimate of the recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amounts.

Recoverable amount is the greater of fair value less costs of disposal and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs of disposal and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(q) Impairment

The Group assesses, at each reporting date, whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's (CGU's) fair value less costs of disposal and its value in use. Recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs of disposal, recent market transactions are taken into account. If no such transactions can be identified, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded companies or other available fair value indicators.

The Group bases its impairment calculation on detailed budgets and forecast calculations, which are prepared separately for each of the Group's CGUs to which the individual assets are allocated. These budgets and forecast calculations generally cover a period of five years. For longer periods, a long-term growth rate is calculated and applied to project future cash flows after the fifth year.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment losses of continuing operations, including impairment on inventories, are recognised in the Statement of Profit or Loss in expense categories consistent with the function of the impaired asset.

For assets excluding goodwill, an assessment is made at each reporting date to determine whether there is an indication that previously recognised impairment losses no longer exist or have decreased. If such indication exists, the Group estimates the asset's or CGU's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the Statement of Profit or Loss unless the asset is carried at a revalued amount, in which case, the reversal is treated as a revaluation increase.

Goodwill is tested for impairment annually at reporting date and when circumstances indicate that the carrying value may be impaired.

Impairment is determined for goodwill by assessing the recoverable amount of each CGU (or group of CGUs) to which the goodwill relates. When the recoverable amount of the CGU is less than its carrying amount, an impairment loss is recognised in the Statement of Profit or Loss. Impairment losses relating to goodwill cannot be reversed in future periods.

Intangible assets with indefinite useful lives are tested for impairment annually at the CGU level, as appropriate, and when circumstances indicate that the carrying value may be impaired.

(r) Borrowing costs

Borrowing costs are recognised as an expense when incurred. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

(s) Cash and cash equivalents

Cash and cash equivalents in the Statement of Financial Position comprise cash at bank and in hand and short-term deposits with an original maturity of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

For the purposes of the Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts. Bank overdrafts are included within interest-bearing loans and borrowings in current liabilities on the Statement of Financial Position.

(t) Employee benefits

(i) Wages, salaries and annual leave

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled within 12 months of the reporting date are recognised in respect of employees' services up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for non-accumulating sick leave are recognised when the leave is taken and are measured at the rates paid or payable.

(ii) Long service leave

The liability for long service leave is recognised and measured in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Consideration is given to expected future wage and salary levels, experience of employee departures, and periods of service. Expected future payments are discounted using market yields at the reporting date on high quality corporate bonds with terms to maturity and currencies that match, as closely as possible, the estimated future cash outflows.

(u) Interest bearing loans and borrowings

All loans and borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Fees paid on the establishment of loan facilities that are yield related are included as part of the carrying amount of the loans and borrowings.

Gains and losses are recognised in profit or loss when the liabilities are derecognised.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(v) Trade and other payables

Trade and other payables are carried at amortised cost and represent liabilities for goods and services provided to the Group prior to the end of the financial year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services. The amounts are unsecured and are usually paid within 30 days of recognition.

(w) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the Statement of Comprehensive Income net of any reimbursement.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the reporting date.

If the effect of the time value of money is material, provisions are discounted using a pre-tax rate that reflects the risks specific to the liability.

Where discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost.

(x) Revenue recognition

Revenue is recognised and measured at fair value of the consideration received or receivable to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Sale of goods

Revenue is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer and the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Linen Lover's membership fees are recognised upfront as a sale of goods when the membership is paid. Refer to 2(dd) (ii) for further discussion.

Interest income

Interest income is recognised as it accrues.

(y) Contributed equity

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction net of tax from the proceeds.

(z) Derivative financial instruments

The Group uses derivative financial instruments such as forward currency contracts to hedge its risks associated with foreign currency fluctuations. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured to fair value. Derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Any gain or losses arising from the changes in the fair value of derivatives, except for those that qualify as cash flow hedges, are taken directly to net profit or loss for the year. The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

For the purposes of hedge accounting, hedges are classified as:

- fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability;
- cash flow hedges when they hedge exposure to variability in cash flows that is attributable either to a particular risk associated with a recognised asset or liability or to a forecast transaction; or
- hedges of a net investment in a foreign operation.

A hedge of the foreign currency risk of a firm commitment is accounted for as a cash flow hedge.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

(i) Cash Flow Hedges

Cash flow hedges are hedges of the Group's exposure to variability in cash flows that is attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction and that could affect profit or loss. The effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while the ineffective portion is recognised in profit or loss.

Amounts taken to equity are transferred to the Statement of Profit or Loss when the hedged transaction affects profit or loss, such as when hedged income or expenses are recognised or when a forecast sale or purchase occurs. When the hedged item is the cost of a non-financial asset or liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability.

If the forecast transaction is no longer expected to occur, amounts previously recognised in equity are transferred to the Statement of Profit or Loss. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction occurs. If the related transaction is not expected to occur, the amount is taken to the Statement of Profit or Loss.

(aa) Investments and other financial assets

Financial assets in the scope of *AASB 139 Financial Instruments: Recognition and Measurement* are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets after initial recognition and, when allowed and appropriate, re-evaluates this designation at each reporting date.

All regular way purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets under contracts that require delivery of the assets within the period established generally by regulation or convention in the Group.

(i) Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in the category 'financial assets at fair value through profit or loss'. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term with the intention of making a profit. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on investments held for trading are recognised in profit or loss and the related other comprehensive income.

(ii) Loans and Receivables

Loans and receivables including loan notes and loans to key management personnel are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using effective interest method. Gains and losses are recognised in profit or loss when the loans and receivable are derecognised or impaired, as well as through the amortisation process.

(iii) Investments in subsidiaries

Investments in subsidiaries are carried at their cost of acquisition in the parent's financial statements.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(bb) Fair value measurement

The Group measures financial instruments such as derivatives at fair value at each reporting date. Fair value related disclosures for financial instruments and non-financial assets that are measured at fair value or where fair values are disclosed are summarised in the following notes:

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible by the Group.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 - Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement directly or indirectly observable
- Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

(cc) Share based payments

Employees (including Senior Executives) of the Group receive remuneration in the form of share-based payments, whereby employees render services as consideration for equity instruments (equity-settled transactions).

Equity-settled transactions

The cost of equity-settled transactions is determined by the fair value at the date when the grant is made using an appropriate valuation model, further details of which are given in Note 23.

That cost is recognised in employee benefits expense, together with a corresponding increase in equity (share based payment reserve), over the period in which the service and, where applicable, the performance conditions are fulfilled (the vesting period). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The expense or credit in the Statement of Profit or Loss for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

Service and non-market performance conditions are not taken into account when determining the grant date fair value of awards, but the likelihood of the conditions being met is assessed as part of the Group's best estimate of the number of equity instruments that will ultimately vest. Market performance conditions are reflected within the grant date fair value. Any other conditions attached to an award, but without an associated service requirement, are considered to be non-vesting conditions. Non-vesting conditions are reflected in the fair value of an award and lead to an immediate expensing of an award unless there are also service and/or performance conditions.

No expense is recognised for awards that do not ultimately vest because non-market performance and/or service conditions have not been met. Where awards include a market or non-vesting condition, the transactions are treated as vested irrespective of whether the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

When the terms of an equity-settled award are modified, the minimum expense recognised is the grant date fair value of the unmodified award, provided the original terms of the award are met. An additional expense, measured as at the date of modification, is recognised for any modification that increases the total fair value of the share-based payment transaction, or is otherwise beneficial to the employee. Where an award is cancelled by the Group or by the counterparty, any remaining element of the fair value of the award is expensed immediately through profit or loss.

(dd) Significant accounting judgments, estimates and assumptions

In applying the Group's accounting policies management continually evaluates judgments, estimates and assumptions based on experience and other factors, including expectations of future events that may have an impact on the Group. All judgments, estimates and assumptions made are believed to be reasonable based on the most current set of circumstances available to management. Actual results may differ from the judgments, estimates and assumptions. Significant judgments, estimates and assumptions made by management in the preparation of these financial statements:

(i) Significant accounting judgments

Recovery of deferred tax assets

Deferred tax assets are recognised for deductible temporary differences as management considers that it is probable that future taxable profits will be available to utilise those temporary differences.

Impairment of non-financial assets other than goodwill

The Group assesses impairment of all assets at each reporting date by evaluating conditions specific to the Group and to the particular assets that may lead to impairment. These include product, manufacturing and retail performance, technology and economic environments and future product expectations. If an impairment trigger exists the recoverable amount of the assets is determined. This involves value in use calculations, which incorporate a number of key estimates and assumptions.

(ii) Significant accounting estimates and assumptions

Impairment of goodwill and intangibles with indefinite useful lives

The Group determines whether goodwill and intangibles with indefinite useful lives are impaired at least on an annual basis. This requires an estimation of the recoverable amount of the cash-generating units to which the goodwill and intangibles with indefinite useful lives are allocated. The assumptions used in this estimation of recoverable amount and the carrying amount of goodwill and intangibles with indefinite useful lives are discussed in Note 9.

Share-based payments

Estimating fair value for share-based payment transactions requires determination of the most appropriate valuation model, which depends on the terms and conditions of the grant. This estimate also requires determination of the most appropriate inputs to the valuation model including the expected life of the share option or appreciation right, volatility and dividend yield and making assumptions about them. The assumptions and models used for estimating fair value for share-based payment transactions are disclosed in Note 23.

Long service leave provision

As discussed in Note 2(t), the liability for long service leave is recognised and measured at the present value of the estimated future cash flows to be made in respect of all employees at reporting date. In determining the present value of the liability, attrition rates and pay increases through promotion and inflation have been taken into account.

Make good provisions

Provision is made for the anticipated costs of future restoration of leased premises. The provision includes future cost estimates associated with dismantling and removal of shop fittings and cleaning. These future cost estimates are discounted to their present value. The calculation of this provision requires assumptions such as store closure dates and removal cost estimates.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Estimation of useful lives of assets

The estimation of the useful lives of assets has been based on historical experience as well as manufacturers' warranties (for plant and equipment) and lease terms (for shop fittings). In addition, the condition of the assets is assessed at least annually and considered against the remaining useful life. Adjustments to useful life are made when considered necessary. Depreciation charges are included in Note 8.

Loyalty program sales

Loyalty program sales are recognised in full at the point of sale as the fee is non-refundable and any customer benefits in the form of discounts and products benefits are accounted for at the time of sale. Additionally, specific loyalty marketing programs are variable in nature subject to general market and sales volume conditions at any given time.

Lay-by sales

A lay-by sale is a contract for the sale of merchandise conditional that the goods are not to pass to the purchaser until the full purchase price is paid. The purchase price of the merchandise is to be paid at some specified future date.

Due to restrictions in the previous ERP and POS systems implemented in prior periods, historically layby sales were treated as revenue at the point where the lay-by contract was signed by the customer and a deposit paid. An allowance for customer cancellations was applied to defer lay-by sales based on the expected pattern of customer cancellations.

The full implementation of a new ERP and POS in the current period provides more accurate data for the Group to better accurately account for its lay-by arrangements. In the current year, revenue is recognised when the goods are delivered to the customer on final instalment and payment is received in full, instead of providing for the expected pattern of customer cancellations. The impact of this change in accounting estimate has been a decrease in sales of goods by \$907,000 and a corresponding increase to other payables.

The impact of the change in estimates in future periods is not practicable to estimate.

Net realisable value of inventories

Inventories are valued at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business. Management has assessed the value of inventory that is likely to be sold below cost using past experience and judgement on the likely sell through rates of various items of inventory, and recorded a provision for this amount.

NOTE 3. REVENUES AND EXPENSES

	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
(a) Revenue from sale of goods		
<i>Sales revenue</i>		
Sale of goods	264,964	253,182
<i>Other income</i>		
Interest income	55	81
Net currency gains	125	-
Other	65	406
	245	487
(b) Depreciation and amortisation expenses included in the Statement of Profit or Loss		
Depreciation of property, plant and equipment	5,164	4,649
Amortisation of computer software	713	617
	5,877	5,266
(c) Finance costs		
Interest paid/payable and other finance costs	1,946	2,006
	1,946	2,006
(d) Salary and employee benefits expense		
Wages and salaries	57,409	54,623
Defined contribution superannuation expense	4,627	4,190
Share based payment expense	58	-
	62,094	58,813
(e) Other expenses		
Bank fees	2,069	1,608
Professional fees	1,451	811
Storage costs	929	533
Postage and stationary	4,163	3,610
Other	5,341	5,246
	13,953	11,808

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4. INCOME TAX

52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
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The major components of income tax expense are:

Statement of Profit or Loss

Current income tax

Current income tax charge	8,031	10,900
Adjustments in respect of current income tax of previous years*	(825)	23

Deferred income tax

Relating to origination and reversal of temporary differences	698	728
Income tax expense reported in the Statement of Profit or Loss	7,904	11,651

Statement of Other Comprehensive Income

Deferred income tax

Relating to origination and reversal of temporary differences	104	(531)
Income tax expense /(benefit) reported in the Statement of Other Comprehensive Income	104	(531)

A reconciliation of income tax expense and the product of accounting profit before income tax multiplied by the Group's applicable income tax rate is as follows:

Accounting profit before income tax	28,921	38,823
At the statutory income tax rate of 30% (2016: 30%)	8,676	11,647
Adjustments in respect of income tax of previous years*	(825)	23
Profit adjustment for tax purposes	-	(23)
Non-deductible expenses	30	4
Effect of foreign tax rates	(7)	-
Other	30	-
Income tax expense reported in the Statement of Profit or Loss	7,904	11,651

* During the 52 weeks ended 2 July 2017, the adjustment in respect of income tax of previous years was due to the utilisation of previously unrecognised tax losses. The availability of the losses was assessed in the current year.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4. INCOME TAX (continued)

	Statement of Financial Position		Statement of Profit or Loss and Other Comprehensive Income	
	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000 (Restated)*	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
Deferred income tax				
Deferred income tax relates to the following:				
<i>Deferred tax liabilities</i>				
Property, plant and equipment	(55)	(51)		
Brand names*	(12,395)	(12,395)		
Unrealised foreign exchange	(96)	-		
Other payables	(13)	(7)		
Total deferred tax liabilities	(12,559)	(12,453)		
<i>Deferred tax assets</i>				
Trade and other receivables	-	15		
Inventory	269	204		
Property, plant and equipment	71	113		
Provisions	3,364	2,902		
Financial instruments	201	305		
Transaction costs	2,124	3,186		
Total deferred tax assets	6,029	6,725		
Amounts (charged) or credited directly to profit and loss			(698)	(728)
Amounts (charged) or credited directly to other comprehensive income			(104)	531
Deferred tax expense			(802)	(197)

* Refer to Note 2(c)(ii) for the accounting policy change.

NOTE 5. CASH AND CASH EQUIVALENTS

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Cash at bank	14,209	14,580
Cash on hand	104	96
Total cash and cash equivalents	14,313	14,676
Reconciliation of the Statement of Cash Flows		
For the purposes of the Statement of Cash Flows, cash and cash equivalents comprise the following at period end:		
Cash at bank	14,209	14,580
Cash on hand	104	96
Total cash and cash equivalents	14,313	14,676

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 5. CASH AND CASH EQUIVALENTS (continued)

STATEMENT OF CASH FLOWS RECONCILIATION

	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
(a) Reconciliation of net profit after tax to net cash flows from operations		
Net profit/(loss) after tax	21,017	27,172
<i>Adjustments and non-cash items</i>		
Depreciation and amortisation expenses	5,877	5,266
Interest income not received in cash	-	(80)
Capitalised borrowing costs charged as finance expenses	199	-
Interest expense not paid in cash	-	32
Share based payments expense	58	-
<i>Changes in assets and liabilities</i>		
(Increase) / Decrease in trade and other receivables	2,111	(1,810)
(Increase) / Decrease in inventories	(6,720)	(3,028)
Increase / (Decrease) in payables	11,003	(8,247)
(Increase) / Decrease in deferred tax assets	802	728
Increase / (Decrease) in provisions	1,353	1,439
Increase / (Decrease) in current tax liabilities	(7,945)	2,264
Increase/(Decrease) in interest bearing liabilities	(111)	121
Cash flow from operations	27,644	23,857

NOTE 6. TRADE AND OTHER RECEIVABLES

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Prepaid expenses	3,320	3,748
Other receivables	697	1,529
Other current assets	471	761
Total current receivables	4,488	6,599
Current	4,488	6,599
Non-current	-	-
Total trade and other receivables	4,488	6,599

Trade debtors are non-interest bearing and no provision for impairment has been recorded as at 2 July 2017 (2016: nil).

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 7. INVENTORIES

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Finished goods at net realisable value	32,992	26,272
Total inventories at lower of cost and net realisable value	32,992	26,272

During the 52 weeks ended 2 July 2017, \$192,000 (2016: \$288,000 written back) was recognised as an expense for inventories carried at net realisable value. This is recognised in cost of sales.

NOTE 8. PROPERTY, PLANT AND EQUIPMENT

	Shop Fixtures & Fittings \$'000	Leasehold Improvements \$'000	Computer Hardware \$'000	Plant & Other Equipment \$'000	Total \$'000
Cost					
As at 28 June 2015	33,377	490	3,434	4,224	41,525
Additions	8,411	100	822	379	9,712
Disposals	-	-	-	-	-
As at 3 July 2016	41,788	590	4,256	4,603	51,237
Additions	8,071	8	782	514	9,375
Disposals	(2,496)	-	(1,686)	(427)	(4,609)
As at 2 July 2017	47,363	598	3,352	4,690	56,003
Depreciation and impairment					
As at 28 June 2015	24,160	458	2,842	3,121	30,581
Depreciation charge for the year	3,796	33	400	420	4,649
Disposals	-	-	-	-	-
As at 3 July 2016	27,956	491	3,242	3,541	35,230
Depreciation charge for the year	4,244	3	522	395	5,164
Disposals	(2,467)	-	(1,685)	(427)	(4,579)
As at 2 July 2017	29,733	494	2,079	3,509	35,815
Net book value					
As at 3 July 2016	13,832	99	1,014	1,062	16,007
As at 2 July 2017	17,630	104	1,273	1,181	20,188

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 9. INTANGIBLE ASSETS

	Computer Software	Brand Names with indefinite useful life	Goodwill	Total
	\$'000	\$'000	\$'000	\$'000
Cost or valuation				
As at 28 June 2015 (Restated)*	3,906	41,317	89,837	135,060
Additions	583	-	-	583
Disposals	-	-	-	-
As at 3 July 2016 (Restated)*	4,489	41,317	89,837	135,643
Additions	1,986	-	-	1,986
Disposals	(1,093)	-	-	(1,093)
As at 2 July 2017	5,382	41,317	89,837	136,536
Amortisation and impairment				
As at 28 June 2015	1,714	-	19,910	21,624
Amortisation	620	-	-	620
As at 3 July 2016	2,334	-	19,910	22,244
Amortisation	713	-	-	713
Disposals	(1,092)	-	-	(1,092)
As at 2 July 2017	1,955	-	19,910	21,865
Net book value				
As at 3 July 2016	2,155	41,317	69,927	113,399
As at 2 July 2017	3,427	41,317	69,927	114,671

* Refer to Note 2(c)(ii) for the accounting policy change.

Impairment testing of goodwill and intangibles with indefinite lives

Goodwill acquired through business combinations and brand names with indefinite lives have been allocated to the CGUs for impairment testing.

Carrying amount of goodwill and brands allocated to the CGUs:

	Adairs \$'000
Goodwill	57,532
Brand	41,317

Adairs CGU

The Group performed its annual impairment test as at 30 April 2017. The Group considers the relationship between its enterprise value and its carrying value, among other factors, when reviewing for indicators for impairment. The recoverable amount of the Adairs CGU has been determined based on the value in use calculation using cash flow projections from financial budgets approved by senior management covering a five year period. The post-tax discount rate applied to cash flow projections is 8.52% (2016: 8.77%) and cash flows beyond the five year period are extrapolated using a 3% growth (2016: 3%). As a result of the analysis, no impairment has been recognised for the period.

Key assumptions used in value in use calculations

The calculation of value in use for Adairs is most sensitive to the following assumptions:

- Gross margin
- Discount rate
- Growth rate

Gross margins - Gross margins are based on average values achieved in the past.

Discount rate - Discount rate calculation is based on the specific circumstances of the Group and is derived from its weighted average cost of capital (WACC). The WACC takes into account both debt and equity. The cost of equity is derived from the expected return of investment by the Group's investors. The cost of debt is based on the interest bearing borrowings the Group is obliged to service. CGU specific risk is incorporated by applying individual risk factors into the WACC.

Growth rate - Rates are based on management's best estimate of anticipated growth in the short to medium term.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 9. INTANGIBLE ASSETS (continued)

Sensitivity to changes in assumptions

There are no reasonable possible changes in key assumptions that could cause the carrying value of the CGUs to exceed its recoverable amount.

NOTE 10. TRADE AND OTHER PAYABLES

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Trade creditors	17,544	7,212
Accrued expenses	4,759	5,335
Other payables	4,090	2,844
Total current trade and other payables	26,393	15,391
Current	26,393	15,391
Non-current	-	-
Total trade and other payables	26,393	15,391

Terms and conditions of the above trade and other liabilities:

- Trade payables are non-interest bearing and are normally settled on 30 to 120 day terms.
- Other payables are non-interest bearing and do not have settlement terms.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11. INTEREST-BEARING LOANS AND BORROWINGS

	Interest rate	Maturity	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
	%			
<i>Current</i>				
Capitalised borrowing costs			(44)	(121)
Total current			(44)	(121)
<i>Non-current</i>				
Bank Loan - Facility A	BBSW + 1.85	8 July 2019	42,000	42,000
Capitalised borrowing costs			(45)	(79)
Total non-current			41,955	41,921
Current			(44)	(121)
Non-current			41,955	41,921
Total interest-bearing loans and borrowings			41,911	41,800

(a) Financing facilities available

At reporting date, the following non-shareholder financing facilities had been negotiated with the bank and were available:

Facilities available at the reporting date:	50,000	50,000
Facilities used at the reporting date:	(42,000)	(42,000)
Facilities unused at the reporting date:	8,000	8,000

NOTE 12. PROVISIONS

(a) Lease provisions

	Lease incentives \$'000	Straight-line lease \$'000	Make good \$'000	Total \$'000
As at 3 July 2016	1,326	2,272	717	4,315
Arising during the year	978	940	55	1,973
Utilised	(529)	(432)	-	(961)
Unwinding of discount rate and changes in the discount rate	-	-	23	23
As at 2 July 2017	1,775	2,780	795	5,350
Current	482	421	6	909
Non-current	1,293	2,359	789	4,441
Total lease provisions	1,775	2,780	795	5,350

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 12. PROVISIONS (continued)

(b) Employee entitlements

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
<i>Current</i>		
Annual Leave	2,516	2,267
Long service leave	741	925
Total current	3,257	3,192
<i>Non-current</i>		
Long service leave	1,378	1,125
Total non-current	1,378	1,125
Total employee entitlements	4,635	4,317
Total current	4,167	3,496
Total non-current	5,818	5,136
Total provisions	9,985	8,632

Nature and timing of provisions

Refer to note 2(t) and 2(dd) for the relevant accounting policy and a discussion of significant estimations and assumptions applied in the measurement of these provisions.

NOTE 13. ISSUED CAPITAL AND RESERVES

(a) Authorised Shares

	As at 2 July 2017 Thousands	As at 3 July 2016 Thousands
Ordinary Shares	165,875	165,875

Ordinary shares are fully-paid and have no par value. They carry one vote per share and the right to dividends. They bear no special terms or conditions affecting income or capital entitlements of the shareholders and are classified as equity.

(b) Share-based payment reserve

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Balance at the beginning of the period	-	-
Share based payment expense	58	-
Balance at the end of the period	58	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 13. ISSUED CAPITAL AND RESERVES (continued)

(c) Foreign currency translation reserve

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Balance at the beginning of the period	-	-
Foreign currency movement	(7)	-
Balance at the end of the period	(7)	-

(d) Cash flow hedge reserve

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Balance at the beginning of the period	(713)	(1,240)
Cash flow hedge movement	242	527
Balance at the end of the period	(471)	(713)

(e) Retained earnings

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Balance at the beginning of the period	27,954	9,076
Net profit for the period	21,017	27,172
Dividends declared	(16,588)	(8,294)
Balance at the end of the period	32,383	27,954

NOTE 14. COMMITMENTS AND CONTINGENCIES

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
<i>Operating lease commitments – Group as a lessee</i>		
Non-cancellable operating lease commitments		
- not later than one year	28,644	24,324
- later than one year and not later than five years	70,909	62,084
- later than five years	6,649	5,181
	106,202	91,589

The Group has entered into operating leases for the rental of shop and office premises and distribution centres. These leases have an average life of between 3 and 7 years with renewal options included in the contracts. There are no restrictions placed upon the lessee by entering lease agreements.

During the 52 weeks ended 2 July 2017, the minimum lease expense incurred was \$30,723,000 (2016: \$26,260,000).

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 15. DERIVATIVE FINANCIAL INSTRUMENTS

	53 weeks ending 3 July 2016 \$'000	53 weeks ending 3 July 2016 \$'000
<i>Current liabilities</i>		
Forward currency contracts - cash flow hedges	657	1,015
	657	1,015
<i>Non-current liabilities</i>		
Forward currency contracts - cash flow hedges	15	3
	15	3

Forward currency contracts - cash flow hedges

The Group buys inventories that are purchased in US Dollars (USD). In order to protect against exchange rate movements and to manage the inventory purchases process, the Group has entered into forward exchange contracts to purchase USD. These contracts are hedging highly probable forecasted inventory purchases and they are timed to mature when payments are scheduled to be made. These derivatives have met the requirements to qualify for hedge accounting with movements recorded in other comprehensive income accordingly.

The cash flows are expected to occur between 0 to 13 months from 2 July 2017 (2016: 0 to 13 months).

NOTE 16. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise receivables, payables, bank loans and overdrafts, cash and short-term deposits and derivatives.

Risk exposures and responses

The Group manages its exposure to key financial risks, including interest rate and currency risk in accordance with the Group's financial risk management policy. The objective of the policy is to support the delivery of the Group's financial targets while protecting future financial security.

With respect to credit risk, the overwhelming majority of the Group's sales are on cash or cash equivalent terms with settlement within 24 hours. As such, the Group's exposure to credit risk is minimal. The Group trades only with recognised, creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant.

The Group enters into derivative transactions, principally forward currency contracts. The purpose is to manage the currency risks arising from the Group's operations. The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk and liquidity risk.

i) Interest rate risk

The Group's exposure to market interest rates relates primarily to the Group's long-term unhedged debt obligations.

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
<i>Financial instruments</i>		
Cash and cash equivalents	14,313	14,676
Bank loans	(41,911)	(41,800)
Net exposure	(27,598)	(27,124)

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 16. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

The following sensitivity analysis is based on the interest rate risk exposures in existence at the reporting date:

As at 2 July 2017, if interest rates had moved, as illustrated in the table below, with all other variables held constant, profit after tax would have been affected as follows due to the higher/lower interest rate costs from variable debt and cash balances:

Judgments of reasonably possible movements:

	52 weeks ending 2 July 2017 \$'000	52 weeks ending 3 July 2016 \$'000
	<u>Profit after tax higher / (lower)</u>	
+1% (100 basis points)	(193)	(190)
-0.5% (50 basis points)	97	95

Significant assumptions used in the interest rate sensitivity analysis include:

- Reasonably possible movements in interest rates were determined based on the Group's current credit rating, relationships with finance institutions, the level of debt that is expected to be renewed as well as a review of the last two years' historical movements and economic forecaster's expectations.
- The net exposure at reporting date is representative of what the Group was and is expecting to be exposed to in the next twelve months from the reporting date.

(ii) Foreign currency risk

As a result of large purchases of inventory denominated in USD, the Group's Statement of Financial Position can be affected significantly by movements in the USD/AUD exchange rates. The Group attempts to mitigate this risk by entering into forward foreign exchange contracts, as detailed below.

At reporting date, the Group had the following exposure to USD foreign currency that is not covered by a designated cash flow hedge.

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
<i>Financial liabilities</i>		
Payables	7,491	2,650

The following sensitivity is based on the foreign currency risk exposures in existence at the reporting date:

As at 2 July 2017, had the AUD moved, as illustrated in the table below, with all other variables held constant, profit after tax would have been affected as follows:

Judgments of reasonably possible movements:

	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
	<u>Profit after tax higher / (lower)</u>	
AUD to USD +15%	684	242
AUD to USD -15%	(925)	(327)

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 16. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

Significant assumptions used in the foreign currency exposure sensitivity analysis include:

- Reasonably possible movements in foreign exchange rates were determined based on a review of the last two years' historical movements and economic forecaster's expectations.
- The net exposure at balance date is representative of what the Group was and is expecting to be exposed to in the next twelve months from reporting date.
- The sensitivity does not include financial instruments that are non-monetary items as these are not considered to give rise to currency risk.

(iii) Liquidity risk

Liquidity risk arises from the financial liabilities of the Group and the Group's subsequent ability to meet their obligations to repay their financial liabilities as and when they fall due.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank overdrafts, bank loans, preference shares and committed available credit lines.

A. Non-derivative financial assets and liabilities

The following liquidity risk disclosures reflect all contractually fixed pay-offs, repayments and interest resulting from recognised financial liabilities as of 2 July 2017. For the other obligations the respective undiscounted cash flows for the respective upcoming fiscal years are presented. The timing of cash flows for assets/liabilities is based on the contractual terms of the underlying contract.

	< 6 months \$'000	6 - 12 months \$'000	1 - 5 years \$'000	> 5 years \$'000	Total \$'000
As at 2 July 2017					
<i>Liquid financial assets</i>					
Cash and cash equivalents	14,313	-	-	-	14,313
Trade and other receivables	4,488	-	-	-	4,488
<i>Financial Liabilities</i>					
Trade and other payables	(26,393)	-	-	-	(26,393)
Interest bearing loans and borrowings	-	-	(42,000)	-	(42,000)
Net outflow	(7,592)	-	(42,000)	-	(49,592)

	< 6 months \$'000	6 - 12 months \$'000	1 - 5 years \$'000	> 5 years \$'000	Total \$'000
As at 3 July 2016					
<i>Liquid financial assets</i>					
Cash and cash equivalents	14,676	-	-	-	14,676
Trade and other receivables	6,599	-	-	-	6,599
<i>Financial Liabilities</i>					
Trade and other payables	(15,391)	-	-	-	(15,391)
Interest bearing loans and borrowings	-	-	(42,000)	-	(42,000)
Net inflow / (outflow)	5,884	-	(42,000)	-	(36,116)

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 16. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

B. Derivative financial liabilities

Due to the unique characteristics and risks inherent to derivative instruments the Group separately monitors the liquidity risk arising from transacting in derivative instruments.

The table below details the liquidity risk arising from the derivative liabilities held by the Group at the reporting date:

	< 6 months \$'000	6 - 12 months \$'000	1 - 5 years \$'000	> 5 years \$'000	Total \$'000
As at 2 July 2017					
Derivatives - forward currency contracts	(447)	(210)	(15)	-	(672)
Net outflow	(447)	(210)	(15)	-	(672)

	< 6 months \$'000	6 - 12 months \$'000	1 - 5 years \$'000	> 5 years \$'000	Total \$'000
As at 3 July 2016					
Derivatives - Forward currency contracts	(623)	(392)	(3)	-	(1,018)
Net outflow	(623)	(392)	(3)	-	(1,018)

(iv) Fair value

The Group uses various methods in estimating the fair value of a financial instrument. The methods comprise:

- Level 1 Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 Valuation techniques for which the lowest level input that is significant to the fair value measurement directly or indirectly observable
- Level 3 Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

Quoted market price represents the fair value determined based on quoted prices on active markets as at the reporting date without any deduction for transaction costs. The fair value of the listed equity investments are based on quoted market prices.

For financial instruments not quoted in active markets, the Group uses valuation techniques such as present value techniques, comparison to similar instruments for which market observable prices exist and other relevant models used by market participants. These valuation techniques use both observable and unobservable market inputs.

Financial instruments that use valuation techniques with only observable market inputs or unobservable inputs that are not significant to the overall valuation include interest rate swaps, forward commodity contracts and foreign exchange contracts not traded on a recognised exchange.

	As at 2 July 2017		As at 3 July 2016	
	Valuation Level 2 \$'000	Total \$'000	Valuation Level 2 \$'000	Total \$'000
<i>Financial liabilities</i>				
Forward exchange contracts	(672)	(672)	(1,018)	(1,018)
	(672)	(672)	(1,018)	(1,018)

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 16. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

Set out below is a comparison, by class, of the carrying amounts and fair value of the Group's financial instruments, other than those with carrying amounts that are reasonable approximations of fair values:

	As at 2 July 2017		As at 3 July 2016	
	Carrying Amount \$'000	Fair Value \$'000	Carrying Amount \$'000	Fair Value \$'000
<i>Financial liabilities</i>				
Forward exchange contracts	(672)	(672)	(1,018)	(1,018)
Interest bearing liabilities	(42,000)	(42,000)	(42,000)	(44,204)
	(42,672)	(42,672)	(43,018)	(45,222)

NOTE 17. CAPITAL MANAGEMENT

For the purpose of the Group's capital management, capital includes issued capital and all other equity reserves attributable to the equity holders of the parent. The primary objective of the Group's capital management is to maximise the shareholder value.

The Group manages its capital structure and makes adjustments in light of changes in economic conditions and the requirements of the financial covenants. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. The Group monitors capital using a gearing ratio, which is net debt divided by the sum of total capital and net debt. The Group's policy is to keep the gearing ratio between 20% and 50%. The Group includes within net debt, interest-bearing loans and borrowings, trade and other payables, less cash and short-term deposits, excluding discontinued operations.

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Interest-bearing loans and borrowings other than convertible preference shares	41,911	41,800
Trade and other payables	26,393	15,391
Less: cash and short-term deposits	(14,313)	(14,676)
Net debt	53,991	42,515
Equity	100,312	95,590
Capital and net debt	154,303	138,105
Gearing ratio	35%	31%

In order to achieve this overall objective, the Group's capital management, amongst other things, aims to ensure that it meets financial covenants attached to the interest-bearing loans and borrowings that define capital structure requirements. Breaches in meeting the financial covenants would permit the bank to immediately call loans and borrowings. There have been no breaches of the financial covenants of any interest-bearing loans and borrowings in the current period.

No changes were made in the objectives, policies or processes for managing capital during the 52 weeks ended 2 July 2017 and 53 weeks ended 3 July 2016.

NOTE 18. INFORMATION RELATING TO ADAIRS LIMITED ('the parent entity')

	As at 2 July 2017 \$'000	As at 3 July 2016 \$'000
Current assets	290	222
Total assets	88,847	85,368
Current liabilities	(129)	(205)
Total liabilities	(688)	(736)
Net assets	88,159	84,632
Issued capital	68,349	68,350
Retained earnings	19,752	16,282
Share-based payment reserve	58	-
Net Equity	88,159	84,632
Loss of the parent entity	(57)	(719)
Total comprehensive loss of the parent entity	(57)	(719)

NOTE 19. RELATED PARTY DISCLOSURES
Terms and conditions of transactions with related parties other than KMP

The purchases from related parties are made on terms equivalent to those that prevail in arm's length transactions. There are no outstanding balances as at the 52 weeks ended 2 July 2017. There have been no guarantees provided or received for any related party receivables or payables.

Compensation of key management personnel of the Group:

	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
Short term employee benefit	1,670	2,245
Post employment benefits	106	103
Termination benefits	388	-
Share based payments	32	-
Total compensation	2,196	2,348

The amounts disclosed in the table are the amounts recognised as an expense during the reporting period related to key management personnel.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 20. EARNINGS PER SHARE

Basic earnings per share (EPS) amounts are calculated by dividing the profit for the year attributable to ordinary equity holders of the Parent by the weighted average number of ordinary shares outstanding during the year.

The following reflects the income and share data used in the basic and diluted EPS computations:

	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
Profit for the year attributable to ordinary equity holders of the Parent	21,017	27,172
Profit attributable to ordinary equity holders of the Parent for basic earnings	21,017	27,172
Interest on convertible preference shares	-	-
Profit attributable to ordinary equity holders of the Parent adjusted for the effect of dilution	21,017	27,172
	As at 2 July 2017 '000	As at 3 July 2016 '000
Weighted average number of ordinary shares for basic EPS	165,875	165,875
Share options	-	-
Weighted average number of ordinary shares for the effect of dilution	165,875	165,875

There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of authorisation of these financial statements.

NOTE 21. INFORMATION RELATING TO SUBSIDIARIES

The consolidated financial statements of the Group include:

Name of Entity	Country of incorporation	Equity Holding	
		2017 %	2016 %
Home & Décor Pty Limited	Australia	100	100
Adairs Holdings Australia Pty Limited	Australia	100	100
Adairs Retail Group Pty Limited	Australia	100	100
Wilder Days Pty Limited	Australia	100	100
Adairs New Zealand Limited	New Zealand	100	100

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22. DIVIDEND

	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
Cash dividends on ordinary shares declared and paid:		
Interim dividend for 2017: 3.5 cents per share (2016: 5 cents)	5,806	8,294
Proposed dividends on ordinary shares:		
Final cash dividend for 2017: 4.5 cents per share (2016: 6.5 cents)	7,464	10,782

Proposed dividends on ordinary shares are subject to approval at the annual general meeting and are not recognised as a liability as at 2 July.

Franking credit balance

The amount of franking credits available for the subsequent financial year are:

	52 weeks ending 2 July 2017 \$'000
Franking account balance as at the end of the period at 30%	13,220
Franking credits that will arise from the payment of income tax payable as at the end of the period	915
Franking debits that will arise from the payment of dividends as at the end of the period	(3,199)
Franking credits that will arise from the receipt of dividends recognised as receivables at the reporting date	-
	10,936

NOTE 23. SHARE-BASED PAYMENTS

In November 2016, 1,860,000 share options were granted to Senior Executives under the Equity Incentive Plan (EIP). The exercise price of the options of \$2.00 was above the market price of the shares on the date of grant. The options vest if the Service and Performance conditions are met. The Service condition requires the participants to be employed on a full time basis by the Company from Grant Date to 30 June 2020. There are two separate Performance conditions, an EPS Performance condition and a Sales Performance condition. If these conditions are not met, the options will lapse immediately. The fair value at grant date is estimated using the Black Scholes Option Pricing Model (BSM), taking into account the terms and conditions upon which the options were granted. The contractual life of each option granted is eight years. There is no cash settlement of the options. The fair value of options granted during the 52 weeks ended 2 July 2017 was estimated on the grant date using the following assumptions:

Dividend yield (%)	4.75%
Expected volatility (%)	32.50%
Risk-free interest rate (%)	2.11%
Expected life of share options (years)	5.80
Exercise share price (\$)	2.00

The fair value of the options on date of grant was \$0.27 per option.

For the 52 weeks ended 2 July 2017, the Group has recognised share-based payment expense of \$58,000 in the Statement of Profit or Loss (2016: nil).

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 24. EVENTS AFTER THE BALANCE SHEET DATE

On 28 August 2017, the directors of Adairs Limited declared a final dividend on ordinary shares in respect of the 2017 financial year. The total amount of the dividend is \$7.46m which represents a fully franked dividend of 4.5 cents per share. The dividend has not been provided for in the 2 July 2017 financial statements.

Other than the above matter, no matters or circumstances have arisen since reporting date which significantly affected or may significantly affect the operations of the company, the results of those operations, or the state of affairs of the Company.

NOTE 25. AUDITORS' REMUNERATION

The auditor of Adairs Limited is Ernst & Young Australia.

	52 weeks ending 2 July 2017 \$'000	53 weeks ending 3 July 2016 \$'000
<i>Amounts received or due and receivable by Ernst & Young Australia for:</i>		
• An audit or review of the financial report of the Company and any other entity in the consolidated group - continuing operations	224	220
• Other services in relation to the Company and any other entity in the consolidated group:		
- Tax compliance	43	17
- Other assurance	12	63
- Other tax	12	29
	291	329