

ANNUAL REPORT

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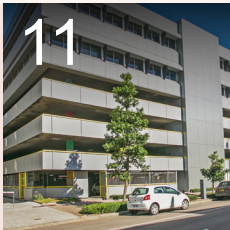
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Review of Operations:

Automotive Leather

Building Materials

Property and Investments



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ABOUT SCHAFFER CORPORATION

A DIVERSIFIED AUSTRALIAN INDUSTRIAL COMPANY

Schaffer Corporation Limited (SFC) is a diversified industrial company with core operating divisions in Automotive Leather, Building Materials, Property and Investment. Originally incorporated in 1955, the company was first listed on the Australian Securities Exchange (ASX) in 1963 and currently employs over 1,200 employees in three countries.

The Automotive Leather division is a world-class, globally competitive automotive leather producer, supplying quality interior leather products to such household names as Land Rover, Audi, Mercedes, Nissan, Toyota and Ford. The division operates leather processing and finishing operations in Slovakia and Australia. Component cutting plants are located in Slovakia and China. Exports account for virtually all sales.

The Building Materials division currently comprises the 100% owned subsidiary, Delta Corporation, which manufactures a range of pre-cast and pre-stressed concrete floor, beam and wall products, together with custom made precast panel and beam products, including TeeRoff beams, for major infrastructure, building and resource projects in Australia.

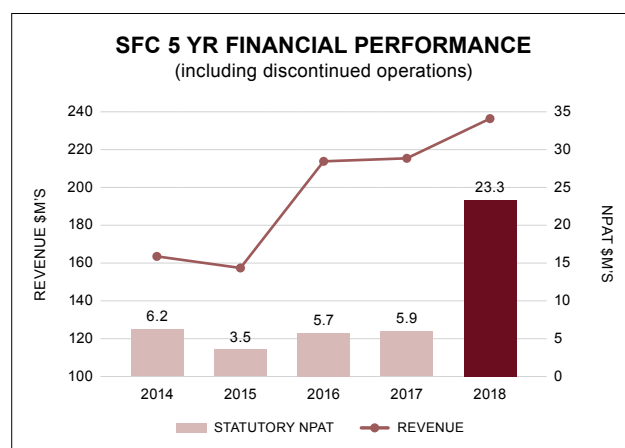
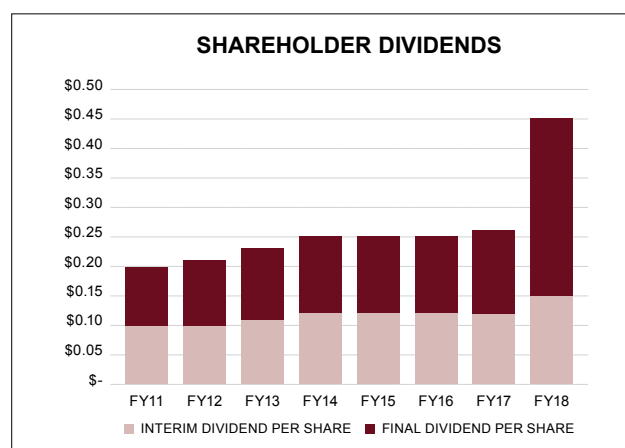
The Group currently has various property and equity investments interests both directly through Schaffer Corporation and via a subsidiary investment company, Gosh Capital. The objective of the land investments in Gosh Capital is to maximise the land asset on which the Gosh Leather business previously operated in North Coogee, Western Australia.

Group property interests also include property held for future development in the Western Australian suburb of Jandakot, and a bulky goods property at Rockingham, Western Australia. The Group also has various syndicated interests in commercial and retail properties across Australia.

Schaffer Corporation's key internal performance measure is Return on Average Capital Employed (ROACE*), which reflects the earnings achieved in relation to the debt and equity capital invested in its businesses. The Company applies the ROACE measure in pursuing its long-term growth strategy to organically develop its core businesses and to acquire businesses, properties or make other investments.

*Please refer to page 5 for definitions and reconciliations for non-IFRS measures

The company has a proud history of paying a dividend in every one of the 55 years since it was originally listed as Calsil Ltd in 1963. For the past 18 years, the company has paid approximately \$128 million in fully-franked dividends to shareholders.



Board of directors



JOHN SCHAFFER AM

ANTON MAYER

DANIELLE BLAIN AM

DAVID SCHWARTZ

MICHAEL PERROTT AM



MANAGING DIRECTOR'S REPORT

EXECUTIVE MANAGEMENT TEAM



John Schaffer AM

BCom(Hons), FCPA
Age 68

Mr Schaffer joined the Group in 1972 and has held the positions of Managing Director since 1987 and Chairman since 1988.



Anton Mayer

Age 76

Mr Mayer joined the Group in 1998. In 2001, Mr Mayer joined the Board of Schaffer Corporation Limited and he is currently Executive Chairman of Howe Automotive Limited.



Dan Birks

BAgrSc, MBA
Age 52

Mr Birks joined the Group in 2000 and was promoted to General Manager of Howe Automotive Ltd in 2016.



Ralph Leib

BComm, BAcc
Age 47

Mr Leib joined the Group in 2016 and was promoted to Chief Financial Officer in July 2017.



Matt Perrella

NPCAA
Age 69

Mr Perrella joined the Group in 1980. From 1989 until 2009, Mr Perrella was General Manager of Delta Corporation Limited. He is currently Executive Director of Delta Corporation.



Jason Walsh

B Bus, MBA
Age 48

Mr Walsh joined the Group in 1999 and was promoted to the position of General Manager of Delta Corporation Limited in 2009.



Jason Cantwell

BBus(Acc), CPA, MBA,
GIA(Cert)
Age 46

Mr Cantwell joined the Group in 2011 as Group Financial Controller and Company Secretary.

| Key Financial Indicators | 18 | 17 | 16 | 15 | 14 | 13 |
|---|--------|--------|--------|--------|--------|--------|
| Revenue - incl. discontinued operations (\$ millions) | 235.7 | 215.0 | 213.6 | 157.3 | 163.6 | 138.4 |
| Net Profit after tax* (\$ millions) | 23.3 | 5.9 | 5.7 | 3.5 | 6.2 | 7.6 |
| Earnings per Share (\$) | \$1.67 | \$0.42 | \$0.41 | \$0.25 | \$0.44 | \$0.54 |
| Return on Average Capital Employed (ROACE*) | 38% | 12% | 10% | 7% | 16% | 14% |
| Ordinary Dividend per Share | \$0.45 | \$0.26 | \$0.25 | \$0.25 | \$0.25 | \$0.23 |

MAINTAINING FOCUS

Schaffer Corporation's primary focus is on creating long-term shareholder value.

Financial Performance

For the 2018 financial year, Schaffer Corporation achieved net profit after tax (NPAT*) of \$23.3 million (2017: \$5.9 million). The current year result included a non-recurring \$4.4 million in NPAT from the sale of the Building Products businesses and a \$3.2 million non-cash after-tax impairment of the Delta precast business assets.

Underlying Profit* increased to \$22.5 million (2017: \$8.2 million).

Automotive Leather

Automotive Leather's NPAT* increased to \$23.7 million with revenue growing 19% to \$203.4 million.

The growth in the number of programs and volumes for Automotive leather over the past two years created the opportunity to establish additional leather finishing and cutting facilities in Slovakia. The new Slovakian facilities and programs have now been operating at "steady state" for over a year, and the additional once-off costs associated with establishing the new operations in Slovakia have now been eliminated from our operating costs. The result is that cost efficiencies from economies-of-scale are enhancing the profitability of our Automotive Leather division. Additionally, new processes and technology are being implemented to create further cost savings as well as improved service and responsiveness to customers.

During the second half of the financial year, CNC (Computer Numerical Controlled) cutting machines have been included in production alongside current leather cutting methods. This technology is realising cost saving benefits and further roll-out is being evaluated.

Favourable movements in foreign exchange rates significantly impacted Automotive Leather's result for the year. The segment's results are in Australian Dollars but approximately 80% of its revenues are denominated in Euro.

During the year, the average Australian Dollar versus Euro depreciated by 6%. This had a significant positive impact on Australian Dollar denominated revenue and margins.

Additionally, approximately 60% of segment costs are priced in US Dollars. Those input costs include semi-finished hides and chemicals. Automotive Leather converts Euro to US Dollars to pay for these purchases. During the year, the average Euro versus the US Dollar rate appreciated by 9%. This resulted in significantly less Euro being required to make those purchases.

Automotive Leather's profit performance for the first half of FY19 is expected to be similar to the prior corresponding period. This expectation is subject to stable exchange rates.

Building Materials

Delta Corporation produces precast and prestressed concrete products. The Western Australian market remains depressed in terms of work volumes. As a result, margin pressures from increased competition between suppliers continues to impact profitability of Delta. As previously reported, the Directors decided to impair the carrying value of Delta's assets at the half-year. The \$3.2 million after-tax impairment is a non-cash item and was recorded at 31 December 2017.

While Delta's revenue increased in 2018 with the inclusion of a large civil infrastructure project, that same project experienced increased complexity, project administration and compliance requirements, and challenging production schedules. As a result, Delta's production costs increased, and profits declined compared to prior year.

Delta's order bank is currently satisfactory, and a positive trend is that it includes a larger number of jobs than it did at the same time last year. SFC expects that Building Materials performance will improve in the first half of FY19 compared to the loss position in the prior corresponding period.

During the year, the Building Products business unit was

*Please refer to page 5 for definitions and reconciliations for non-IFRS measures

sold in two transactions. The unit supplied paving and walling products to the residential and commercial building sectors.

On 15 August 2017, the limestone quarry tenements and production assets were sold.

On 22 November 2017, we sold the UrbanStone paving, masonry and natural stone manufacturing and distribution business. Schaffer Corporation retained the land and buildings of the UrbanStone factory at Jandakot, Western Australia and leased those premises for a 10-year initial term at over \$0.6 million a year.

The businesses were sold for higher than book value. This contributed \$4.4 million after tax to the annual result. The sales enable more management focus on Automotive Leather, Delta and the growing portfolio of property assets and investments.

Property

The Group's property portfolio, including SFC's share of Gosh Capital, has an estimated current market value of \$111.6 million (2017: \$90.5 million).

Most of the increase in value relates to a recent valuation of the property at Jandakot, Western Australia following the gazettal of a local Scheme Amendment that increases the scope and area of light industrial and commercial uses on 38.8 hectares of the land. We advise that subsequently the local Council approved a Local Development Plan which added an additional native vegetation buffer on one boundary, restricting development on 5.5 hectares. The recent valuation including the impact of the 'buffer' put the property at \$37.2 million (previously \$19.1 million) on an "as is" basis.

Schaffer Corporation carries property assets in its accounts at their depreciated book values, except units in property unit trusts, which are at fair value. The market values are supported by ongoing, recent independent accredited valuations. The difference between book and market values represents \$73.8 million before tax (\$51.7 million after tax) of unrealised property value.

SFC Investments

SFC Investments includes Schaffer Corporation's interests in syndicated property investments, group-owned property for development and/or leasing activities, and equity investments.

The division contributed NPAT of \$1.1 million for the year (2017: \$0.7 million).

Schaffer Corporation retained the Jandakot land and building assets occupied by the UrbanStone manufacturing business and leased that site (Lot 701 Jandakot Road) to the purchaser of the UrbanStone business.

We expect profit of the division to modestly increase in the first half of FY19 compared to prior corresponding period, with a full six months' contribution from the lease of Lot 701 Jandakot Road.

Gosh Investments

Schaffer Corporation owns 83% of Gosh Capital. It has interests in direct-owned property, including the land at North Coogee which was operated by the Group's former Gosh Leather business. Gosh Capital continues to reinvest profits in a range of investments including syndicated property trusts and equities.

At 30 June 2018, the market value of its asset portfolio was \$32.4 million (\$26.4 million net of debt).

In the 2018 financial year, the division contributed NPAT of

\$0.4 million (2017: \$0.4 million).

Similar profit is forecast for the first half of FY19 compared to prior corresponding period.

Group Cash Flow and Net Debt

Proceeds from the sale of the Building Products division in the first-half of the financial year and strong cash generation from operations over the year saw Group net debt decrease by \$42.5 million to just \$1.3 million. The Group's low gearing provides capacity to fund future growth opportunities. Those opportunities include the development of Group properties at Jandakot and North Coogee in Western Australia, and other investments.

The Group net debt position as at 30 June 2018 is set out in more detail below:

| All amounts in \$m | Automotive Leather | Building Materials and Corporate | Syndicate Investment Properties | Gosh Capital | Total 30 June 2018 |
|--------------------------|--------------------|----------------------------------|---------------------------------|--------------|--------------------|
| Type of Debt | | | | | |
| Bank debt – recourse | - | - | 2.3 | - | 2.3 |
| Bank debt – non-recourse | - | - | 16.8 | 6.1 | 22.9 |
| Equipment finance | 8.1 | - | - | - | 8.1 |
| | 8.1 | - | 19.1 | 6.1 | 33.3 |
| Maturity Profile | | | | | |
| FY19 | 2.3 | - | - | - | 2.3 |
| FY20 | 2.4 | - | 8.1 | 6.1 | 16.6 |
| FY21 | 2.2 | - | 11.0 | - | 13.2 |
| FY22 and beyond | 1.2 | - | - | - | 1.2 |
| | 8.1 | - | 19.1 | 6.1 | 33.3 |
| Net Debt Position | | | | | |
| Gross debt | 8.1 | - | 19.1 | 6.1 | 33.3 |
| Cash and term deposits | (14.7) | (16.1) | (1.2) | - | (32.0) |
| Net (Cash)/Debt | (6.6) | (16.1) | 17.9 | 6.1 | 1.3 |

The debts associated with the Syndicate Investment Property portfolio, Automotive Leather and Gosh Capital are primarily on a non-recourse basis to the other assets of the Group.

People, Health, Safety and Environment

Our global workforce is now around 1,200 which is a decrease on last year due to efficiencies within the Automotive Leather division and the sale of the Building Products division.

Schaffer Corporation is committed to providing all our employees with a safe and healthy working environment. Our Lost Time Injury Frequency Rate (LTIFR) has decreased by 16% over the past 3 years. SFC continues to review and improve occupational health and safety management to further improve outcomes.

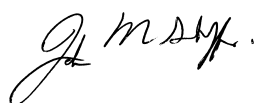
Schaffer Corporation is continuously improving its environmental impact. The Automotive Leather division has commenced Life Cycle Assessments for its products. The studies identify the environmental impact of producing cut automotive leather components from "cradle to customer". The division is then able to focus on the areas with the greatest potential for improving the environmental performance of our products and identify the products that can be marketed as having better environmental performance to customers. The Automotive Leather division is continuously upgrading technology so that chemicals, energy usage and production waste is minimised.

Dividends

Schaffer Corporation's long-standing policy is to pay dividends to its shareholders. On an ongoing basis, the directors manage the proportion of earnings paid out as dividends. The Board has regard to capital expenditure requirements, acquisition activity, liquidity needs and the availability of franking credits. We also reflect on prevailing economic conditions and uncertainty in setting dividends.

For the 2018 financial year, Schaffer Corporation has declared fully-franked dividends totalling \$0.45 per share, which is \$0.19 per share (73%) more than the prior year.

As always, I look forward to seeing as many shareholders as possible at Schaffer Corporation's Annual General Meeting. This year's meeting will be held on Wednesday, 14 November 2018 at 11:30am, at which time I will provide a further update on the outlook for the 2019 financial year.



JOHN SCHAFFER AM
Managing Director

Non-IFRS measures

* Schaffer Corporation results are reported under Australian Accounting Standards and International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board. The Company discloses certain non-IFRS financial measures. The non-IFRS measures should only be considered in addition to, and not as a substitute for, other measures of financial performance prepared in accordance with IFRS.

The following are non-IFRS measures that are important to management as additional means to evaluate the Group's performance:

1. Return on Average Capital Employed (ROACE) is calculated as EBIT divided by the average of total assets (excluding cash and cash equivalents, term deposits, and deferred income tax assets) less trade and other payables, and provisions over the period.
2. Net Profit After Tax (NPAT) is profit/(loss) for the period attributable to owners of the parent.
3. Non-recurring costs are defined as those costs that resulted from unusual or once-off events that are unlikely to occur again in the normal course of business.

Non-recurring costs (unaudited) are as follows:

| | Full-Year Ending | |
|---|------------------|------------|
| | June 2018 | June 2017 |
| Redundancy and Facility Shutdown Costs - Automotive Leather | 473 | 480 |
| Redundancies – Building Materials | - | 245 |
| Asset disposals and write-downs – Automotive Leather | - | 45 |
| Total non-recurring costs after tax and minority interests | 473 | 770 |

Underlying profit (unaudited) is reconciled as follows:

| | Full-Year Ending | |
|---|------------------|-----------|
| | June 2018 | June 2017 |
| Underlying Profit Reconciliation (\$000's) <i>All items after tax and minority interests</i> | | |
| NPAT | 23,292 | 5,856 |
| Profit on sale of Building Products division | (4,393) | - |
| Impairment of assets | 3,150 | 1,629 |
| Non-recurring costs | 473 | 770 |
| Profit on sale of Space 207 trust assets | - | (64) |
| Underlying Profit | 22,522 | 8,191 |

The directors believe that the presentation of non-IFRS financial information is useful for investors as the measures are utilised by the Group for rewarding performance and they reflect the underlying performance of the businesses.

Non-IFRS financial information has been extracted from the audited financial statements.

AUTOMOTIVE LEATHER



A GLOBAL BUSINESS IN A GLOBAL INDUSTRY

Supplier of leather to automotive manufacturers
in Europe and Asia.

Schaffer Corporation owns 83% of the Automotive Leather division, which produces high-quality leather for the global automotive industry and focuses on supplying premium OEM customers such as Jaguar Land Rover, Audi and Mercedes.

Production facilities are located globally to separately service both the European and Asian markets; for Europe, the leather finishing and cutting are located together in Kosice, Slovakia; for Asia, the leather finishing is located at the head office site in Thomastown, Victoria and the cutting in Shanghai, China.

The division's global footprint provides a local presence in the key European and Asian automotive markets. This allows Howe to be close to its key customers and provides the opportunity to remain competitive and responsive in a highly demanding global environment.

Revenue increased by 19% compared to the previous year as a result of the full year production of a number of new programs plus the significant benefit of favourable exchange rates.

During the 2018 financial year, the division had a major focus on reviewing and implementing new technologies in all aspects of its business. These have provided further operational efficiency and better customer responsiveness.

The global automotive industry continues to grow and adapt to the needs of its consumers. The shift to electric and autonomous vehicles is well publicised. Management's strategy to predominantly supply global premium OEMs will see the business well positioned to take advantage of the shifting interior requirements of the electric vehicles to a more luxurious environment.

All products are sold in foreign currency and translated back to Australian Dollars for financial reporting purposes. Fluctuations in the Euro, US Dollar and Chinese Renminbi against the Australian Dollar can have a significant impact on the financial performance of the Automotive Leather division, and accordingly management utilises hedges to manage these risks.

FEATURE PROJECT

Daimler – Interiors for electric vehicles

Daimler's goal is to always provide their customers with the most luxurious interior experience possible. That applies to their electric vehicle families as well.

Daimler's Head of Interior Design, Harmut Sinkwitz, explains that Daimler wants to continue to offer its customers the possibility to choose from a range of classic materials, such as metal, leather and wood, which create a feeling of comfort and luxury, though they will be adapted to suit Daimler's new design language.

The Automotive Leather division is proud to be involved in Daimler's future vision and has been successful in being awarded the supply of leather to new programs including the electric versions. Supply will commence from early 2021.





BUILDING MATERIALS

PROFITABLE NICHE FOCUS

Delta deliver niche products and design solutions for the construction, resource and landscaping markets.



SCHAFFER CORPORATION'S BUILDING MATERIALS DIVISION CONSISTS OF DELTA CORPORATION WHICH IS WA'S PRE-EMINENT MANUFACTURER OF PRECAST AND PRESTRESSED CONCRETE PRODUCTS.

Delta Corporation

www.deltacorp.com.au

Construction activity, according to the Civil Contractors Federation 2018 Western Australian Infrastructure Report, fell nearly 30% in WA during 2016/17 and was 40% lower than the 2013/14 peak. This sharp downturn in construction work leading into the 2017/18 financial year, combined with an oversupply of production capacity within the precast concrete industry, has resulted in an extremely challenging market environment. Subsequently, margins have come under increasing pressure as all stakeholders throughout the industry continue to aggressively price projects to win new business.

Notwithstanding these challenges, Delta was successful in securing the NorthLink Stage 2 Project. Unfortunately, due to some initial delays in ramping up to full production, turnover has been lower than budget. This, coupled with numerous design issues, increased complexity of the beams and a significant increase in technical documentation and quality requirements has resulted in cost overruns.

Our current work on hand provides some visibility for the first half of 2018/19 and recent indications of increased activity from the large iron ore mining companies Fortescue, BHP and Rio Tinto, should provide opportunities in the future.

In addition, a number of large shopping centre expansions are currently underway with Karrinyup and Garden City Shopping Centres set to commence construction within the next few months. This should also help absorb excess capacity in the WA construction industry.

We anticipate little change in the levels of competition in the marketplace over the next twelve months, and Delta will continue to undertake cost cutting measures to match market conditions and demand.

We will continue to partner and develop the relationships with those clients who build essential infrastructure and facilities needed across the state. We are proud to have successfully completed all the projects we have undertaken to the highest of quality standards and in accordance with respective programs.

Major projects successfully completed during the year included:

- Christ Church Grammar School
- Murdoch University Bush West
- Treendale - Collie River Bridge 5370
- NorthLink Stage 2 Column Formers
- QVI Landscaping
- Air Traffic Control Tower Pearce
- Prince Alfred College - New Boarding House SA
- Park on Parade St Clair Adelaide
- Sacred Heart College - Champagnat Campus Adelaide
- 293 Pirie Street Adelaide Apartments

However, we are continuing to manufacture TeeRoff Beams for the NorthLink Stage 2 Project with 30% of the beams left to make. Other contracts on hand include the Kings Square Fremantle, Curtin University Building 200 and the Arthur Philip High School Parramatta NSW.

FEATURE PROJECT

Challenger Institute TAFE Murdoch Stage 4 Development



The Challenger Institute of Technology's Stage 4 building is the most recent addition to the South Metropolitan TAFE campus in Murdoch, Western Australia.

The new three-storey multipurpose facility provides flexible training environments for students, offering a hub for educational, social, and TAFE administration services.

In this project, precast concrete has proved to be an integral part of the centre's functional and aesthetic benefits, aligning with the project's vision of improving overall student experience.

With precast concrete taking the spotlight within the development's architectural vision, Delta, in collaboration with the designers, was invited to develop a cost-effective precast concrete screen façade.

It is a striking precast concrete lattice screen that has a dual function - to simultaneously provide shade to the glass curtain wall and to stand out as an architectural feature. In doing so, the screen also provides privacy and comfort to the internal occupants, without hindering the campus view.

The project specifics were intricate and complex, and the resulting design is a uniquely-shaped lattice with a smooth Class 2 off-form finish to all formed surfaces.

Offering advantageous sustainability benefits and an architectural masterpiece, the 76 irregular-shaped lattice panels provide a substantial 120-metre-long veranda to the major street frontage. In order to form the complex shapes, Delta invested a significant amount of resources into the research and development of the materials and the manufacturing process—all while maintaining the high-quality finish demanded by the architect.

The concrete for the lattice panels had been specified in a crisp white colour by the architect and, using their in-house technical capabilities, Delta developed a successful mix design using white cement with the addition of white oxide. Two prototype panels were produced to ensure that manufacture was possible and that the specified finishes were achievable.

The intricate design of the screen façade, alongside the need for a high-quality concrete finish, posed a challenge for all stages of the project, particularly during the initial manufacturing phase. The multiple shapes and thin walls within the screen meant that the panels could not be reinforced with conventional reinforcement. Delta provided a solution that hinged on the use of stainless steel fibre for the reinforcement. Delta and the design team's solution resulted in the panels meeting the design requirements while also having sufficient structural strength.

As well as the intricacies of the product's design creating a manufacturing obstacle, the handling of the products presented a further challenge that existed not only during manufacture, but during delivery and installation as well.

The fragile nature of the panels meant that great care and attention to detail was essential to ensure minimal risk of damage. A special steel-handling frame was fabricated to minimise the stresses on the screen panels during the entire process.

SFC INVESTMENTS – PROPERTY AND OTHER

QUALITY INVESTMENTS AND LAND ASSETS WITH REDEVELOPMENT POTENTIAL

Lot 701, 702 & 703 Jandakot Road

Schaffer Corporation owns land at Jandakot, Western Australia, which is partially occupied by the UrbanStone manufacturing operations. The overall site has substantial development potential. The Western Australian Minister for Planning approved a Scheme Amendment in November 2017 which was formally gazetted in February 2018 to increase the scope of Additional Uses to allow Warehouses, Showrooms, Masonry Production and Nurseries over approximately 39 hectares. A Local Development Plan was subsequently approved by the local Council which required an additional 5.5-hectare buffer on one boundary that further reduced the developable area.

A revised market valuation was completed subsequent to year-end which valued the property at \$37.2 million on an "as is" basis, up from the previous valuation of \$19.1 million.

Syndicated Property

As at 30 June 2018, Schaffer Corporation's Syndicated Investment Property portfolio consisted of the following:

| Property name/location | Year acquired | Schaffer interest |
|---|---------------|-------------------|
| IBM Centre, Hay St, West Perth, WA | 1995 | 22% |
| Parks Shopping Centre, Bunbury, WA | 1999 | 17% |
| Hometown Shopping Centre, Albany Highway, Cannington, WA | 1998 | 25% |
| Neerabup, WA | 2007 | 20% |
| Symonston, ACT | 2018 | 6% |

Other Investments

During the 2018 financial year, Schaffer Corporation has invested in several managed equity funds with exposure to both local and international equities.

Gosh Capital

This separate 83% owned subsidiary within Schaffer Corporation was established as its own division in the 2014 financial year with a mandate to maximise the value of the land asset on which the Gosh Leather business previously operated at 10 Bennett Avenue, North Coogee, Western Australia. The mandate also involves the reinvestment of profits to grow the available capital for investment.

The division currently owns a range of investments, other than the land holding in North Coogee, including direct ownership of a bulky goods retail centre in Western Australia and various investments in syndicated property unit trusts, managed funds and shares.

The market value of Gosh Capital investments including minority interest at 30 June 2018 was \$31.7 million, \$25.7 million net of debt.

The following table represents the entire property holdings of the Group:

| Address | Description | Ownership structure | Land Size (sqm) | Current Lettable Area (sqm) | SFC Ownership % | SFC Share of Book Value (\$m) | SFC Share of Market Value (\$m) | SFC Share of Debt (\$m) | Tax on Capital Gain (\$m) | Net Equity Value (\$m) |
|--|-------------|---------------------|-----------------|-----------------------------|-----------------|-------------------------------|---------------------------------|-------------------------|---------------------------|------------------------|
| Property used by SFC operations | | | | | | | | | | |
| 218 Campersic Road Herne Hill, WA | Delta | SFC Direct | 134,305 | - | 100% | 6.0 | 9.5 | - | (1.0) | 8.5 |
| 1305 Hay Street West Perth, WA | Head Office | SFC Direct | 413 | - | 100% | 0.7 | 1.9 | - | (0.4) | 1.5 |
| | | | | | | 6.7 | 11.4 | - | (1.4) | 10.0 |
| Rental Properties | | | | | | | | | | |
| Lot 701 Jandakot Road, Jandakot, WA | Industrial | SFC Direct | 62,097 | - | 100% | 3.3 | 11.2 | | (2.4) | 8.8 |
| IBM Centre, 1060 Hay Street West Perth, WA | Office | Syndicate | 5,797 | 8,466 | 22% | 1.1 | 12.4 | (7.2) | (3.4) | 1.8 |
| Hometown, 1480 Albany Hwy Cannington, WA | Retail | Syndicate | 59,319 | 20,637 | 25% | 5.5 | 15.9 | (7.1) | (3.1) | 5.7 |
| Parks Shopping Centre Bunbury, WA | Retail | Syndicate | 30,804 | 10,622 | 17% | 2.0 | 6.9 | (3.8) | (1.5) | 1.6 |
| 39 Dixon Road Rockingham, Western Australia | Bulky Goods | Gosh Direct | 12,047 | 5,434 | 83% | 7.7 | 8.2 | (5.1) | (0.1) | 3.0 |
| Inghams, Port Wakefield Rd Burton, SA | Industrial | Gosh - Unit Trust | 53,300 | 13,437 | 4% | 0.8 | 0.8 | - | - | 0.8 |
| Pacific Suites, Canberra, ACT | Hotel | Gosh - Unit Trust | - | 16,045 | 2% | 0.9 | 0.9 | - | - | 0.9 |
| Copic Logistics – 7 properties nationwide | Industrial | Gosh - Unit Trust | 78,042 | 23,575 | 3% | 0.4 | 0.3 | - | - | 0.3 |
| Auburn Megamall 265 Paramatta Road, NSW | Bulky Goods | Gosh - Unit Trust | 24,690 | 32,348 | 2% | 1.2 | 1.2 | - | (0.2) | 1.0 |
| Symonston, ACT | Industrial | SFC - Unit Trust | 7,360 | 3,479 | 6% | 0.5 | 0.5 | - | - | 0.5 |
| | | | | | | 23.4 | 58.3 | (23.2) | (10.7) | 24.4 |
| Development sites | | | | | | | | | | |
| Lot 703 Jandakot Road Jandakot, WA | Vacant | SFC Direct | 449,639 | - | 100% | 3.8 | 19.5 | - | (4.7) | 14.8 |
| Lot 702 Jandakot Road Jandakot, WA | Commercial | SFC Direct | 32,442 | 500 | 100% | 0.3 | 6.5 | - | (1.9) | 4.6 |
| 10 Bennett Avenue North Coogee, WA | Residential | Gosh Direct | 21,035 | - | 83% | 1.6 | 11.3 | - | (2.9) | 8.4 |
| 170 Flynn Drive Neerabup, WA | Industrial | Syndicate | 260,000 | - | 20% | 1.5 | 4.0 | (1.0) | (0.7) | 2.3 |
| Lot 561 Paris Road Australind, WA | Commercial | Gosh - Unit Trust | 12,000 | - | 4% | 0.4 | 0.4 | - | - | 0.4 |
| Part Lot 602 Yanchep Beach Road, WA | Residential | Gosh - Unit Trust | 42,600 | - | 3% | 0.2 | 0.2 | - | - | 0.2 |
| | | | | | | 7.7 | 41.9 | (1.0) | (10.2) | 30.7 |
| Total SFC Property Value | | | | | | 37.8 | 111.6 | (24.2) | (22.3) | 65.1 |

2018

SCHAFER CORPORATION LIMITED
ABN 73 008 675 689

FINANCIAL REPORT

at 30 June 2018

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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME for the year ended 30 June 2018

| | | Consolidated | |
|--|-------|---------------------|---------------|
| | | 2018 | 2017 |
| | Note | \$'000 | \$'000 |
| Revenue | | | |
| Sale of goods | | 204,135 | 166,930 |
| Construction services | | 17,033 | 16,251 |
| Rental income | 3(a) | 5,559 | 5,275 |
| Finance income | 3(b) | 272 | 46 |
| Distribution from managed funds | | 37 | – |
| Revenue | | 227,036 | 188,502 |
| Cost of sales and services rendered | | (164,413) | (160,105) |
| Gross profit | | 62,623 | 28,397 |
| Impairment of property, plant & equipment | 13(a) | (4,500) | – |
| Other (losses)/income | 3(c) | 240 | (992) |
| Marketing expenses | | (613) | (563) |
| Administrative expenses | | (21,374) | (12,098) |
| Profit before tax and finance costs | | 36,376 | 14,744 |
| Finance costs | 3(b) | (2,112) | (2,860) |
| Profit before income tax | | 34,264 | 11,884 |
| Income tax expense | 5 | (10,349) | (3,057) |
| Profit after income tax from continuing operations | | 23,915 | 8,827 |
| Profit/(loss) after tax from discontinued operations | 34 | 4,245 | (1,281) |
| Net profit for the period | | 28,160 | 7,546 |
| Other comprehensive income | | | |
| Items that may be reclassified subsequently to profit or loss: | | | |
| Net fair value gains on available-for-sale financial assets | | 620 | 2,152 |
| Income tax on items of other comprehensive income | 5 | (209) | (732) |
| | | 411 | 1,420 |
| Foreign currency translation gains/(losses) attributable to parent | | 711 | (98) |
| | | 1,122 | 1,322 |
| Items that may not be reclassified subsequently to profit or loss: | | | |
| Net fair value gains on available-for-sale financial assets attributable to non-controlling interest | | 78 | 288 |
| Foreign currency translation gains/(losses) attributable to non-controlling interest | | 144 | (20) |
| Other comprehensive income for the period, net of tax | | 1,344 | 1,590 |
| Total comprehensive income for the period | | 29,504 | 9,136 |
| Profit for the period is attributable to: | | | |
| Non-controlling interest | 30 | 4,868 | 1,690 |
| Owners of the parent | 23 | 23,292 | 5,856 |
| | | 28,160 | 7,546 |
| Total comprehensive income for the period is attributable to: | | | |
| Non-controlling interest | | 5,089 | 1,957 |
| Owners of the parent | | 24,415 | 7,179 |
| | | 29,504 | 9,136 |
| Earnings per share (EPS) | | | |
| Basic EPS | 31 | 166.7¢ | 41.8¢ |
| Diluted EPS | 31 | 166.0¢ | 40.6¢ |
| Dividends paid per share | | 45.0¢ | 26.0¢ |

The above Consolidated Statement of Comprehensive Income should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION as at 30 June 2018

| | | Consolidated | |
|---|------|----------------|----------------|
| | | 2018 | 2017 |
| | Note | \$'000 | \$'000 |
| ASSETS | | | |
| Current assets | | | |
| Cash and cash equivalent | 4 | 25,938 | 11,417 |
| Trade and other receivables | 7 | 42,762 | 44,630 |
| Inventories | 8 | 39,604 | 49,415 |
| Prepayments and deposits | 9 | 2,065 | 2,127 |
| Derivative financial instruments | | 1,413 | – |
| Other financial assets | 10 | 6,000 | – |
| | | 117,782 | 107,589 |
| Non-current assets classified as held for sale | | – | 4,254 |
| Total current assets | | 117,782 | 111,843 |
| Non-current assets | | | |
| Receivables | | – | 216 |
| Property, plant and equipment | 13 | 27,645 | 37,290 |
| Investment properties | 14 | 28,678 | 25,406 |
| Deferred income tax asset | 5 | 6,076 | 2,284 |
| Goodwill | 15 | 1,299 | 1,299 |
| Other financial assets | 16 | 13,733 | 6,620 |
| Total non-current assets | | 77,431 | 73,115 |
| Total assets | | 195,213 | 184,958 |
| LIABILITIES | | | |
| Current liabilities | | | |
| Trade and other payables | 17 | 28,894 | 32,435 |
| Interest bearing loans and borrowings | 18 | 2,356 | 15,355 |
| Income tax payable | | 9,992 | 1,361 |
| Provisions | 19 | 10,600 | 7,892 |
| Derivative financial instruments | 33 | 46 | 895 |
| | | 51,888 | 57,938 |
| Non-current liabilities classified as held for sale | | – | 5 |
| Total current liabilities | | 51,888 | 57,943 |
| Non-current liabilities | | | |
| Interest bearing loans and borrowings | 20 | 30,894 | 39,859 |
| Deferred income tax liabilities | 5 | 2,390 | 2,186 |
| Provisions | 21 | 7,455 | 1,265 |
| Total non-current liabilities | | 40,739 | 43,310 |
| Total liabilities | | 92,627 | 101,253 |
| Net assets | | 102,586 | 83,705 |
| EQUITY | | | |
| Equity attributable to equity holders of the parent | | | |
| Issued capital | 22 | 14,540 | 16,583 |
| Reserves | 23 | 4,221 | 4,935 |
| Retained earnings | 23 | 72,101 | 52,867 |
| Total parent entity interest in equity | | 90,862 | 74,385 |
| Non-controlling interests | 30 | 11,724 | 9,320 |
| Total equity | | 102,586 | 83,705 |

The above Consolidated Statement of Financial Position should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY for the year ended 30 June 2018

| | Attributable to Equity Holders of the Parent | | | | | | | Non-controlling interest | Total equity | |
|---|--|-------------------|-------------------|---------------------------|---------------------------------|-------------------------------|--------|--------------------------|--------------|------------------------------|
| | Issued capital | Retained earnings | Reserves | | | | Total | | | |
| | | | Asset revaluation | Share-based payment EPU's | Share-based payment SFC options | Net unrealised gains/(losses) | | | | Foreign currency translation |
| | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | |
| At 1 July 2016 | 16,583 | 50,512 | 2,585 | 709 | 115 | 111 | 31 | 70,646 | 8,541 | 79,187 |
| Profit for the year | – | 5,856 | – | – | – | – | – | 5,856 | 1,690 | 7,546 |
| Other comprehensive income | – | – | – | – | – | 1,420 | (98) | 1,322 | 267 | 1,589 |
| Total comprehensive income for the year | – | 5,856 | – | – | – | 1,420 | (98) | 7,178 | 1,957 | 9,135 |
| Transactions with owners in their capacity as owners: | | | | | | | | | | |
| Share-based payments | – | – | – | 62 | – | – | – | 62 | – | 62 |
| Equity dividends | – | (3,501) | – | – | – | – | – | (3,501) | (1,178) | (4,679) |
| At 30 June 2017 | 16,583 | 52,867 | 2,585 | 771 | 115 | 1,531 | (67) | 74,385 | 9,320 | 83,705 |
| At 1 July 2017 | 16,583 | 52,867 | 2,585 | 771 | 115 | 1,531 | (67) | 74,385 | 9,320 | 83,705 |
| Profit for the year | – | 23,292 | – | – | – | – | – | 23,292 | 4,868 | 28,160 |
| Other comprehensive income | – | – | – | – | – | 411 | 711 | 1,122 | 221 | 1,343 |
| Total comprehensive income for the year | – | 23,292 | – | – | – | 411 | 711 | 24,414 | 5,089 | 29,503 |
| Transactions with owners in their capacity as owners: | | | | | | | | | | |
| Shares acquired under buy-back scheme | (2,043) | – | – | – | – | – | – | (2,043) | – | (2,043) |
| Share-based payments | – | – | – | 23 | 17 | – | – | 40 | – | 40 |
| Change in estimated settlement of EPUs (refer note 27(c)) | – | – | – | (1,876) | – | – | – | (1,876) | (194) | (2,070) |
| Equity dividends | – | (4,058) | – | – | – | – | – | (4,058) | (2,491) | (6,549) |
| At 30 June 2018 | 14,540 | 72,101 | 2,585 | (1,082) | 132 | 1,942 | 644 | 90,862 | 11,724 | 102,586 |

The above Consolidated Statement of Changes in Equity should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CASH FLOWS for the year ended 30 June 2018

| | | Consolidated | |
|---|------|-----------------|-----------------|
| | | 2018 | 2017 |
| | Note | \$'000 | \$'000 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | | |
| Receipts from customers | | 241,347 | 215,292 |
| Payments to suppliers and employees | | (188,024) | (184,674) |
| Other revenue | | 81 | 15 |
| Interest paid | | (2,113) | (2,869) |
| Income taxes paid | | (5,204) | (4,204) |
| Goods and services tax paid | | (1,066) | (1,316) |
| Net cash flows from operating activities | 4 | 45,021 | 22,244 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | |
| Interest income | | 282 | 56 |
| Net proceeds on sale of building materials business and assets | 34 | 17,377 | – |
| Investment in term deposits | | (6,000) | – |
| Acquisition of property, plant and equipment | 13 | (5,575) | (3,430) |
| Proceeds on sale of property, plant and equipment | | 5 | 590 |
| Acquisition/improvements to investment properties | | (549) | (820) |
| Acquisition of available-for-sale investments | | (6,416) | (250) |
| Distribution from realised gain on available-for-sale investments | | – | 302 |
| Capital distribution from available-for-sale investment | | – | 260 |
| Net cash flows used in investing activities | | (876) | (3,292) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | |
| Finance lease principal payments | | (1,741) | (2,134) |
| Dividends paid | 6(a) | (6,549) | (4,679) |
| Proceeds from borrowings | | 7,920 | 5,049 |
| Repayment of borrowings | | (28,143) | (13,008) |
| Shares acquired under share buy-back scheme | | (2,043) | – |
| Net cash flows used in financing activities | | (30,556) | (14,772) |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | | | |
| Net foreign exchange differences | | 932 | 169 |
| Cash and cash equivalents at the beginning of the period | | 11,417 | 7,068 |
| Cash and cash equivalents at the end of the period | 4 | 25,938 | 11,417 |

The Consolidated Statement of Cash Flows should be read in conjunction with the accompanying notes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 1 CORPORATE INFORMATION

The consolidated financial report of Schaffer Corporation Limited and its controlled entities (the Group or Consolidated Entity) for the year ended 30 June 2018 was authorised for issue in accordance with a resolution of the Directors on 21 September 2018.

Schaffer Corporation Limited (SFC, the Parent or the Company) is a for profit company limited by shares incorporated in Australia whose shares are publicly traded on the Australian Securities Exchange. The Company is domiciled in Australia.

The nature of the operations and principal activities of the Group are described in note 28.

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 and Australian Accounting Standards. The financial report has been prepared on a historical cost basis, except for derivative financial instruments and available-for-sale investments which have been measured at fair value.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars (\$'000) unless otherwise stated under the option available to the Company under ASIC Instrument 2016/191 Corporations (Rounding in Financial/Directors Report). The Company is an entity to which the instrument applies.

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

(b) New accounting standards and interpretations

Adoption of new accounting standards

The consolidated entity has adopted the following standards and interpretations as of 1 July 2017:

AASB 2016-1 Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses

This Standard makes amendments to AASB 112 *Income Taxes* to clarify the accounting for deferred tax assets for unrealised losses on debt instruments measured at fair value. This standard has no material impact on the Group.

AASB 2016-2 Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107

The amendments to AASB 107 *Statement of Cash Flows* are part of the IASB's Disclosure Initiative and help users of financial statements better understand changes in an entity's debt. The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses).

This amendment increases the disclosure requirements of the Group as presented in note 32(f).

AASB 2017-2 Amendments to Australian Accounting Standards – Further Annual Improvements 2014-2016 Cycle

This Standard clarifies the scope of AASB 12 *Disclosure of Interests in Other Entities* by specifying that the disclosure requirements apply to an entity's interests in other entities that are classified as held for sale or discontinued operations in accordance with AASB 5 *Non-current Assets Held for Sale and Discontinued Operations*. These amendments have no material impact on the Group.

The Consolidated Entity has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

New Accounting Standards and Interpretations not yet applicable

Applicable Australian Accounting Standards and Interpretations that have recently been issued or amended but are not yet effective have not been adopted by the Group for the annual reporting period ended 30 June 2018.

| Pronouncement | Title | Summary | Application date of standard | Application date for Group |
|---|------------------------------|---|------------------------------|----------------------------|
| AASB 9, and relevant amending standards | <i>Financial Instruments</i> | <p>AASB 9 replaces AASB 139 <i>Financial Instruments: Recognition and Measurement</i>.</p> <p>Except for certain trade receivables, an entity initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVTPL), transaction costs.</p> <p>Debt instruments are subsequently measured at FVTPL, amortised cost, or fair value through other comprehensive income (FVOCI), on the basis of their contractual cashflows and the business model under which the debt instruments are held.</p> <p>There is a fair value option (FVO) that allows financial assets on initial recognition to be designated as FVTPL if that eliminates or significantly reduces an accounting mismatch.</p> <p>Equity instruments are generally measured at FVTPL. However, entities have an irrevocable option on an instrument-by-instrument basis to present changes in the fair value of non-trading instruments in other comprehensive income (OCI) without subsequent reclassification to profit or loss.</p> <p>For financial liabilities designated as FVTPL using the FVO, the amount of change in the fair value of such financial liabilities that is attributable to changes in credit risk must be presented in OCI. The remainder of the change in fair value is presented in profit or loss, unless presentation in OCI of the fair value change in respect of the liability's credit risk would create or enlarge an accounting mismatch in profit or loss.</p> <p>All other AASB 139 classification and measurement requirements for financial liabilities have been carried forward into AASB 9, including the embedded derivative separation rules and the criteria for using the FVO.</p> <p>The incurred credit loss model in AASB 139 has been replaced with an expected credit loss model in AASB 9.</p> <p>The requirements for hedge accounting have been amended to more closely align hedge accounting with risk management, establish a more principle-based approach to hedge accounting and address inconsistencies in the hedge accounting model in AASB 139.</p> | 1 January 2018 | 1 July 2018 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

| Pronouncement | Title | Summary | Application date of standard | Application date for Group |
|--|--|--|------------------------------|----------------------------|
| AASB 15, and relevant amending standards | <i>Revenue from Contracts with Customers</i> | <p>AASB 15 replaces all existing revenue requirements in Australian Accounting Standards (AASB 111 <i>Construction Contracts</i>, AASB 118 <i>Revenue</i>, AASB Interpretation 13 <i>Customer Loyalty Programmes</i>, AASB Interpretation 15 <i>Agreements for the Construction of Real Estate</i>, AASB Interpretation 18 <i>Transfers of Assets from Customers</i> and AASB Interpretation 131 <i>Revenue – Barter Transactions Involving Advertising Services</i>) and applies to all revenue arising from contracts with customers, unless the contracts are in the scope of other standards, such as AASB 117 <i>Leases</i> (or AASB 16 <i>Leases</i>, once applied).</p> <p>The core principle of AASB 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods or services. An entity recognises revenue in accordance with the core principle by applying the following steps:</p> <ul style="list-style-type: none"> ▶ 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. | 1 January 2018 | 1 July 2018 |
| AASB 2016-5 | <i>Amendments to Australian Accounting Standards – Classification and Measurement of Share-based Payment Transactions</i> | <p>This Standard amends AASB 2 <i>Share-based Payment</i>, clarifying how to account for certain types of share-based payment transactions. The amendments provide requirements on the accounting for:</p> <ul style="list-style-type: none"> ▶ The effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments ▶ Share-based payment transactions with a net settlement feature for withholding tax obligations ▶ A modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled. <p>These changes are not expected to be material to the Group.</p> | 1 January 2018 | 1 July 2018 |
| AASB 2017-1 | <i>Amendments to Australian Accounting Standards – Transfers of Investments Property, Annual Improvements 2014-2016 Cycle and Other Amendments</i> | <p>The amendments clarify certain requirements in:</p> <ul style="list-style-type: none"> ▶ AASB 1 <i>First-time Adoption of Australian Accounting Standards</i> – deletion of exemptions for first-time adopters and addition of an exemption arising from AASB Interpretation 22 <i>Foreign Currency Transactions and Advance Consideration</i> ▶ AASB 12 <i>Disclosure of Interests in Other Entities</i> – clarification of scope ▶ AASB 128 <i>Investments in Associates and Joint Ventures</i> – measuring an associate or joint venture at fair value ▶ AASB 140 <i>Investment Property</i> – change in use. <p>These changes are not expected to be material to the Group.</p> | 1 January 2018 | 1 July 2018 |
| AASB Interpretation 22 | <i>Foreign Currency Transactions and Advance Consideration</i> | <p>The Interpretation clarifies that in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine a date of the transaction for each payment or receipt of advance consideration.</p> <p>These changes are not expected to be material to the Group.</p> | 1 January 2018 | 1 July 2018 |
| AASB 16 | <i>Leases</i> | <p>AASB 16 requires lessees to account for all leases under a single on-balance sheet model in a similar way to finance leases under AASB 117 <i>Leases</i>. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset).</p> <p>Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.</p> <p>Lessees will be required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset.</p> <p>Lessor accounting is substantially unchanged from today's accounting under AASB 117. Lessors will continue to classify all leases using the same classification principle as in AASB 117 and distinguish between two types of leases: operating and finance leases.</p> | 1 January 2019 | 1 July 2019 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(b) New accounting standards and interpretations (continued)

| Pronouncement | Title | Summary | Application date of standard | Application date for Group |
|---|---|--|------------------------------|----------------------------|
| AASB 2017-6 | <i>Amendments to Australian Accounting Standards— Prepayment Features with Negative Compensation</i> | <p>This Standard amends AASB 9 <i>Financial Instruments</i> to permit entities to measure at amortised cost or fair value through other comprehensive income particular financial assets that would otherwise have contractual cashflows that are solely payments of principal and interest but do not meet that condition only as a result of a prepayment feature. This is subject to meeting other conditions, such as the nature of the business model relevant to the financial asset. Otherwise, the financial assets would be measured at fair value through profit or loss.</p> <p>The Standard also clarifies in the Basis for Conclusion that, under AASB 9, gains and losses arising on modifications of financial liabilities that do not result in derecognition should be recognised in profit or loss.</p> <p>These changes are not expected to be material to the Group.</p> | 1 January 2019 | 1 July 2019 |
| AASB 2017-7 | <i>Amendments to Australian Accounting Standards— Long-term Interests in Associates and Joint Ventures</i> | <p>This Standard amends AASB 128 <i>Investments in Associates and Joint Ventures</i> to clarify that an entity is required to account for long-term interests in an associate or joint venture, which in substance form part of the net investment in the associate or joint venture but to which the equity method is not applied, using AASB 9 <i>Financial Instruments</i> before applying the loss allocation and impairment requirements in AASB 128.</p> <p>These changes are not expected to be material to the Group.</p> | 1 January 2019 | 1 July 2019 |
| AASB 2018-1 | <i>Annual Improvements to IFRS Standards 2015-2017 Cycle</i> | <p>The amendments clarify certain requirements in:</p> <ul style="list-style-type: none"> ▶ AASB 3 <i>Business Combinations</i> and AASB 11 <i>Joint Arrangements</i> – previously held interest in a joint operation ▶ AASB 112 <i>Income Taxes</i> – income tax consequences of payments on financial instruments classified as equity ▶ AASB 123 <i>Borrowing Costs</i> – borrowing costs eligible for capitalisation. <p>These changes are not expected to be material to the Group.</p> | 1 January 2019 | 1 July 2019 |
| AASB Interpretation 23, and relevant amending standards | <i>Uncertainty over Income Tax Treatments</i> | <p>The Interpretation clarifies the application of the recognition and measurement criteria in AASB 112 <i>Income Taxes</i> when there is uncertainty over income tax treatments. The Interpretation specifically addresses the following:</p> <ul style="list-style-type: none"> ▶ Whether an entity considers uncertain tax treatments separately ▶ The assumptions an entity makes about the examination of tax treatments by taxation authorities ▶ How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates ▶ How an entity considers changes in facts and circumstances. <p>These changes are not expected to be material to the Group.</p> | 1 January 2019 | 1 July 2019 |
| Not yet issued by the AASB | <i>Conceptual Framework for Financial Reporting, and relevant amending standards</i> | <p>The revised Conceptual Framework includes some new concepts, provides updated definitions and recognition criteria for assets and liabilities and clarifies some important concepts. It is arranged in eight chapters, as follows:</p> <ul style="list-style-type: none"> ▶ Chapter 1 – The objective of financial reporting ▶ Chapter 2 – Qualitative characteristics of useful financial information ▶ Chapter 3 – Financial statements and the reporting entity ▶ Chapter 4 – The elements of financial statements ▶ Chapter 5 – Recognition and derecognition ▶ Chapter 6 – Measurement ▶ Chapter 7 – Presentation and disclosure ▶ Chapter 8 – Concepts of capital and capital maintenance <p><i>Amendments to References to the Conceptual Framework in IFRS Standards</i> has also been issued, which sets out the amendments to affected standards in order to update references to the revised Conceptual Framework. The changes to the Conceptual Framework may affect the application of IFRS in situations where no standard applies to a particular transaction or event. In addition, relief has been provided in applying IFRS 3 and developing accounting policies for regulatory account balances using IAS 8, such that entities must continue to apply the definitions of an asset and a liability (and supporting concepts) in the 2010 Conceptual Framework, and not the definitions in the revised Conceptual Framework.</p> <p>These changes are not expected to be material to the Group.</p> | 1 January 2020 | 1 July 2020 |
| AASB 2014-10 | <i>Amendments to Australian Accounting Standards— Sale or Contribution of Assets between an Investor and its Associate or Joint Venture</i> | <p>The amendments clarify that a full gain or loss is recognised when a transfer to an associate or joint venture involves a business as defined in AASB 3 <i>Business Combinations</i>. Any gain or loss resulting from the sale or contribution of assets that does not constitute a business, however, is recognised only to the extent of unrelated investors' interests in the associate or joint venture.</p> <p>AASB 2015-10 deferred the mandatory effective date(application date) of AASB 2014-10 so that the amendments were required to be applied for annual reporting periods beginning on or after 1 January 2018 instead of 1 January 2016. AASB 2017-5 further defers the effective date of the amendments made in AASB 2014-10 to periods beginning on or after 1 January 2022.</p> <p>These changes are not expected to be material to the Group.</p> | 1 January 2022 | 1 July 2022 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(b) New accounting standards and interpretations (continued)

Impact of new accounting standards on Schaffer Corporation:

AASB 9 Financial Instruments

This standard will impact the Group's recognition of unrealised gains or losses on the revaluation of the Group's available-for-sale investments to fair value.

To 30 June 2018, gains or losses on available-for-sale equity instruments are recorded to other comprehensive income through the asset revaluation reserve on the consolidated statement of changes in equity.

From 1 July 2018, all equity instruments held for sale will be revalued to fair value through the net profit for the period. Further, the Group has made the election that any equity instruments not held for trading with also be fair valued through the net profit for the period from 1 July 2018.

The impact on the net profit attributable to shareholders for the period to 30 June 2018, if the standard had been early adopted, would have been a \$411,000 gain. Fluctuations in fair value of equity instruments is expected to have an impact on the periodic financial performance of the Group from 1 July 2018.

AASB 9 will impact the impairment provisioning model for financial assets of the Group. Currently assessment of impaired trade receivables occurs when there is objective evidence that the Group will not be able to collect the receivable. AASB 9 requires that a 12-month expected losses for performing assets such as trade receivables be recorded upfront at the time of revenue recognition. There would have been no impact on the financial statements of the Group as at 30 June 2018 had the standard been early adopted because the provision recorded based on objective evidence of expected losses against the trade receivables balance was higher than the average 12-month history of losses against trade income.

On transition, the new standard is to be applied retrospectively without the restatement of comparatives and is not expected to have any impact on the financial position of the group.

AASB 15 Revenue from Contracts with Customers

AASB 15 is applicable to the Group from 1 July 2018. The scope of the new standard applies to the sale of goods revenue stream of the Automotive Leather segment, and the construction services revenue stream of the Building Materials segment. Other items currently recognised in revenue, including rental income, dividends and interest, will be not be included in revenue from contracts on adoption of the standard.

Contracts for each revenue stream have been selected, reviewed and analysed for potential impact by AASB 15. The outcome of the review is that the current accounting policies for each revenue stream concur with the requirements of AASB15 and that there would have been no impact on the financial performance or financial position of the Group if the standard were early adopted. On transition, the Group will utilise the modified retrospective transition method without the restatement of comparatives and expects to include more comprehensive disclosures in its annual financial statements as required by the new standard.

AASB 16 Leases

The Group has identified certain operating leases with terms longer than 12 months that will be recognised as assets and liabilities on the Company's statement of financial position from 1 July 2019 when the new standard is implemented. The future minimum rentals payable under these leases are disclosed in Note 26.

The Group is currently evaluating the impact of the new standard on the financial position and financial performance of the Group.

(c) Basis of consolidation

The consolidated financial statements comprise the financial statements of Schaffer Corporation Limited and its subsidiaries (the Group) as at 30 June each year. 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:

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

When the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- (i) the contractual arrangement with the other vote holders of the investee;
- (ii) rights arising from other contractual arrangements; and
- (iii) the Group's voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the Consolidated Statement of Comprehensive Income from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income (OCI) are attributed to the equity holders of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

Non-controlling interests represent the portion of profit or loss and net assets in Howe Automotive Limited and Gosh Holdings Pty Limited not held by the Group and are presented separately in the Consolidated Statement of Comprehensive Income and within equity in the Consolidated Statement of Financial Position.

(d) Significant accounting judgments, estimates and assumptions

(i) *Significant accounting judgments*

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 are outlined below:

Operating lease commitments – Group as Lessor

The Group has entered into commercial property leases on its Investment Property portfolio. The Group has determined that it retains all the significant risks and rewards of ownership of these properties and has thus classified the leases as operating leases.

(ii) *Significant accounting estimates and assumptions*

The carrying amounts of certain assets and liabilities are often determined based on estimates and assumptions of future events. The key estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of certain assets and liabilities within the next annual reporting period are:

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the recoverable amount of the cash-generating units to which the goodwill is allocated. The assumptions used in this estimation of recoverable amount and the carrying amount of goodwill are discussed in note 15.

Employee participation units

The Group measures the cost of cash-settled EPU termination payments in accordance with a valuation formula based on the future three-year average of 5.5 times Howe Automotive Limited's estimated earnings before interest and tax minus the future three-year average estimated debt, discounted based on the estimated period until payment using a risk-free rate of return. The valuation has sensitivity to the estimate of future earnings. Refer note 27(c).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Basis of consolidation (continued)

(ii) Significant accounting estimates and assumptions (continued)

Construction contracts

Refer note 2(t).

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 asset that may lead to impairment. These include product and manufacturing performance, technology, economic and political environments and future product expectations. If an impairment trigger exists, the recoverable amount of the asset is determined.

(e) Foreign currency translation

Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Both the functional and presentation currency of Schaffer Corporation Limited and its Australian subsidiaries is Australian dollars.

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date. All exchange differences arising from the above procedures are taken to the Consolidated Statement of Comprehensive Income.

As at the reporting date the assets and liabilities of overseas subsidiaries (refer note 12) are translated into the presentation currency of Schaffer Corporation Limited at the rate of exchange ruling at the balance date and the Consolidated Statement of Comprehensive Income is translated at the average exchange rates for the year.

The exchange differences arising on the translation are taken directly to other comprehensive income.

On disposal of a foreign entity, the deferred cumulative amount recognised in the component of other comprehensive income relating to that particular foreign operation and attributable to the parent entity is recognised in the Consolidated Statement of Comprehensive Income.

(f) Investment properties

Investment properties are measured at cost less accumulated depreciation.

Investment properties are derecognised either when they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in the Consolidated Statement of Comprehensive Income in the year of retirement or disposal.

Depreciation is calculated on a straight-line basis over the estimated useful life as follows:

- buildings over 40 years
- land is not depreciated
- improvements – over 5 to 15 years

(g) Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Such cost includes the cost of replacing parts that are eligible for capitalisation when the cost of replacing the parts is incurred.

Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

- land – not depreciated
- buildings – over 40 years
- leasehold improvements – the shorter of the lease term and the asset's useful life
- plant and equipment – over 5 to 15 years

(i) Impairment

The carrying values of property, plant and equipment are reviewed for impairment at each reporting date, with recoverable amount being estimated when events or changes in circumstances indicate the carrying value may be impaired.

The recoverable amount of property, plant and equipment is the greater of fair value less costs of disposal and value in use. 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.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of an asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

(h) Goodwill

Goodwill is initially recognised at cost (being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interest and any previous interest held over the net identifiable assets acquired and the liabilities assumed). If the fair value of the net assets acquired is in excess of the aggregate consideration transferred, the Group re-assesses whether it has correctly identified all of the assets acquired and all of the liabilities assumed and reviews the procedures used to measure the amounts to be recognised at the acquisition date. If the reassessment still results in an excess of the fair value of the net assets acquired over the aggregate consideration transferred, then the gain is recognised in profit or loss.

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

Goodwill is not amortised.

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

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units expected to benefit from the combination's synergies.

Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates.

Where 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 is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation.

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

Impairment losses for goodwill are not subsequently reversed.

(i) Impairment of non-financial assets other than goodwill

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of its fair value less costs of disposal and its value in use and 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 and the asset's value in use cannot be estimated to be close to its fair value. In such cases the asset is tested for impairment as part of the cash-generating unit to which it belongs. When the carrying amount of an asset or cash-generating unit exceeds its recoverable amount, the asset or cash-generating unit is considered impaired and is written down to its recoverable amount.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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. Impairment losses relating to continuing operations are recognised in those expense categories consistent with the function of the impaired asset unless the asset is carried at revalued amount (in which case the impairment loss is treated as a revaluation decrease).

An assessment is also made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount.

That increased amount cannot 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 profit or loss unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase. After such a reversal, the depreciation charge is adjusted in future period to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

(j) Investments and other financial assets

Financial assets in the scope of AASB 139 *Financial Instruments: Recognition and Measurement* are classified as 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 directly attributable transaction costs. The Group determines the classification of its financial assets on initial recognition.

(i) Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated as available for sale or not classified in any of the other categories. They are included in current assets unless the Group intends to dispose of the investment longer than 12 months after the balance sheet date.

After initial recognition, these financial assets are measured at fair value. Gains or losses are recognised as a separate component of equity until the financial asset is sold, collected or otherwise disposed, or until the financial asset is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the Consolidated Statement of Comprehensive Income.

For financial instruments traded in organised financial markets, fair value is the current quoted market bid price for an asset or offer price for a liability.

Dividends or distributions on available-for-sale equity instruments are recognised in the Consolidated Statement of Comprehensive Income when the Group's right to receive payments as dividends or distributions is established.

Purchases and sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place are recognised on the trade date i.e. the date that the Group commits to purchase the asset.

(ii) Loans and receivables

Loans and receivables 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 the effective interest method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

(k) Inventories

Inventories are valued at the lower of cost and net realisable value except for contract work in progress.

Costs incurred in bringing each product to its present location and condition are accounted for as follows:

- Raw materials – purchase cost on a first-in, first-out basis.
- Finished goods – cost of direct materials and labour and a proportion of manufacturing overheads based on normal operating capacity but excluding borrowing costs. Costs are assigned on the first-in first-out basis.

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

(l) Trade and other receivables

Trade receivables, which generally have 30-90 day terms, are recognised and carried at original invoice amount less an allowance for any uncollectible amounts. The carrying amount approximates fair value.

Collectability of trade receivables is reviewed on an ongoing basis at an operating unit level. Individual debts that are known to be uncollectable are written off when identified. An impairment allowance is recognised when there is objective evidence that the Group will not be able to collect the receivable. Financial difficulties of the debtor or default payments are considered objective evidence of impairment. The amount of the impairment loss is the portion of the individual receivable carrying amount estimated to be uncollectable.

Contract work in progress

Contract work in progress for the construction of precast concrete elements within the Building Materials segment is stated at cost plus profit recognised to date calculated in accordance with the percentage of completion method, less a provision for foreseeable losses and progress payments received to date.

A contract is not considered complete until the defects liability period has expired and monies withheld have been received. Any expected losses on a contract are recognised immediately in the period the loss becomes foreseeable. That is, when it becomes probable that total contract costs will exceed total contract revenues.

Cost includes all variable and fixed costs directly related to specific construction contracts, those costs related to contract activity in general which can be allocated to specific contracts on a reasonable basis and other costs specifically chargeable under the contract. Also included are costs expected to be incurred under penalty clauses and rectification provisions.

The gross amount due from customers for contract work for all contracts in progress for which costs incurred plus recognised profits (less recognised losses) exceed progress billings, is generally presented as an asset.

The gross amount due to customers for contract work for all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less recognised losses) are presented as current liabilities.

(m) Cash and short-term deposits

Cash and short-term deposits in the Consolidated Statement of Financial Position comprise cash at banks and on hand and short-term deposits with a maturity of three months or less.

For the purpose of the Consolidated Statement of Cash Flows, cash and cash equivalents consist of cash and short-term deposits as defined above, net of outstanding bank overdrafts.

(n) 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.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(o) 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 Consolidated Statement of Comprehensive Income net of any reimbursement.

If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, 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 finance cost.

Restructure provisions

Provisions relating to restructures are recognised when:

- the Group has a detailed formal plan for the restructuring; and
- has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement it or by announcing its main features to those affected.

(p) Employee entitlements

Provision is made for employee entitlement benefits accumulated as a result of employees rendering services up to the reporting date. These benefits include wages and salaries, annual leave and long service leave, and associated taxes and on-costs. Liabilities arising in respect of employee entitlements expected to be settled within twelve months of the reporting date are measured at the amounts expected to be settled. All other employee entitlement liabilities are measured at the present value of the estimated future cash outflows to be made in respect of services provided by employees up to the reporting date.

In determining the present value of future cash outflows, the interest rates attaching to national corporate bonds which have terms to maturity approximating the terms of the related liability are used. Employee entitlements, expenses and revenues arising in respect of the following categories:

- wages and salaries, non-monetary benefits, annual leave, long service leave and other leave entitlements;
- other types of employee entitlements;

are charged against profit or loss on a net basis in their respective categories.

Contributions to defined contribution superannuation plans are expensed when incurred.

(q) Executive share option arrangement

The Directors of Schaffer Corporation Limited may grant in their absolute discretion, without payment, share options to employees under an employee share scheme approved by shareholders at the Annual General Meeting in November 1999. Each option is convertible into one ordinary share of Schaffer Corporation Limited on payment of the exercise price, after a vesting period, but prior to the expiry date.

The exercise price is determined at the grant date at the absolute discretion of the Directors but not less than the greater of:

- (1) the weighted average of the last sale price on the Australian Stock Exchange Limited of the shares in the Company for each of the five trading days on which a sale of the Company's shares was effected immediately preceding the date on which any options are issued to any participant; and
- (2) 20 cents.

The options hold no voting or dividend rights and are not transferable. Schaffer Corporation Limited does not provide any loans or guarantees to enable executives to finance the exercise of their options. When an executive ceases to be employed by the entity any unexercised options automatically lapse and are forfeited.

The cost of these equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined using a Black-Scholes model.

In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of Schaffer Corporation Limited (market conditions).

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (vesting date).

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) the Group's best estimate of the number of equity instruments that will ultimately vest. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date. The Consolidated Statement of Comprehensive Income charge or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

If the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any modification that increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee, as measured at the date of modification.

If an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award and designated as a replacement award on the date that it is granted, the cancelled and new award are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect, if any, of outstanding options is reflected as additional share dilution in the computation of earnings per share (refer note 31).

(r) Employee participation units

A controlled entity Howe Automotive Limited (Howe) may grant employee participation units (EPUs) in accordance with its Employee Incentive Plan adopted by Howe shareholders on 20 December 2001. For conditions refer to note 27(c).

An EPU provides an employee with a right on termination of employment under certain conditions and in certain other circumstances to receive a cash payment from Howe. Schaffer Corporation Limited has the option to compel the employee to use the whole or part of that cash payment to subscribe for Schaffer Corporation Limited shares.

On 1 November 2017, a change in accounting was implemented based on the higher probability that in the future SFC would not equity settle these transactions by compelling employees to use the whole or part of the cash payment received on termination to subscribe for SFC shares. However, this accounting judgment does not limit the existing option for SFC to compel employees in the future to use the whole or part of the cash payment to subscribe for SFC shares.

The Group now records a provision for EPU termination entitlements calculated using estimates of the probable future EPU cash payments for issued EPUs discounted based on the estimated period until payment using a risk-free rate of return. The amount estimated for EPU cash payments on termination is calculated in accordance with an equity valuation formula based on the three-year average, including one full year following termination, of 5.5 times Howe Automotive Limited's estimated earnings before interest and tax minus debt.

EPU's are cancelled once they are paid out. EPU's are also cancelled if the employee ceases to be an employee prior to the third anniversary of the grant date for any reason other than death or permanent disablement, if the employee acts in competition with Howe after the third anniversary but prior to pay out, or if the employee is a director or general manager and does not provide a minimum of 90 days notice of intention to terminate employment.

Howe may at any time amend this plan, but amendments cannot prejudice the accrued rights of an employee without consent of not less than 75% in the number of employees who hold EPUs at the time of the amendment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(s) 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 arrangements is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

(i) Group as Lessee

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 property 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 Consolidated Statement of Comprehensive Income.

Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term.

Operating lease payments are recognised as an expense in the Consolidated Statement of Comprehensive Income on a straight-line basis over the lease term.

(ii) Group as Lessor

Leases where the Group retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as the rental income.

(t) Revenue recognition

Revenue is recognised and measured at the fair value of the consideration received or receivable to the extent 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 can be measured reliably. Risks and rewards are considered passed to the buyer at the time control of the goods has passed to the customer.

Interest income

Revenue is recognised as the interest accrues (using the effective interest method, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset).

Dividends

Revenue is recognised when the shareholders' right to receive the payment is established.

Rental income

Rental income arising on investment properties is accounted for on a straight-line basis over the lease term. Contingent rental income is recognised as income in the periods in which it is earned.

Sale of land

Revenue on the sale of land is brought to account when the sale is unconditional.

Construction contracts

For construction contracts, revenues and expenses are recognised on an individual contract basis using the percentage of completion method. Once the outcome of a construction contract can be estimated reliably based on a review of the terms and conditions applicable to each individual contract, contract revenues and expenses are recognised in the Consolidated Statement of Comprehensive Income in proportion to the stage of completion of the contract. The stage of completion is measured by reference to actual costs incurred to date as a percentage of estimated total costs for each contract. The Group has determined that the outcome of its construction contracts can usually be reliably estimated at the commencement of the contract. Where the outcome of a contract cannot be reliably determined, contract costs are expensed as incurred. Where it is probable that the costs

will be recovered, revenue is recognised to the extent of costs incurred. Where it is probable that a loss will arise from a construction contract, the excess of total expected costs over revenue is recognised as an expense immediately.

(u) Income tax

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance date.

Deferred income tax is provided on all temporary differences at the balance 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:

- where 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 that at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- where taxable temporary differences associated with investments in subsidiaries, associates and undivided interests, and the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences 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:

- where the deferred income tax asset relating to the deductible temporary differences 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
- where the deductible temporary differences is associated with investments in subsidiaries, or interests in joint ventures, in which case a deferred tax asset is only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance 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 balance 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 balance date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in the profit or loss.

Deferred tax assets and deferred tax liabilities are offset only if a legally enforceable right exists to set off 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.

The Company and all its wholly-owned Australian resident subsidiaries are part of a tax consolidated group. The Company, being the head entity in a tax consolidated group, assumes the current tax liability and any deferred tax assets arising from tax losses and other unused tax credits of the subsidiaries in the tax consolidated group. Deferred tax balances of the subsidiaries in the tax consolidated group are not assumed by the Parent entity.

The Group allocates the tax balances for the period using the Group allocation approach, and a tax funding arrangement is in place to reimburse the parent entity for any liabilities of the subsidiaries it assumes and conversely, for the parent entity to reimburse the subsidiaries for any recognised tax losses it assumes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(v) Other taxes

Revenues, expenses and assets are recognised net of the amount of goods and services tax ('GST') except:

- where 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 as applicable; and
- receivables and payables 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 Consolidated Statement of Financial Position.

Cash flows are included in the Consolidated 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.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(w) Derivative financial instruments

The Group uses derivative financial instruments such as forward currency contracts and interest rate swaps to manage its risks associated with foreign currency and interest rate 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 remeasured to fair value. Derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

The Group has determined that these derivatives do not qualify for hedge accounting and as such, any gains or losses arising from changes in fair value are taken directly to the Consolidated Statement of Comprehensive Income.

Forward exchange contracts

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

Interest rate swaps

The fair value of interest rate swap contracts is determined by reference to market values for similar instruments.

(x) Contributed equity

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

(y) Earnings per share

Basic earnings per share is calculated as net profit attributable to members of the Parent adjusted to exclude costs of servicing equity (other than dividends), divided by the weighted average number of ordinary shares outstanding during the period, adjusted for any bonus element. Diluted earnings per share, is calculated as net profit attributable to members adjusted for:

- costs of servicing equity (other than dividends);
- the after-tax effect of dividends and interest associated with dilutive potential ordinary shares that have been recognised as expenses; and
- other non-discretionary changes in revenues or expenses during the period that would result from the dilution of potential ordinary shares;

divided by the weighted average number of ordinary shares outstanding during the period and dilutive potential ordinary shares, adjusted for any bonus element.

(z) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset (i.e. an asset that necessarily takes a substantial period of time to get ready for its intended use or sale) are capitalised as part of the cost of that asset. All other borrowing costs are expensed in the period they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

(aa) Trade and other payables

Trade payables and other payables are carried at amortised costs 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 become obliged to make future payments in respect of the purchase of these goods and services. The carrying amount approximates fair value.

(ab) Research costs

Research costs are expensed as incurred.

(ac) Business combinations

Business combinations are accounted for using the acquisition method. The consideration transferred in a business combination shall be measured at fair value, which shall be calculated as the sum of the acquisition date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree, the equity issued by the acquirer, and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic conditions, the Group's operating or accounting policies and other pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured at fair value as at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability will be recognised in accordance with AASB 139 either in profit or loss or in other comprehensive income. If the contingent consideration is classified as equity, it shall not be remeasured.

The excess of the cost of the business combination over the net fair value of the Group's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the Group's share of the net fair value of the identifiable net assets of the subsidiary, the difference is recognised as a gain in the Consolidated Statement of Comprehensive Income, but only after a reassessment of the identification and measurement of the net assets acquired.

(ad) Discontinued operations

A discontinued operation is a component of the entity that has been disposed of or is classified as held for sale and that represents a separate major line of business or geographical area of operations, is part of a single coordinated plan to dispose of such a line of business or area of operations, or is a subsidiary acquired exclusively with a view to resale. The results of discontinued operations are presented separately on the face of the Consolidated Statement of Comprehensive Income and the assets and liabilities are presented separately on the face of the Consolidated Statement of Financial Position.

(ae) Non-current assets held for sale

Non-current assets classified as held for sale are measured at the lower of their carrying amount and fair value less costs of disposal. Non-current assets are classified as held for sale if their carrying amounts will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Property, plant and equipment and intangible assets once classified as held for sale are not depreciated or amortised.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

| | Consolidated | |
|---|--------------|---------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| NOTE 3 | | |
| REVENUES AND EXPENSES | | |
| (a) Net rental income | | |
| Rental property income | 5,559 | 5,275 |
| | 5,559 | 5,275 |
| Rental property expenses | (2,828) | (2,841) |
| Net rental income | 2,731 | 2,434 |
| (b) Finance (costs)/income | | |
| Bank and other loans and overdrafts – interest | (1,954) | (2,670) |
| Finance charges payable under finance leases | (158) | (199) |
| Total finance costs | (2,112) | (2,869) |
| Bank interest revenue | 272 | 46 |
| Total finance income | 272 | 46 |
| (c) Other (losses)/income | | |
| Loss on disposal of property, plant and equipment | – | (337) |
| Net loss on derivatives | (153) | (622) |
| Net foreign currency profit/(loss) | 393 | (144) |
| Realised gains on available-for-sale investments | – | 110 |
| Other | – | 1 |
| | 240 | (992) |
| (d) Depreciation and amortisation included in the consolidated statement of comprehensive income | | |
| Depreciation and amortisation included in: | | |
| Cost of sales | 3,973 | 3,343 |
| Rental property expenses | 559 | 591 |
| Marketing and administrative expenses | 278 | 172 |
| | 4,810 | 4,106 |
| (e) Lease payments included in the consolidated statement of comprehensive income | | |
| Included in cost of sales: | | |
| Minimum lease payments – operating lease | 3,651 | 3,376 |
| Included in marketing and administrative expenses: | | |
| Minimum lease payments – operating lease | 575 | 9 |
| | 4,226 | 3,385 |
| (f) Employee benefit expense | | |
| Wages, salaries and bonuses | 43,606 | 35,346 |
| Post-employment benefit provision | 5,627 | 9 |
| Long service leave provisions | (65) | 122 |
| Worker's compensation costs | 343 | 301 |
| Superannuation costs | 1,004 | 1,165 |
| Expense of share-based payments | 40 | 62 |
| | 50,555 | 37,005 |
| (g) Other expenses | | |
| Allowance for doubtful debts | 8 | 190 |
| | 8 | 190 |

| | Consolidated | |
|---|---------------|---------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| NOTE 4 | | |
| CASH AND SHORT-TERM DEPOSITS | | |
| (a) Reconciliation of cash | | |
| Cash balance comprises: | | |
| Cash at bank and on hand | 16,423 | 11,417 |
| Short-term deposits (under three months to maturity) | 9,515 | – |
| Closing cash balance per Consolidated Statement of Cash Flows | 25,938 | 11,417 |
| (b) Reconciliation of operating profit after income tax to the net cash flows from operations | | |
| Net profit | 28,160 | 7,546 |
| Adjustment for: | | |
| Depreciation, amortisation and impairment | 4,810 | 5,306 |
| Interest received | (282) | (56) |
| Profit on sale of building materials business | (5,037) | – |
| Share-based payments expense | 40 | 62 |
| Loss/(profit) on disposal of property, plant and equipment | – | 337 |
| Net loss/(gain) on foreign exchange | 119 | (65) |
| Realised gains on available-for-sale investments | – | (110) |
| Impairment of assets | 4,500 | 2,327 |
| Changes in assets and liabilities: | | |
| Decrease/(increase) in trade and other receivables | 1,825 | (4,462) |
| Decrease in inventories | 4,241 | 9,814 |
| Increase in prepayments | (24) | (414) |
| Increase in deferred income tax asset | (3,792) | (301) |
| (Decrease)/increase in trade and other payables | (3,884) | 2,734 |
| Increase in employee entitlement provisions through net profit | 7,096 | 553 |
| Increase/(decrease) in income tax payable | 8,630 | (1,401) |
| Increase in deferred tax liability through net profit | 881 | 9 |
| (Increase)/decrease in derivatives | (2,262) | 365 |
| Net cash flows from operating activities | 45,021 | 22,244 |
| (c) Bank facilities (refer note 20). | | |
| (d) Non-cash financing activities | | |
| During the current financial year plant costing \$2,940,000 (2017 – \$3,328,000) was subject to sale and leaseback finance. | | |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

| | Consolidated | |
|--|---------------------|---------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |

NOTE 5 INCOME TAX

The major components of income tax expense are:

Consolidated statement of comprehensive income

Current income tax

| | | |
|---|--------|-------|
| Current income tax charge | 13,711 | 3,585 |
| Adjustment in respect of current income tax of previous years | 110 | (782) |

Deferred income tax

| | | |
|---|---------|-------|
| Total deferred income tax recognised for the period | (3,588) | 440 |
| Income tax on discontinued operations relating to origination and reversal of temporary differences | (576) | 546 |
| Deferred tax recognised in consolidated statement of changes in equity | 692 | (732) |

| | | |
|---|--------|-------|
| Income tax expense reported in the consolidated statement of comprehensive income | 10,349 | 3,057 |
|---|--------|-------|

Consolidated statement of changes in equity

Deferred income tax related to items charged or credited directly to equity

| | | |
|--|-------|-----|
| Change in the estimated settlement of EPU's (refer note 27(c)) | (901) | – |
| Unrealised gain on available-for-sale investments | 209 | 732 |
| Income tax expense reported in equity | (692) | 732 |

A reconciliation between 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 tax from continuing operations | 34,264 | 11,884 |
|---|--------|--------|

| | | |
|--|--------|-------|
| At the Group's statutory income tax rate of 30% (2017 – 30%) | 10,279 | 3,565 |
| – overseas currency translation adjustment | (32) | 33 |
| – expenses not allowable for income tax purposes | 102 | 82 |
| – other items | (110) | 159 |
| – over-provision of current income tax of previous years | 110 | (782) |

| | | |
|---|--------|-------|
| Income tax expense reported in the consolidated statement of comprehensive income – continuing operations | 10,349 | 3,057 |
|---|--------|-------|

| | | |
|---|-----|-------|
| Income tax on discontinued operations relating to origination and reversal of temporary differences | 576 | (546) |
|---|-----|-------|

| | | |
|---|--------|-------|
| Total income tax expense reported in the consolidated statement of comprehensive income | 10,925 | 2,511 |
|---|--------|-------|

NOTE 5 INCOME TAX (CONTINUED)

Deferred income tax

Deferred income tax at 30 June relates to the following:

Consolidated

Deferred tax liabilities

| | | | | |
|--|---------|---------|-------|-------|
| Accelerated depreciation for tax purposes | 952 | 1,417 | 465 | 118 |
| Expenses deducted for income tax purposes but deferred for accounting purposes | 65 | 78 | 13 | 18 |
| Deferred gains and losses on foreign exchange contracts and translations | 50 | – | (50) | – |
| Income taken up for accounting purposes currently not assessable for income tax purposes | 136 | 101 | (35) | (32) |
| Unrealised gain on available-for-sale investments to fair value | 999 | 790 | (209) | (732) |
| Deferred gain for income tax purposes on rollover of freehold property | 1,265 | 1,265 | – | – |
| Gross deferred income tax liabilities | 3,467 | 3,651 | | |
| Offset | (1,077) | (1,465) | | |
| | 2,390 | 2,186 | | |

Consolidated

Deferred tax assets

| | | | | |
|--|---------|---------|-------|-------|
| Employee entitlements | 3,670 | 1,791 | 1,879 | (431) |
| Allowance for doubtful debts | 6 | 7 | (1) | (7) |
| Accelerated depreciation for accounting purposes | 1,381 | 258 | 1,123 | 156 |
| Deferred gains and losses on foreign exchange contracts and translations | – | 599 | (599) | (284) |
| Expenses not immediately deductible for income tax purposes | 537 | 560 | (23) | 309 |
| Lease liability deductible for income tax purposes | – | 2 | (2) | – |
| Deferred losses on interest rate swap contracts | 14 | 49 | (35) | (38) |
| Losses carried forward | 1,545 | 483 | 1,062 | 483 |
| Gross deferred income tax assets | 7,153 | 3,749 | | |
| Offset | (1,077) | (1,465) | | |
| | 6,076 | 2,284 | | |
| Deferred tax benefit/(expense) | | | 3,588 | (440) |

| Consolidated Statement of Financial Position | | Consolidated Statement of Comprehensive Income | |
|---|---------------|---|---------------|
| 2018 | 2017 | 2018 | 2017 |
| \$'000 | \$'000 | \$'000 | \$'000 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|--|------|--------------------------------|----------------|
|--|------|--------------------------------|----------------|

NOTE 6

DIVIDENDS PROVIDED FOR OR PAID

(a) Dividends paid

| | | | |
|--|----|-------|-------|
| Final 2017 – 14¢ per share paid in September 2017 (2017 – 13¢) | | 1,961 | 1,821 |
| Interim 2018 – 15¢ per share paid in March 2018 (2017 – 12¢) | | 2,097 | 1,680 |
| Fully-franked dividends paid by the Parent | | 4,058 | 3,501 |
| Dividend paid by controlled entity to minority shareholder fully-franked | 30 | 2,491 | 1,178 |
| Total fully-franked dividends paid | | 6,549 | 4,679 |

(b) Not recognised as a liability as at 30 June 2018

| | | | |
|--|----|-------|-------|
| Dividends on ordinary shares | | | |
| Final franked dividend for 2018 – 30¢ (2017 – 14¢) | 35 | 4,152 | 1,961 |

The dividends were declared subsequent to 30 June 2018

(c) The tax rate at which dividends have or will be franked is interim 30% (2017 – 30%), final 30% (2017 – 30%)

Franking account balance

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

The franking account balance disclosures have been calculated using the franking rate at 30 June 2018

| | | |
|---|---------|---------|
| Franking account balance brought forward | 4,391 | 2,158 |
| Fully-franked dividends paid | (1,739) | (1,501) |
| Tax paid | – | 1,239 |
| Franked dividends received from other corporations | 5,275 | 2,495 |
| Franking account balance at the end of the financial year | 7,927 | 4,391 |

Franking credits that will arise/(reduce) from the payment/(refund) of income tax payable/(refundable) as at the end of the financial year by the parent

| | |
|---|---|
| – | – |
|---|---|

Franking credits that will be available on payment/(refund) of income tax payable/(refundable) as at the end of the financial year by the parent

| | |
|-------|-------|
| 7,927 | 4,391 |
|-------|-------|

The above franking account is expressed on a tax paid basis

Fully-franked dividends which can be paid from the above franking credits available amount

| | |
|--------|--------|
| 18,496 | 10,246 |
|--------|--------|

NOTE 7

TRADE AND OTHER RECEIVABLES (CURRENT)

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|--------------------------------------|-------|--------------------------------|----------------|
| Trade debtors | (i) | 31,259 | 38,111 |
| Allowance for doubtful debts | (i) | (330) | (322) |
| | | 30,929 | 37,789 |
| Sundry debtors | (ii) | 8,988 | 5,874 |
| Contract work in progress receivable | (iii) | 2,845 | 967 |
| | | 42,762 | 44,630 |

Terms and conditions relating to the above financial instruments:

Collectability of trade receivables is reviewed on an ongoing basis at an operating unit level. Individual debts that are known to be uncollectible are written off when identified.

- (i) Trade debtors are non-interest bearing and generally on 30-day terms. An allowance for doubtful debts is made when there is objective evidence that a trade receivable is impaired. Financial difficulties of the debtor, default payments or debts more than 120 days overdue are considered objective evidence of impairment. An allowance of \$330,000 (2017 – \$322,000) has been recognised for the current year for specific debtors for which such evidence exists. The amount of the allowance has been measured as the difference between the carrying amount of the trade receivables and the estimated future cash flows expected to be received from the relevant debtors. Refer note 32(d) for credit risk disclosure.
- (ii) Sundry debtors and other receivables are non-interest bearing and have repayment terms between 30 and 90 days.

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|--|------|--------------------------------|----------------|
| Movement in allowance for doubtful debts | | | |
| At 1 July | | 322 | 132 |
| Provided during the year | | 8 | 190 |
| At 30 June | | 330 | 322 |

The carrying amount of the trade and other receivables approximates their fair value.

| | | | |
|--|--|----------|----------|
| (iii) Contract work in progress receivable | | | |
| Construction costs incurred to date: | | | |
| Gross cost plus profit recognised to date | | 14,577 | 11,812 |
| Less: Progress billings | | (12,155) | (11,051) |
| Net construction work in progress | | 2,422 | 761 |

Represented by:

| | | | |
|---|----|-------|-------|
| Amounts due to customers – trade and other payables | 17 | (423) | (206) |
| Amounts due from customers | | 2,845 | 967 |
| | | 2,422 | 761 |

NOTE 8

INVENTORIES

| | | |
|--|--------|--------|
| Work in progress – at cost | 9,521 | 13,147 |
| Finished goods – at cost | 7,455 | 11,104 |
| Finished goods – at net realisable value | – | 9 |
| Raw materials – at cost | 22,628 | 25,155 |
| | 39,604 | 49,415 |

Inventories recognised as an expense for the year ended 30 June 2018 totalled \$164,888,000 (2017 – \$179,926,000) for the Group, which includes inventory write-downs recognised as an expense totalling \$475,000 (2017 – \$1,394,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 9 PREPAYMENTS AND DEPOSITS

| | Consolidated 2018 \$'000 | 2017 \$'000 |
|-------------|--------------------------------|----------------|
| Prepayments | 2,065 | 2,127 |

Prepayments relate to insurance, raw materials and interest.

NOTE 10 OTHER FINANCIAL ASSETS (CURRENT)

| | | |
|---|-------|---|
| Short-term deposits (over 3 months to maturity) | 6,000 | – |
| | 6,000 | – |

| | | |
|--|----------------|----------------|
| | 2018 \$'000 | 2017 \$'000 |
|--|----------------|----------------|

NOTE 11 PARENT ENTITY INFORMATION

Information relating to Schaffer Corporation Limited:

| | | |
|---|--------|--------|
| Current assets | 16,631 | 826 |
| Total assets | 59,576 | 44,537 |
| Current liabilities | 1,512 | 11,496 |
| Total liabilities | 22,595 | 23,942 |
| Issued capital | 13,804 | 15,847 |
| Retained earnings | 20,728 | 2,350 |
| Share-based payments reserve – SFC options | 132 | 115 |
| Net unrealised gains reserve | 32 | – |
| Asset revaluation reserve | 2,283 | 2,283 |
| Total shareholders' equity | 36,979 | 20,595 |
| Profit of the parent entity | 22,436 | 4,704 |
| Total other comprehensive income of the parent entity | 32 | – |

The parent entity has entered into Deeds of Cross Guarantee with controlled entities as disclosed in note 12.

Tax consolidation

The Company and its wholly-owned Australian resident subsidiaries have formed a tax-consolidated group with effect from 1 July 2003 and are therefore taxed as a single entity from that date. The head entity within the tax-consolidated group is Schaffer Corporation Limited.

Members of the Group have entered into a tax sharing agreement that provides for the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations. No amounts have been recognised in the financial statements in respect of this agreement on the basis that the possibility of default is remote.

Tax expense/income, deferred tax liabilities and deferred tax assets arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using the group allocation approach. Current tax liabilities and assets and deferred tax assets arising from unused tax losses and tax credits of the members of the tax-consolidated group are recognised by the Company (as head entity in the tax-consolidated group).

Due to the existence of a tax funding arrangement between the entities in the tax-consolidated group, amounts are recognised as payable to or receivable by the Company and each member of the Group in relation to the tax contribution amounts paid or payable between the parent entity and the other members of the tax-consolidated group in accordance with the arrangement.

NOTE 11 PARENT ENTITY INFORMATION (CONTINUED)

Tax consolidation contributions by (or distributions to) equity participants

The net amount recognised for the period under tax consolidation contributions by (or distributions to) equity participants, its major components and the accounts affected are as follows:

| | 2018 \$'000 | 2017 \$'000 |
|---|----------------|----------------|
| Major components of tax consolidation contributions by (or distributions to) equity participants | | |
| Net assumptions of tax liabilities of members of the tax-consolidated group | (35) | 57 |
| Tax funding contribution receivable from controlled entities | 35 | (57) |
| Excess of tax funding contributions over tax liabilities assumed | – | – |

NOTE 12 CONTROLLED ENTITIES

| Controlled entity | Beneficial percentage held by the Group | | Place of incorporation and business | Principle Activities |
|--|---|-----------|-------------------------------------|---|
| | 2018 % | 2017 % | | |
| Schaffer Properties Pty Ltd* | 100 | 100 | Australia | Property investments |
| Delta Corporation Limited* | 100 | 100 | Australia | Precast concrete manufacture |
| Garden Holdings Pty Ltd* (formerly Urbanstone Pty Ltd) | 100 | 100 | Australia | Inactive |
| Gosh Holdings Pty Ltd | 83.17 | 83.17 | Australia | Holding company |
| Gosh Capital Pty Ltd | 83.17 | 83.17 | Australia | Property and other investments |
| Howe Automotive Limited** | 83.17 | 83.17 | Australia | Parent company of Howe Group |
| Rosedale Leather Pty Ltd** | 83.17 | 83.17 | Australia | Inactive |
| Australian Leather Upholstery Pty Ltd** | 83.17 | 83.17 | Australia | Holding company |
| Howe & Company Pty Ltd** | 83.17 | 83.17 | Australia | Manufacture and sale of cut automotive leather components |
| Howe Slovensko S.R.O. | 83.17 | 83.17 | Slovakia | Contract manufacture of cut automotive leather components |
| Howe Leather (Shanghai) Co. Ltd*** | 83.17 | 83.17 | China | Manufacture and sale of cut automotive leather components |
| Howe Hong Kong Pty Limited | 83.17 | 83.17 | Hong Kong | Holding company |

* Pursuant to the ASIC Corporations (Wholly-owned Companies) Instrument 2016/785 relief has been granted to various controlled entities from the Corporations Act 2001 requirements for preparation, audit and lodgement of their financial reports. As a condition of the Instrument, Schaffer Corporation Limited and the controlled entities subject to the Instrument (the Schaffer 'Closed Group') entered into Deeds of Cross Guarantee at various dates. The effect of the deeds is that Schaffer Corporation Limited has guaranteed to pay any deficiency in the event of winding up of the controlled entities. The controlled entities have also given a similar guarantee in the event that Schaffer Corporation Limited is wound up.

** Pursuant to the ASIC Corporations (Wholly-owned Companies) Instrument 2016/785 relief has been granted to various controlled entities from the Corporations Act 2001 requirements for preparation, audit and lodgement of their financial reports. As a condition of the Instrument, Howe Automotive Limited and the controlled entities subject to the Instrument (the Howe Automotive 'Closed Group') entered into Deeds of Cross Guarantee at various dates. The effect of the deeds is that Howe Automotive Limited has guaranteed to pay any deficiency in the event of winding up of the controlled entities. The controlled entities have also given a similar guarantee in the event that Howe Automotive Limited is wound up.

*** Howe Leather (Shanghai) Co. Ltd has a 1 January to 31 December financial year to coincide with local tax and statutory reporting requirements. Financial statements for this subsidiary are prepared and audited for the year to 30 June for the purposes of Group consolidation. All other entities have 1 July to 30 June financial years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 12 CONTROLLED ENTITIES (CONTINUED)

The Consolidated Statement of Financial Performance and Consolidated Statement of Financial Position of the entities which are members of the Schaffer 'Closed Group' are as follows:

| | Schaffer Closed Group | |
|---|-----------------------|---------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| CONSOLIDATED STATEMENT OF FINANCIAL PERFORMANCE AND RETAINED EARNINGS RECONCILIATION | | |
| Profit from continuing operations before income tax | 9,897 | 1,796 |
| Income tax expense | 1,651 | 1,529 |
| Net profit for the year | 11,548 | 3,325 |
| Other comprehensive income | 32 | – |
| Total comprehensive income | 11,580 | 3,325 |
| Retained earnings at the beginning of the year | 23,612 | 23,788 |
| Net profit for the year | 11,548 | 3,325 |
| Dividends provided for or paid | (4,058) | (3,501) |
| Retained earnings at the end of the year | 31,102 | 23,612 |
| CONSOLIDATED STATEMENT OF FINANCIAL POSITION | | |
| ASSETS | | |
| Current assets | | |
| Cash and short-term deposits | 11,216 | 2,845 |
| Trade and other receivables | 5,714 | 6,704 |
| Inventories | 1,621 | 7,895 |
| Other financial assets | 6,000 | – |
| Prepayments and deposits | 419 | 528 |
| | 24,970 | 17,972 |
| Non-current assets classified as held for sale | – | 4,254 |
| Total current assets | 24,970 | 22,226 |
| Non-current assets | | |
| Other financial assets | 19,780 | 14,598 |
| Property, plant and equipment | 8,906 | 20,538 |
| Investment properties | 17,579 | 14,144 |
| Goodwill | 84 | 84 |
| Deferred income tax assets | 3,538 | 1,900 |
| Total non-current assets | 49,887 | 51,264 |
| Total assets | 74,857 | 73,490 |
| LIABILITIES | | |
| Current liabilities | | |
| Trade and other payables | 4,137 | 4,714 |
| Interest bearing loans and borrowings | 7 | 13,635 |
| Derivative financial instruments | 46 | 165 |
| Provisions | 1,853 | 3,541 |
| | 6,043 | 22,055 |
| Non-current liabilities classified as held for sale | – | 5 |
| Total current liabilities | 6,043 | 22,060 |
| Non-current liabilities | | |
| Interest bearing loans and borrowings | 19,067 | 7,086 |
| Provisions | 1,144 | 1,237 |
| Total non-current liabilities | 20,211 | 8,323 |
| Total liabilities | 26,254 | 30,383 |
| Net assets | 48,603 | 43,107 |
| EQUITY | | |
| Issued capital | 14,752 | 16,795 |
| Reserves | 2,749 | 2,700 |
| Retained profits | 31,102 | 23,612 |
| Total equity | 48,603 | 43,107 |

NOTE 12 CONTROLLED ENTITIES (CONTINUED)

MATERIAL PARTLY-OWNED SUBSIDIARIES

Accumulated profit balances of material non-controlling interest:

| | Howe Automotive Ltd | Gosh Holdings Pty Ltd |
|---|---------------------|-----------------------|
| | \$'000 | \$'000 |
| 2018 | 9,820 | 1,904 |
| 2017 | 7,567 | 1,753 |
| Profit allocated to material non-controlling interest: | | |
| 2018 | 4,794 | 74 |
| 2017 | 1,608 | 82 |

Summarised statement of profit or loss for the year ended 30 June 2018

| | Howe Automotive Ltd | Gosh Holdings Pty Ltd |
|---|---------------------|-----------------------|
| | \$'000 | \$'000 |
| Revenue | 203,382 | 1,358 |
| Profit before tax and finance costs | 42,071 | 795 |
| Finance costs | (1,134) | (212) |
| Profit before tax | 40,937 | 583 |
| Income tax | (12,429) | (147) |
| Profit for the year | 28,508 | 436 |
| Other comprehensive income | 855 | 456 |
| Total comprehensive income | 29,363 | 892 |
| Attributable to non-controlling interests | 4,942 | 151 |
| Dividends paid to non-controlling interests | 2,491 | – |

Summarised statement of profit or loss for the year ended 30 June 2017

| | Howe Automotive Ltd | Gosh Holdings Pty Ltd |
|---|---------------------|-----------------------|
| | \$'000 | \$'000 |
| Revenue | 170,906 | 1,352 |
| Profit before tax and finance costs | 12,653 | 903 |
| Finance costs | (1,739) | (206) |
| Profit before tax | 10,914 | 697 |
| Income tax | (3,071) | (209) |
| Profit for the year | 7,843 | 488 |
| Other comprehensive income/(loss) | (118) | 1,707 |
| Total comprehensive income | 7,725 | 2,195 |
| Attributable to non-controlling interests | 1,300 | 369 |
| Dividends paid to non-controlling interests | 1,178 | – |

Summarised statement of financial position at 30 June 2018

| | Howe Automotive Ltd | Gosh Holdings Pty Ltd |
|--------------------------|---------------------|-----------------------|
| | \$'000 | \$'000 |
| Current assets | 92,591 | 269 |
| Non-current assets | 23,559 | 19,661 |
| Current liabilities | (45,729) | (119) |
| Non-current liabilities | (12,073) | (8,510) |
| Total equity | 58,348 | 11,301 |
| Attributable to: | | |
| Equity holders of parent | 48,528 | 9,397 |
| Non-controlling interest | 9,820 | 1,904 |

Summarised statement of financial position at 30 June 2017

| | Howe Automotive Ltd | Gosh Holdings Pty Ltd |
|--------------------------|---------------------|-----------------------|
| | \$'000 | \$'000 |
| Current assets | 88,876 | 957 |
| Non-current assets | 20,308 | 17,828 |
| Current liabilities | (35,702) | (182) |
| Non-current liabilities | (29,697) | (8,292) |
| Total equity | 43,785 | 10,411 |
| Attributable to: | | |
| Equity holders of parent | 36,416 | 8,658 |
| Non-controlling interest | 7,369 | 1,753 |

Summarised cash flow information for the year ending 30 June 2018

| | Howe Automotive Ltd | Gosh Holdings Pty Ltd |
|--|---------------------|-----------------------|
| | \$'000 | \$'000 |
| Operating | 45,316 | 509 |
| Investing | (4,251) | (1,212) |
| Financing | (35,117) | 50 |
| Net increase in cash and cash equivalents | 5,948 | (653) |

Summarised cash flow information for the year ending 30 June 2017

| | Howe Automotive Ltd | Gosh Holdings Pty Ltd |
|--|---------------------|-----------------------|
| | \$'000 | \$'000 |
| Operating | 24,235 | 644 |
| Investing | (3,066) | (18) |
| Financing | (16,029) | 23 |
| Net increase in cash and cash equivalents | 5,140 | 649 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 13 PROPERTY, PLANT AND EQUIPMENT

| | Consolidated | |
|---|---------------------|---------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Freehold land | | |
| At cost | 1,698 | 2,986 |
| Buildings on freehold land | | |
| At cost | 12,496 | 17,625 |
| Accumulated depreciation | (4,998) | (6,828) |
| | 7,498 | 10,797 |
| Leasehold quarries | | |
| At cost | – | 5,250 |
| Accumulated depreciation | – | (2,330) |
| | – | 2,920 |
| Leasehold improvements | | |
| At cost | – | 1,044 |
| Accumulated amortisation | – | (872) |
| | – | 172 |
| Net carrying amount of land and buildings | 9,196 | 16,875 |
| Plant and equipment | | |
| At cost | 41,652 | 57,783 |
| Accumulated depreciation | (34,444) | (42,790) |
| Net carrying amount | 7,208 | 14,993 |
| Plant and equipment under lease and hire purchase | | |
| At cost | 14,552 | 11,832 |
| Accumulated amortisation | (3,311) | (2,156) |
| | 11,241 | 9,676 |
| Net carrying amount of plant and equipment | 18,449 | 24,669 |
| Total property, plant and equipment | | |
| At cost | 70,398 | 96,520 |
| Accumulated depreciation and amortisation | (42,753) | (54,976) |
| Total net carrying amount of property, plant and equipment | 27,645 | 41,544 |
| Less property, plant and equipment classified as held for sale | – | (4,254) |
| Total property, plant and equipment not classified as held for sale | 27,645 | 37,290 |

The Directors do not consider there is any impairment loss on property, plant or equipment at 30 June 2018 apart from amounts already provided for during the year.

Assets pledged as security

Included in the balances of property, plant and equipment are assets over which charges have been granted as security over bank facilities (refer notes 18 and 20). The terms of the charges preclude the assets being sold or being used as security for further charges without the permission of the charge holders. The charges also require buildings that form part of the security to be fully insured at all times. Assets under lease are pledged as security for the associated lease liabilities (refer notes 18 and 20).

NOTE 13 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

The carrying values of assets pledged as security are:

| | Consolidated | |
|--|---------------------|---------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Property, plant and equipment | 19,492 | 41,544 |
| Reconciliations of the carrying amounts | | |
| Freehold land | | |
| Carrying amount at beginning | 2,986 | 2,986 |
| Reclassification to investment property | (413) | – |
| Disposal of building materials business | (875) | – |
| | 1,698 | 2,986 |
| Buildings on freehold land | | |
| Carrying amount at beginning | 10,797 | 11,360 |
| Impairment write down | – | (200) |
| Reclassification to investment property | (2,998) | – |
| Additions | – | 37 |
| Depreciation expense | (301) | (400) |
| | 7,498 | 10,797 |
| Leasehold quarries | | |
| Carrying amount at beginning | 2,920 | 4,905 |
| Impairment write down | – | (1,976) |
| Disposal of building materials business | (2,920) | – |
| Amortisation expense | – | (9) |
| | – | 2,920 |
| Leasehold improvements | | |
| Carrying amount at beginning | 172 | 352 |
| Impairment write down | – | (151) |
| Disposal of building materials business | (172) | – |
| Amortisation expense | – | (29) |
| | – | 172 |
| Net carrying amount of land and buildings | 9,196 | 16,875 |
| Plant and equipment | | |
| Carrying amount at beginning | 14,993 | 19,292 |
| Additions | 5,575 | 3,393 |
| Transfers to leased plant | (2,461) | (3,859) |
| Depreciation expense | (2,445) | (3,112) |
| Impairment write down | (4,500) | – |
| Foreign currency translation adjustment | 256 | (32) |
| Disposals of building materials business | (4,210) | – |
| Disposals | – | (689) |
| | 7,208 | 14,993 |
| Plant and equipment under lease | | |
| Carrying amount at beginning | 9,676 | 7,243 |
| Additions | – | – |
| Transfer from plant and equipment | 2,461 | 3,859 |
| Depreciation expense | (1,378) | (1,165) |
| Foreign currency translation adjustment | 482 | (21) |
| Disposals | – | (240) |
| | 11,241 | 9,676 |
| Total carrying amount of plant and equipment | 18,449 | 24,669 |

Note

(a)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 13

PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

(a) The carrying values of cash generating units are reviewed for impairment at each reporting date, with recoverable amount being estimated when events or changes in circumstances indicate the carrying value may be impaired. The Delta precast cash-generating unit, included in the building material segment incurred a loss for the half-year to 31 December 2017, so an impairment assessment was conducted.

The recoverable amount of a cash generating unit is the greater of fair value less costs of disposal and value in use. 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. The Delta value in use model is a 5-year model and assumes revenue growth excluding CPI of 1.8%, pre-tax discount rate of 14% (June 2017: 14%) and a termination multiple of 6 times EBITDA. An oversupply created by competitors in the West Australian precast market has intensified competition and eroded margins, so the anticipated gross margin assumption has been reduced.

An impairment exists when the carrying value of an asset or cash-generating units exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount. The outcome of the Delta impairment assessment was that the carrying value of the Delta precast cash generating unit assets exceeded the recoverable value of \$11,418,000 by \$4,500,000. The Delta cash-generating unit property, plant and equipment were written down by this amount at 31 December 2017. At 30 June 2018, no additional impairment triggers were identified.

| | Consolidated | |
|--|--------------|--------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |

NOTE 14

INVESTMENT PROPERTIES

Land and buildings

| | | |
|--------------------------|---------------|---------------|
| At cost | 33,300 | 27,563 |
| Accumulated depreciation | (6,532) | (4,130) |
| | 26,768 | 23,433 |

Improvements

| | | |
|--------------------------|--------------|--------------|
| At cost | 4,284 | 4,203 |
| Accumulated depreciation | (2,374) | (2,230) |
| | 1,910 | 1,973 |

Total

| | | |
|--|---------------|---------------|
| At cost | 37,584 | 31,766 |
| Accumulated depreciation | (8,906) | (6,360) |
| Net carrying amount of investment properties | 28,678 | 25,406 |

Investment properties are recognised at cost less accumulated depreciation. The fair value of the investment property at 30 June 2018 as estimated by Directors is \$100,243,000 (2017 \$70,059,000) based on valuations not older than 2 years by certified independent valuers who hold recognised and relevant professional qualifications and licenses, and who specialise in valuing these types of investment properties. Valuers have carried out inspections of the properties and undertaken market research with respect to available sales and rental evidence.

| | Consolidated | |
|--|--------------|--------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |

| | | |
|---|-------------------|--------------|
| Rental income derived from investment properties | 5,559 | 5,275 |
| Direct operating expenses (including repairs and maintenance) generating rental income (included in cost of sales) | (2,708) | (2,717) |
| Direct operating expenses (including repairs and maintenance) that did not generate rental income (included in cost of sales) | (120) | (124) |
| Profit arising from investment properties carried at cost | 3(a) 2,731 | 2,434 |

NOTE 14

INVESTMENT PROPERTIES (CONTINUED)

Valuers used the following approaches when assessing properties in accordance with the specific characteristics of the property and availability of market evidence:

For leased offices and retail properties – a combination of the capitalisation and discounted cash flow (DCF) approach.

The capitalisation approach capitalises the assessed net market income at an appropriate market yield to establish the fully leased value of the property. Appropriate adjustments are then made to reflect the specific cash flow profile and the general characteristics of the property.

The DCF approach involves the discounting of the net cash flows over an assumed cash flow period of 10 years at an appropriate rate to reflect risk to derive a market value. Inputs to the calculations are discount rate percentage (range 7.8% to 10.5%), terminal yield percentage, acquisition costs, disposal costs, market rental escalation percentage (range 2.0% per annum to 3.8% per annum), ongoing capital expenditure, tenant retention profile, and lease renewal fees. Where relevant, valuers have used a combination of the capitalisation and discounted cash flow approach when assessing the Group's investment properties.

For vacant land – the market comparison approach which involves the analysis of the comparable sales evidence on a rate per square metre of land area, making adjustments for any varying points of difference in order to assess an appropriate market value. The valuation takes into account current zoning, approved uses and the potential for a higher use/zoning.

The approaches for the valuation of the Group's investment properties are classified as Level 3 as the fair value is estimated using inputs that are not based on observable market data.

| |
|--|
| Valuation technique non-market observable inputs (Level 3) |
|--|

| | |
|---|----------------|
| Valuation approach | \$'000 |
| Capitalisation and discounted cash flow | 56,648 |
| Market comparison | 43,595 |
| | 100,243 |

Assets pledged as security

Included in the balances of investment properties are assets over which first mortgages have been granted as security over bank loans (refer note 20). The terms of the first mortgages preclude the assets being sold or being used as security for further mortgages without the permission of the first mortgage holder. The mortgage also requires investment properties that form part of the security to be fully insured at all times.

| | Consolidated | |
|--|--------------|--------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |

| | | |
|--|---------------|---------------|
| The carrying values of assets pledged as security are: | | |
| Investment properties | 19,433 | 23,536 |

Reconciliations of the carrying amounts

Land and buildings

| | | |
|---|---------------|---------------|
| Carrying amount at beginning | 23,433 | 23,260 |
| Reclassification to investment property | 3,411 | – |
| Additions | 470 | 588 |
| Depreciation expense | (546) | (415) |
| Total carrying amount | 26,768 | 23,433 |

Improvements

| | | |
|--|---------------|---------------|
| Carrying amount at beginning | 1,973 | 1,917 |
| Additions | 77 | 232 |
| Disposal of interest in joint operations | – | – |
| Depreciation expense | (140) | (176) |
| Total carrying amount | 1,910 | 1,973 |
| Total carrying amount of investment properties | 28,678 | 25,406 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 15 GOODWILL

Goodwill at cost

(a) Carrying amount of goodwill, allocated to each of the cash generating units

| | Automotive Leather | Investment Properties | Total |
|---------------------|-----------------------|--------------------------|---------------|
| Consolidated | \$'000 | \$'000 | \$'000 |
| 2018 | 1,215 | 84 | 1,299 |
| 2017 | 1,215 | 84 | 1,299 |

Goodwill is not amortised but is subject to impairment testing.

(b) Impairment testing of goodwill

Goodwill acquired through business combinations has been allocated to two individual cash generating units, which are reportable segments, for impairment testing as follows:

- Automotive Leather
- Investment Property

Automotive Leather

The recoverable amount of the Leather unit has been determined based on a value in use calculation using both historical performance and future cash flow projections based on volume forecasts for awarded programmes and budget projections approved by senior management related to specific circumstances for this cash generating unit. Key assumptions include a pre-tax discount rate of 14%, expected revenue and margins. Management did not identify an impairment for this cash generating unit.

Investment Property

The recoverable amount of the Investment Property portfolio has been determined based on a fair value less costs of disposal, supported by independent property valuations of the underlying properties, which are typically reviewed at least every three years (refer to note 14). Management did not identify an impairment for this cash generating unit.

NOTE 16 OTHER FINANCIAL ASSETS (NON-CURRENT)

Available for sale investments at fair value

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|-----------------------------------|------|---|------------------------------|
| Units in property unit trusts (a) | (a) | 5,635 | 3,995 |
| Units in managed equity funds | | 5,248 | 250 |
| Listed shares | | 2,850 | 2,375 |
| | | 13,733 | 6,620 |

(a) Units and shares in property investments consists of units in four property unit trusts and shares in an unlisted residential land development company, each with no fixed rate of return. Fair value of the units and shares is determined by the calculation of the Group's percentage ownership multiplied by the total net assets of the unit trust or company at fair value.

NOTE 17 TRADE AND OTHER PAYABLES (CURRENT)

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|--|------|---|------------------------------|
| Trade creditors | | 28,009 | 31,509 |
| Goods and services tax (net) | | 128 | 425 |
| Other creditors | | 334 | 295 |
| Amounts due to customers – contract work in progress | 7 | 423 | 206 |
| | | 28,894 | 32,435 |

The carrying value of all trade and other payables approximates their fair values.

Terms and conditions relating to the above financial instruments:

All current payables are non-interest bearing and are normally settled on 30-day terms.

NOTE 18 INTEREST BEARING LOANS AND BORROWINGS (CURRENT)

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|--|------|---|------------------------------|
| Cash advances/commercial bills – secured | (a) | – | 1,500 |
| Lease liability – secured | (b) | 2,356 | 1,865 |
| Bank loan – secured | (c) | – | 11,990 |
| | | 2,356 | 15,355 |

The fair value of the above approximates the carrying value.

(a) The facility expired on 31 August 2017 and was not renewed.

(b) Finance leases have an average term of 5 years. The average discount rate implicit in the leases is 2.00% per annum (2017 – 2.73% per annum).

(c) Bank loans (refer note 20(a)).

For details of financing facilities available refer to note 20.

NOTE 19 PROVISIONS (CURRENT)

| | | | |
|-----------------------|-------|---------------|-------|
| Employee entitlements | 27(a) | 10,600 | 7,892 |
|-----------------------|-------|---------------|-------|

NOTE 20 INTEREST BEARING LOANS AND BORROWINGS (NON-CURRENT)

| | | | |
|---------------------------|-----|---------------|---------------|
| Bank loan – secured | (a) | 19,067 | 7,072 |
| Lease liability – secured | (b) | 5,767 | 5,059 |
| Government loan – secured | (c) | – | 10,000 |
| Commercial bills | (d) | 6,060 | 6,060 |
| Revolving loan facility | (e) | – | 11,668 |
| | | 30,894 | 39,859 |

The fair value of the above approximates the carrying value.

(a) Bank loans

The bank loans are secured by a first registered mortgage over all the assets and undertakings of undivided interests in property syndicates. Included in bank loans is the consolidated entity's share of joint operations borrowings.

| Maturity Date | Interest Rate | Group's Share of Loans at 30 June 2018 | | Carrying Value of Assets pledged as Security \$'000 |
|---------------|----------------|---|-----------------------|---|
| | | Current \$'000 | Non-current \$'000 | |
| Jul 2019 | 6.31% Variable | – | 976 | 1,572 |
| Oct 2019 | 4.05% Variable | – | 3,536 | |
| Oct 2019 | 3.95% Fixed* | – | 3,536 | 1,836 |
| Dec 2020 | 6.56% Fixed | – | 3,841 | 2,344 |
| Feb 2021 | 3.62% Variable | – | 7,178 | 6,142 |
| | | – | 19,067 | 11,894 |

| Maturity Date | Interest Rate | Group's Share of Loans at 30 June 2017 | | Carrying Value of Assets pledged as Security \$'000 |
|---------------|----------------|---|-----------------------|---|
| | | Current \$'000 | Non-current \$'000 | |
| Jul 2017 | 6.52% Variable | 971 | – | 1,567 |
| Dec 2017 | 6.56% Fixed* | 3,841 | – | 2,315 |
| Feb 2018 | 2.99% Variable | 4,125 | – | |
| Feb 2018 | 4.70% Fixed* | 3,053 | – | 6,273 |
| Oct 2019 | 3.78% Variable | – | 7,072 | 1,802 |
| | | 11,990 | 7,072 | 11,957 |

*Fixed Interest Rate loans are variable interest rate loans hedged with a corresponding interest rate swap at a fixed interest rate for the term of the loan.

(b) Finance leases

Finance leases have an average lease term of 5 years. The average discount rate implicit in the leases is 2.00% per annum (2017 – 2.73% per annum). The lease liability is secured by a charge over the leased assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 20 INTEREST BEARING LOANS AND BORROWINGS (NON-CURRENT) (CONTINUED)

(c) Government loan

During the 2012 financial year, the Government of Australia entered into a new Loan Agreement with Howe Automotive Ltd and Howe & Company Pty Ltd, controlled entities of Schaffer Corporation Limited, to the value of \$25,000,000. The loan was drawn down on 1 February 2012 which coincided with the expiry of the previous Government Loan agreements. The loan was repayable in equal instalments over 10 years and is subject to an interest rate of 425 basis points above the indicator rate for 10-year Commonwealth bonds. The loan was repaid early and in full during the financial year.

(d) Commercial bills

During the 2014 financial year, the Group established a commercial bill facility to fund the acquisition of an investment property by the Gosh Capital division. The facility is 100% secured by the property acquired and has an expiry date of 31 December 2019. The effective interest rate is 3.56% (2017 – 3.22%).

(e) Revolving Loan Facility

Howe Automotive has a Revolving Loan facility with a maturity date of 30 September 2019, to be available for working capital requirements. The facility limit at 30 June 2018 was €13,000,000 and the interest rate is bank bill rate plus a margin. The amount available to draw down is limited to 80% of total working capital of all Howe Automotive subsidiaries, excluding Howe Shanghai, and also excluding all receivables past 30 days overdue, uninsured receivables, and obsolete inventory. At 30 June 2018, drawings from this facility amounted to €Nil (2017 – €7,836,000). The facility limit reduces by €1,995,000 within 12 months.

Under the facility agreement, Howe Automotive has granted first priority security up to \$20,000,000 over all of its assets and undertakings, with the exclusion of Howe Shanghai.

Financing facilities available

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|---|------|--------------------------------|----------------|
| <i>Financing facilities used and available</i> | | | |
| At reporting date, the following financing facilities had been negotiated and were available: | | | |
| Total facilities | | | |
| – bank overdraft | | – | 500 |
| – banker's undertakings | | 8,280 | 9,450 |
| – cash advances | | – | 8,000 |
| – finance leases | | 8,123 | 8,788 |
| – bank loans | | 19,067 | 19,062 |
| – revolving loan facility | | 20,431 | 16,379 |
| – government loan | | – | 10,000 |
| – commercial bills | | 6,060 | 6,060 |
| | | 61,961 | 78,239 |

Facilities used at reporting date

| | | | |
|---------------------------|-------|---------------|---------------|
| – bank overdraft | | – | – |
| – banker's undertakings | 26(c) | 7,169 | 7,662 |
| – cash advances | | – | 1,500 |
| – finance leases | | 8,123 | 6,924 |
| – bank loans | | 19,067 | 19,062 |
| – revolving loan facility | | – | 11,668 |
| – government loan | | – | 10,000 |
| – commercial bills | | 6,060 | 6,060 |
| | | 40,419 | 62,876 |

Facilities unused at reporting date

| | | | |
|---------------------------|--|---------------|---------------|
| – bank overdraft | | – | 500 |
| – banker's undertakings | | 1,111 | 1,788 |
| – cash advances | | – | 6,500 |
| – finance leases | | – | 1,864 |
| – bank loans | | – | – |
| – revolving loan facility | | 20,431 | 4,711 |
| – government loan | | – | – |
| – commercial bills | | – | – |
| | | 21,542 | 15,363 |

Total facilities

| | | | |
|-------------------------------------|--|---------------|---------------|
| Facilities used at reporting date | | 40,419 | 62,876 |
| Facilities unused at reporting date | | 21,542 | 15,363 |
| | | 61,961 | 78,239 |

The Group has complied with all covenants in relation to the above facilities at all times during the year.

| | Note | Consolidated 2018 \$'000 | 2017 \$'000 |
|--|------|--------------------------------|----------------|
|--|------|--------------------------------|----------------|

NOTE 21 PROVISIONS (NON-CURRENT)

| | | | |
|--|-------|--------------|--------------|
| Employee entitlements | 27(a) | 7,455 | 1,270 |
| Less employee entitlements classified as held for sale | | – | (5) |
| | | 7,455 | 1,265 |

NOTE 22 CONTRIBUTED EQUITY

a) Issued and paid up capital

As at 30 June 2018

13,840,878 ordinary fully paid shares
(2017 – 14,005,373)

14,540 16,583

| | 2018 Number of shares | \$'000 | 2017 Number of shares | \$'000 |
|--|-----------------------------|--------|-----------------------------|--------|
|--|-----------------------------|--------|-----------------------------|--------|

b) Movement in ordinary shares on issue

| | | | | |
|---|-------------------|---------------|-------------------|---------------|
| At the beginning of the financial year | 14,005,373 | 16,583 | 14,005,373 | 16,583 |
| Shares acquired under a share buy-back scheme | (164,495) | (2,043) | – | – |
| At the end of the financial year | 13,840,878 | 14,540 | 14,005,373 | 16,583 |

For details of movement in options and details of employee share options plan refer to note 25 and 27.

c) Terms and conditions of contributed equity

Ordinary shares

Ordinary shares have the right to receive dividends as declared and, in the event of winding up the company, to participate in the proceeds from the sale of all surplus assets in proportion to the number of and amounts paid up on shares held. Ordinary shares entitle their holder to one vote, either in person or by proxy, at a meeting of the company.

Share options

The Company has a share-based payment option scheme under which options to subscribe for the company's shares can be granted to certain executives and other employees (refer note 27).

The share option holders carry no rights to dividends and no voting rights.

| | Consolidated 2018 \$'000 | 2017 \$'000 |
|--|--------------------------------|----------------|
|--|--------------------------------|----------------|

NOTE 23 RESERVES AND RETAINED PROFITS

Reserves

| | | |
|--------------------------------------|--------------|--------------|
| Asset revaluation | 2,585 | 2,585 |
| Share-based payment – EPU's | (1,082) | 771 |
| Share-based payment – SFC options | 132 | 115 |
| Net unrealised gains reserve | 1,942 | 1,531 |
| Foreign currency translation reserve | 644 | (67) |
| | 4,221 | 4,935 |

Nature and purpose of reserve

Asset revaluation

The asset revaluation reserve was used to record increments and decrements in the value of non-current assets prior to the adoption of Australian Equivalents to International Reporting Standards with effect from 1 July 2005. Currently the accounting policy is to record all assets at cost. The reserve can be used to pay dividends in limited circumstances.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 23 RESERVES AND RETAINED PROFITS (CONTINUED)

Share-based payment – EPU's

This reserve is used to record the value of EPU's provided to employees and directors as part of their remuneration. Refer to note 27(c) for further details of this plan.

Share-based payment – SFC options

This reserve represents the amount expensed for the value of options issued. Refer to note 27(b) for further details of this plan.

Foreign currency translation reserve

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Net unrealised gains reserve

The net unrealised gains reserve is used to record increments and decrements in the fair value of available-for-sale investments net of tax.

| | Consolidated | |
|---|---------------------|----------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Retained profits | | |
| Balance 1 July | 52,867 | 50,512 |
| Net profit attributable to members of the parent entity | 23,292 | 5,856 |
| Dividends provided for or paid | (4,058) | (3,501) |
| Balance 30 June | 72,101 | 52,867 |

NOTE 24 AUDITORS REMUNERATION

Amounts received or due and receivable by Ernst & Young (Australia) for an audit or review of the financial report of the parent and any other entity in the consolidated group.

| | | |
|---|----------------|----------------|
| – Ernst & Young Australia | 176,801 | 190,524 |
| – Ernst & Young Slovakia | 35,000 | 29,737 |
| Other services – tax compliance, research and development claims. | 101,092 | 108,990 |
| | 312,893 | 329,251 |

Amounts received or due and receivable by non-Ernst & Young audit firms for audit services.

| | | |
|--|---------------|---------------|
| | 12,000 | 12,000 |
|--|---------------|---------------|

NOTE 25 DIRECTORS AND EXECUTIVES DISCLOSURES

(a) Details of Key Management Personnel (KMP)

(i) *Remuneration of Key Management Personnel*
Refer to Remuneration Report in the Directors' Report

(ii) *Remuneration by category: Key Management Personnel*

| | Consolidated | |
|----------------------|---------------------|------------------|
| | 2018 | 2017 |
| | \$ | \$ |
| Short term | 4,792,291 | 3,383,156 |
| Long term incentives | 35,411 | 231,282 |
| Share based payments | 16,685 | 67,824 |
| Post-employment | 2,458,177 | 453,872 |
| | 7,302,564 | 4,136,134 |

(b) Option holdings of Key Management Personnel 30 June 2018

| | Balance at 30 June 2017 | Granted as remuneration | Options exercised | Balance at end of period | Vested as at 30 June 2018 | | |
|-------------------|-------------------------|-------------------------|-------------------|--------------------------|---------------------------|-----------------|---------------|
| | | | | | Total | Not exercisable | Exercisable |
| Executives | | | | | | | |
| R Leib | – | 50,000 | – | 50,000 | 12,500 | – | 12,500 |
| J M Cantwell | – | 20,000 | – | 20,000 | 5,000 | – | 5,000 |
| Total | – | 70,000 | – | 70,000 | 17,500 | – | 17,500 |

There have been no other transactions concerning shares between entities in the reporting entity and directors of the reporting entity or their related entities. Disclosure on the EPU holdings of Key Management Personnel are included at Note 29(b).

NOTE 26 CONTINGENT LIABILITIES AND EXPENDITURE COMMITMENTS

(a) Commitments under lease agreements

The Group has entered into commercial leases on certain motor vehicles and also office, factory and retail premises. These leases have a life of between 1 and 10 years with renewal options of between 5 to 10 years included in the contracts. There are no restrictions placed upon the lessee by entering into these leases. In the case of motor vehicles, a fully maintained vehicle is provided.

Future minimum rentals payable under non-cancellable operating leases as at 30 June are as follows:

| | Consolidated | |
|---|---------------------|---------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Operating leases – office, factory and retail premises | | |
| – payable not later than 1 year | 3,701 | 3,938 |
| – later than 1 year and not later than 5 years | 8,902 | 12,125 |
| – later than 5 years | 3,623 | 3,486 |
| – aggregate lease expenditure contracted for at balance date | 16,226 | 19,549 |
| Operating leases – motor vehicles | | |
| – payable not later than 1 year | 10 | 16 |
| – later than 1 year and not later than 5 years | 7 | 17 |
| – aggregate lease expenditure contracted for at balance date | 17 | 33 |

The Group has finance leases and hire purchase contracts for various items of plant and machinery. These leases have a purchase option but no terms of renewal.

Future minimum lease payments under finance leases and hire purchase contracts together with the present value of the minimum lease payments are as follows:

| | Consolidated | | | |
|--|-------------------------------|--|-------------------------------|--|
| | 2018 | | 2017 | |
| | Minimum lease payments | Present value of lease payments | Minimum lease payments | Present value of lease payments |
| | \$'000 | \$'000 | \$'000 | \$'000 |
| Within one year | 2,493 | 2,356 | 2,008 | 1,865 |
| After one year but not more than five years | 5,901 | 5,767 | 5,233 | 5,059 |
| Total minimum lease payments | 8,394 | 8,123 | 7,241 | 6,924 |
| Less amounts representing future finance costs | (271) | – | (317) | – |
| Present value of minimum lease payments | 8,123 | 8,123 | 6,924 | 6,924 |

Finance leases have an average lease term of 5 years and an average implicit interest rate of 2.00% per annum. Assets that are the subject of finance leases include motor vehicles and large items of plant and machinery (refer notes 18 and 20).

| | Consolidated | |
|--|---------------------|---------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |

(b) Expenditure commitments

Estimated expenditure contracted for at balance date but not provided for:

| | | |
|---------------------------------|--------------|------------|
| – payable not later than 1 year | 5,212 | 386 |
|---------------------------------|--------------|------------|

(c) Banker's undertakings

First mortgages have been registered over the assets and undertakings of controlled entities by banks which have issued performance guarantees to third parties on behalf of the consolidated entity. The aggregate of the performance guarantees issued by the banks amounted to:

| | | |
|--|--------------|--------------|
| | 7,169 | 7,662 |
|--|--------------|--------------|

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 27

EMPLOYEE BENEFITS AND SUPERANNUATION COMMITMENTS

| | | Consolidated | |
|---|------|--------------|--------|
| | | 2018 | 2017 |
| | Note | \$'000 | \$'000 |
| The aggregate employee entitlement liability is comprised of: | | | |
| Accrued wages, salaries and on costs | | 84 | 113 |
| Provisions (current) | 19 | 10,600 | 7,892 |
| Provisions (non-current) | 21 | 7,455 | 1,265 |
| Non-current liabilities held for sale | | — | 5 |
| | | 18,139 | 9,275 |

(a) Superannuation commitments

The consolidated entity contributes to superannuation plans elected by individual employees, generally at the rate of 9.5% of gross salaries and wages.

The company complies with the Superannuation Guarantee Charge obligations legislated in the *Superannuation Guarantee (Administration) Act 1992*.

The amount of superannuation expense for the year ended 30 June 2018 is \$1,004,000 (2017 – \$1,165,000).

(b) Employee share option plan

An employee share option plan has been established. The plan was approved by shareholders at the Annual General Meeting in November 1999. The plan permits the granting of options (at the absolute discretion of the Board) to Group employees to acquire ordinary shares in Schaffer Corporation Limited. The options issued for nil consideration, are issued in accordance with performance guidelines established by the Directors of Schaffer Corporation Limited. Once issued, the options cannot be transferred and will not be quoted on the ASX. The number of options which can be issued is limited to 5% of the number of shares on issue.

Options may be exercised as follows:

- (1) during the first 12 months of each option period and including each date of issue, no more than 25% of the options issued to that participant on that date of issue;
- (2) during the period of 24 months from and including each date of issue exercise no more than 50% of the options issued to that participant on that date of issue;
- (3) during the period of 36 months from and including each date of issue exercise no more than 75% of the options issued to that participant on that date of issue;
- (4) after 36 months 100% of the options may be exercised.

Options issued over ordinary shares as part of an employee share scheme are as follows:

- There were 70,000 options on issue at 30 June 2018 (2017 – Nil).
- 70,000 options were issued during the year ended 30 June 2018 (2017 – Nil).

(c) Employee participation units

A controlled entity, Howe Automotive Limited, has established a Howe Automotive Limited shareholder approved employee incentives plan which permits the granting of employee participation units (EPUs) at the discretion of its shareholders' up to an EPU limit. The EPU limit is 10% of the fully diluted share capital of Howe Automotive Limited, which is calculated as if each EPU already issued was deemed to be one issued Howe Automotive Limited share.

An EPU provides an employee with a right to receive a cash payment from Howe Automotive Limited in the following circumstances:

- (a) If an employee dies or becomes permanently disabled at any time after the grant date.
- (b) If an employee ceases employment after the three year initial vesting period.
- (c) Upon a liquidity event (trade sale or listing on an Australian or overseas stock exchange).
- (d) On issue of a compulsory payment notice by Schaffer Corporation Limited.

The amount of the cash payment is dependent on vesting and the financial performance of Howe Automotive Limited (refer to remuneration report for details). The vesting requirements are:

- (a) up to 3 years – nil
- (b) 3 years to 4 years – 33.3%
- (c) 4 years to 5 years – 66.7%
- (d) over 5 years – 100%

Note: Employees are ineligible to receive any payment in the following circumstances:

- (i) termination due to misconduct;
- (ii) failure to provide 90 days written notice of intention to terminate employment;
- (iii) acting in competition prior to the payment date (payment date is at least 12 months after termination).

The amount of payment is calculated in accordance with an equity valuation formula based on 5.5 times Howe Automotive Limited's earnings before interest and tax minus net debt. The formula uses a three year average including one full year following termination.

Schaffer Corporation Limited has the option to compel the employee to use the whole or part of that cash payment in subscribing for Schaffer Corporation Limited shares based on the average Schaffer Corporation Limited share price for the same three year period.

| EPU Tranche | Issue number | Grant date | Number issued | Number redeemed | Number cancelled | Balance of EPU's outstanding | Balance as a % of Howe's capital | Number vested |
|-------------|--------------|------------------|-------------------|------------------|------------------|------------------------------|----------------------------------|------------------|
| Series 1 | | 4 October 2000 | 3,383,634 | 1,883,555 | 958,697 | 541,382 | 0.9% | 541,382 |
| Series 2 | Issue 1 | 21 December 2001 | 2,884,434 | 658,290 | 1,679,257 | 546,887 | 0.9% | 546,887 |
| | Issue 2 | 1 July 2002 | 120,000 | 20,000 | 40,000 | 60,000 | 0.1% | 60,000 |
| | Issue 3 | 1 July 2003 | 245,000 | 96,667 | 98,333 | 50,000 | 0.1% | 50,000 |
| | Issue 4 | 1 July 2004 | 57,672 | – | 32,672 | 25,000 | 0.0% | 25,000 |
| | Issue 5 | 16 May 2005 | 150,000 | – | 150,000 | – | 0.0% | – |
| | Issue 6 | 1 July 2005 | 1,350,000 | 350,000 | 500,000 | 500,000 | 0.9% | 500,000 |
| | Issue 7 | 21 August 2006 | 500,000 | – | – | 500,000 | 0.9% | 500,000 |
| | Issue 8 | 1 July 2007 | 200,000 | – | – | 200,000 | 0.3% | 200,000 |
| | Issue 9 | 1 July 2017 | 1,450,000 | – | 100,000 | 1,350,000 | 2.3% | – |
| Series 3 | Issue 1 | 1 January 2008 | 1,150,000 | 233,333 | 416,667 | 500,000 | 0.9% | 500,000 |
| | Issue 2 | 1 July 2009 | 100,000 | 100,000 | – | – | – | – |
| | Issue 3 | 1 January 2011 | 250,000 | – | – | 250,000 | 0.4% | 250,000 |
| | Issue 4 | 1 July 2013 | 1,075,000 | 100,000 | 275,000 | 700,000 | 1.2% | 466,667 |
| | Issue 5 | 1 July 2014 | 200,000 | – | 133,333 | 66,667 | 0.1% | 66,667 |
| | Issue 6 | 1 July 2016 | 330,000 | – | 30,000 | 300,000 | 0.5% | – |
| | | | 13,445,740 | 3,441,845 | 4,413,959 | 5,589,936 | | 3,706,603 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 27 EMPLOYEE BENEFITS AND SUPERANNUATION COMMITMENTS (CONTINUED)

(c) Employee participation units (continued)

During the year, the Company changed its accounting for employee participation units (EPUs).

A controlled entity, Howe Automotive Limited (Howe), may grant EPUs in accordance with its Employee Incentive Plan adopted by Howe shareholders on 20 December 2001.

An EPU provides an employee with a right on termination of employment under certain conditions and in certain other circumstances to receive a cash payment from Howe. Schaffer Corporation Limited (SFC) has the option to compel the employee to use the whole or part of that cash payment to subscribe for SFC shares.

Prior to the change, the cost of these SFC equity-settled transactions with employees was measured by reference to the fair value at the date at which they are granted. The fair value was determined using a binominal model. In valuing the equity-settled transactions, no account was taken of any performance conditions, other than conditions linked to the price of the SFC shares (market conditions).

The cost of equity-settled transactions was recognised, together with a corresponding increase in equity, over the period in which the performance conditions were fulfilled, ending on the date on which the relevant employees become fully entitled to the award (vesting date).

The cumulative expense recognised for SFC equity-settled transactions at each reporting date until vesting date reflected (i) the extent to which the vesting period has expired and (ii) the Group's best estimate of the number of equity instruments that will ultimately vest. No adjustment was made for the likelihood of market performance conditions being met as the effect of these conditions was included in the determination of fair value at grant date. The Consolidated Statement of Comprehensive Income charge or credit for a period represented the movement in cumulative expense recognised as at the beginning and end of that period.

On 1 November 2017, a change in accounting was implemented based on the higher probability that in the future SFC would not equity settle these transactions by compelling employees to use the whole or part of the cash payment received on termination to subscribe for SFC shares. However, this accounting judgment does not limit the existing option for SFC to compel employees in the future to use the whole or part of the cash payment to subscribe for SFC shares.

Immediately following the accounting change, the Consolidated Entity recorded a provision for EPU termination entitlements calculated using estimates of the probable future EPU cash payments for issued EPUs discounted based on the estimated period until payment using a risk-free rate of return. The amount estimated for EPU cash payments on termination is calculated in accordance with an equity valuation formula based on the three-year average, including one full year following termination, of 5.5 times Howe Automotive Limited's estimated earnings before interest and tax minus debt.

The change in accounting is applied prospectively. On the date SFC changed its estimated settlement method for these EPU's, the provision for employee termination entitlements was recorded and equity attributable to the holders of the parent was decreased through the share-based payments reserve.

After initial recognition, changes in the valuation of the provision for EPU termination entitlements are recorded in the profit or loss for the period. The increase to the provision for EPU termination payments from 1 November 2017 to 30 June 2018 was \$5,600,000.

NOTE 28 SEGMENT INFORMATION

Identification of reportable segments

The Group has identified its operating segments based on the internal reports that are reviewed and used by the executive management team (the chief operating decision makers) in assessing performance in determining the allocations of resources.

The operating segments are identified by management based on the nature of the product and customer supplied, and services provided and the identity of service line manager. Discrete financial information about each of these operating businesses is reported to the executive management team on a monthly basis.

The reportable segments are based on aggregated operating segments determined by the similarity of economic characteristics, the products produced and sold and/or the services provided, as these are the sources of the Group's major risks and have the most effect on the rates of return.

The Group comprises the following reportable segments:

The Automotive Leather segment is a manufacturer and supplier of leather in the automotive industries.

The Building Materials segment comprising Delta Corporation Limited and sells concrete paving, pre-cast and pre-stressed concrete elements.

The SFC Investments – Property & Other segment includes the Group's share of syndicated property, 100% owned investment property, investments in managed equity funds and direct investments in equity instruments, excluding those properties and investments owned by Gosh Capital. The activities of the segment include the leasing of office and retail properties, the development and sale of property assets, and general investing.

The Gosh Capital segment manages the assets of the previously operated Gosh Leather business, and invests profits earned from those assets in investment opportunities.

Major customers

The Group has a number of major clients to which it provided both products and services. There were two customers within the Automotive Leather segment which individually accounted for more than 10% of Group revenue (2017 – two customers).

Sales to major customers

| | 2018 | | 2017 | |
|------------------------------------|---------|--------------------|---------|--------------------|
| | \$'000 | % of total revenue | \$'000 | % of total revenue |
| Customer 1 | 50,219 | 22% | 35,699 | 17% |
| Customer 2 | 43,921 | 19% | 21,628 | 10% |
| Sales to major customers | 94,140 | 41% | 57,327 | 27% |
| Revenue from continuing operations | 227,036 | | 214,974 | |

The accounting policies used by the Group in reporting segments internally are the same as those contained in note 2 to the accounts and in the prior period. There are no inter-segment transactions.

Allocation of assets

It is the Group's policy that if items of revenue and expense are not allocated to operating segments then any associated assets are also not allocated to segments. This is to avoid asymmetrical allocations within segments which management believe would be inconsistent.

Operating segments

The following table presents revenue and profit information and certain asset and liability information regarding operating segments for the years ended 30 June 2018 and 30 June 2017.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 28 SEGMENT INFORMATION (CONTINUED)

Operating segment information

Revenue

| | Automotive Leather | | Building Materials | | SFC Investments – Property and Other | | Gosh Capital | | Consolidated | |
|---|-----------------------|----------------|-----------------------|----------------|---|----------------|-----------------|----------------|----------------|----------------|
| | 2018 \$'000 | 2017 \$'000 | 2018 \$'000 | 2017 \$'000 | 2018 \$'000 | 2017 \$'000 | 2018 \$'000 | 2017 \$'000 | 2018 \$'000 | 2017 \$'000 |
| Total revenue from ordinary activities external customers | 203,382 | 170,906 | 17,039 | 11,515 | 5,012 | 4,719 | 1,358 | 1,352 | 226,791 | 188,492 |
| Unallocated interest and dividend revenue | | | | | | | | | 245 | 10 |
| Total Revenue | | | | | | | | | 227,036 | 188,502 |

Results

Underlying net profit/(loss) after tax

| | | | | | | | | | | |
|--|---------|---------|---------|-------|-------|-----|------|------|---------|---------|
| – continuing operations | 29,053 | 10,187 | (982) | (561) | 1,073 | 734 | 436 | 411 | 29,580 | 10,771 |
| Impairment of assets after tax | – | – | (3,150) | – | – | – | – | – | (3,150) | – |
| Restructuring costs after tax | (568) | (632) | – | (65) | – | – | – | – | (568) | (697) |
| Profit of sale of trust assets after tax | – | – | – | – | – | – | – | 77 | – | 77 |
| Net profit/(loss) after tax – continuing operations | 28,485 | 9,555 | (4,132) | (626) | 1,073 | 734 | 436 | 488 | 25,862 | 10,151 |
| Less profit/(loss) attributable to non-controlling interests | (4,794) | (1,608) | – | – | – | – | (74) | (82) | (4,868) | (1,690) |
| Profit/(loss) attributable to owners of the parent | 23,691 | 7,947 | (4,132) | (626) | 1,073 | 734 | 362 | 406 | 20,994 | 8,461 |

Unallocated items

| | | | | | | | | | | |
|---|--|--|--|--|--|--|--|--|---------|---------|
| Discontinued operations after tax | | | | | | | | | 4,245 | (1,281) |
| Finance income and dividends | | | | | | | | | 245 | 12 |
| Finance costs | | | | | | | | | (42) | (74) |
| Corporate overheads | | | | | | | | | (3,069) | (2,290) |
| Income tax expense – continuing operations | | | | | | | | | 919 | 1,028 |
| Profit after tax from continuing operations | | | | | | | | | 23,292 | 5,856 |

Assets

| | | | | | | | | | | |
|----------------------------------|---------|---------|--------|--------|--------|--------|--------|--------|---------|---------|
| Total segment non-current assets | 22,489 | 18,351 | 9,749 | 20,794 | 22,719 | 14,209 | 19,651 | 17,882 | 74,608 | 71,236 |
| Unallocated | | | | | | | | | 2,823 | 1,379 |
| Total non-current assets | | | | | | | | | 77,431 | 72,615 |
| Total segment assets | 115,080 | 107,227 | 17,074 | 41,029 | 24,321 | 15,929 | 19,920 | 18,839 | 176,395 | 183,024 |
| Unallocated | | | | | | | | | 18,818 | 1,934 |
| Total assets | | | | | | | | | 195,213 | 184,515 |

Liabilities

| | | | | | | | | | | |
|---------------------------------------|--------|--------|-------|-------|--------|--------|-------|-------|--------|---------|
| Segment liabilities | 57,802 | 62,443 | 4,301 | 8,055 | 19,440 | 19,501 | 8,569 | 8,428 | 90,112 | 98,427 |
| Unallocated | | | | | | | | | 2,515 | 4,223 |
| Total liabilities | | | | | | | | | 92,627 | 102,650 |
| Other segment information | | | | | | | | | | |
| Segment capital expenditure | 4,251 | 3,213 | 1,317 | 208 | 503 | 747 | 46 | 73 | 6,117 | 4,241 |
| Unallocated | | | | | | | | | 7 | 9 |
| Total capital expenditure | | | | | | | | | 6,124 | 4,250 |
| Segment depreciation and amortisation | 3,003 | 2,531 | 1,215 | 2,155 | 353 | 390 | 206 | 201 | 4,777 | 5,277 |
| Unallocated | | | | | | | | | 33 | 29 |
| Total depreciation and amortisation | | | | | | | | | 4,810 | 5,306 |
| Other non-cash expenses/(revenues) | 4,226 | 784 | 7,571 | (372) | (118) | (124) | – | – | 11,679 | 288 |

Each segment result is a measure of the segment profit from continuing operations before tax and finance costs.

Unallocated assets and liabilities including the following material items:

Non-current assets

Property plant and equipment

Deferred income tax asset

Liabilities

Trade creditors

Provision for employee entitlements

Revenue from external customers by geographical locations is detailed below. Revenue is attributed to geographic location based on the location of the customers.

| | 2018 \$'000 | 2017 \$'000 |
|---------------|----------------|----------------|
| Australia | 24,128 | 46,117 |
| Asia | 42,075 | 33,947 |
| Europe | 160,833 | 134,910 |
| Total revenue | 227,036 | 214,974 |

Non-current assets (excluding deferred tax assets and financial instruments) by geographic location comprise:

| | Australia \$'000 | Asia \$'000 | Europe \$'000 | Total \$'000 |
|---------------------------|---------------------|----------------|------------------|-----------------|
| Non-current assets | | | | |
| 2018 | | | | |
| Plant and equipment | 12,143 | 489 | 15,013 | 27,645 |
| Investment properties | 28,678 | – | – | 28,678 |
| Goodwill | 1,299 | – | – | 1,299 |
| | 42,120 | 489 | 15,013 | 57,622 |
| 2017 | | | | |
| Plant and equipment | 23,951 | 337 | 13,002 | 37,290 |
| Investment properties | 25,406 | – | – | 25,406 |
| Goodwill | 1,299 | – | – | 1,299 |
| | 50,656 | 337 | 13,002 | 63,995 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 29 RELATED PARTY DISCLOSURES

The following related party transactions occurred during the financial year within the consolidated entity.

(a) Transactions with related parties

Schaffer Corporation Limited holds 83.17% (2017: 83.17%) of the share capital of Howe Automotive Limited of which Mr J M Schaffer AM and Mr A K Mayer are Directors. Dividends were received during the year amounting to \$12,309,195 (2017: \$5,821,923).

(b) EPU holdings of Key Management Personnel

30 June 2018

| Executives | Balance at beginning of period | Granted as remuneration | Redeemed during the period | Cancelled during the period | Balance at end of period | Vesting status as at 30 June 2018 | |
|--------------|--------------------------------|-------------------------|----------------------------|-----------------------------|--------------------------|-----------------------------------|----------------|
| | | | | | | Vested | Not vested |
| D Birks | 1,000,000 | 200,000 | — | — | 1,200,000 | 966,667 | 233,333 |
| R Leib | — | 300,000 | — | — | 300,000 | — | 300,000 |
| Total | 1,000,000 | 500,000 | — | — | 1,500,000 | 966,667 | 533,333 |

30 June 2017

| Executives | Balance at beginning of period | Granted as remuneration | Redeemed during the period | Cancelled during the period | Balance at end of period | Vesting status as at 30 June 2017 | |
|--------------|--------------------------------|-------------------------|----------------------------|-----------------------------|--------------------------|-----------------------------------|---------------|
| | | | | | | Vested | Not vested |
| D Birks | 1,000,000 | — | — | — | 1,000,000 | 933,333 | 66,667 |
| N Filipovic* | 1,320,627 | — | — | (100,000) | 1,220,627 | 1,220,627 | — |
| Total | 2,320,627 | — | — | (100,000) | 2,220,627 | 2,153,960 | 66,667 |

*Mr Filipovic ceased employment on 12 December 2016.

(c) Option/holding of key management personnel

| Executives | Balance at beginning of period | Granted as remuneration | Options exercised | Balance at end of period | Exercise ability as at 30 June 2018 | |
|--------------|--------------------------------|-------------------------|-------------------|--------------------------|-------------------------------------|-----------------|
| | | | | | Exercisable | Not Exercisable |
| R Leib | — | 50,000 | — | 50,000 | 12,500 | 37,500 |
| J M Cantwell | — | 20,000 | — | 20,000 | 5,000 | 15,000 |
| Total | — | 70,000 | — | 70,000 | 17,500 | 52,500 |

For details of terms and conditions for each grant refer to note 27.

NOTE 30 NON-CONTROLLING INTEREST

Reconciliation of non-controlling interest in controlled entities:

| | 2018 \$'000 | 2017 \$'000 |
|---|----------------|----------------|
| At 1 July | 9,320 | 8,541 |
| — Add share of operating profit | 4,868 | 1,690 |
| — Share of foreign currency translation reserve movement | 144 | (20) |
| — Share of unrealised gains reserve movement | 77 | 287 |
| — Transferred to reserves due to change in settlement of EPU's (refer note 27(c)) | (194) | — |
| — Dividends paid (refer note 12) | (2,491) | (1,178) |
| At 30 June | 11,724 | 9,320 |

NOTE 31 EARNINGS PER SHARE

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

Diluted earnings per share amounts are calculated by dividing the net profit attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares (in cents).

The following reflects the income and share data used in the calculation of basic and diluted earnings per share:

| | 2018 \$'000 | 2017 \$'000 |
|---|----------------|----------------|
| Net profit attributable to ordinary equity holders of the parent from continuing operations | 23,292 | 5,856 |
| Number of Shares | | |
| | 2018 | 2017 |
| Weighted average number of ordinary shares for basic earnings per share | 13,971,077 | 14,005,373 |
| Weighted average number of ordinary shares adjusted for the effect of dilution | 14,028,995 | 14,424,617 |

There have been no other transactions involving ordinary shares.

Consolidated 2018 2017

166.7¢ 41.8¢

166.0¢ 40.6¢

Consolidated 2018 2017 \$'000 \$'000

Number of Shares 2018 2017

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 32 FINANCIAL INSTRUMENTS

Financial risk management, objectives and policies

The Group's financial instruments comprise bank loans, overdrafts, finance leases and hire purchase contracts, foreign exchange contracts, interest rate swaps, cash and short-term deposits, trade and other payables, available for sale investments, and trade and other receivables.

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in note 2 to the financial statements.

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

The Group enters into derivative transactions, principally interest rate swaps, and forward currency contracts. The purpose is to manage the interest rate and currency risks arising from the Group's operations and its sources of finance. Trading in derivatives has also been undertaken, specifically in forward currency contracts. These derivatives do not qualify for hedge accounting and are based on limits set by the Board. The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The Group uses different methods to measure and manage different types of risks to which it is exposed.

These include monitoring by the Board of levels of exposure to interest rate and foreign exchange risk and assessments of market forecasts for interest rate, foreign exchange and commodity prices. Ageing analyses and monitoring of specific credit allowances are undertaken to manage credit risk. Liquidity risk is monitored through the development of future rolling cash flow forecasts.

(a) Cash flow interest rate risk

The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's long-term debt obligations with a floating interest rate.

In respect of the Group's syndicated property borrowings, the funding and interest rate decision are managed externally by unanimous consent amongst the joint operators, including the use of interest rate swaps (refer note 33(ii)).

At balance date the Group had the following mix of financial assets and liabilities exposed to Australian variable interest rate risk that are not designated cash flow hedges:

| | Consolidated | |
|------------------------------|---------------------|-----------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Financial Assets | | |
| Cash and short-term deposits | 25,938 | 11,417 |
| | 25,938 | 11,417 |
| Financial Liabilities | | |
| Bank loans | (11,690) | (12,168) |
| Cash advances | – | (1,500) |
| Commercial bills | (6,060) | (6,060) |
| Government loan | – | (10,000) |
| Revolving Loan | – | (11,668) |
| | (17,750) | (41,396) |
| Net exposure | 8,188 | (29,979) |

Cash not required immediately is used to either reduce cash advances or invested on the short term money market.

The Group's policy is to manage its finance costs using a mix of fixed and variable rate debt. At 30 June 2018 approximately 46.6% of the Group's borrowings are at a fixed rate of interest (2017 – 25.0%).

The Group constantly analyses its interest rate exposure. Within this analysis consideration is given to potential renewals of existing positions, alternative financing, alternative hedging positions and the mix of fixed and variable interest rates.

NOTE 32 FINANCIAL INSTRUMENTS (CONTINUED)

The following sensitivity analysis is based on the interest rate risk exposures in existence at the balance date. At 30 June 2018, if interest rates had moved, as illustrated in the table below, with all other variables held constant, after tax profit and equity would have been affected as follows:

| | 2018 | 2017 |
|---|---------------|---------------|
| | \$'000 | \$'000 |
| Judgments of reasonably possible movements: | | |
| Consolidated | | |
| +0.25 (25 basis points) | 14 | (52) |
| –0.25 (25 basis points) | (14) | 52 |

The movements in profit are due to higher/lower interest costs from variable rate debt and cash balances. The sensitivity is lower in 2018 than 2017 because of the reduced level of variable rated net debt.

For 2018 and 2017 the sensitivity has been based on an increase/decrease of 25 basis points and this is management's best estimate of movement in interest rates in the forthcoming year.

(b) Assets pledged as security

The carrying amount of assets pledged as security for current and non-current interest bearing liabilities are:

| | Consolidated | |
|--|---------------------|----------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Current | | |
| <i>Floating charges</i> | | |
| Cash and cash equivalent | 25,810 | 10,762 |
| Receivables | 37,486 | 43,661 |
| Inventories | 39,604 | 50,382 |
| Total current assets pledged as security | 102,900 | 104,805 |
| Non-current | | |
| <i>First mortgages</i> | | |
| Freehold land and buildings | 3,232 | 13,783 |
| Investment properties | 19,433 | 23,536 |
| Leasehold quarries | – | 2,920 |
| | 22,665 | 40,239 |
| <i>Finance leases and hire purchases</i> | | |
| Plant and equipment | 11,241 | 9,676 |
| <i>Floating charges</i> | | |
| Plant and equipment | 4,709 | 14,993 |
| Leasehold improvements | – | 172 |
| Total non-current assets pledged as security | 4,709 | 15,165 |

The terms and conditions relating to the financial assets are as follows:

Cash and cash equivalents, inventories, receivables, freehold land and buildings, available-for-sale financial assets and plant and equipment are pledged against the bank overdraft facility, cash advance facility and revolving loan facility on an ongoing floating basis (refer notes 18 and 20 for more details).

Investment properties are pledged as security for bank loans (refer note 20(a)) and commercial bills (refer note 20(d)).

(c) Net fair values

Foreign exchange contracts, available for sale investments, and interest rate swaps are carried on the balance sheet at fair value.

The carrying values of all other financial assets and liabilities have been recognised at the balance date at amounts which approximate fair value.

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

- Level 1 – the fair value is calculated using quoted prices in active markets.
- Level 2 – the fair value is estimated using inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices).
- Level 3 – the fair value is estimated using inputs for the asset or liability that are not based on observable market data.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 32 FINANCIAL INSTRUMENTS (CONTINUED)

(c) Net fair values (continued)

The fair value of the financial instruments carried at fair value, as well as the methods used to estimate the fair value, are summarised in the table below:

| | Quoted market price (Level 1) | Valuation technique market observable inputs (Level 2) | Valuation technique non- market observable inputs (Level 3) | Total |
|--------------------------------|-------------------------------------|---|--|--------|
| | \$'000 | \$'000 | \$'000 | \$'000 |
| Year ended 30 June 2018 | | | | |
| Consolidated | | | | |
| Financial assets | | | | |
| Available-for-sale investments | | | | |
| Listed investments | 2,850 | – | – | 2,850 |
| Unlisted investments | 5,248 | – | 5,635 | 10,883 |
| Foreign exchange contracts | – | 1,413 | – | 1,413 |
| | 8,098 | 1,413 | 5,635 | 15,146 |
| Financial liabilities | | | | |
| Derivative instruments | | | | |
| Interest rate swaps | – | 46 | – | 46 |
| | – | 46 | – | 46 |
| Year ended 30 June 2017 | | | | |
| Consolidated | | | | |
| Financial assets | | | | |
| Available-for-sale investments | | | | |
| Listed investments | 2,375 | – | – | 2,375 |
| Unlisted investments | 250 | – | 3,995 | 4,245 |
| | 2,625 | – | 3,995 | 6,620 |
| Financial liabilities | | | | |
| Derivative instruments | | | | |
| Foreign exchange contracts | – | 730 | – | 730 |
| Interest rate swaps | – | 165 | – | 165 |
| | – | 895 | – | 895 |

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 and investments in unlisted managed equity funds are based on quoted market prices.

For unlisted property trust investments, the fair value is determined by the calculation of the Group's percentage ownership in the investment entity multiplied by the total net assets of the investment entity at fair value (refer note 16).

Reconciliation of the fair value measurement of unlisted property trust investments

| | 2018 \$'000 | 2017 \$'000 |
|---|----------------|----------------|
| Balance as at 1 July | 3,995 | 3,734 |
| Purchase of units in unlisted property unit trusts | 1,279 | – |
| Profit received from disposal of trust asset | – | (192) |
| Re-measurement recognised in other comprehensive income | 11 | 714 |
| Capital distribution | – | (261) |
| | 5,285 | 3,995 |

(d) Credit risk exposures

Credit risk is the risk that a customer or counterparty to a financial instrument will fail to perform or fail to pay amounts due causing financial loss to the Group and arises from cash and cash equivalents, derivative financial instruments and deposits with financial institutions and particularly from credit exposures to customers relating to outstanding receivables.

The consolidated entity's maximum exposure to credit risk at balance date in relation to each class of recognised financial assets, is the carrying amount of those assets as indicated in the Consolidated Statement of Financial Position.

Concentrations of credit risk

The consolidated entity minimises concentrations of credit risk in relation to trade receivables by undertaking transactions with a large number of customers within the specified industries both within Australia and overseas.

The consolidated entity minimises concentration of credit risk in relation to cash by investing only in reputable banking facilities.

Refer also to note 28 – Segment Information.

Concentration of credit risk on trade receivables arises in the following industries:

| Industry | Maximum credit risk exposure | | | |
|--------------------|------------------------------|-----------|----------------|----------------|
| | Consolidated | | | |
| | Trade debtors | | Trade debtors | |
| | 2018 % | 2017 % | 2018 \$'000 | 2017 \$'000 |
| Automotive leather | 92 | 84 | 28,789 | 31,917 |
| Building materials | 8 | 16 | 2,470 | 6,194 |
| Total | 100 | 100 | 31,259 | 38,111 |

There are no trade debtors held in the parent entity.

Credit risk in trade receivables is managed in the following ways:

Leather and Building Materials

The Group has a credit policy that is designed to ensure that consistent processes are in place throughout the Group to measure and control credit risk. Credit risk is considered as part of the risk-reward balance of doing business. On entering into any business contract, the extent to which the arrangement exposes the Group to credit risk is considered. Key requirements of the policy are formal delegated authorities to the divisional accountant to incur credit risk to a specialised credit function to set counterparty limits; the establishment of credit systems and processes to ensure that counterparties are rated and limits set; and systems to monitor exposure against limited and report regularly on those exposures, and immediately on any excesses, and to track and report credit losses.

Before trading with a new counterparty can start, its creditworthiness is assessed by referring to a credit reporting agency. The assessment process takes into account all available qualitative and quantitative information about the counterparty and the Group, if any, to which the counterparty belongs. The counterparty's business activities, financial resources and business risk management processes are taken into account in the assessment, to the extent that this information is publicly available or otherwise disclosed to the Group by the counterparty, together with external credit ratings, if any. Creditworthiness continues to be evaluated after transactions have been initiated and a watch list of higher-risk counterparties is maintained. Once assessment is complete, each counter-party is allocated a maximum exposure limit.

A balance is maintained of providing sufficient credit so as not to jeopardise potential sales but at the same time not put the company to undue risk. In addition, the Leather division purchases insurance to cover the estimated credit risk exposure of the division's individual debtors.

The maximum credit risk exposure for the Group does not take into account the value of any collateral or other security held, in the event other entities/parties fail to perform their obligations under the financial instruments in question. The only security provided is in the form of director's personal guarantees from debtors, which cannot be quantified due to the continual changing circumstances of the guarantee provider.

At 30 June, the ageing analysis of trade receivables is as follows:

| | Consolidated | |
|---|----------------|----------------|
| | 2018 \$'000 | 2017 \$'000 |
| Trade receivables at 30 June | | |
| Neither impaired nor past due – 30 days or less | 17,119 | 24,197 |
| Not impaired and past due in the following periods: | | |
| 31 to 60 days | 9,276 | 10,095 |
| 61 to 90 days | 3,377 | 2,124 |
| Over 90 days | 1,487 | 1,695 |
| Impaired debtors over 90 days | (330) | (322) |
| | 30,929 | 37,789 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 32 FINANCIAL INSTRUMENTS (CONTINUED)

(e) Liquidity risk

Liquidity risk is the risk that suitable sources of funding for the Group's business activities may not be available. The Group's liquidity is managed centrally with operating units forecasting their cash and currency requirements. Unless restricted by location regulations, subsidiaries pool their cash surpluses which can be used to fund other subsidiaries' requirements or invest any net surplus in the market or arrange for necessary external borrowings, while managing the Group's overall net currency positions.

In managing its liquidity risk, the Group has access to a wide range of funding at competitive rates through capital markets and banks. The Group centrally co-ordinates relationships with banks, borrowing requirements, foreign exchange requirements and cash management. The Group believes it has access to sufficient funding through the commercial paper markets and by using undrawn committed borrowing facilities to meet foreseeable borrowing requirements.

Prudent liquidity risk management implies maintaining sufficient, cash and marketable securities, as well as the availability of funding through an adequate amount of committed credit facilities to meet expected future payment liabilities. The Group's liquidity management plan includes the preparation of annual cash flow forecasts, which are updated monthly, and the establishment and maintenance of adequate credit facilities to meet all expected future cash liabilities identified in these cash flow forecasts.

At 30 June 2018, the Group has the following undrawn borrowing facilities available (refer note 20).

| | 2018 | | 2017 | |
|--|---------------|----------|---------------|----------|
| | \$'000 | Expiry | \$'000 | Expiry |
| <i>Australian Banks</i> | | | | |
| Bank overdraft | – | – | 500 | 2017 |
| Bankers' undertaking | 1,111 | 2018 | 1,788 | 2017 |
| Cash advances | – | – | 6,500 | 2017 |
| Finance leases | – | – | 1,864 | 2017 |
| <i>Global Finance Company</i> | | | | |
| Revolving loan facility | 20,431 | 2019 | 4,711 | 2018 |
| | <u>21,542</u> | | <u>15,363</u> | |
| In addition, there are the following banker's undertakings issued at 30 June 2018 (refer note 20). | | | | |
| Performance guarantees to third parties (refer note 26(c)) | 3,286 | < 1 year | 1,801 | < 1 year |
| | <u>3,883</u> | > 1 year | <u>5,861</u> | > 1 year |
| | <u>7,169</u> | | <u>7,662</u> | |

The table below shows the timing of cash outflows relating to trade and other payables. The amounts shown for bank loans in the table below include interest payments resulting from recognised financial liabilities over the term of the loan and the future minimum lease payments with respect to finance leases. Derivative financial instruments consist of interest rate swaps (refer note 33(ii)).

Cash advances and commercial bills are shown in the period when the facility expires.

Cash flows for financial liabilities without fixed amount or timing are based on the conditions existing at balance date.

| Consolidated | Trade and other payables | Finance leases | Cash advances | Commercial bills | Bank loans | Government loan | Revolving loan | Derivative financial instruments |
|---------------|--------------------------|----------------|---------------|------------------|---------------|-----------------|----------------|----------------------------------|
| | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 |
| 2018 | | | | | | | | |
| Within 1 year | 28,894 | 2,493 | – | 216 | 856 | – | – | 84 |
| 1 to 2 years | – | 2,471 | – | 6,169 | 8,660 | – | – | – |
| 2 to 3 years | – | 2,240 | – | – | 11,321 | – | – | – |
| 3 to 4 years | – | 863 | – | – | – | – | – | – |
| 4 to 5 years | – | 327 | – | – | – | – | – | – |
| Over 5 years | – | – | – | – | – | – | – | – |
| | <u>28,894</u> | <u>8,394</u> | <u>–</u> | <u>6,385</u> | <u>20,837</u> | <u>–</u> | <u>–</u> | <u>84</u> |
| 2017 | | | | | | | | |
| Within 1 year | 32,436 | 2,008 | 1,507 | 195 | 12,568 | 685 | 234 | 128 |
| 1 to 2 years | – | 1,788 | – | 195 | 267 | 3,185 | 11,760 | 50 |
| 2 to 3 years | – | 1,584 | – | 6,158 | 7,162 | 3,014 | – | – |
| 3 to 4 years | – | 1,584 | – | – | – | 2,843 | – | – |
| 4 to 5 years | – | 277 | – | – | – | 2,671 | – | – |
| Over 5 years | – | – | – | – | – | – | – | – |
| | <u>32,436</u> | <u>7,241</u> | <u>1,507</u> | <u>6,548</u> | <u>19,997</u> | <u>12,398</u> | <u>11,994</u> | <u>178</u> |

Debt associated with Automotive Leather, Investment Property, and Gosh Capital divisions represents 100% (2017 – 97%) of Group borrowings. At 30 June, 93% (2017 – 93%) of Group debt was non-recourse to the Parent.

Debt associated with the Investment Property division totals \$19,067,000 at 30 June 2018 (2017 – \$19,062,000). SFC's minority property interests are managed external to the Group. Accordingly, SFC does not control the funding structure.

SFC's objective is for property borrowing to be predominantly non-recourse to SFC. At 30 June 2018, 88% (2017 – 88%) of the property borrowings were non-recourse to the Parent.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 32 FINANCIAL INSTRUMENTS (CONTINUED)

(f) Changes in liabilities arising from financing activities

| | 1 July 2017 | Cash Payments | Cash Receipts | Change in fair value | Re-classification | 30 June 2018 |
|---|---------------|---------------|---------------|----------------------|-------------------|---------------|
| | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 |
| Current interest-bearing loans and borrowings | 13,490 | (1,500) | – | – | (11,990) | – |
| Current obligations under finance leases and hire purchase contracts | 1,865 | (1,741) | 2,940 | – | (708) | 2,356 |
| Non-current interest-bearing loans and borrowings | 34,800 | (26,643) | 4,980 | – | 11,990 | 25,127 |
| Non-current obligations under finance lease and hire purchase contracts | 5,059 | – | – | – | 708 | 5,767 |
| Derivatives | 895 | – | – | (849) | – | 46 |
| Total liabilities from financial activities | 56,109 | 29,884 | 7,920 | (849) | – | 33,296 |

| | 1 July 2016 | Cash Payments | Cash Receipts | Change in fair value | Re-classification | 30 June 2017 |
|---|---------------|-----------------|---------------|----------------------|-------------------|---------------|
| Current interest-bearing loans and borrowings | 15,072 | (5,000) | 1,500 | – | 1,918 | 13,490 |
| Current obligations under finance leases and hire purchase contracts | 1,589 | (2,134) | 3,328 | – | (918) | 1,865 |
| Non-current interest-bearing loans and borrowings | 44,505 | (8,008) | 221 | – | (1,918) | 34,800 |
| Non-current obligations under finance lease and hire purchase contracts | 4,141 | – | – | – | 918 | 5,059 |
| Derivatives | 530 | – | – | 365 | – | 895 |
| Total liabilities from financial activities | 65,837 | (15,142) | 5,049 | 365 | – | 56,109 |

(g) Foreign exchange risk

The consolidated entity operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the EUR, USD and RMB. Foreign exchange risk arises from commercial transactions for the purchase of unfinished leather hides, and the processing, finishing and cutting of these hides, as well as foreign exchange risk from the sale of leather products in EUR, USD and RMB.

To manage the foreign exchange risk arising from future commercial transactions the entity regularly considers the use of forward foreign exchange contracts with reference to currency exposure levels, sensitivity, and financial capacity to tolerate rate fluctuations. The foreign exchange risk management policy allows up to 100% of net future foreign exchange exposure to the USD and EUR to be managed using forward foreign exchange hedge contracts, for a maximum tenor of 24 months.

At 30 June 2018, the Group had the following exposure to USD foreign currency that is not designated in cash flow hedges:

| | Consolidated (AUD) | |
|------------------------------|--------------------|-----------------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Financial assets | | |
| Cash and cash equivalents | 4,612 | 1,037 |
| Trade and other receivables | 5,440 | 1,651 |
| Forward rate agreements | 18,543 | 14,524 |
| | 28,595 | 17,212 |
| Financial liabilities | | |
| Trade and other payables | (18,242) | (19,543) |
| | (18,242) | (19,543) |
| Net exposure | 10,353 | (2,331) |

At 30 June 2018, the Group had the following exposure to EUR foreign currency that is not designated in cash flow hedges:

| | Consolidated (AUD) | |
|------------------------------|--------------------|-----------------|
| | 2018 | 2017 |
| | \$000 | \$000 |
| Financial assets | | |
| Cash and cash equivalents | 6,907 | 5,439 |
| Trade and other receivables | 26,106 | 26,482 |
| | 33,013 | 31,921 |
| Financial liabilities | | |
| Trade and other payables | (7,249) | (2,370) |
| Finance leases | (8,116) | (6,766) |
| Revolving loan | – | (11,668) |
| Forward rate agreements | (55,472) | (17,123) |
| | (70,837) | (37,927) |
| Net exposure | (37,824) | (6,006) |

At 30 June 2018, the Group had the following exposure to RMB foreign currency that is not designated in cash flow hedges:

| | Consolidated (AUD) | |
|------------------------------|--------------------|----------------|
| | 2018 | 2017 |
| | \$000 | \$000 |
| Financial assets | | |
| Cash and cash equivalents | 987 | 807 |
| Trade and other receivables | 10,545 | 8,471 |
| | 11,532 | 9,278 |
| Financial liabilities | | |
| Trade and other payables | (4,365) | (1,760) |
| | (4,365) | (1,760) |
| Net exposure | 7,167 | 7,518 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 32 FINANCIAL INSTRUMENTS (CONTINUED)

(g) Foreign exchange risk (continued)

At 30 June 2018 had the Australian dollar moved as illustrated in the table below, with all other variables held constant, after tax profit would have been affected as follows:

Judgments of reasonably possible movements

| | Change in foreign exchange rate | | Effect on profit after tax | |
|--|---------------------------------|------------|----------------------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| | | | \$'000 | \$'000 |
| Consolidated | | | | |
| AUD/USD | US\$0.07 | US\$0.08 | (630) | 154 |
| AUD/USD | (US\$0.07) | (US\$0.08) | 763 | (190) |
| <i>Sensitivity has increased due to an increase in net USD foreign currency assets including a change in the level of hedging.</i> | | | | |
| AUD/EUR | €0.06 | €0.07 | 2,282 | 1,900 |
| AUD/EUR | (€0.06) | (€0.07) | (2,757) | (2,329) |
| <i>Sensitivity has increased due to an increase in net EUR denominated liabilities including a change in the level of hedging.</i> | | | | |
| AUD/RMB | ¥0.49 | ¥0.52 | (459) | (478) |
| AUD/RMB | (¥0.49) | (¥0.52) | 562 | 585 |
| <i>Sensitivity has decreased due to a decrease in working capital denominated in RMB.</i> | | | | |

Currency movements used above are what management considers as representative of any likely movement in the next 12 months based on historical movements and economic forecasters' expectations.

Net unhedged foreign currency assets and liabilities:

| | USD | EUR | RMB | HKD |
|-----------------------------|----------|----------|----------|--------|
| | 000's | 000's | 000's | 000's |
| 2018 | | | | |
| Cash and bank balances | 3,391 | 4,395 | 4,796 | 21 |
| Trade and other receivables | 4,000 | 16,611 | 51,262 | – |
| Trade and other payables | (13,413) | (4,612) | (21,222) | (54) |
| Finance leases | – | (5,165) | – | – |
| Revolving loan | – | – | – | – |
| Forward rate agreements | 13,635 | (35,297) | – | – |
| Net FX exposure | 7,613 | (24,068) | 34,836 | (33) |
| Year-end exchange rates | 0.7353 | 0.6363 | 4.8614 | 5.7703 |
| 2017 | | | | |
| Cash and bank balances | 795 | 3,653 | 4,195 | 37 |
| Trade and other receivables | 1,265 | 17,785 | 44,041 | – |
| Trade and other payables | (14,976) | (1,592) | (9,150) | (33) |
| Finance leases | – | (4,544) | – | – |
| Revolving loan | – | (7,836) | – | – |
| Forward rate agreements | 11,130 | (11,500) | – | – |
| Net FX exposure | (1,786) | (4,034) | 39,086 | 4 |
| Year-end exchange rates | 0.7663 | 0.6716 | 5.1991 | 5.9809 |

(h) Capital management

When managing capital, management's objective is to ensure the entity continues as a going concern as well as to maintain optimal returns to shareholders and benefits for other stakeholders. Management also aims to maintain a capital structure that ensures the lowest cost of capital available to the entity.

The Group's total capital is defined as Schaffer Corporation Limited's shareholders' funds plus amounts attributable to non-controlling shareholders plus net debt. This amounted to \$109,898,000 at 30 June 2018 (2017 – \$127,502,000).

Management are constantly adjusting the capital structure to take advantage of favourable costs of capital or high returns on assets. As the market is constantly changing, management may change the amount of dividends to be paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

Schaffer Corporation Limited does not have a target debt/equity ratio, but has a policy of maintaining a flexible financing structure so as to be able to take advantage of new investment opportunities that may arise.

The Group currently maintains back up liquidity by way of a revolving loan facility and banker's undertaking facilities. Facilities undrawn at 30 June 2018 amounted to \$21,542,000 (2017 – \$15,363,000). The Group's committed and standby credit facilities contain financial undertakings relating to interest cover and borrowing base ratios. A compliance certificate must be produced quarterly attesting to compliance with the covenants.

During 2018, the Company paid dividends of \$4,058,000 (2017 – \$3,501,000). The Board maintains its payout ratio policy of balancing returns to shareholders with the need to fund growth and to maintain financial strength and capacity during uncertain and volatile economic conditions. In line with that policy, the Company has paid a final dividend of \$0.30 per share (fully-franked), bringing the dividends for the 2018 financial year to \$0.45 per share (fully-franked).

Management monitor capital through the gearing ratio (net debt/total capital). The gearing ratios based on continuing operations at 30 June 2018 and 2017 were as follows:

| | Consolidated | |
|--------------------------------|--------------|----------|
| | 2018 | 2017 |
| | \$'000 | \$'000 |
| Total borrowings* | 33,250 | 55,214 |
| Less cash and cash equivalents | (25,938) | (11,417) |
| Net debt | 7,312 | 43,797 |
| Total equity | 102,586 | 83,705 |
| Total capital | 109,898 | 127,502 |
| Gearing ratio | 7% | 34% |

* Includes interest bearing loans and borrowings

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 33 DERIVATIVE FINANCIAL INSTRUMENTS

Current Assets

Forward foreign exchange contracts – classified as held for trading

1,413 –

Current liabilities

Interest rate swap contracts – classified as held for trading

46 165

Forward foreign exchange contracts – classified as held for trading

– 730

46 895

Instruments used by the Group

Derivative financial instruments are used by the Group in the normal course of business to protect against exposure to fluctuations in interest and foreign exchange rates.

(i) Forward currency contracts – classified as held for trading

The Group has the following contracts outstanding at balance date:

| | 2018 \$'000 | 2017 \$'000 | 2018 Average Exchange Rate | 2017 Average Exchange Rate |
|--|----------------|----------------|-------------------------------------|-------------------------------------|
| Sell Euro € / Buy US \$ | | | | |
| Maturity 0-12 months | 18,867 | 7,130 | 1.3076 | 1.0969 |
| Sell Euro € / Buy Australian \$ | | | | |
| Maturity 0-12 months | 39,012 | 7,306 | 1.5686 | 1.4613 |
| Sell Australian \$ / Buy US \$ | | | | |
| Maturity 0-12 months | – | 5,319 | – | 0.7520 |

Such contracts are fair valued by comparing the contracted rate to the market rates for contracts with the same length of maturity. All movements in fair value are recognised in the Consolidated Statement of Comprehensive Income in the period they occur. The net fair value movement on foreign currency derivatives during the year was \$153,000 loss for the Group (2017 – \$622,000 loss).

(ii) Interest Rate Swaps

Interest bearing loans of the Group currently bear an average variable interest rate of 3.91% (2017 – 3.73%). In order to protect against rising interest rates the Group has entered into interest rate swap contracts under which it has a right to receive interest at variable rates and to pay interest at fixed rates. Swaps in place cover approximately 20% (2017 – 36%) of the principal outstanding.

At 30 June 2018, the notional principal amounts and period of expiry of the interest rate swap contracts are as follows:

| | Consolidated 2018 \$'000 | 2017 \$'000 |
|-------------|--------------------------------|----------------|
| 0 – 1 years | 3,841 | 3,053 |
| 1 – 2 years | – | 3,841 |
| | 3,841 | 6,894 |

The Group has entered into interest rate swaps which do not satisfy the requirements for hedge accounting.

The fair value of interest rate swaps at 30 June 2018 is a liability of \$46,000 (2017 – \$165,000 liability) which is recorded on the Consolidated Statement of Financial Position.

NOTE 34 DISCONTINUED OPERATIONS

During the financial period the Building Products division was sold in two transactions. The limestone quarry tenements and production assets on 15 August 2017 and the UrbanStone paving, masonry and natural stone manufacturing and distribution business on 22 November 2017. In accordance with AASB 5 – *Non-Current Assets Held for Sale and Discontinued Operations*, the financial results of the Building Products division sold during the year have been classified as “discontinued operations”.

(a) Proceeds on sale of Building Products division

| | Limestone quarry assets \$000's | UrbanStone business \$000's | Total \$000's |
|-----------------------------|---------------------------------------|-----------------------------------|------------------|
| Proceeds on sale | 4,883 | 13,318 | 18,201 |
| Costs incurred | (33) | (791) | (824) |
| Net proceeds on sale | 4,850 | 12,527 | 17,377 |

(b) Profit on sale of Building Products division

| | | | |
|--|---------|---------|----------|
| Assets sold: | | | |
| Leasehold land | 875 | – | 875 |
| Leasehold quarries | 2,920 | – | 2,920 |
| Leasehold improvements | 170 | 2 | 172 |
| Plant and equipment | 397 | 3,813 | 4,210 |
| Total property, plant and equipment | 4,362 | 3,815 | 8,177 |
| Inventory | 644 | 4,926 | 5,570 |
| Prepayments | 24 | 62 | 86 |
| Sundry debtors (supplier deposits paid) | – | 259 | 259 |
| Total assets sold | 5,030 | 9,062 | 14,092 |
| Employee entitlements transferred to purchaser | (167) | (993) | (1,160) |
| Creditors (customer deposits received) | – | (592) | (592) |
| Net assets sold | 4,863 | 7,477 | 12,340 |
| Net proceeds on sale | 4,850 | 12,527 | 17,377 |
| Less net assets sold | (4,863) | (7,477) | (12,340) |
| (Loss)/profit on sale | (13) | 5,050 | 5,037 |
| Tax expense | | | (644) |
| Profit on sale after tax | | | 4,393 |

(c) Financial performance of the discontinued operations

| | 2018 \$'000 | 2017 \$'000 |
|--|----------------|----------------|
| Revenue | 8,668 | 26,472 |
| Expenses | (8,883) | (28,290) |
| Operating (loss)/income | (215) | (1,818) |
| Finance costs | (1) | (9) |
| (Loss)/profit before tax from discontinued operations before sale | (216) | (1,827) |
| Tax benefit/(expense) related to (loss)/profit before tax from discontinued operations before sale | 68 | 546 |
| (Loss)/profit after tax from discontinued operations before sale | (148) | (1,281) |
| After tax profit on sale (refer note 34(b)) | 4,393 | – |
| Profit after tax from discontinued operations | 4,245 | (1,281) |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

year ended 30 June 2018

NOTE 34

DISCONTINUED OPERATIONS (CONTINUED)

(d) Net cash flows of discontinued operations

| | | |
|---|--------|-------|
| Cash flow from/(used in) | | |
| Operating activities | 2,516 | 976 |
| Investing activities | (78) | (340) |
| Net proceeds on sale (refer note 34(a)) | 17,377 | – |
| Net cash flow from/(used in) discontinued operations | 19,815 | 636 |

(e) Discontinued operations earnings per share information

| | | |
|----------------------------------|-------|--------|
| Basic earnings cents per share | | |
| – discontinued operations | 30.4¢ | (9.1¢) |
| Diluted earnings cents per share | | |
| – discontinued operations | 30.3¢ | (8.9¢) |

NOTE 35

SIGNIFICANT EVENTS AFTER BALANCE DATE

Following the end of the reporting period, a final fully-franked dividend of 30¢ per share to shareholders has been declared payable on 14 September 2018.

No other matter or circumstance has arisen since the end of the financial year 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 in subsequent financial periods.

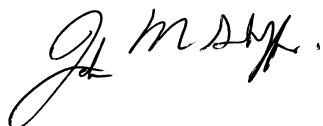
DIRECTORS' DECLARATION

year ended 30 June 2018

In accordance with a resolution of the Directors of Schaffer Corporation Limited, we state that:

1. In the opinion of the Directors:
 - a) the financial statements and notes of the consolidated entity 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 30 June 2018 and of its performance for the year 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 in accordance with section 295A of the Corporations Act 2001 for the financial period ended 30 June 2018.
3. As at the date of this declaration, there are reasonable grounds to believe that the members of the Closed Group identified in note 12 will be able to meet any obligation or liabilities to which they are or may become subject to, by virtue of the Deed of Cross Guarantee.

On behalf of the Board



J M Schaffer AM

Chairman and Managing Director

Perth, 21 September 2018

**INDEPENDENT AUDITOR'S REPORT
TO THE MEMBERS OF SCHAFFER CORPORATION LIMITED**
year ended 30 June 2018



Ernst & Young
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Independent auditor's report to the members of Schaffer Corporation Limited

Report on the audit of the financial report

Opinion

We have audited the financial report of Schaffer Corporation Limited (the Company) and its subsidiaries (collectively 'the Group'), which comprises the consolidated statement of financial position as at 30 June 2018, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information and the Directors' Declaration.

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

- (i) giving a true and fair view of the consolidated financial position of the Group as at 30 June 2018 and of its consolidated financial performance for the year ended on that date; and
- (ii) 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 *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia; and we have 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 the matters 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 statements. The results of our audit procedures, including the procedures performed to address the matter below, provide the basis for our audit opinion on the accompanying financial report.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCHAFFER CORPORATION LIMITED year ended 30 June 2018



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Impairment assessment of non-current assets

Why significant

On an annual basis the Group performs an assessment of whether there are any indicators of possible impairment of its non-current assets. Where indicators are identified the Group performs an impairment test in accordance with Australian Accounting Standards.

Impairment charges totalling \$4.5m relating to assets within the Delta Cash Generating Unit (CGU) were recorded during the year.

The Howe Automotive CGU contains goodwill of \$1.2m. The Group is required to perform an impairment test for this CGU on an annual basis.

Impairment tests require the assessment of the recoverable value of each CGU and incorporates significant judgment in respect of factors such as future cash flows, contracts, margins, capital costs and economic assumptions such as discount rates and inflation rates.

How our audit addressed the key audit matter

Our audit procedures included the following:

- ▶ Assessed the Group's identification of indicators of impairment.
- ▶ Assessed the appropriateness of the Group's determination of individual CGUs.
- ▶ For those CGUs where there were indicators of impairment identified or where material goodwill existed we:
 - ▶ Evaluated the Group's assumptions and estimates to determine the recoverable value of its CGU's, including those relating to existing and prospective contracts, gross margin, capital expenditure, inflation and discount rates. In doing so, we involved our valuation specialists to compare certain assumptions against external market data and we considered the assumptions based on our knowledge of the Group and its industries.
- ▶ Assessed the mathematical accuracy of the discounted cash flow models.
- ▶ Ensured cash flows reflected Board approved budgets.
- ▶ Performed sensitivity analyses on CGU's with a higher risk of impairment.
- ▶ Considered the historical accuracy of the Group's forecasts.
- ▶ Assessed the adequacy of the Group's disclosures in respect of asset carrying values and impairment testing.

Revenue recognition - percentage of completion

Why significant

Revenue for certain sales contracts is determined on a percentage of completion basis. For the year ending 30 June 2018, the construction work in progress receivables amounted to \$2.4 million in respect of these contracts.

Revenue is recognised by the Group after assessing all factors relevant to each contract, including specifically assessing the following as applicable:

- ▶ The stage of completion at reporting date.
- ▶ The estimation of total contract revenue and costs including the estimation of cost contingencies.
- ▶ The determination of contractual entitlement and assessment of customer approval of variations and acceptance of claims.
- ▶ The estimation of the project completion date.

Determining percentage of completion requires significant estimation and gives rise to a risk of incorrect revenue recognition. Accordingly, this was considered to be a key audit matter.

How our audit addressed the key audit matter

Our procedures included the following:

- ▶ Assessed the estimates applied within the percentage of completion calculation by focusing our work on the costs incurred for work undertaken to year end and assessing the estimated cost to completion for a sample of contracts. In assessing the estimated cost to completion, we considered the historical accuracy of the Group's forecasts as well as consistency of margins applied.
- ▶ Evaluated the significant judgments made by the Group. In doing so, we examined project documentation and enquired of the status of projects under construction with representatives of the Group.
- ▶ Examined evidence to support scope variations and claims including evidence of client approval.
- ▶ We enquired with the Group as to whether there were any outstanding legal proceedings in respect of construction contracts and confirmed their response through an assessment of legal confirmations received.
- ▶ Based on the determined percentage of completion we recalculated the revenue that should be recorded.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCHAFFER CORPORATION LIMITED year ended 30 June 2018



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Employee participation units (EPU's)

Why significant

EPU's were issued to certain employees of Howe Automotive Limited, a controlled entity of the Group ("Howe") as a performance incentive. At the time of redemption, EPU holders are paid a cash bonus from Howe calculated based on the terms of the Employee Incentive Plan Rules. The Group then has the option to compel EPU participants to subscribe to Schaffer Corporation Limited ('SFC') shares with this cash. Up to 31 October 2017, the Company expected to compel the EPU participants to subscribe to SFC shares and this was considered to be an equity settled share based payment.

On 1 November 2017 there was a change in expectation based on a higher probability, that in the future the Company would not compel employees to use the whole of part of the cash payment received to subscribe to SFC shares, but rather let the employees retain the cash paid. There were no changes to the plan rules and the Company retains the option to compel EPU Participants to subscribe to shares if it so chooses.

Due to the new expectation that EPU participants would retain the cash payment, a provision was recognised. The amount recognised was based on a number of assumptions, as described in Note 27 (c).

How our audit addressed the key audit matter

Our procedures included the following:

- ▶ Our valuation experts assessed whether the model used by the Group to calculate the provision was appropriate based on the rules of the EPU's.
- ▶ Tested the mathematical accuracy of the model.
- ▶ We assessed the reasonableness of the assumptions applied by:
 - ▶ Agreeing the expected earnings to Board approved budgets.
 - ▶ Evaluating the Group's assumptions regarding timing and probability of payment by considering historical payments made.
 - ▶ Determining whether the discount rate applied was appropriate.

Information other than the financial report and auditor's report

The directors are responsible for the other information. The other information comprises the information included in the Company's 2018 Annual Report, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and we do not express any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

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, 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.

Directors' responsibilities 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.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCHAFFER CORPORATION LIMITED year ended 30 June 2018



Building a better
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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 related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or 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 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 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 entity'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 in the preparation of the financial report. We also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events and conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the disclosures in the financial report about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial report. However, future events or conditions may cause an entity 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 consolidated financial statements represent 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.

**INDEPENDENT AUDITOR'S REPORT
TO THE MEMBERS OF SCHAFFER CORPORATION LIMITED**
year ended 30 June 2018



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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 Remuneration Report

Opinion on the Remuneration Report

We have audited the Remuneration Report included in the Directors' Report for the year ended 30 June 2018.

In our opinion, the Remuneration Report of Schaffer Corporation Limited for the year ended 30 June 2018 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

Philip Teale
Partner
Perth
21 September 2018

DIRECTORS' REPORT

year ended 30 June 2018

DIRECTORS' REPORT

Your directors submit their report for the year ended 30 June 2018 made in accordance with a resolution of the Directors.

DIRECTORS

Details of the Directors of the company during the financial year and up to the date of this report are:

| | |
|--|---|
| J M SCHAFFER AM BCom(Hons) FCPA Managing Director Executive Director since 6/9/1972 | Mr John Schaffer AM joined the company in 1972. Mr Schaffer has held the position of Managing Director since 1987. |
| D E BLAIN AM BA Non-executive Director Appointed 5/6/1987 | Mrs Danielle Blain AM joined the company in 1987. Mrs Blain served as Managing Director of Gosh Leather Pty Ltd from 1993 to 2001. Mrs Blain has diverse experience serving on a number of NGO boards and is also a past Pro Chancellor of Edith Cowan University. |
| A K MAYER Executive Director Appointed 21/11/2001 | Mr Anton Mayer is the Executive Chairman of Howe Automotive Limited. Mr Mayer has over 50 years of international leather experience, broad business skills and a global business perspective. |
| M D PERROTT AM BCom FAIM FAICD Independent Director Appointed 23/2/2005 | Mr Michael Perrott AM joined the Board as an independent director in February 2005. Mr Perrott has over 40 years' experience in the construction and contracting industry. During the past three years, Mr Perrott has also served as a director of the following other listed companies: GME Resources Ltd 21 November 1996 – 17 March 2017 |
| D J SCHWARTZ Independent Director Appointed 29/6/1999 | Mr David Schwartz joined the Board as an independent director in June 1999. He has over 25 years' experience negotiating acquisitions and overseeing the development of property. Over the past 40 years, Mr Schwartz has been involved in many different businesses including retail, manufacturing and distribution. |

Directors were in office for the entire period unless otherwise stated.

COMPANY SECRETARY

J M CANTWELL BBus(Acc) CPA MBA GIA(Cert)

Mr Jason Cantwell joined the company in 2011 and has over 20 years' experience in senior financial management roles within both private and publicly listed companies. Mr Cantwell is a Member of CPA Australia and a Certificated Member of the Governance Institute of Australia.

ATTENDANCE AT BOARD MEETINGS

During the year, eight directors' meetings were held. The number of meetings attended by each director is as follows:

| | Meetings eligible to attend | Meetings attended |
|-----------------|-----------------------------|-------------------|
| J M Schaffer AM | 8 | 8 |
| D E Blain AM | 8 | 8 |
| A K Mayer | 8 | 8 |
| M D Perrott AM | 8 | 8 |
| D J Schwartz | 8 | 8 |

In accordance with the Articles of Association:

At the SFC Annual General Meeting scheduled for 14 November 2018, Mr A K Mayer and Mrs D E Blain AM will retire by rotation and being eligible, will offer themselves for re-election.

ATTENDANCE AT AUDIT COMMITTEE MEETINGS

During the year, two audit committee meetings were held. Mr D J Schwartz, Mr M D Perrott AM and Mrs D E Blain AM attended both meetings. These committee members are also directors of the company.

ATTENDANCE AT NOMINATION AND REMUNERATION COMMITTEE MEETINGS

The SFC Board established the Nomination and Remuneration Committee on 23 February 2005. The members of this Board sub-committee are Mrs D E Blain AM, Mr M D Perrott AM and Mr D J Schwartz. The Nomination and Remuneration Committee held one meeting during the year with all committee members attending.

INTERESTS IN THE SHARES OF THE COMPANY AND RELATED BODIES CORPORATE

On 21 September 2018 the economic interest of the Directors, including their related parties, in the shares of the Company were:

| | Schaffer Corporation Limited | |
|-----------------|------------------------------|------------------------------|
| | Ordinary shares | Options over ordinary shares |
| J M Schaffer AM | 2,756,930 | – |
| D E Blain AM | 1,562,360 | – |
| A K Mayer | 347,185 | – |
| M D Perrott AM | 1,000 | – |
| D J Schwartz | 585,726 | – |

PRINCIPAL ACTIVITIES

The principal activities of the entities within the consolidated entity, in the course of the financial year were automotive leather, paving, concrete and limestone product manufacture, property and equity investing, and property leasing.

RESULTS

The consolidated entity's operating profit after tax for the financial year was a profit of \$28,160,000 (2017 – \$7,546,000).

OPERATING AND FINANCIAL REVIEW

Please refer to Managing Director's report for details.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

In the opinion of the Directors of the consolidated entity, there has not arisen during the financial year, or in the interval between the end of the financial year and the date of this report, any matter or circumstance that has significantly affected or may significantly affect the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in subsequent financial years.

DIVIDENDS

The following dividends have been paid or declared by the company since the commencement of the financial year.

Dividends paid for the year ended 30 June 2018:

| | \$'000 |
|---|--------------|
| On ordinary shares | |
| – 14¢ per share final, paid on 15 September 2017 | 1,961 |
| – 15¢ per share interim, paid on 16 March 2018 | 2,097 |
| | <u>4,058</u> |
| Dividends paid for the year ended 30 June 2017 | |
| On ordinary shares | |
| – 13¢ per share final, paid on 16 September 2016 | 1,821 |
| – 12¢ per share interim, paid on 17 March 2017 | 1,680 |
| | <u>3,501</u> |
| Not recognised as a liability as at 30 June 2018 | |
| Final franked dividend declared for 2018 – 30¢ (2017 – 14¢) | <u>4,152</u> |

REVIEW OF OPERATIONS

The consolidated entity's revenue from continuing operations increased by 20% to \$227,036,000 from \$188,502,000 this year. This resulted in a pre-tax operating profit of \$34,264,000 compared to \$11,884,000 for last year. The consolidated entity's net profit after tax, excluding non-controlling interests, increased by 298% to \$23,292,000 from \$5,856,000.

DIRECTORS' REPORT

year ended 30 June 2018

LIKELY DEVELOPMENTS AND EXPECTED RESULTS

Other than the discussion of the Company's operations and outlook already set out from pages 1-12 of this Annual Report, the Directors have no further comment to make on likely developments in the operations of the consolidated entity and the expected results of those operations in subsequent financial years.

ENVIRONMENTAL REGULATION AND PERFORMANCE

Schaffer Corporation Limited is subject to a range of environmental regulations. During the financial year Schaffer Corporation Limited met all reporting requirements under any relevant legislation. There were no incidents which required reporting. The Company aims to continually improve its environmental performance.

SIGNIFICANT EVENTS AFTER BALANCE DATE

Following the end of the reporting period, a final fully-franked dividend of 30¢ per share has been declared payable on 14 September 2018.

No other matter or circumstance has arisen since the end of the financial year 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 in subsequent financial periods.

INDEMNIFICATION AND INSURANCE OF DIRECTORS

During or since the financial year, the company has agreed to indemnify directors against a liability for costs and expenses incurred in defending proceedings brought against them for a liability incurred in their role as directors of the company other than in respect of any wilful misconduct. The total amount of insurance contract premiums paid is not disclosed due to a confidentiality clause within the insurance policy.

INDEMNIFICATION OF AUDITORS

To the extent permitted by law, the Company has agreed to indemnify its auditors, Ernst & Young, 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.

REMUNERATION REPORT (AUDITED)

This remuneration report outlines the director and executive remuneration arrangements of the Company and the Group in accordance with the requirements of the Corporations Act 2001 and its Regulations. For the purposes of this report, Key Management Personnel (KMP) of the Group are defined as those persons having authority and responsibility for planning, directing and controlling the major activities of the Company and the Group, directly or indirectly, including any director (whether executive or otherwise) of the parent company.

Details of Key Management Personnel

Directors

| | |
|-----------------|--------------------------------------|
| J M Schaffer AM | Managing Director |
| D E Blain AM | Director (non-executive) |
| A K Mayer | Director (executive) |
| M D Perrott AM | Director (non-executive/independent) |
| D J Schwartz | Director (non-executive/independent) |

Executives

| | |
|------------|--|
| D Birks | General Manager, Howe Automotive Limited |
| R Leib | Chief Financial Officer |
| M Perrella | Executive Director, Delta Corporation Limited |
| J Walsh | General Manager, Delta Corporation Limited |
| J Cantwell | Group Financial Controller and Company Secretary |

This report outlines the remuneration arrangements in place for directors and executives of the Schaffer Corporation Limited Group of companies.

Remuneration philosophy

SFC's remuneration policy is directed at attracting, motivating and retaining quality directors and executives. SFC's key internal performance measures at the business unit and consolidated levels are earnings before interest and tax (EBIT) and return on average capital employed (ROACE). EBIT and ROACE have been chosen by the Group as measures of executive performance because they align the interests of management with those of all SFC shareholders.

Remuneration committee

The SFC Board operates a Nomination and Remuneration Sub-Committee to support and advise the SFC Board in fulfilling its responsibility to shareholders to ensure that the company has remuneration policies and practices which enable it to attract and retain directors and executives who will best contribute towards achieving positive outcomes for shareholders. The committee determines the remuneration and other conditions of service of the chief executive officer and executive directors, if any. The committee makes recommendations to the Board on the remuneration of non-executive directors within the aggregate approved by shareholders in general meeting from time to time. The committee considers individual performance, company performance, internal relativity and fairness in setting levels of remuneration and may seek appropriate independent external advice to assist in its decision making. The structure of non-executive director and executive remuneration are separate and distinct.

SENIOR MANAGER AND EXECUTIVE DIRECTOR REMUNERATION

Objective

SFC's remuneration policy aims to remunerate executives with a level and mix of remuneration commensurate with their position and responsibilities within the Group.

Structure

The remuneration of SFC's senior executive consists of fixed remuneration and variable remuneration (annual and long term incentives). The company aims to reward executives for Company, business unit and individual performance, align executive remuneration with the interests of shareholders, link rewards with the strategic goals such as profitability or return on capital employed and ensure that total remuneration is effective in retaining and motivating senior executives and executive directors.

Fixed remuneration

This includes base salary and the statutory Superannuation Guarantee Contribution (SGC) which comprises the cash component, and other non-cash benefits such as a motor vehicle. Where non-cash benefits are elected, it is intended that the cost to the company is not greater than the cost that would otherwise have been incurred had that portion of the salary been provided as cash. The Schaffer Corporation Limited Superannuation Fund is available to executives for superannuation contributions and life insurance. Premiums for life insurance are deducted from member accounts. Executives can elect to have the company contribute superannuation beyond the statutory SGC level by way of a salary sacrifice in lieu of cash salary. Fixed remuneration is reviewed annually by the Nomination and Remuneration Committee in respect of each executive director. The fixed remuneration of executives is reviewed annually by the SFC Managing Director in the case of the Building Materials and Corporate divisions and by the Howe Automotive Limited General Manager in the case of the Automotive Leather division. The review process considers company-wide, business unit and individual performance in the context of any annual change during the preceding 12-month period to the consumer price index and wages cost index as published by the Australian Bureau of Statistics. For the year beginning 1 July 2018, a 2% increase was applied for Senior Executives.

Variable remuneration – Short-Term Incentive

The Group has performance-based incentive plans in place at each of its operations in which management and the labour force participate. The level of remuneration payable to participating executives is linked to the financial performance of their business. Executives are provided with cash incentives provided profitability thresholds are met. A summary of the annual incentive schemes for the Automotive Leather, Building Materials and Corporate divisions is provided below:

Automotive Leather Division – Profit Participation Scheme

Howe Automotive Limited operates a profit participation scheme for the staff and management of the Automotive Leather division. Prior to the commencement of each financial year, the division management submits an annual budget for consideration and approval by the Howe Automotive Limited Managing Director and the SFC Board. The scheme provides for a bonus pool of 5% of actual EBIT, which becomes payable provided actual EBIT exceeds budgeted EBIT and a specified return on capital employed (ROCE) has been achieved as at 30 June balance date. The profit participation bonus is subject to audited financials of each business unit and approval by the shareholders of Howe Automotive Limited. A full year 2018 bonus was approved (2017 – approved). Actual EBIT performance versus Budgeted EBIT performance and a threshold ROCE have been chosen as the relevant performance conditions as these performance measures are readily monitored and available and EBIT and ROCE performance aligns the interest of management with those of shareholders. The scheme has been designed to incentivise a wide range of the Automotive Leather division workforce from top executive management to factory floor personnel.

DIRECTORS' REPORT

year ended 30 June 2018

Building Materials Division – Management Bonus Incentive Scheme

The Company operates a Management Bonus Incentive Scheme (MBIS) for the management group of the Building Materials division. Prior to the commencement of each financial year the Building Materials division management submits an annual budget for consideration by SFC's Managing Director and the SFC Board. Upon approval of the budget by the Board, a cash bonus (as a percentage of each participant's fixed remuneration) is payable on a tiered basis provided actual EBIT profitability thresholds are met/exceeded as at 31 December and 30 June balance dates. The MBIS payment for EBIT performance is subject to reviewed/audited financial statements of each business unit and is payable at the discretion of the Managing Director in the following period. Neither a half-year bonus nor full-year bonus was approved for the year ended 30 June 2018 (2017 – no bonuses approved). A bonus is forfeited for a financial year where an employee has ceased employment prior to the end of that financial year.

Actual EBIT performance versus Budgeted EBIT performance has been chosen as the relevant performance condition as this performance measure is readily monitored and available, and EBIT performance aligns the interest of management with those of shareholders. The scheme may be discontinued at any time by the SFC Managing Director without prior notice.

Corporate – Short-Term Incentive Plan

SFC has implemented a formal Short Term Incentive (STI) Plan for the Group Managing Director, Chief Financial Officer and Group Financial Controller approved by the Nomination and Remuneration Committee. These executives can earn a cash bonus with a value of up to 30% of their base annual remuneration, based on actual performance against defined objectives. This equates to a maximum of \$256,023 for the Group Managing Director, \$75,000 for the Chief Financial Officer and \$63,011 for the Group Financial Controller, for the year ended 30 June 2018. The minimum possible award for the Group Managing Director, Chief Financial Officer and the Group Financial Controller is nil. 60% of any STI award is based on financial performance against the annual budget, however no STI bonus is payable if the annual net profit after tax (NPAT) is less than the prior year. The members of the Nomination and Remuneration Committee have the discretion to adjust the NPAT for STI purposes to eliminate the financial impact of "one off" abnormal issues which may positively or negatively affect NPAT, including adjustments related to accounting judgments on factors which may or may not eventuate and that are not reflective of management performance. 40% of any STI award is based on performance against pre-agreed KPI's which are critical to the company's future success. The Nominations and Remuneration Committee approved STI awards for the 2018 year on 14 August 2018. The managing director received an STI award of 97.5% (2017: 82.5%) of the maximum possible award. The Chief Financial Officer received an STI award of 100% (2017: N/A). The Group Financial Controller received an STI award of 98.5% (2017: 90%) of the maximum possible award.

Variable remuneration – Long-Term Incentive

Long-term incentive grants are typically made to executives who are able to influence the generation of shareholder wealth and thus have a direct impact on the Company's performance. Howe Automotive Limited operates the Employee Participation Unit (EPU) Plan for its executives. SFC's senior executives (other than Mr Schaffer and Mr Mayer) can participate in SFC's Employee Share Option Plan (ESOP). The Howe Automotive Limited EPU and SFC ESOP plans have long-term vesting provisions and are designed to align the interests of the participating executives with those of all SFC shareholders. A summary of the long-term incentive schemes is provided below:

Howe Automotive Limited Employee Participation Units Plan

Howe Automotive Limited operates an employee incentives plan which permits the granting of employee participation units (EPUs) at the discretion of its shareholders up to an EPU limit. The EPU limit is 10% of the fully diluted share capital of Howe Automotive Limited, which is calculated as if each EPU already issued was deemed to be one issued Howe Automotive Limited share. Howe Automotive Limited dividends, divided by the total number of shares and EPUs on issue, is applied to reduce a bonus threshold for each EPU until the balance of the bonus threshold is reduced to nil. Once the threshold is nil, each EPU receives a remuneration bonus payment when Howe Automotive Limited makes a dividend payment, calculated based on the total dividends divided by the total number of shares and EPUs on issue.

An EPU provides an employee with a right to receive either, at the discretion of SFC, a cash payment from Howe Automotive Limited or shares in SFC in the following circumstances:

- If an employee dies or becomes permanently disabled at any time after the grant date.
- If an employee ceases employment after the three year initial vesting period.
- Upon a liquidity event (trade sale or listing on an Australian or overseas stock exchange).
- On issue of a compulsory payment notice by SFC.

The amount of the payment is dependent on vesting and the financial performance of Howe Automotive Limited. The vesting requirements are:

- up to 3 years – nil
- 3 years to 4 years – 33.3%
- 4 years to 5 years – 66.7%
- over 5 years – 100%

Note: Employees are ineligible to receive any payment in the following circumstances:

- termination due to misconduct.
- failure to provide 90 days' written notice of intention to terminate employment.
- acting in competition prior to the payment date (payment date is at least 12 months after termination).

The performance hurdle to be eligible for a payment is a positive equity valuation for Howe Automotive Limited. The eligibility and amount of payment is calculated in accordance with an equity valuation formula based on 5.5 times Howe Automotive Limited's earnings before interest and tax minus net debt. The formula uses a three-year average including one full year following termination. This formula is designed to incentivise EPU holders in respect of building the long term value of Howe Automotive Limited and provides a fair and readily calculable means for valuing that long term interest.

SFC has the option to compel the employee to use the whole or part of that cash payment in subscribing for SFC shares based on the average SFC share price for the same three-year period.

SFC Employee Share Option Plan (ESOP)

An employee share option plan has been established. The plan was approved by shareholders at the Annual General Meeting in November 1999. The plan permits the granting of options (at the absolute discretion of the Board) to Group employees to acquire ordinary shares in SFC. The options issued for nil consideration, are issued in accordance with performance guidelines established by the Directors of SFC. The options cannot be transferred and will not be quoted on the ASX. The number of options which can be issued is limited to 5% of the number of shares on issue. At the date of this report, there were 140,000 options on issue (2017: 70,000)

Options may be exercised as follows:

- during the first 12 months of each option period and including each date of issue, no more than 25% of the options issued to that participant on that date of issue;
- during the period of 24 months from and including each date of issue exercise no more than 50% of the options issued to that participant on that date of issue; and
- during the period of 36 months from and including each date of issue exercise no more than 75% of the options issued to that participant on that date of issue.

After 36 months, 100% of the options may be exercised.

While the ESOP contains vesting conditions, the exercising of ESOP options is not dependent on a performance condition because (1) ESOP options have been issued with an exercise price at or above the VWAP of the share price on five preceding days that SFC shares traded on the ASX before the issue date; (2) ESOP options do not participate in dividends; and (3) are not transferable or saleable. Accordingly, ESOP options only provide an economic benefit to the recipient in the event the share price (which adjusts for dividends paid) significantly exceeds the exercise price (which is not adjusted for dividends paid) over the option vesting period thereby aligning the interests of management with those of all shareholders.

DIRECTORS' REPORT

year ended 30 June 2018

The following table details the proportion of fixed remuneration and variable remuneration paid for the year ended 30 June 2018 as detailed in this report:

| | 2018 Remuneration Structure | |
|-----------------------------|-----------------------------|------------|
| | % Fixed | % Variable |
| Specified Directors | | |
| J M Schaffer AM | 73 | 27 |
| D E Blain AM | 100 | — |
| A K Mayer | 67 | 33 |
| M D Perrott AM | 100 | — |
| D J Schwartz | 100 | — |
| Specified Executives | | |
| D Birks | 11 | 89 |
| R Leib | 28 | 72 |
| J Walsh | 100 | — |
| M Perrella | 100 | — |
| J Cantwell | 75 | 25 |

Non-executive Director Remuneration

SFC's non-executive directors receive fees for their services (including statutory superannuation) and the reimbursement of reasonable expenses. The Constitution and the ASX Listing Rules specify that the aggregate remuneration of non-executive directors shall be determined from time to time by a general meeting. An amount not exceeding that amount is then divided between the non-executive directors as agreed. The latest determination was at the Annual General Meeting held 19 November 2003 when shareholders approved an aggregate remuneration limit of \$250,000 per annum. The amount of aggregate remuneration to be approved by shareholders and the manner in which it is to be apportioned amongst the non-executive directors is reviewed annually. This limit is not currently fully utilised. The fee pool is payable only to non-executive directors. The amount payable to non-executive directors is set by the Board after having taken regard to the size of the Company and Board, the responsibilities, demands and accountabilities faced by those directors in discharging their duties and after seeking external advice to ensure the fees are in line with market standards. All three non-executive directors are members of the Audit Committee and the Nomination and Remuneration Committee and the fixed annual fee received by non-executive directors is inclusive of these sub-committee commitments. It is current SFC policy that non-executive directors do not receive shares, options or other securities and are not eligible to participate in SFC's Employee Share Option Plan. Payment of fees (including statutory superannuation) and the

reimbursement of reasonable expenses are the only remuneration payable to Mrs Blain AM, Mr Schwartz and Mr Perrott AM.

Non-executive directors appointed prior to July 2003 are entitled to a retirement benefit equivalent to one year's annual director's fees. The retirement benefit was reduced from three years' to one year's annual director's fees in July 2003 (a three-year retirement benefit was in place at the time Mrs Blain AM and Mr Schwartz accepted their appointment to the Board). SFC considers the reduced benefit modest and appropriate given the benefit which historically existed. It is SFC's policy that no retirement benefit apply to new directors appointed after July 2003.

It is not a requirement of the Constitution of the Company that directors hold shares in the Company.

Relationship of Company Performance to Shareholder Wealth

Total Shareholder Return

Total shareholder return (TSR) is an accepted and understood measure of performance. SFC calculates TSR as follows:

- movement in Share Price (including bonus issues)
- plus Dividends Paid
- plus Dividend Imputation Credits

The chart below itemises the constituents to SFC's TSR by year for each of the past five years. SFC's average TSR for the past five years is 42%.

| | Sept 2014 | Sept 2015 | Sept 2016 | Sept 2017 | Sept 2018 |
|-------------------|-----------|-----------|-----------|-----------|-----------|
| Tax Rate | 30% | 30% | 30% | 30% | 30% |
| Share Price | \$6.00 | \$4.81 | \$5.46 | \$7.55 | \$17.05 |
| Ord Dividends | \$0.25 | \$0.25 | \$0.25 | \$0.26 | \$0.45 |
| Imputation Credit | \$0.11 | \$0.11 | \$0.11 | \$0.11 | \$0.19 |
| TSR | \$1.30 | (\$0.83) | \$1.01 | \$2.46 | \$10.14 |
| TSR | 26% | (14%) | 21% | 45% | 134% |

At the date of this report, on an aggregate dollars paid basis, SFC paid to shareholders \$6.3 million fully-franked dividends in respect of 2018 and a total of \$20.4 million was paid in fully-franked ordinary and special dividends over the past 5 years.

Earnings Per Share (EPS)

SFC's average EPS over the past five years has been 63.7¢.

| | June 2014 | June 2015 | June 2016 | June 2017 | June 2018 |
|-----|-----------|-----------|-----------|-----------|-----------|
| EPS | 44.1¢ | 25.2¢ | 40.6¢ | 41.8¢ | 166.7¢ |

Remuneration of Key Management Personnel for the year ended 30 June 2018

| | Short term | | Long term benefits | | Post employment | | Total | Performance related |
|---------------------|---------------|------------------------|-----------------------------------|--|-----------------|--------------------------|-----------|---------------------|
| | Salary & fees | Cash bonus | Long service leave ⁽²⁾ | Share-based payment-EPU's ⁽⁴⁾ | Superannuation | Termination benefit | | |
| 30 June 2018 | \$ | \$ | \$ | | \$ | \$ | \$ | |
| Directors | | | | | | | | |
| J M Schaffer AM | 872,354 | 349,622 ⁽³⁾ | 29,314 | — | 25,000 | 17,068 | 1,293,358 | 27.03% |
| D E Blain AM | 54,778 | — | — | — | 25,000 | 1,596 | 81,374 | 0.00% |
| A K Mayer | 509,862 | 251,373 | — | — | — | — | 761,235 | 33.02% |
| M D Perrott AM | 79,778 | — | — | — | — | — | 79,778 | 0.00% |
| D J Schwartz | 79,778 | — | — | — | — | 3,022 | 82,800 | 0.00% |
| Executives | | | | | | | | |
| D Birks | 332,712 | 1,061,560 | (18,997) | — | 25,000 | 1,783,582 ⁽¹⁾ | 3,183,857 | 89.36% |
| R Leib | 233,993 | 207,716 | 7,596 | 11,918 | 20,049 | 489,181 ⁽¹⁾ | 970,453 | 71.81% |
| J Walsh | 331,234 | — | 6,701 | — | 25,000 | — | 362,935 | 0.00% |
| M Perrella | 160,977 | — | 6,760 | — | 25,000 | — | 192,737 | 0.00% |
| J Cantwell | 191,936 | 74,618 | 4,037 | 4,767 | 18,679 | — | 294,037 | 25.38% |
| | 2,847,402 | 1,944,889 | 35,411 | 16,685 | 163,728 | 2,294,449 | 7,302,564 | |

⁽¹⁾ Termination benefits for Mr Birks and Mr Leib include a provision for EPU's based on projections of future earnings.

This provision can increase or decrease based on profit expectations of Howe Automotive Limited

⁽²⁾ Net of long service leave taken during the period.

⁽³⁾ \$100,000 of Mr Schaffer's cash bonus relates to performance for the year ending 30 June 2017.

⁽⁴⁾ Includes the value of options issued under the SFC Employee Share Options Plan (ESOP) using the Black-Scholes model.

DIRECTORS' REPORT

year ended 30 June 2018

The amounts included in the table below represent the entire bonus earned by the following Key Management Personnel:

| | Percentage paid during the year | Percentage payable subsequent to year end |
|----------------|---------------------------------|---|
| JM Schaffer AM | 29% | 71% |
| A Mayer | 100% | – |
| R Leib | – | 100% |
| D Birks | 40% | 60% |
| J Cantwell | 17% | 83% |

The portion of bonus accrued at 30 June 2018 was 59.6%.

The elements of emoluments have been determined on the basis of the cost to the company and the consolidated entity.

Executives are those directly accountable for the operational management and strategic direction of the company and the consolidated entity.

Remuneration of Key Management Personnel for the year ended 30 June 2017

| | Short term | | Long term benefits | | Post-employment | | Total | Performance related |
|----------------------------|---------------|------------|-----------------------------------|--|-----------------|---------------------|-----------|---------------------|
| | Salary & fees | Cash bonus | Long service leave ⁽⁴⁾ | Share-based payment-EPU's ⁽¹⁾ | Superannuation | Termination benefit | | |
| 30 June 2017 | \$ | \$ | \$ | \$ | \$ | \$ | \$ | |
| Directors | | | | | | | | |
| J M Schaffer AM | 830,630 | 207,077 | 18,949 | – | 35,000 | 16,734 | 1,108,390 | 18.68% |
| D E Blain AM | 43,214 | – | – | – | 35,000 | 1,870 | 80,084 | 0.00% |
| A K Mayer | 532,631 | – | – | – | – | – | 532,631 | 0.00% |
| M D Perrott AM | 78,214 | – | – | – | – | – | 78,214 | 0.00% |
| D J Schwartz | 78,214 | – | – | – | – | 7,637 | 85,851 | 0.00% |
| Executives | | | | | | | | |
| D Birks ⁽²⁾ | 270,533 | 13,305 | 14,205 | 783 | 25,632 | – | 324,458 | 4.10% |
| N Filipovic ⁽³⁾ | 177,852 | – | 3,403 | 969 | 15,834 | 427,631 | 625,689 | 0.00% |
| M Perrella | 149,201 | – | 7,027 | – | 33,958 | – | 190,186 | 0.00% |
| J Walsh | 293,107 | – | 9,491 | – | 28,432 | – | 331,030 | 0.00% |
| J Cantwell | 197,458 | 48,028 | 3,473 | – | 22,426 | – | 271,385 | 19.38% |
| | 2,651,054 | 268,410 | 56,548 | 1,752 | 196,282 | 453,872 | 3,627,918 | |

⁽¹⁾ Includes the value of employee participation units (EPUs) using the Black-Scholes model.

⁽²⁾ Mr D Birks appointed to General Manager – Howe Automotive Limited on 5 December 2016.

⁽³⁾ Mr N Filipovic employed as Managing Director – Howe Automotive Limited to 12 December 2016.

⁽⁴⁾ Net of long service leave taken during the period

The amounts included in the table below represent the entire bonus earned by the following Key Management Personnel:

| | Percentage paid during the year | Percentage payable subsequent to year end |
|-----------------|---------------------------------|---|
| J M Schaffer AM | – | 100% |
| J Cantwell | – | 100% |
| D Birks | 100% | – |

The portion of bonus accrued at 30 June 2017 was 95%.

The following information is provided in relation to s300A(1)(e)(ii) – (vi) of the Corporations Act:

SHAREHOLDING OF KEY MANAGEMENT PERSONNEL

Economic interests in the shares of Schaffer Corporation Limited held by Directors of the reporting entity and their related parties are as follows:

| As at 30 June 2018 | Balance at beginning of year | Net change other | Balance at end of year |
|-----------------------------|------------------------------|------------------|------------------------|
| Specified directors | | | |
| D E Blain AM | 1,562,360 | – | 1,562,360 |
| A K Mayer | 347,185 | – | 347,185 |
| M D Perrott AM | 1,000 | – | 1,000 |
| J M Schaffer AM | 2,655,927 | 101,003 | 2,756,930 |
| D J Schwartz | 585,726 | – | 585,726 |
| Specified executives | | | |
| J Cantwell | 450 | – | 450 |
| J Walsh | 2,500 | – | 2,500 |
| M Perrella | 59,834 | – | 59,834 |
| Total | 5,214,982 | 101,003 | 5,315,985 |

DIRECTORS' REPORT

year ended 30 June 2018

SHARE OPTIONS

a) Options issued over ordinary shares as part of an employee share scheme are as follows:

| Date issued | No. on issue 30 June 2017 | Issued during the year | Forfeited during the year | Exercised during the year | No. on issue 30 June 2018 | Exercise price | First exercise date | Last exercise date |
|-------------|------------------------------|---------------------------|---------------------------|------------------------------|------------------------------|----------------|------------------------|-----------------------|
| 6 Sep 2017 | – | 70,000 | – | – | 70,000 | \$7.54 | 6 Sep 2017 | 6 Sep 2022 |

b) Remuneration options: Granted and vested during the year

During the financial year options were granted as equity compensation benefits to certain executives as disclosed below. The options were issued free of charge. Each option entitles the holder to subscribe for one fully paid ordinary share in the entity at an exercise price of \$7.54.

| | Granted number | Grant date | Value per option at grant date | Exercise price per share | Vested No. during year | Vested as at 30 June 2018 | |
|-------------------|----------------|------------|-----------------------------------|-----------------------------|---------------------------|------------------------------|---------------|
| | | | | | | Vested | Not vested |
| Executives | | | | | | | |
| R Leib | 50,000 | 6 Sep 2017 | \$0.86 | \$7.54 | 12,500 | 12,500 | 37,500 |
| J M Cantwell | 20,000 | 6 Sep 2017 | \$0.86 | \$7.54 | 5,000 | 5,000 | 15,000 |
| Total | 70,000 | | | | 17,500 | 17,500 | 52,500 |

EPU's held by Key Management Personnel

| | Balance at beginning of period | Granted as remuneration | Redeemed during the period | Cancelled during the period | Vested as at 30 June 2018 | | |
|-------------------|--------------------------------------|----------------------------|-------------------------------|--------------------------------|-----------------------------|----------------|----------------|
| 30 June 2018 | | | | | Balance at end of period | Vested | Not vested |
| Executives | | | | | | | |
| D Birks | 1,000,000 | 200,000 | – | – | 1,200,000 | 966,667 | 233,333 |
| R Leib | – | 300,000 | – | – | 300,000 | – | 300,000 |
| Total | 1,000,000 | 500,000 | – | – | 1,500,000 | 966,667 | 533,333 |

| | Balance at beginning of period | Granted as remuneration | Redeemed during the period | Cancelled during the period | Vested as at 30 June 2017 | | |
|-------------------------------|--------------------------------------|----------------------------|-------------------------------|--------------------------------|-----------------------------|------------------|---------------|
| 30 June 2017 | | | | | Balance at end of period | Vested | Not vested |
| Directors / executives | | | | | | | |
| D Birks | 1,000,000 | – | – | – | 1,000,000 | 933,333 | 66,667 |
| N Filipovic | 1,320,627 | – | – | (100,000) | 1,220,627 | 1,220,627 | – |
| Total | 2,320,627 | – | – | (100,000) | 2,220,627 | 2,153,960 | 66,667 |

Shares issued on exercise of compensation options and EPU's

No shares were issued during the current or previous year.

Employment contracts

Mr Schaffer, SFC's Managing Director, is employed under a Service Agreement. The service agreement was entered into on 18 July 1984. Mr Schaffer's employment continues until terminated by Mr Schaffer or the Company. Under the terms of the service agreement, the agreement may be terminated by the Company or Mr Schaffer after the expiration of one month's notice in writing given to one of them by the other. Upon termination of this agreement, Mr Schaffer is entitled to receive from the Company a lump sum equal to the annual remuneration paid immediately preceding that termination, except if the termination is for reasons of gross misconduct, fraud or dishonesty resulting in a material loss or injury to the Company or if Mr Schaffer is found guilty of wilful disobedience or any other conduct resulting in a material prejudice to the Company or such as to bring the Company into disrepute.

Mr Mayer provides management services to the Automotive Leather division pursuant to a Consultancy Agreement. The agreement was renewed for the period 1 July 2018 to 30 June 2021. The Consultancy Agreement may be terminated sooner:

- by the consultee without prior notice for cause (i.e. wilful misconduct, wilfully wrongful act, gross negligence, criminal act or a prohibition by law in company management);
- by either party for any reason upon 90 days prior written notice to the other party;
- by the consultee 30 days after giving notice of termination to Mr Mayer for reason of his physical or mental incapacity on a permanent basis;
- on the death of Mr Mayer.

The Consultancy Agreement with Mr Mayer does not provide for a termination payment upon termination of the agreement.

All other senior executives are employed under standard employment contracts that define the role, duties, remuneration and benefits, leave entitlements, dismissal and confidentiality of information conditions of employment. Notice periods are typically one month.

End of remuneration report

TAX CONSOLIDATION

Effective 1 July 2003, for purposes of income tax, Schaffer Corporation Limited and its 100% owned subsidiaries have formed a tax consolidated group.

Effective 1 July 2003 for purposes of income tax, Howe Automotive Limited and its 100% owned Australian resident subsidiaries for tax purposes have formed a tax consolidated group.

ROUNDING

The amount contained in this report and in the financial statements has been rounded to the nearest \$1,000 under the option available to the company under ASIC Instrument 2016/191 Corporations (Rounding in Financial/Directors Report).

CORPORATE GOVERNANCE

In recognising the need for the highest standards of corporate behaviour and accountability, the directors of Schaffer Corporation Limited support the principles contained in the company's corporate governance statement in the corporate governance section of this annual report.

AUDITOR'S INDEPENDENCE AND NON-AUDIT SERVICES

The directors received the following declaration from the auditor of Schaffer Corporation Limited.

DIRECTORS' REPORT

year ended 30 June 2018



Building a better
working world

Ernst & Young
11 Mounts Bay Road
Perth WA 6000 Australia
GPO Box M939 Perth WA 6843

Tel: +61 8 9429 2222
Fax: +61 8 9429 2436
ey.com/au

Auditor's Independence Declaration to the Directors of Schaffer Corporation Limited

As lead auditor for the audit of Schaffer Corporation Limited for the financial year ended 30 June 2018, 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 audit; and
- b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Schaffer Corporation Limited and the entities it controlled during the financial year.

A handwritten signature in cursive script that reads 'Ernst & Young'.

Ernst & Young

A handwritten signature in cursive script that reads 'Philip Teale'.

Philip Teale
Partner
21 September 2018

DIRECTORS' REPORT

year ended 30 June 2018

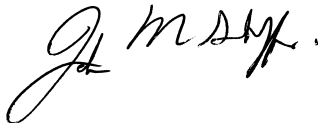
NON-AUDIT SERVICES

The following non-audit services were provided by the entity's Auditor, Ernst & Young. The directors are satisfied that the provision of non-audit services is compatible with the general standard of independence for auditors imposed by the Corporations Act. The nature and scope of each type of non-audit service provided means that auditor independence was not compromised.

Ernst & Young received or are due to receive the following amounts for the provision of non-audit services:

Tax compliance, research and development claims \$101,092

Signed in accordance with a resolution of the directors.

A handwritten signature in black ink, appearing to read 'J M Schaffer', with a stylized flourish at the end.

J M Schaffer AM
Chairman and Managing Director
Perth, 21 September 2018

STATEMENT OF CORPORATE GOVERNANCE PRACTICES

year ended 30 June 2018

ASX Corporate Governance Council issued its third edition of the Corporate Governance Principles and Recommendations on 27 March 2014 with effect from 1 July 2014.

"Corporate Governance is the framework of rules, relationships, systems and processes within and by which authority is exercised and controlled in corporations. It encompasses the mechanisms by which companies, and those in control, are held to account. Different entities may legitimately adopt different governance practices, based on a range of factors, including their size, complexity, history and corporate culture." (ASX Corporate Governance Principles and Recommendations, March 2014).

The Board of SFC is committed to best practice in corporate governance where the Board considers these practices are appropriate and add shareholder value to a company and board of SFC's size and structure.

This Corporate Governance Statement outlines the main corporate governance practices of Schaffer in the context of the Principles adopted by the ASX Corporate Governance Council (Council). Unless otherwise stated below, the Company has complied with the Council's Recommendations.

LAY SOLID FOUNDATIONS FOR MANAGEMENT AND OVERSIGHT

The strategic control of the business of the Group is vested with the Board. The Board's objective to create, build and sustain shareholder value is carried out in accordance with their duties and obligations to act honestly, fairly, diligently as are imposed upon them by the Constitution, regulatory authorities and ethical standards. Key matters reserved for the Board include the following:

- Approval of the Strategic Business Plan
- Approval of the Annual Budgets
- Review of the operating results and approval of the financial accounts
- Setting the Corporate Governance practices within the Group
- Determining SFC's dividend policies
- Approval of the Group financial policies
- Approval of the Group risk management strategies
- Review of Board nominations and composition
- Determining the terms and conditions for and evaluate the performance of the Managing Director
- Delegation of authority to the Managing Director and senior management on operational matters, or approval of matters in excess of any discretion which may have been delegated from time to time
- Acquisition, establishment, disposal or cessation of any significant business of SFC
- Approving the issue of any securities in SFC
- Approving the capital management strategy of SFC
- Approving the appointment of SFC's External Auditor

The Board has delegated authority for the management of the Group through the Managing Director to executive management. Accordingly, the Group's executive management team are charged with implementing Board directives and the day-to-day management and reporting of the Group's activities. The Board has a formal Charter setting out the roles of Board and Management. Consistent with Council Principle 1, the Board Charter has been posted to the corporate governance section of the Company's website – www.schaffer.com.au

STRUCTURE THE BOARD TO ADD VALUE

The Schaffer Board currently consists of five directors: two independent; one non-executive; and two executive directors namely the Executive Chairman of the Leather division and the Group Managing Director and Chairman. The Board considers that between them, the directors bring the range of skills, knowledge and experience (both local and international) necessary to successfully direct the Group's operations.

The Board of Directors consists of:

John Schaffer AM *Chairman and Managing Director*
(Age 68)

John joined the Company in 1972 and has held the positions of Managing Director since 1987 and Chairman since 1988. John holds a Bachelor of Commerce degree with honours from the University of Western Australia and is an FCPA.

Danielle Blain AM *Non-executive Director*
(Age 74)

Danielle joined the Board in 1987. Mrs Blain served as a director of Howe Automotive Limited from 1993 to 2005 and as Managing Director of Gosh Leather Pty Ltd (the furniture division) from 1993 to 2001. Mrs Blain holds a Bachelor of Arts degree from the University of Western Australia and is a member on several NGO boards. Mrs Blain is a member of the Board's Audit Committee and the Nomination and Remuneration Committee.

Michael Perrott AM *Independent Director*
(Age 72)

Michael joined the Board as an independent director in February 2005 and is a member of the Board's Audit Committee and the Nomination and Remuneration Committee. Mr Perrott has been involved in industries associated with construction, contracting, mining and land development since 1969.

Anton Mayer *Executive Director*
(Age 76)

Anton joined the Board in 2001. Anton is the Executive Chairman of Howe Automotive Limited, and held the position of Howe Automotive Limited Managing Director from 1998 to June 2007. Anton is also a director of a number of the Howe Automotive Limited Group subsidiaries. Anton has over 50 years of international leather experience, broad business skills and a global business perspective.

David Schwartz *Independent Director*
(Age 64)

David joined the Board in 1999 and is independent Chairman of the Board's Audit Committee and the Nomination and Remuneration Committee. David has many years' experience in successfully managing manufacturing and distribution businesses in Australia and South Africa, and over 25 years' experience negotiating acquisitions and overseeing the development of property. Mr Schwartz is Chairman of Stefani Pure Water Australasia Pty Limited and a director of Primewest Management Ltd.

The names of Schaffer's current directors, their year of appointment, status as non-executive, executive or independent directors, their economic interest in SFC and whether they retire at the next Annual General Meeting is summarised in the table below.

| Director | Year appointed | Classification | Audit Committee | Nomin. & Remun. Committee | Economic Interest in SFC | Retiring at next AGM | Seeking Re-election |
|-----------------|----------------|--------------------|-----------------|---------------------------|--------------------------|----------------------|---------------------|
| J M Schaffer AM | 1972 | Chairman/Executive | – | – | 19.9% | No | N/A |
| D E Blain AM | 1987 | Non-executive | Member | Member | 11.3% | Yes | Yes |
| A K Mayer | 2001 | Executive | – | – | 2.5% | Yes | Yes |
| M D Perrott AM | 2005 | Independent | Member | Member | – | No | N/A |
| D J Schwartz | 1999 | Independent | Chairman | Chairman | 4.2% | No | N/A |

STATEMENT OF CORPORATE GOVERNANCE PRACTICES

year ended 30 June 2018

BOARD COMMITTEES

The Board may from time to time establish committees where the Board is of the belief that the establishment of such a committee will improve the performance of the Board in accomplishing its duties.

The Board operates an Audit Committee and a Nomination and Remuneration Committee. Both committees comply with Council guidelines. The Charter of each committee is summarised later in this section. Full details of SFC Audit Committee and Nomination and Remuneration Committee can be found on the Company's website. The Board does not believe the Board is of sufficient size to warrant the establishment of additional dedicated Board Committees.

BOARD MEETINGS

Management provides the Board with information in a form, timeframe and quality that facilitates the Board in effectively discharging its duties. The Board meets at least 8 times per year. Board papers are, where possible, provided to directors at least four days prior to the relevant meeting. The non-executive Board members are joined at Board meetings by the Group's Managing Director, the Executive Chairman of Howe Automotive Limited and the Company's Company Secretary.

BOARD AND MANAGEMENT EVALUATION

Under the Board Charter, the Chairman is responsible for ensuring that board meetings are conducted competently and ethically and that Directors individually and as a group have opportunities to air differences, explore ideas and generate the collective views and wisdom necessary for the proper operation of the Board and Company. In this context, the Chairman undertakes a continuous review of the performance and contribution of individual Directors, whilst the Board as a whole, conducts an ongoing evaluation of its performance and that of its committees.

The Nomination and Remuneration Committee annually assess the performance of the Managing Director. The Managing Director conducts annual reviews of all Senior Executives. Annual reviews were conducted during the reporting period.

DIRECTOR INDEPENDENCE

The Board applies the Council's independence criteria in assessing director independence. Mr Schwartz and Mr Perrott are considered by the Board to be independent directors. In analysing Mr Schwartz's independence, the Board considered the materiality of Mr Schwartz's minority interests in the relevant syndicated property interests of the Company. Accordingly, the Board confirms Mr Schwartz's independence on the basis that (i) operating revenue from SFC's property interests represents less than 10% of Group revenue; and (ii) no interest held by Mr Schwartz represents a controlling interest in any single property. While the Board considers Mr Schwartz independent for the above reasons, standard Board meeting procedures and governance principles apply whereby in respect of any property business where Mr Schwartz has an interest, Mr Schwartz does not receive the relevant Board papers and does not attend that part of the Board meeting where the matter is being discussed or considered. In addition, the mere fact that Mr Schwartz and Mr Perrott have served on the Board for a substantial period does not mean that they have become too close to management to not be considered independent. Mr Schwartz and Mr Perrott contribute unbiased and differing ideas and wisdom to the Board generated from their individual and independent experience across numerous other businesses and industries.

Directors classified as not being independent directors are Mrs Blain, Mr Schaffer and Mr Mayer on the basis that:

- Mr Schaffer is an executive director, a substantial shareholder of SFC (with an economic interest of 19.9%) and has served on the Board in since 1972;
- Mrs Blain is a substantial shareholder of SFC (with an economic interest of 11.3%), served as an executive director of Howe from 1993 to 2001 and has served on the SFC Board since 1987; and
- Mr Mayer is an executive director of SFC by virtue of his role as Executive Chairman of Howe Automotive Limited.

The Board does not currently comply with Council guidelines in respect of majority independence, Chairman independence and separation of the Chairman and Managing Director roles. However, the Board is currently of the view that having a competent, cohesive and functioning Board whose members have a balance of practical experience and skills relevant to SFC's business is more beneficial to maximising returns to shareholders than it would be to expand the Board by two additional members simply for the purpose of achieving majority independence pursuant to the Council's definition. Further, the Board is not in entire agreement with the definition of independence as defined by the Council's guidelines.

In the Board's view, independence is about having individuals on the Board whose interests are directly aligned with shareholders (i.e. they have a significant stake in the company) and have the capability to question and challenge management's decision making process. On this basis, your Board is independent. Collectively the Board has a financial interest in approximately 38% of SFC's issued capital representing a large proportion of each director's personal asset base. When the shareholders gain, so does the Board; when shareholders lose, the Board loses significantly.

Similarly, based on the strong alignment of shareholders with the Chairman, it is not considered that having an Independent Chairman and separating the roles of Chairman and Managing Director would add shareholder value at this stage.

As a result of the Company's departure from the Council Recommendations contained in this Principle, governance practices employed by the Board to support its objective and competent operation are:

Disclosure of interests and conflicts

A director is required to disclose to all directors any material personal interest they may have, or may reasonably be perceived to have, in a matter which relates to the affairs of the Company. A director is expected to disclose their interest as soon as practicable after the director becomes aware of that interest.

In the event a potential material conflict of interest arises, the director concerned does not receive the relevant Board papers and leaves the Board meeting while the matter is discussed and considered. Directors must keep the Board advised on an ongoing basis of any interests which could cause, or may reasonably be perceived to cause, a conflict with the interests of the Company.

The minutes of the meeting should record the decision taken by those directors who do not have an interest in the matter.

Independent legal advice

With the consent of the Chairman, individual directors may seek independent professional advice at the Company's expense on any matter connected with the discharge of their responsibilities. The Chairman requires the submission of a cost estimate by a director in order to establish the reasonableness of the projected fee. The Chairman's consent will not be unreasonably withheld.

Period of office

Shareholders are given the opportunity to vote on the composition of the Board such that at each Annual General Meeting, one third of the Directors (excluding the Managing Director) must retire but may stand for re-election. Each director who is required by the Constitution to retire cannot hold office for more than three years without retiring within that time frame and standing for re-election. Any director who is appointed to the Board to fill a casual vacancy during a year may only hold office until the next Annual General Meeting but may stand for re-election at that meeting.

PROMOTE RESPONSIBLE AND ETHICAL DECISION MAKING

Conduct and ethics

The Company operates under a Code of Conduct a copy of which is posted to the corporate governance section of the Company's website – www.schaffer.com.au

The Company's Code of Conduct describes how SFC relates to its employees, customers, suppliers, shareholders and the community. SFC is committed to promoting integrity and maintaining the highest standard of ethical conduct in all of its activities.

Our business success is dependent on the development and maintenance of trusting relationships, underpinned by the continuous demonstration of corporate integrity.

The purpose of this Code of Conduct is to provide a common behavioural framework for all SFC personnel which recognises social responsibility, complies with applicable laws and standards, and is in keeping with the spirit and rules of the Australian and international markets in which SFC operates. This Code of Conduct applies to SFC and its controlled affiliates.

SFC's directors and management team lead by example, demonstrating their commitment to this Code of Conduct at all times through their personal behaviour and through guidance provided to our personnel.

STATEMENT OF CORPORATE GOVERNANCE PRACTICES

year ended 30 June 2018

Securities trading policy

SFC's Securities Trading Policy regulates dealing by SFC Directors and senior executives in SFC securities. Restrictions imposed by law on prohibiting anyone dealing in SFC's securities if in possession of unpublished SFC price-sensitive information have been supplemented by Board imposed restrictions specific to SFC Directors and senior executives. Price sensitive information is information a reasonable person would expect to have a material effect on the price or value of SFC securities.

This policy provides that in addition to Directors and senior executives being prohibited from trading in the Company's securities at any time if they possess any unpublished price sensitive information, Directors and senior executives may buy or sell the Company's securities only within limited trading windows.

The periods within which a Director or senior executive may buy or sell SFC securities is:

- from 24 hours to 4 weeks after the Company has made any Scheduled Announcement. A scheduled announcement refers to the announcement by SFC of its (i) results for the half year, (ii) preliminary final year result, (iii) Chairman's Address to the Annual General Meeting;
- from 24 hours to 4 weeks after the Company has made any Unscheduled Announcement. An unscheduled announcement refers to any other announcement of new information made by SFC pursuant to ASX Listing Rule 3.1; and
- during the period when a prospectus for securities is released by SFC until the last day for acceptance of securities issued pursuant to that prospectus.

SFC Directors and senior executives are prohibited from trading at all other times. For the purposes of clarity, any unscheduled ASX Listing Rule 3.1 announcement made within 4 weeks prior to a Scheduled Announcement does not enable SFC Directors and senior executives to trade SFC securities. The senior executives Group to which these restrictive trading periods apply includes all General Manager personnel at Howe & Company Pty Ltd, Urbanstone Pty Ltd and Delta Corporation Limited, and SFC's Chief Financial Officer, Group Financial Controller & Company Secretary and Group Chief Accountant.

The policy also requires that Directors and senior executives do not buy or sell the Company's securities on a short-term basis.

These rules also apply to trading by a related party of any SFC Director or senior executive. This Policy does not restrict participation by SFC senior executives in SFC's Employee Share Options Plan (ESOP), but applies in respect of the trading of SFC's securities to which plan participants become entitled under the ESOP.

A copy of the Company's Securities Trading Policy can be accessed from the corporate governance section of the Company's website – www.schaffer.com.au

Diversity policy

SFC recognises the benefits to be gained from a variety of skills, backgrounds and experiences being applied to specific work objectives. Therefore, SFC is committed to diversity throughout our workforce.

SFC has established a diversity policy which includes the requirement for the Board to establish measurable objectives for achieving gender diversity and for the Board to assess annually both the objectives and progress in achieving them. The copy of the Company's Diversity Policy can be accessed from the corporate governance section of the Company's website – www.schaffer.com.au

Our commitment to diversity will be supported by:

Communication – SFC will maintain an inclusive workplace culture via the organisation-wide awareness of workplace diversity principles and benefits. Management will ensure ongoing communication of these principles to the workforce.

Human Resource strategies – SFC Human Resource strategies and policies including recruitment, promotion and employee development will incorporate diversity principles to encourage a diverse workforce at all levels of the organisation. Where appropriate opportunities exist, and strong candidates are available for recruitment or promotion, diversity will be a consideration.

Action against inappropriate workplace behaviour – SFC does not tolerate discrimination, harassment, bullying, victimisation and/or vilification in the workplace. Action will be taken against these types of behaviour that do not value diversity.

Flexible work practices – where appropriate, flexible work practices will be accepted to meet the differing needs of a diverse workforce.

The table below outlines the gender diversity objectives established by the Board and the progress against each objective.

| Objectives | Progress |
|---|--|
| Comply with the Workplace Gender Equality Agency Act as determined by the Workplace Gender Equality Agency (WGEA) | The annual compliance notification was received on 26 June 2018 from WGEA. |
| Ensure reporting systems satisfy the reporting requirements as stipulated by the WGEA | The monthly Board reporting includes statistics on the numbers of each gender represented in senior executive positions and the total workforce at various business units and locations. Reporting systems are established to collate Group-wide information for reporting on the gender equality indicators stipulated by the WGEA. |
| Provide ongoing communication, education and updates on issues related to equal opportunity in the workplace. | Staff memorandums have been distributed and displayed at various SFC business unit locations presenting SFC's policy on diversity, and encouraging contribution and communication on diversity within the workplace. |
| Implement and revise Business Unit specific diversity plans. | Business Unit specific plans are being continually developed, reviewed and revised according to the specific circumstances of each Business Unit. |

At 30 June 2018, women represented 52% (2017: 48%) of the Group's workforce, 19% (2017: 14%) of senior executive positions, and 20% (2017: 20%) of the Board.

SAFEGUARD INTEGRITY IN FINANCIAL REPORTING

Written declaration by management

SFC's Managing Director and CFO report in writing to the Audit Committee that the consolidated financial statements of SFC and its controlled entities for any accounting period are based on a sound system of risk management and present a true and fair view in all material respects of the Group's financial condition and that operational results are in accordance with accounting standards. This statement is in turn supported by written statements provided by the senior management of all subsidiary companies within the Group.

Audit Committee

The SFC Audit Committee was established by the Board in 1996. The Audit Committee has adopted a formal Charter, a copy of which can be accessed from the corporate governance section of the Company's website – www.schaffer.com.au

The Audit Committee's purpose is to provide assistance to the Board in fulfilling its corporate governance and oversight responsibilities in relation to the company's financial reporting, risk management systems and the external audit functions. In doing so, it is the responsibility of the Audit Committee to maintain free and open communication between the Committee, external auditors and management of the Company.

In discharging its oversight role, the Audit Committee is empowered to investigate any matter brought to its attention with full access to all books, records, facilities, and personnel of the Company and the authority to engage independent counsel and other advisers as it determines necessary to carry out its duties.

Council guidelines require the Audit Committee to consist of at least three directors and have an independent Chairperson who is not Chairperson of the Board.

The members of the SFC's Audit Committee are Mr Schwartz (Independent Chairman), Mrs Blain (Non-executive Director) and Mr Perrott (Independent Director). Accordingly, SFC's Audit Committee complies with the Council's Audit Committee structure guidelines.

STATEMENT OF CORPORATE GOVERNANCE PRACTICES

year ended 30 June 2018

MAKE TIMELY AND BALANCED DISCLOSURE

Continuous disclosure policy

The Board is committed to ensuring that information that is expected to have a material effect on the price or value of SFC's shares is immediately notified to the ASX for dissemination to the market in accordance with the ASX Listing Rules. The Company's Continuous Disclosure Policy sets out the key obligations of the Board and senior management to ensure that SFC complies with its disclosure obligations pursuant to the ASX Listing Rules and the Corporations Act. In fulfilling its obligations of continuous disclosure SFC has adopted and adheres to the following practices.

- SFC's Managing Director, Chief Financial Officer and Company Secretary constitute the executive team charged with management of all elements of the Company's activities. This team is responsible for assessing the materiality of information and drafting all disclosures. For administrative convenience, SFC's Company Secretary is the nominated officer of the Company responsible for communications with the ASX.
- Information is released firstly via electronic means via the ASX. Further dissemination to analysts and investors does not occur until after ASX confirms the information has been released to the market.
- The information is posted to SFC's website at www.schaffer.com.au in order to make the information accessible to the widest audience. Investor information is posted to an area on SFC's website separate from any promotional material about the Company or its products.
- SFC's Managing Director, Chief Financial Officer and Company Secretary, and Howe Automotive Limited's Executive Directors are the officers authorised to speak on SFC's behalf at investor briefings and to the media. These officers understand that when speaking on behalf of the Company it is in respect of explanation and clarification of information previously released via the ASX. As these officers have knowledge of all information previously released to the ASX (they form part of the executive team responsible for the information disclosures), the risk of inadvertent disclosure of price sensitive information when speaking to investor briefings and the media is minimised. Presentations used in briefings which may have content which would trigger a continuous disclosure obligation are lodged with ASX prior to the briefing. All presentations are posted to SFC's website.
- Comments on analysts' financial projections are confined to errors in factual information and underlying assumptions. The Company will not provide price sensitive information or earnings forecast guidelines to analysts unless it has already done so to the market via the ASX.
- Unless the executive team responsible for information disclosures believes it has an obligation to make a statement on a particular matter, SFC's policy is not to respond to market rumours or speculation.

RESPECT THE RIGHTS OF SHAREHOLDERS

Shareholder communications strategy

SFC aims to ensure that investors and the market are kept informed of all major developments affecting the Company.

Information is communicated to investors and the market in accordance with SFC's periodic and continuous disclosure obligations pursuant to the ASX Listing Rules and the Corporations Act. SFC's disclosure practices are aimed at ensuring timely access for all investors to Company information.

To achieve these objectives and to satisfy regulatory requirements, SFC provides information to investors and the market in a number of ways:

- SFC's principal communication with investors is by provision of the Annual Report and financial statements, the Interim Report and the Annual General Meeting.
- Periodic and continuous disclosure announcements are released directly to the market via the ASX using ASX's electronic lodgement service. These announcements are immediately placed on the Company's website, at www.schaffer.com.au and typically mailed to shareholders.
- The release of Interim and Final results is typically followed by investor briefings and road shows. The purpose of the investor briefings/road shows is for explanation and clarification of previously released information and non-material company or industry specific information. Site visits are also arranged to give those who advise investors a better understanding of the Groups operating facilities.

- SFC's website contains further information about the Group and its activities, including copies of recent Annual and Interim Reports, the full text of notices of meetings and explanatory notes and copies of road-show presentations and presentations to brokers/analysts.
- The Annual General Meeting provides an opportunity for the Board to communicate with shareholders and investors through the presentation of the Chairman's Address and shareholders, through the Chairman, are given the opportunity to ask general questions of directors. SFC's external auditor attends each Annual General Meeting and is available to answer any questions shareholders may have, that are relevant to the conduct of the audit. The meeting, when possible, is held at the same convenient location on the same weekday and time each year in order to encourage shareholder participation.
- SFC's senior management meets regularly to consider its continuous disclosure obligations and assess the appropriateness of its policy in the context of any legislative amendments to the disclosure regime. Unless SFC has an obligation to make a statement on a particular matter, the Company's policy is not to respond to market rumours and media speculation.

RECOGNISE AND MANAGE RISK

Risk management

The Board has formal written policies on risk oversight and management. SFC's risk management policy provides the framework to manage the risks associated with SFC's business activities.

The purpose of the policy is to identify, assess, monitor and manage risk with the objective of minimising losses and maximising shareholder value.

SFC prepares risk profiles including a description of material risks, both financial and non-financial. SFC reviews and updates its risk profile as required.

SFC implements a systematic process to assist in the identification, assessment, treatment and monitoring of risks.

SFC provides the necessary tools and resources to management and staff to support the effective management of risks.

SFC ensures that the Board is adequately informed of significant risk management issues and the actions undertaken to manage risks in a timely manner.

The Board has considered the need for an internal audit function and concluded that the size and nature of the Group's operations do not warrant such a function as present. Responsibility for implementation and effective conduct of SFC's risk management system rests with the Board, Chief Executive Officer, Chief Financial Officer, Company Secretary, General Managers and all employees. The Managing Director and the Chief Financial Officer are required to state in writing to the Board in respect of any accounting period that:

- The statement given in accordance with the ASX Corporate Governance Council's Best Practice recommendation 4.1 (the integrity of financial statements) is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the Board; and
- SFC's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.

The SFC Board are able to oversee the entity's risk management system efficiently and effectively without establishing a separate risk committee. Executive management report to the Board on the effectiveness of our management of material business risks and they are satisfied that the risk management process enables material risks to be appropriately identified, prioritised, monitored and managed. Strategic risks are reported to the board on an ongoing basis.

The Automotive Leather division of SFC is materially exposed to the economic risk of foreign exchange fluctuations. To manage the foreign exchange risk arising from future commercial transactions the entity regularly considers the use of natural hedges and forward foreign exchange contracts, with reference to currency exposure levels, sensitivity, and financial capacity to tolerate rate fluctuations.

SFC does not have any material environmental or social sustainability risks.

STATEMENT OF CORPORATE GOVERNANCE PRACTICES year ended 30 June 2018

REMUNERATE FAIRLY AND RESPONSIBLY

Executive remuneration

SFC's Nomination and Remuneration Committee operates to support and advise the Board in fulfilling its responsibility to shareholders to ensure that the company has remuneration policies and practices which enable it to attract and retain directors and executives who will best contribute towards achieving positive outcomes for shareholders. The committee determines the remuneration and other conditions of service of the chief executive officer and executive directors, if any. The committee makes recommendations to the Board on the remuneration of non-executive directors within the aggregate approved by shareholders in general meeting from time to time. The committee considers individual performance, company performance, internal relativity and fairness in setting levels of remuneration and may seek appropriate independent external advice to assist in its decision making.

SFC's remuneration policy is directed at attracting, motivating and retaining quality people.

The remuneration of SFC's senior executive consists of fixed remuneration and annual and long term incentives.

Fixed Remuneration – This includes base salary and the statutory Superannuation Guarantee Contribution (SGC) which comprises the cash component; and other non-cash benefits such as a motor vehicle.

The Schaffer Corporation Limited Superannuation Fund is available to executives for superannuation contributions and life insurance. Premiums for life insurance are deducted from member accounts. Executives can elect to have the company contribute superannuation beyond the statutory SGC level by way of a salary sacrifice in lieu of cash salary.

Annual Incentive – The Company has performance-based incentive plans in place at each of its operations in which management and the labour force participate. The level of remuneration payable to participating executives is linked to the financial performance of their business. Executives are provided with cash incentives provided profitability thresholds are met.

Long Term Incentive – SFC's senior executives (other than Mr Schaffer and Mr Mayer) participate in SFC's Employee Share Option Plan (ESOP). Howe Automotive Limited operates the Employee Participation Unit (EPU) Plan for its executives. These incentive plans have long-term vesting provisions and are designed to align the interests of the participating executives with those of all SFC shareholders.

Non-executive Director remuneration

SFC's non-executive directors receive fees for their services (including statutory superannuation) and the reimbursement of reasonable expenses. The amount payable to non-executive directors is set by the Board after having taken regard to the size of the Company and Board, the responsibilities, demands and accountabilities faced by those directors in discharging their duties and after seeking independent advice to ensure the fees are in line with market standards. It is current SFC policy that non-executive directors do not receive shares, options or other securities and are not eligible to participate in SFC's Employee Share Option Plan.

A directors' pool limit of \$250,000 per annum was approved by shareholders at SFC's 2003 Annual General Meeting. This limit is not currently fully utilised. The fee pool is payable only to non-executive directors. Non-executive directors were paid annual fees for the 2018 financial year of \$79,778 each from the fee pool (inclusive of superannuation). Non-executive directors appointed prior to July 2003 are entitled to a retirement benefit equivalent to one year's annual director's fees. The retirement benefit was reduced from three years' to one year's annual director's fees in July 2003 (a three year retirement benefit was in place at the time Mrs Blain AM and Mr Schwartz accepted their appointment to the Board). SFC considers the reduced benefit modest and appropriate given the benefit which historically existed. It is SFC's policy that no retirement benefit apply to new directors appointed after July 2003.

ASX ADDITIONAL INFORMATION

year ended 30 June 2018

Additional information required by the Australian Securities Exchange is as follows.

TOTAL SHARE CAPITAL

Issued as at 1 September 2018 – 13,835,596 ordinary fully paid shares.

SHARE REGISTRY ADDRESS

C/o Computershare Investor Services Pty Ltd
Level 11
172 St George's Terrace
Perth WA 6000
Australia

Postal Address:
GPO Box D182
Perth WA 6840
Australia

SECURITIES EXCHANGE LISTING

The shares of the Company are listed on the Australian Securities Exchange. The home exchange is Perth.

VOTING RIGHTS

Subject to any restrictions from time to time being attached to any class or classes of shares at general meetings of Members or classes of Members:

- (1) each Member entitled to vote may vote in person or by proxy, attorney or representative;
- (2) on a show of hands, every person present who is a Member or a proxy, attorney or representative of a Member has one vote;
- (3) on a poll, every person present who is a Member or a proxy, attorney or representative of a Member shall, in respect of each fully paid share held by him, or in respect of which he is appointed a proxy, attorney or representative, have one vote for the share, but in respect of partly paid shares, shall have a fraction of a vote for each partly paid share. The fraction must be equivalent to the proportion which the amount paid (not credited) is of the total amounts paid and payable (excluding amounts credited). Amounts paid in advance of a call are ignored when calculating the proportion.

DISTRIBUTION OF HOLDINGS AS AT 1 SEPTEMBER 2018

| Shareholdings | Shareholders |
|--------------------|--------------|
| 1 – 1,000 | 641 |
| 1,001 – 5,000 | 464 |
| 5,001 – 10,000 | 102 |
| 10,001 – 100,000 | 95 |
| 100,001 – and over | 22 |

Number of shareholders holding less than a marketable parcel i.e. less than 30 shares: 52.

SUBSTANTIAL SHAREHOLDERS

As at 1 September 2018, the substantial shareholders of the company summarised below, were:

| | Number of shares | Economic interest as a percentage of issued ordinary shares |
|---|------------------|---|
| Mr J M Schaffer AM & Associates | 2,104,243 | 15.21% |
| 50% of interest held by Swan Holdings Pty. Ltd. | 652,687 | 4.72% |
| | 2,756,930 | 19.93% |
| Mrs D E Blain AM & Associates | 909,673 | 6.57% |
| 50% of interest held by Swan Holdings Pty. Ltd. | 652,687 | 4.72% |
| | 1,562,360 | 11.29% |
| * Combined interest of Mr Schaffer & Mrs Blain | 4,319,290 | 31.22% |
| Sterling Equity Pty Limited and subsidiaries | 1,239,119 | 8.96% |

* Pursuant to the Corporation Act (2001), by virtue of the Swan Holdings Pty Ltd Voting Deed conferring on Mr Schaffer the power to vote all Swan Holdings Pty Ltd's interest in Schaffer Corporation Limited's shares, Mr Schaffer is also deemed to have an interest in all the Schaffer Corporation Limited shares held by Mrs Blain and her associates, and vice versa. The consequence of this is that each of the Substantial Shareholder notices lodged with the Regulatory Authorities by Mr Schaffer and Mrs Blain show Mr Schaffer's and Mrs Blain's combined interest at 31%, not their individual economic interests of 20% and 11% respectively.

TWENTY LARGEST SHAREHOLDERS

As at 1 September 2018

| | Number of shares | Percentage of issued ordinary shares |
|---|------------------|--------------------------------------|
| Swan Holdings Pty Ltd | 1,305,374 | 9.43 |
| Cimbrook Nominees Pty Ltd | 980,482 | 7.09 |
| National Nominees Pty Ltd | 961,577 | 6.95 |
| Mrs Danielle Eva Blain | 907,570 | 6.56 |
| Mr John Michael Schaffer | 799,554 | 5.78 |
| Jobling Investments Pty Ltd | 507,812 | 3.67 |
| JP Morgan Nominees Australia Limited | 466,196 | 3.37 |
| Mr David Schwartz <David Schwartz Fam Hlds A/C> | 359,170 | 2.60 |
| Mr Christopher Stephan Mayer | 344,263 | 2.49 |
| Mr Kenneth John Beer <Beer Super Fund A/C> | 261,769 | 1.89 |
| HSBC Custody Nominees (Australia) Limited | 246,629 | 1.78 |
| Maitri Pty Ltd <Coci Super Fund A/C> | 232,227 | 1.68 |
| The Sports Café (Australia) Pty Ltd | 226,072 | 1.63 |
| Frederick Bruce Wareham | 160,006 | 1.16 |
| Glennlin Pty Ltd <Marilyn May Bookham Disk A/C> | 143,252 | 1.04 |
| Shann Investments Pty Ltd <Lynda Mae Jobling Disc A/C> | 143,252 | 1.04 |
| SCE Superannuation Pty Ltd <SCE Superannuation A/C> | 140,000 | 1.01 |
| Ago Pty Ltd <Superannuation Fund A/C> | 136,980 | 0.99 |
| Mr Milton Yannis | 136,520 | 0.99 |
| Citicorp Nominees Pty Limited | 135,516 | 0.98 |
| | 8,594,221 | 62.12 |

ANNUAL GENERAL MEETING

The Annual General Meeting of Schaffer Corporation Limited will be held at Perth on Wednesday, 14 November 2018 at 11:30am. Further information regarding the meeting including the business to be dealt with is contained in the separate notice of meeting.

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Corporate Timetable

| | |
|---|-------------------|
| Final 2018 dividend record date | 31 August 2018 |
| Final 2018 dividend payment date | 14 September 2018 |
| Despatch of 2018 Annual Report and notice of AGM | 10 October 2018 |
| Annual General Meeting | 14 November 2018 |
| 2019 half-year earnings release and dividend announcement | February 2019 |
| Interim 2019 dividend payment date | March 2019 |

SHAREHOLDER INFORMATION

Annual General Meeting

Schaffer Corporation will hold its Annual General Meeting on Wednesday 14 November 2018 at 11:30am at Pagoda Resort and Spa, 112 Melville Parade, Como, Western Australia.

Direct Credit of Dividends

Schaffer Corporation provides shareholders with the option to have dividends paid electronically to a nominated bank, building society or credit union account. Payments are credited electronically on the dividend date and confirmed by a payment advice by mail.

The Company encourages shareholders not already using this facility to contact Computershare Investor Services Pty Limited, who can arrange for an instruction advice to be sent to shareholders for completion.

Change of addresses/provide or update banking details

Shareholders who have changed their address or banking particulars should advise our share registry of their new details:

Computershare Investor Services
Pty Limited
GPO Box D182
Perth WA 6840
Australia
Telephone: 1300 557 010 (in Australia)
or +61 8 9323 2000
Facsimile: +61 8 9323 2033
Website: www.computershare.com/au

Corporate Directory

Schaffer Corporation Limited
ABN 73 008 675 689

ASX Code: **SFC**

Head Office and Registered Office

1305 Hay Street
West Perth WA 6005
Australia
Telephone: +61 8 9483 1222
Facsimile: +61 8 9481 0439
Website: www.schaffer.com.au

Board of Directors

Executive Directors

JM Schaffer AM BCom(Hons), FCPA
(Chairman and Managing Director)
AK Mayer (Executive Chairman –
Howe Automotive Ltd)

Non-executive Directors

DE Blain AM, BA
MD Perrott AM, BCom, FAIM FAICD
DJ Schwartz

Chief Financial Officer

Ralph Leib BComm, BAcc

Group Financial Controller and Company Secretary

J Cantwell B Bus(Acc), CPA,
MBA, GIA(Cert)

Share Registry

Computershare Investor
Services Pty Limited
GPO Box D182
Perth WA 6840
Australia
Telephone: 1300 557 010 (in Australia)
or +61 8 9323 2000
Facsimile: +61 8 9323 2033
Website: www.computershare.com/au

Auditors

Ernst & Young
11 Mounts Bay Road
Perth WA 6000
Australia
Telephone: +61 8 9429 2222
Facsimile: +61 8 9429 2436

Solicitors

Ashurst
Level 32 Exchange Plaza
2 The Esplanade
Perth WA 6000
Australia
Telephone: +61 8 9366 8000
Facsimile: +61 8 9366 8111

