Michael Hill International Limited
ABN 25 610 937 598
Appendix 4E
Results for announcement to the market
Year ended report 30 June 2018

Reporting period

Reporting period:	12 months ending 30 June 2018
Previous reporting period:	12 months ending 30 June 2017

Results for announcement to the market

				$'000
Revenue from ordinary activities	Up	4.4%	to	575,549
Earnings before interest and taxation (EBIT) from continuing operations*	Down	19.5%	to	50,147
Normalised EBIT before one-off items*	Down	16.6%	to	40,106
Net profit after tax (from ordinary activities) for the period attributable to members	Down	85.9%	to	4,610

* EBIT and Normalised EBIT are Non-IFRS Information and are unaudited. Please refer to Non-IFRS Information on page 10 of the Directors Report for an explanation of Non-IFRS information and a reconciliation of EBIT from continuing operations and Normalised EBIT.

Brief explanation of figures reported above to enable the figures to be understood

This report is based on the consolidated financial statements which have been audited and an unqualified opinion given. For commentary on the results, please refer to the attached full financial report for all other disclosures in respect of the Appendix 4E.

Dividends

	Amount per security	Franked amount per security
Interim dividend (cents per share)	2.50	-
Final dividend (cents per share)	2.50	-

Record date for determining entitlements to the final dividend is 14 September 2018. The payment date is 28 September 2018.

	2018	2017
Net tangible assets		
Net tangible asset backing per ordinary security	**$0.46**	$0.50

Emma Hill

Emma Hill
Chair

Brisbane
24 August 2018

Webcast scheduled to take place at 1.00pm (AEST) on Monday 27 August 2018. Please use the following link to register.
https://edge.media-server.com/m6/p/jzp4h9s6

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Michael Hill International Limited

ABN 25 610 937 598

Directors' report and annual financial report for the year ended 30 June 2018

Michael Hill International Limited
ABN 25 610 937 598
Directors' report and annual financial report - 30 June 2018

Contents

DISCLAIMER

Certain statements in this announcement constitute forward-looking statements. Forward-looking statements are statements (other than statements of historical fact) relating to future events and the anticipated or planned financial and operational performance of Michael Hill International Limited and its related bodies corporate (the Company). The words “targets,” “believes,” “expects,” “aims,” “intends,” “plans,” “seeks,” “will,” “may,” “might,” “anticipates,” “would,” “could,” “should,” “continues,” “estimates” or similar expressions or the negatives thereof, identify certain of these forward-looking statements. Other forward-looking statements can be identified in the context in which the statements are made. Forward-looking statements include, among other things, statements addressing matters such as the Company’s future results of operations; financial condition; working capital, cash flows and capital expenditures; and business strategy, plans and objectives for future operations and events, including those relating to ongoing operational and strategic reviews, expansion into new markets, future product launches, points of sale and production facilities.

Although the Company believes that the expectations reflected in these forward-looking statements are reasonable, such forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause the Company’s actual results, performance, operations or achievements or industry results, to differ materially from any future results, performance, operations or achievements expressed or implied by such forward-looking statements.

Such risks, uncertainties and other important factors include, among others: global and local economic conditions; changes in market trends and end-consumer preferences; fluctuations in the prices of raw materials, currency exchange rates, and interest rates; the Company’s plans or objectives for future operations or products, including the ability to introduce new jewellery and non-jewellery products; the ability to expand in existing and new markets and risks associated with doing business globally and, in particular, in emerging markets; competition from local, national and international companies in the markets in which the Company operates; the protection and strengthening of the Company’s intellectual property rights, including patents and trademarks; the future adequacy of the Company’s current warehousing, logistics and information technology operations; changes in laws and regulations or any interpretation thereof, applicable to the Company’s business; increases to the Company’s effective tax rate or other harm to the Company’s business as a result of governmental review of the Company’s transfer pricing policies, conflicting taxation claims or changes in tax laws; and other factors referenced to in this presentation.

Should one or more of these risks or uncertainties materialise, or should any underlying assumptions prove to be incorrect, the Company’s actual financial condition, cash flows or results of operations could differ materially from that described herein as anticipated, believed, estimated or expected.

The Company does not intend, and do not assume any obligation, to update any forward-looking statements contained herein, except as may be required by law. All subsequent written and oral forward-looking statements attributable to us or to persons acting on the Company’s behalf are expressly qualified in their entirety by the cautionary statements referred to above and contained elsewhere in this announcement.

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The Directors present their report on the consolidated entity (referred to hereafter as the 'Group') consisting of Michael Hill International Limited ACN 610 937 598 ('Michael Hill International' or the 'Company') and all controlled subsidiaries for the year ended 30 June 2018.

Principal activities

The Group operates predominately in the retail sale of jewellery and related services sector in Australia, New Zealand and Canada.

During the year, the Group exited its US operations and is in the process of exiting the Emma & Roe brand. These segments have been reclassified as discontinued operations for the 2017 and 2018 financial year. There have been no other significant changes in the nature of the Group's activities during the year.

Dividends

Dividends paid to members during the financial year were as follows:

	2018 $'000	2017 $'000
Final ordinary dividend for the year ended 30 June 2017 of AU 2.5 cents (2016 - AU 2.5 cents) per fully paid share paid on 29 September 2017 (2016 - 6 October 2016)	**9,685**	9,578
Interim ordinary dividend for the year ended 30 June 2018 of AU 2.5 cents (2017 - AU 2.5 cents) per fully paid share paid on 29 March 2018 (2017 - 31 March 2017)	**9,686**	9,686
The Directors have declared the payment of a final dividend of AU 2.5 cents per fully paid ordinary share* (2017 - AU 2.5 cents). The final dividend will be unfranked for Australian shareholders and fully imputed for New Zealand shareholders. The aggregate amount of the proposed dividend expected to be paid on 28 September 2018 out of retained earnings, but not recognised as a liability at year end, is	**9,686**	9,686

* This will not be declared as conduit foreign income, therefore Australian withholding tax will be deducted from the dividend payment for foreign (non-Australian tax resident) shareholders.

Significant changes in the state of affairs

During the year the Group exited its loss making retail operations in the US and is in the process of exiting the Emma & Roe brand. Assets in both segments were impaired as appropriate. As at 30 June 2018, all US stores have been closed. Of the 30 Emma and Roe stores, 24 stores were closed as at 30 June 2018. The closure programme for the final six Emma & Roe stores is still in progress. Impaired assets on hand relating to the Emma & Roe closures will be disposed of when it is determined they will not be redeployed.

Likely developments and expected results of operations

Information on likely developments in the Group's operations and the expected results of operations have been included in the Operational Review and Outlook sections of this report.

Review of operations

In Australian dollars, the Group has reported operating revenue from continuing operations of $575.5m, producing earnings before interest and tax ('EBIT') for continuing operations of $50.1m. The Group reported a net profit after tax ('NPAT') from continuing operations of $34.8m for the 2018 financial year, and a statutory net profit after tax of $4.6m. Normalised EBIT for the Group was $40.1m for the year. Normalised EBIT excludes one off costs, including Emma & Roe and US closure costs and significant items per the Non-IFRS Information note on page 10.

* EBIT and Normalised EBIT are Non-IFRS Information and are unaudited. Please refer to Non-IFRS Information on page 10 of the Directors Report for an explanation of Non-IFRS information and a reconciliation of EBIT from continuing operations and Normalised EBIT.

Cash, Cash flow and Dividends

The Group has an equity ratio of 50.4% at 30 June 2018 (52.0% in 2017), and a working capital ratio of 2.6:1 (3.0:1 in 2017). Net operating cash flows were $54.9m compared to $39.8m the previous year. Net debt at 30 June 2018 was $28.0m compared to $39.4m at 30 June 2017.

The Group remains in a strong financial position to continue to invest in improvements to its systems, infrastructure and capabilities, and position the business for future growth opportunities.

Despite the one off costs and operating losses associated with the discontinued Emma & Roe and US operations, which impacted statutory profit after tax, the Group's debt levels reduced with higher operational cash flows. Accordingly, for shareholders, the dividend for the year was maintained at AU 5.0 cents (2017 - AU 5.0 cents) per share. There will be a final dividend of AU 2.5 cents per share payable on 28 September 2018. The final dividend will be unfranked for Australian shareholders and fully imputed for New Zealand shareholders.

Operational Review

The Group achieved the following key outcomes for the 2018 financial year:

- Revenue from continuing operations increased 4.4% to $575.5m
- Statutory net profit after tax for the Group of $4.6m ($34.8m profit after tax from continuing operations)
- Same store sales from continuing operations were up 0.4%
- Online sales grew by 57.4% to $10.3m
- Canadian segment continues to gain market share with same store sales increase of 3.8% and a record EBIT for the year of CA$14.6m
- EBIT from continuing retail segments (Australia, New Zealand, Canada) of $89.1m down 1.6% from prior year of $90.5m.
- Branded collection sales increased to 18.0% of total product sales, up from 14.2% on the prior year
- Sale of Professional Care Plans ('PCP') amounted to $35.7m for continuing operations, increasing deferred revenue on the balance sheet from PCP sales to $80.0m
- Gross margin increased in all continuing retail segments (Australia +0.7%, New Zealand +0.3%, Canada +1.1%), offset by stock provisions, including for Emma & Roe, leaving gross margin for the Group flat on prior year at 63.7%
- Dividend of 5.0 cents in line with prior year
- Net operating cash inflow was $54.9m, up on $39.8m in prior year
- Net debt of $28.0m down from $39.4m
- EBIT before one-off items of $40.1m, down from $48.1m
- One off costs including write-down and disposal of assets and lease settlement costs relating to US and Emma & Roe exits amounting to $25.5m. Significant items include a $1.4m employee benefits revaluation.
- 17 Michael Hill stores were opened and five were closed within our three core markets during the year. 24 Emma & Roe stores and 9 stores in the US were closed. There was a total of 312 stores trading as at 30 June 2018, including 6 Emma & Roe stores.

Review of operations (continued)

Operational Review (continued)

2017-18 was a year of recalibration and repositioning which saw the Group undertake a strategic review.

Despite significant investment into the US business, the Group's lack of scale combined with the competitor dynamic and sector outlook in that market led to the conclusion that we would not generate an adequate return on further investment in the business, and the decision was made in January 2018 to close all US stores.

The decision was also made to close the Emma & Roe brand, which had failed to meet performance projections. This followed an in-depth review and analysis of the global jewellery market and emerging trends which identified an opportunity to reposition the Emma and Roe brand, however it was determined that this was not an immediate strategic priority. The Emma & Roe proposition remains a compelling opportunity to be explored at the appropriate time.

The Group’s operational results were impacted materially due to a combination of closure costs for the US and Emma & Roe businesses and performance deterioration in these segments once closure was announced.

Revenue from continuing operations grew 4.4%, with same store sales up 0.4%. Canada produced pleasing same store sales growth of 3.8% and a record EBIT result. New Zealand had solid same store sales growth of 2.3% and EBIT slightly down on last year, while Australia did not meet performance projections with flat sales and a decline in EBIT contribution.

Gross margin grew across all continuing retail segments (Australia +0.7%, New Zealand +0.3%, Canada +1.1%) as a result of our proprietary collection strategy commanding a premium.

During the 2017-18 year the Group implemented a new Point of Sale system, with all 171 Australian stores changed over during the 12 months, with New Zealand and Canadian stores to be completed in the first quarter of 2018-19. This was a major investment for the business and is a key enabler as part of a larger strategic roadmap for the Group’s information systems. The Group is undertaking a staged program of investment in its finance, human resourcing, customer experience and inventory management systems and supporting cloud based infrastructure.

PCP revenue has again provided strong cash flow for the Group. The PCP program is designed to provide a comprehensive suite of care services to our customers so they can maintain their jewellery in pristine condition. Total sales from these plans for continuing operations amounted to $35.7m, and at 30 June 2018 there was $80.0m of deferred PCP revenue held on the statement of financial position. $31.9m in PCP revenue was recognised for continuing operations in the 2017-18 year, down 0.6% on the previous year.

In-house credit now represents 28.0% of Canadian sales. The North American loan book was $20.5m at 30 June 2018 compared to $17.7m at 30 June 2017, with bad debts running at 4.7% of in-house credit sales for the year, which is in alignment with expectations for credit default rates. The US book is being closely monitored as the US book winds down following US store closures. While US default rates have lifted, this was anticipated, it is being managed and an uptick in default rates has been provided for.

The Group's e-commerce platform continues to support the retail segments well with revenue increasing by 57.4%, driven by increased visitation and higher online conversion. e-commerce sales now represent over 1.8% of the Group's total revenue.

As at 30 June 2018, the Group operated Michael Hill e-commerce sites in all of the countries we operate in and an Emma & Roe e-commerce site in the Australian market which is expected to operate for at least part of the coming financial year, to facilitate stock clearance for that brand.

Review of operations (continued)

Operational Review (continued)

There were 306 Michael Hill stores and 6 Emma & Roe stores trading as at 30 June 2018.

Review of 2017-2018 Priorities

Same stores sales growth in all markets and for both brands of above 2%	Same stores sale growth of 0.4% occurred within the Michael Hill segments of Australia, New Zealand and Canada. Below target Australian performance prevented attainment of our 2% goal.
Open at least 10 new Michael Hill stores across all markets	17 new Michael Hill stores were opened during the year, well ahead of our original goal.
Continue to review the Emma & Roe brand and adjust the brand and offering	A review of the Emma and Roe business in early 2018 lead to the decision to close the brand.
To reduce the US operating losses and develop a viable model	A decision to exit the US market was announced during the year and all stores have now been closed
Branded collection sales to reach 18%	Michael Hill branded collections sales reached 18.0% of total sales.
Improved inventory management delivering increase in GMROI (gross margin return on investment) and stock turn	GMROI was 1.48, up on prior year of 1.42. This was a pleasing improvement achieved through a combination of inventory range refinement and improved margin management. Stock turn was 1.11 for the year, in line with prior year.
Continue to develop the e-commerce business and grow to 2% of Group revenue	e-commerce sales grew 57.4% to $10.3m, amounting to 1.8% of total sales for the financial year. The business continued to plan and invest in better online capabilities, which will reap benefits in the years ahead when fully evolved.
Continued information systems investment to migrate the organisation onto a highly integrated ERP environment	There was a continued investment in technology and key systems during the period consistent with the approved roadmap for our IT systems. New IT systems and investment in the development of future systems amounted to $6.5m during the year.

Segment Results

The operational segments reported below reflect the performance of the Michael Hill and Emma & Roe retail operations in each geographic segment, including the discontinued operations of Emma & Roe and Michael Hill United States. The operational segments include trading activity from our online presence and our North American in-house credit function. The segments exclude revenue and expenses that do not relate directly to the relevant Michael Hill or Emma & Roe retail segments, and are treated as unallocated. These predominately relate to corporate costs and Australian based support costs, but also include the manufacturing activities, warehouse and distribution, interest and company tax.

The Michael Hill United States and Emma & Roe segments were classified as Discontinued Operations during the year following the announcement of their planned closure. As a result, the Michael Hill United States and Emma & Roe segments were removed from the Group’s total segment result reported in the consolidated financial statements.

The results below are expressed in local currency.

Review of operations (continued)

Michael Hill Australia

OPERATING RESULTS (AU $000)	2018	2017	2016	2015	2014
Revenue	325,709	321,981	309,457	294,442	298,474
Gross profit	206,303	201,707	194,152	183,582	187,381
Gross profit as a % of revenue	63.3%	62.6%	62.7%	62.3%	62.8%
EBIT	48,621	51,688	49,975	45,933	47,493
As a % of revenue	14.9%	16.1%	16.1%	15.6%	15.9%
Number of stores	171	166	168	167	164

The Australian retail segment revenue increased by 1.2% to $325.7m, with same store sales 0.9% down on prior year. A focus by management on margin management helped gross profit grow from 62.6% to 63.3% during the year. However, rising costs combined with a challenging retail environment resulted in EBIT reducing to $48.6m. A decision was made during the year to split the management of the large Australian segment into two businesses each led by a Retail General Manager with their own regional management teams.

Seven stores were opened in Australia during the period as follows:

- Belmont Forum, Western Australia
- DFO Essendon, Victoria
- DFO Moorabbin, Victoria
- George Street Sydney CBD, New South Wales
- Mandurah, Western Australia
- Mildura, Victoria
- Palmerston, Northern Territory

Two stores closed during the period. There were 171 stores trading at 30 June 2018. The Group plans to expand its store footprint by four new stores during the 2018-19 year. It is anticipated there will be store closures occurring in the coming year as part of the Group's active management of its store portfolio.

Michael Hill New Zealand

OPERATING RESULTS (NZ $000)	2018	2017	2016	2015	2014
Revenue	125,239	121,970	122,903	113,983	109,693
Gross profit	77,673	75,204	75,895	70,488	67,799
Gross profit as a % of revenue	62.0%	61.7%	61.8%	61.8%	61.8%
EBIT	27,800	27,836	27,136	23,545	22,102
As a % of revenue	22.2%	22.8%	22.1%	20.7%	20.1%
Number of stores	52	52	52	52	52
FX rate for profit translation	1.09	1.06	1.09	1.07	1.10

The New Zealand retail segment revenue increased 2.7% to NZ$125.2m for the 12 months, and the segment achieved a solid EBIT result of NZ$27.8m, in line with the prior year. The focus on this mature market has been to improve store locations where possible, build average store sales through a broadening of our product offer and improving our online sales channel.

Two stores were opened in New Zealand as follows:

- Silverdale, Auckland
- Victoria Street, Wellington

Two stores closed during the period. There were 52 stores trading at 30 June 2018. There are currently plans to open one new store during 2018-19.

Review of operations (continued)

Michael Hill Canada

OPERATING RESULTS (CA $000)	**2018**	**2017**	**2016**	**2015**	**2014**
Revenue	130,762	112,721	95,423	79,097	69,025
Gross profit	81,576	69,078	59,252	48,689	42,466
Gross profit as a % of revenue	62.4%	61.3%	62.1%	61.6%	61.5%
EBIT	14,605	12,386	8,929	6,041	3,923
As a % of revenue	11.2%	11.0%	9.4%	7.6%	5.7%
Number of stores	83	76	67	60	54
FX rate for profit translation	0.98	1.00	0.97	0.97	0.98

The Canadian retail segment revenue increased by 16.0% for the twelve months to CA$130.8m, with same store sales increasing 3.8% and gross margin lifting to 62.4%. The Canadian segment continues to show good growth as we achieve scale and increase market share with EBIT increasing to a record CA$14.6m, 11.2% of revenue. While sales did slow during the 2017-18 year, in the second half in particular, the Company is confident that continued growth can be achieved in the coming year.

Eight stores were opened in Canada during the period, as follows:

- Conestoga Mall, Ontario
- Edmonton Outlet, Alberta
- Fairview Mall, Ontario
- McAllister Place, Ontario
- Orchard Park Mall, British Colombia
- Park Place, Alberta
- Regent Mall, New Brunswick
- Vaughan Mills, Ontario

One store closed during the period. There were 83 stores trading at 30 June 2018. There is potential for up to 100 stores in Canada, and the Group plans to open at least five stores during the 2018-19 year, subject to availability of suitable sites.

Michael Hill USA

OPERATING RESULTS (US $000)	**2018**	**2017**	**2016**	**2015**	**2014**
Revenue	9,320	12,498	14,203	11,290	9,994
Gross profit	5,420	7,564	8,363	6,535	5,971
Gross profit as a % of revenue	58.2%	60.5%	58.9%	57.9%	59.7%
EBIT	(9,840)	(3,821)	(2,599)	(1,916)	(2,283)
As a % of revenue	(105.6%)	(30.6%)	(18.3%)	(17.0%)	(22.8%)
Number of stores	-	9	10	9	8
FX rate for profit translation	0.78	0.75	0.73	0.83	0.92

Included in EBIT figures above:					
Impairment and disposal of assets	2,775	595			
Lease settlement and onerous lease provision	3,958	71			

The Group exited the US operations during the year and closed all stores. No stores were trading as at 30 June 2018.

Review of operations (continued)

Emma & Roe

OPERATING RESULTS (AU $000)	2018	2017	2016	2,015
Revenue	16,934	15,448	9,539	4,879
Gross profit	11,216	10,201	6,663	3,374
Gross profit as a % of revenue	66.2%	66.0%	68.9%	69.2%
EBIT	(21,790)	(7,051)	(2,418)	(2,884)
As a % of revenue	(128.7%)	(45.6%)	(25.3%)	(59.1%)
Number of stores	6	29	16	8

Included in EBIT figure above:				
Impairment and disposal of assets	7,412			
Lease settlement and onerous lease provision	6,037			

Emma & Roe reported sales of $16.9m for the year. Emma & Roe results during the second half of the year were impacted by the announcement to reduce the brand's store footprint by 24 stores, with 5 closing in April and 19 closing in June. The closure programme for the final six Emma & Roe stores is still in progress.

Strategic Update

In the latter half of the year, a detailed strategic review was conducted. The purpose of the review was to identity performance improvement opportunities for the Group within the context of the rapidly changing retail environment and changes in how customers shop.

Five strategic shifts have been identified, designed to reposition Michael Hill from a traditional retailer to a differentiated omni-channel brand.

Implementation of these changes is intended to increase market share through improved customer engagement across all channels and increased frequency of visit.

The five key strategic shifts are:

1. **Omni-channel:** *Building capability to deliver a seamless customer experience.*
   Evolving our online experience, including integration of digital and social channels with our store network, to enable a seamless experience for customers where and when they engage with us.
2. **Customer loyalty:** *Building data capability to better service customers.*
   Using data driven customer insights to deliver tailored customer experiences to drive brand loyalty and advocacy.
3. **Unique branded collections:** *Escalate our growth of branded collections.*
   Through enhanced designer capability, create unique branded collections to meet growing customer demand for differentiated products.
4. **Brand position:** *Strengthen and grow brand loyalty.*
   Based on recent brand review, we will reposition our brand in market to meet the changing consumer landscape.
5. **Operational excellence:** *Enhance execution capability and agility.*
   Build capability and agility throughout the organisation to adapt quickly to a fast changing retail environment.

Review of operations (continued)

To deliver against this ambition, investment will be made in capability and infrastructure. We will add capability to the Group through the addition of a Chief Operating Officer and Chief People Officer at the executive level. A dedicated project management team has been established to execute and manage initiatives in support of the five strategic shifts identified above. Significant investment is being made in additional roles in data and digital, together with capital investment in enabling systems and infrastructure. This will require the investment of additional unallocated corporate costs of ~$3m in the coming 2018-19 year, with total planned capex across new and refurbished stores, IT systems, tools and infrastructure of ~$25m (2017-18: $24.6m).

2018-19 is a foundational year with benefits from these investments to be progressively realised. A differentiated offer in brand, product and experience would provide a platform to establish new channels and markets if considered appropriate in the coming years.

Outlook

We are committed to expanding the Michael Hill brand in all three markets of Australia, New Zealand and Canada with plans to open a minimum of 10 new stores in 2018-19 across these three markets, subject to site availability. With this store growth, underpinned by the five identified strategic shifts, it is planned that our differentiated offer will deliver growth in all markets and take market share. The business will be focussed on quality of earnings and continued strong gross margin performance.

In the 2018-19 year we will work to deliver a better quality in-store customer experience. Proprietary branded collections revenue is planned to continue to grow as we increase investment in these ranges. Branded collections provide a unique product offering to our customers and in doing so, builds strong brand equity in the markets we operate in.

While the Australian segment has reached maturity in terms of overall store numbers, it still offers potential for improved EBIT performance through a combination of increased productivity from the retail teams, improved margins, property portfolio refinements, online revenue growth, new product collections and an enhanced customer experience.

The New Zealand business is expected to continue to perform well and will benefit from increased online revenue, extended product offering, improved margins, a continued refinement of the property portfolio and improved cost efficiencies, together with exploring opportunities to tap into the growing Asian consumer market.

Canada still has opportunities for further store growth and we will continue to work to build its profitability through its maturing store portfolio, online revenue growth, optimisation of its in-house credit program, and increased productivity of its retail teams.

e-commerce revenue is planned to continue to grow steadily in coming years as we refine our offer and optimise the online channels. Further planned investment in our e-commerce capability will take full advantage of this growth opportunity.

Continued strong operational cash flows enable further debt reduction and capital investment levels to be maintained, while also leaving the Group well placed to explore opportunities aligned with the five strategic shifts.

Review of operations (continued)

Priorities for 2018-19

Open at least 10 new Michael Hill stores across all markets
Reposition Michael Hill from a traditional retailer to a unique omni-channel retailer.
Branded Collection sales to grow as a percentage of total revenue.
Continued improvement in inventory management to deliver further improvement in GMROI (gross margin return on investment).
Continue to invest in and develop the e-commerce business.

Risk Management

Risk	Strategies and mitigation
Inadequate business continuity program and/or disaster recovery strategies	The process of updating the Group's business continuity plan and disaster recovery processes will continue into the coming year. Additional internal resource has been put in place and external consultants continue to be used to help with penetration testing and to provide other technical assessments.
Insufficient leadership talent to meet growth plans	The decision was made recently to appoint a Chief People Officer to the executive team in an effort to strengthen our focus on people planning, talent acquisition and development of this vital resource. We are confident our people and talent strategies will continue to deliver sufficient quality resource to the business.
Systems capability does not meet demands of business	A structured plan of system review involving significant investment has begun to facilitate the upgrade of our key business systems.
Risk of a disruptor or new competition entering our markets	We are committed to improving and differentiating the brand from our existing competitors to create a point of difference and acquire market share. This in itself helps mitigate the risk of other competitors entering our key markets and taking material market share.
Breach of regulation or law in one of our jurisdictions in an ever increasingly complex legal compliance environment.	The Company invests via an in-house legal team who are focused on compliance in our three markets and by utilising external legal firms for specialised legal advice when required.
Inability to adjust to the rapidly changing consumer segment and retail environment	As mentioned in the strategic update, the Group is in the process of investing in improved infrastructure and capabilities with a goal to meet the rapidly changing retail environment and the consumer of tomorrow.

Non-IFRS Financial Information

This report contains certain non-IFRS financial measures of historical financial performance. Non-IFRS financial measures are financial measures other than those defined or specified under all relevant accounting standards. The measures therefore may not be directly comparable with other companies' measures. Many of the measures used are common practice in the industry in which MHI operates. Non-IFRS financial information should be considered in addition to, and is not intended to be a substitute for, or more important than, IFRS measures. The presentation of non-IFRS measures is in line with Regulatory Guide 230 issued by Australian Securities and Investments Commission (ASIC) to promote full and clear disclosure for investors and other uses of financial information, and minimise the possibility of those users being misled by such information.

Non-IFRS Financial Information (continued)

The measures are used by management and Directors for the purpose of assessing the financial performance of the Group and individual segments. The Directors also believe that these non-IFRS measures assist in providing additional meaningful information on the drivers of the business, performance and trends, as well as the position of the Group. Non-IFRS financial measures are also used to enhance the comparability of information between reporting periods by adjusting for non-recurring or controllable factors which affect IFRS measures, to aid the user in understanding the Group's performance. Consequently, non-IFRS measures are used by the Directors and management for performance analysis, planning, reporting and incentive setting. These measures are not subject to audit.

The non-IFRS measures used in describing the business performance include:

- Same store sales
- Earnings before Interest, tax, depreciation and amortisation (EBITDA)
- Earnings before Interest and tax (EBIT)
- Normalised EBIT
- Significant item

Calculation of Normalised EBIT

Normalised EBIT has been calculated as follows:

	$000's
EBIT from continuing operations	50,147
EBIT from discontinuing operations	(36,937)
Group EBIT	**13,210**
Add back E&R and US closure costs:	
Lease settlements	9,833
Impairment and asset disposals	11,188
Make good expenses	177
Employee redundancies	1,743
Provision for stock obsolescence	1,600
Other expenses (Including consulting, legal fees, packaging, stationery, travel)	964
Add back significant item:	
Revaluation of employee benefits	1,391
Normalised EBIT	**40,106**

Environmental regulation

The Group has determined that no particular or significant environmental regulations apply to it.

Information on Directors

Information on Directors of Michael Hill International Limited in office during the financial year and until the date of this report are set out below.

Information on Directors (continued)

Emma Jane Hill (Chair) B.Com, M.B.A	
Experience and expertise	Emma was appointed a Director of the Company on 9 June 2016. Emma has over 30 years' experience with subsidiaries of the Company commencing on the shop floor in Whangarei, New Zealand. She held a number of management positions in the Australian company before successfully leading the expansion of the Group into Canada as Retail General Manager in 2002. In 2011 Emma was appointed as Deputy Chair of the listed New Zealand entity and was appointed by the Board as Executive Chair of that company in December 2015. Emma holds a Bachelor of Commerce degree and an MBA from Bond University.
Other current directorships	None
Former directorships in last 3 years	None
Responsibilities	Chair Non-Executive Director Member People Development and Remuneration Committee
Interests in shares and options	167,487,526 Ordinary Shares

Sir Richard Michael Hill K.N.Z.M.	
Experience and expertise	Sir Michael was appointed a Director of the Company on 9 June 2016. Sir Michael is the founder of Michael Hill Jeweller and was appointed as a Director of Michael Hill New Zealand Limited on 30 March 1990. He had 23 years of jewellery retailing experience before establishing Michael Hill in 1979, which then listed on the New Zealand Stock Exchange in 1987. Sir Michael's visionary leadership has been the foundation for the Company's successful international expansion. In 2008 he was recognised as Ernst & Young's 'Entrepreneur of the Year' and in 2011 was appointed a Knight Companion of the New Zealand Order of Merit for services to business and the arts. Sir Michael was appointed Founder President of the New Zealand listed entity in 2015 in recognition of his special connection with Michael Hill for over 35 years. Sir Michael led the Group as Chairman from 1987 until December 2015.
Other current directorships	None
Former directorships in last 3 years	None
Responsibilities	Non-Executive Director
Interests in shares and options	148,330,600 Ordinary Shares

Information on Directors (continued)

Gary Warwick Smith B.Com, F.C.A., F.A.I.C.D.	
Experience and expertise	Gary was appointed a Director of the Company upon incorporation on 24 February 2016. Gary has had extensive Director experience. He is Chairman of Flight Centre Travel Group, one of Australia’s top 100 public companies and is a member of their Audit and Remuneration sub-committee. He is a Chartered Accountant and a Fellow of the Australian Institute of Company Directors. He is also a Director of Tourism Events Queensland and Chair of its Audit and Risk Committee.
Other current directorships	Flight Centre Travel Group Limited Tourism Events Queensland
Former directorships in last 3 years	None
Responsibilities	Non-Executive and Independent Director Chair Audit and Risk Management Committee Member People Development and Remuneration Committee
Interests in shares and options	30,000 Ordinary Shares

Robert Ian Fyfe BEng, F.E.N.Z.	
Experience and expertise	Rob was appointed a Director of the Company on 9 June 2016. Rob served as CEO of Air New Zealand between 2005 and 2012, a period that saw a resurgence in Air New Zealand to become one of the most recognised and awarded airlines in the world and one of the best performers in a tough industry. Prior to Air New Zealand, Rob had gained extensive general management experience in various retail businesses operating in New Zealand, Australia and Great Britain.
Other current directorships	Antarctica New Zealand Air Canada
Former directorships in last 3 years	Icebreaker Limited
Responsibilities	Non-Executive and Independent Director Chair People Development and Remuneration Committee Member Audit and Risk Management Committee
Interests in shares and options	63,640 Ordinary Shares

Information on Directors (continued)

Janine Suzanne Allis	
Experience and expertise	Janine was appointed a Director of the Company on 9 June 2016. Janine is the Founder and Executive Director of Retail Zoo Pty Ltd which currently owns three brands - Boost Juice, Salsa's Fresh Mex Grill and Cibo. The Retail Zoo network has over 500 stores in 13 countries. Janine's strong retail experience was obtained by creating Boost Juice Bars and turning it into an iconic Australian brand with over 95% awareness rate in the Australian market. Drive and passion have translated into over $2 billion in global sales from inception and has earned Janine many accolades, including Telstra Businesswoman of the Year, Amex Franchisor of the Year and ARA Retailer of the Year. She was inducted into the Australian Business Women Hall of Fame as well as BRW listing Janine in the top 15 people who have changed the way we do business in the last 20 years. Janine now shares her knowledge with others, including through her role as a 'Shark', investor and mentor on Channel Ten's Shark Tank.
Other current directorships	Retail Zoo Pty Ltd
Former directorships in last 3 years	None
Responsibilities	Non-Executive and Independent Director Member Audit and Risk Management Committee
Interests in shares and options	150,000 Ordinary Shares

Company secretary

The Company Secretary is K A Hammond LLB (Hons), BA, GradDipLegPrac. Katherine was appointed to the position of Company Secretary on 22 January 2018, the same day she joined the Group.

Katherine holds a Bachelor of Laws with Honours and a Bachelor of Arts from the University of Queensland and is admitted to practice as a Solicitor of the Supreme Court of Queensland. Prior to her appointment as Company Secretary, Katherine practiced law for 8 years in the areas of mergers & acquisitions, capital markets and corporate advisory, which included advising listed and unlisted entities on governance, compliance and transactional matters.

Mary-Anne Greaves was appointed as Company Secretary on 11 July 2016 and resigned on 15 December 2017. Andrew Lowe, Chief Financial Officer, was appointed as Company Secretary on 15 December 2017 and resigned as Company Secretary on 22 January 2018, upon the appointment of Katherine Hammond.

Meetings of directors

The numbers of meetings of the Company's Board of Directors and of each Board committee held during the year ended 30 June 2018, and the numbers of meetings attended by each Director were:

	Full meetings of Directors		Meetings of committees			
			Audit and Risk Management		People Development and Remuneration	
	A	B	A	B	A	B
E J Hill	13	13	-	-	4	4
Sir R M Hill	10	13	-	-	-	-
G W Smith	10	13	2	2	3	4
R I Fyfe	11	13	2	2	4	4
J S Allis	13	13	2	2	-	-

A = Number of meetings attended
B = Number of meetings held during the time the Director held office or was a member of the committee during the year

Committee membership

As at the date of this report, Michael Hill International Limited has an Audit and Risk Management Committee and a People Development and Remuneration Committee.

Audit and Risk Management Committee

Gary Smith (c)
Janine Allis
Rob Fyfe

People Development and Remuneration Committee

Rob Fyfe (c)
Emma Hill
Gary Smith

(c) Designates chair of the committee

Remuneration report (audited)

The Directors present the 2018 Michael Hill International Limited remuneration report, outlining key aspects of our remuneration policy and framework, and remuneration awarded during the 2018 financial year.

Remuneration framework

The information provided in this remuneration report has been audited as required by section 308(3C) of the *Corporations Act 2001*.

Principles of compensation

Remuneration is referred to as compensation throughout this report.

Key management personnel ('KMP'), including Directors of the Company and other executives, have authority and responsibility for planning, directing and controlling the activities of the Group.

For the 2018 financial year, it was determined that the KMP of Michael Hill International were:

- Chief Executive Officer (CEO) - Phil Taylor
- Chief Financial Officer (CFO) - Andrew Lowe (appointed 4 December 2017)
- Chief Information Officer (CIO) - Matt Keays
- Group Executive Supply Chain (GESC) - Galina Hirtzel
- Chief Customer Officer (CB&CO) - Vanessa Brennan (appointed 15 January 2018)
- Group Executive Human Resources (GEHR) - Stewart Silk

Remuneration report (audited) (continued)

Principles of compensation (continued)

Compensation levels for key management personnel of the Group are competitively set to attract and retain appropriately qualified and experienced directors and executives. The People Development and Remuneration Committee obtains independent advice every three years on the appropriateness of compensation packages of the Group given trends in comparative companies both locally and internationally, and the objectives of the Group’s compensation strategy.

The compensation structures explained below are designed to attract suitably qualified candidates, reward the achievement of strategic objectives, and achieve the broader outcome of creation of value for shareholders. The compensation structures take into account the capability and experience of the KMP, and the KMP's ability to control the relevant segments performance.

The Executive Remuneration framework consists of:

(1) Total Fixed Remuneration ('TFR') - includes fixed cash remuneration and superannuation component.
(2) Short term incentive ('STI') - on target performance is determined as a percentage of TFR, 70% of the STI is directly aligned to achieving the Group EBIT return on average total assets ('ROA') hurdle (15% ROA) and 30% based on achievement of individual performance plans.
(3) Long term incentive ('LTI') - alignment of executive incentives with the long term performance is achieved by way of a deferred remuneration component. An issue of share rights is made to participants of the scheme, the quantum being a % of the STI earned.

The current remuneration policy settings for the KMP are as follows:

CEO	TFR set at 90% of market median On target STI set at 75% of TFR LTI set at 30% of STI achieved
CFO	TFR set at 90% of market median On target STI set at 50% of TFR LTI set at 30% of STI achieved
CB&CO	TFR set at 90% of market median On target STI set at 35% of TFR LTI set at 30% of STI achieved
CIO	TFR set at 90% of market median On target STI set at 35% of TFR LTI set at 30% of STI achieved
GESC	TFR set at 90% of market median On target STI set at 35% of TFR LTI set at 30% of STI achieved
GEHR	TFR set at 70% of market median On target STI set at 35% of TFR LTI set at 30% of STI achieved

Total fixed compensation

Fixed compensation consists of base compensation as well as leave entitlements and employer contributions to superannuation funds.

Compensation levels are reviewed annually by the People Development and Remuneration Committee through a process that considers individual, segment and overall performance of the Group. In addition, external consultants provide analysis and advice every three years to ensure the Directors’ and senior executives’ compensation is competitive in the market place. A senior executive’s compensation is also reviewed on promotion.

Remuneration report (audited) (continued)

Performance linked compensation

Performance linked compensation includes both short-term and long-term elements, and is designed to reward senior executives for meeting or exceeding their financial and personal objectives. The STI is an ‘at risk’ annual cash payment, while the LTI is a deferred compensation plan providing rights over ordinary shares of the Company under the rules of the executive incentive plan.

Short-term incentive

The short term incentive scheme is comprised of two components; 70% of the STI for key management personnel is linked to achievement of the Group's EBIT return on average total assets hurdle (15% ROA) for the year and 30% is linked to the achievement of key performance indicators ('KPI's') that are agreed in personal performance plans ('PPP's'), at the start of the reporting period.

The process and scheme provides an ongoing performance management system, along with integrated reporting for visibility and transparency of progress by each senior executive. The framework aligns the senior executive KPIs to delivery of the strategic plan, divisional business plans along with critical operational measures and leadership measures of each role. The following points outline the framework:

- The policy and framework cascades from the CEO to Group Executives with the intention in 2018-19 to cascade relevant KPIs further down through the levels of management. This aims to ensure key aspects of the Group’s strategic plan, divisional business plans, along with critical drivers of business outcomes are clearly identified at each level of leadership. This includes personal development plans, and leadership performance.
- The metrics are assessed monthly (on a YTD basis) and along with normal operational metrics, provides the basis for monthly work in progress ('WIP') reviews.

Long-term incentive

Options were issued under the Executive Incentive Plan (made in accordance with thresholds set in plans approved by shareholders). The ability to exercise the options is conditional on continuing employment with the Group. The options issued during the year relates to the entitlements set in the prior years. Options previously issued are detailed in this report and most recent Appendix 3B.

The Company introduced a deferred compensation plan ('LTI') involving the granting of share rights to eligible participants in the 2015-16 financial year and was approved by shareholders at the Company’s Annual General Meeting held on 31 October 2016.

Under the plan, an executive may be granted share rights by the Company. Each share right represents a right to receive one ordinary share in the Company, subject to the terms and conditions of the rules of the plan. An allocation of share rights is made to each eligible participant on an annual basis to a value of 30% of the STI payment earned[1]. The share rights progressively vest[2] over a 3, 4 and 5 year period from the date of issue and are only retained on exiting the business in the event that the participant is deemed a 'Good Leaver' pursuant to the LTI plan rules.

Feature	Description
Opportunity/ Allocation	30% of respective STI which is issued to the Executive by way of share rights which are granted and vest in 3 tranches. Each right represents a right to acquire one ordinary share in the Company.
Tranches	Year 3 - provided participant remains employed with the Company, 25% will vest Year 4 - provided participant remains employed with the Company, 25% will vest Year 5 - provided participant remains employed with the Company, 50% will vest
Exercise	Once the rights have vested, Participants can exercise them. They can be exercised by completing and returning to the Company an Exercise Notice.
Expiry	Rights will expire on the date 15 years from the grant date

Remuneration report (audited) (continued)

Long-term incentive (continued)

In addition to the share rights issued to the CEO and other eligible senior executives of the Group under the incentive plan, the CEO was granted share rights as part of the CEO package, which were granted to Mr Taylor during his tenure as interim CEO between 8 August 2016 and 6 March 2017. An allocation of share rights equal to 75% of 2016 TFR ($325,500) per annum for 3 years from 1 September 2016 were made to the CEO. Each tranche of share rights will vest at a date which is 3 years from the date of issue and are only retained provided Mr Taylor is employed by the Group at the commencement of the financial year in which the share right vesting is scheduled to occur. Termination of employment prior to each corresponding 3 year period will result in all unvested share rights being forfeited[3].

1 The number of share rights in each tranche, is based on the prescribed dollar value for each tranche divided by the volume weighted average share price of Michael Hill International shares over 5 trading days following the Michael Hill International shares trading on an ex-dividend basis.
2 On vesting each share right represents a right to receive one (1) ordinary share in the Company. No exercise price is payable upon the exercise of any share rights.
3 The additional share rights component of Mr Taylor's remuneration package is a continuation of the existing plan agreed to upon Mr Taylor's appointment as interim CEO. As a consequence, the deemed issue date for the second tranche of share rights was 18 October 2017 and the corresponding vesting date is 1 July 2020. The third tranche of share rights is anticipated to be issued later this year and the corresponding vesting date will be 1 July 2021.

Short-term and long-term incentive structure

The People Development and Remuneration Committee considers that the above performance-linked compensation structure is generating the desired outcome.

The scheme is already demonstrating a close correlation between executive remuneration, achievement of budget targets and share price performance as desired.

In 2017-18, the performance linked component of compensation comprises approximately 13% of total payments to senior executives (2016-17: 7%).

In the current year the Group didn't meet its overall Board targets, and as a consequence bonuses earned by KMP's in the current financial year were between 50 and 70% lower than the targeted STI% of TFR.

Remuneration policy and link to performance

Our People Development and Remuneration Committee is made up of two independent non-executive Director's and the Chair of the Board of Directors. The committee reviews and determines our remuneration policy and structure annually to ensure it remains aligned to business needs, and meets the Group's remuneration principles. The Committee also engages external remuneration consultants every three years to assist with this review.

The People Development and Remuneration Committee is a committee of the Board. It is primarily responsible for making recommendations to the Board on:

- the over-arching executive remuneration framework
- operation of the incentive plans which apply to the senior executives (the executive team), including key performance indicators and performance hurdles
- remuneration levels of executives, and
- non-executive Director fees.

Remuneration report (audited) (continued)

Remuneration policy and link to performance (continued)

Their objective is to ensure that remuneration policies and structures are fair and competitive and aligned with the long-term interests of the Company.

The Corporate Governance Statement provides further information on the role of this committee. The ASX Corporate Governance Principles and Recommendations rules and principles may materially differ from NZX's Corporate Governance rules and NZX Code.

In particular, the Board aims to ensure that remuneration practices are:

- competitive and reasonable, enabling the Company to attract and retain key talent
- aligned to the Company's strategic and business objectives and the creation of shareholder value
- transparent and easily understood, and
- acceptable to shareholders.

Figure 1: Remuneration framework

Element	**Purpose**	**Performance metrics**	**Potential value**	**Changes for FY 2019**
Total fixed remuneration (TFR)	Provide competitive market salary including superannuation and non-monetary benefits	All executives are reviewed in line with personal performance plans	Positioned at a percentage of median market rate	Reviewed in line with market
STI	Reward for in-year performance	70% of the target STI is calculated on a return on total assets basis. 30% of the target STI is based on a range of KPI's	CEO: 75% of TFR CFO: 50% of TFR Execs: 35% of TFR	Nil
LTI	Alignment to long-term shareholder value	Nil	CEO: 30% of STI CFO: 30% of STI Execs: 30% of STI	Nil

Balancing short-term and long-term performance

Annual incentives are set between 35% and 75% of TFR, in order to drive performance without encouraging undue risk-taking.

Long-term incentives are assessed over a 3 to 5 year period and are designed to promote long-term stability in shareholder returns and talent retention.

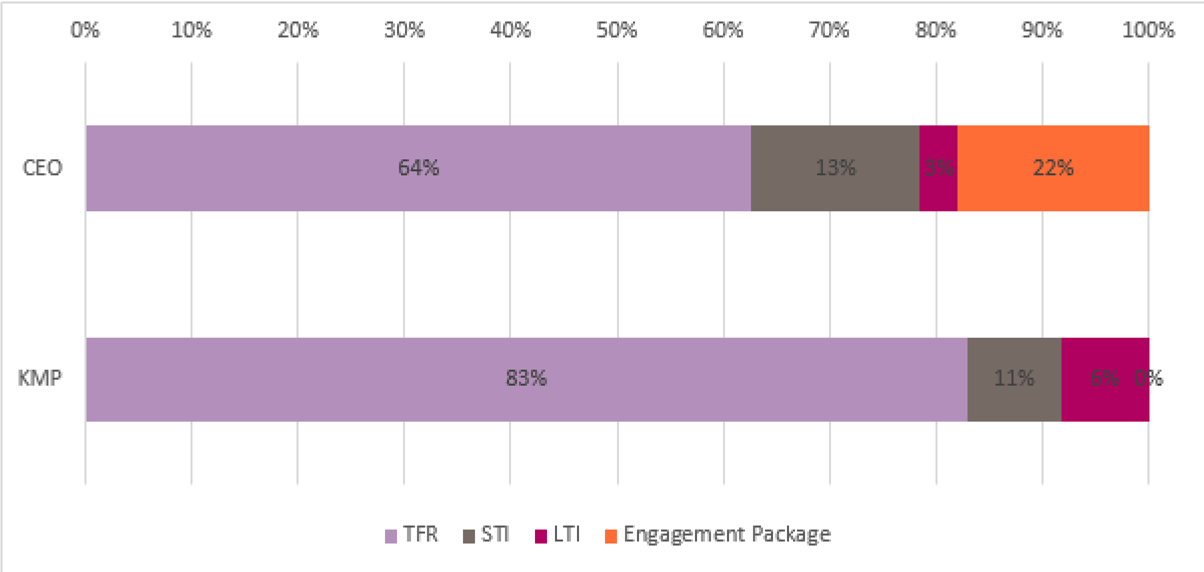
The actual remuneration mix for FY 2018 is shown in figure 2 below and target remuneration mix for 2019 is in figure 3 below. It reflects the STI opportunity for the 2018-19 year that will be available if the performance conditions are satisfied at target, and the value of the LTI rights and options granted for the year, as determined at the grant date.

Remuneration report (audited) (continued)

Remuneration policy and link to performance (continued)

Balancing short-term and long-term performance (continued)

Figure 2: Actual remuneration mix for FY 2018

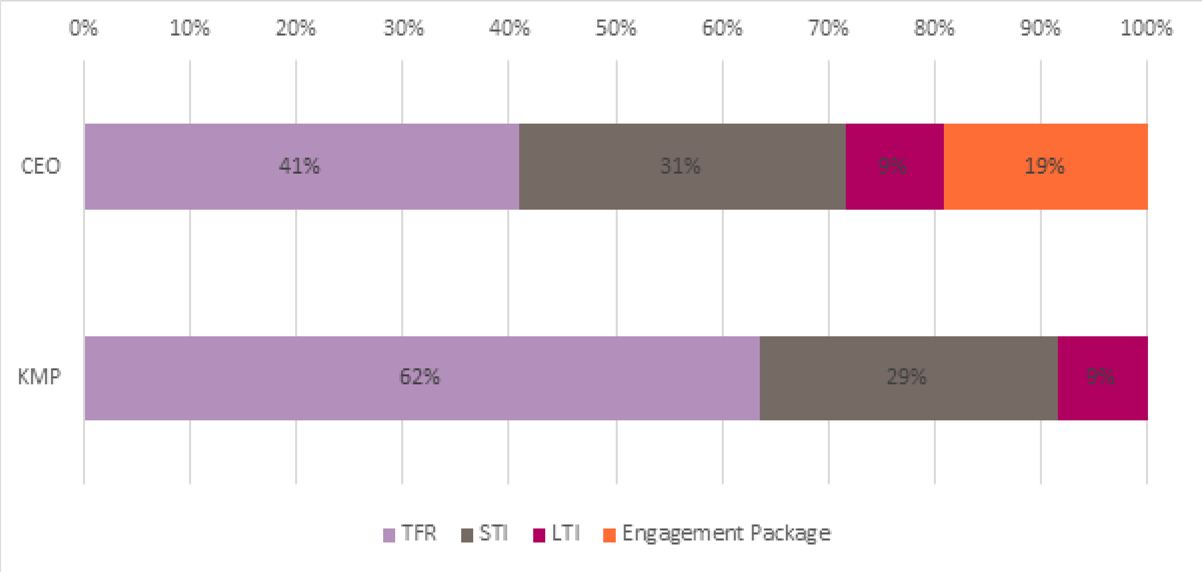


Remuneration report (audited) (continued)

Remuneration policy and link to performance (continued)

Balancing short-term and long-term performance (continued)

Figure 3: Target remuneration mix for FY 2019



Remuneration report (audited) (continued)

Remuneration policy and link to performance (continued)

Assessing performance and claw-back of remuneration

The People Development and Remuneration Committee is responsible for assessing performance against KPIs and determining the STI and LTI to be paid.

In the event of serious misconduct or a material misstatement in the Company's financial statements, the People Development and Remuneration Committee can cancel or defer performance-based remuneration.

Consequences of performance on shareholder wealth

In considering the Group's performance and benefits for shareholder wealth, the People Development and Remuneration Committee have regard to the following indices in respect of the current financial year and the previous four financial years.

	2018 **$'000**	**2017** $'000	**2016** $'000	**2015** $'000	**2014** $'000
NPAT	4,610	32,648	19,577	27,754	25,041
NPAT from continuing operations	34,818	44,132	26,330	33,219	28,171
EBIT*	13,210	48,117	47,058	42,061	42,151
EBIT from continuing operations*	50,147	62,332	54,424	48,558	45,212
Normalised EBIT*	40,106	48,117	47,058	42,061	42,151
Dividends payments ($'000)	19,371	19,264	17,490	23,176	22,336
Share price as at 30 June (NZ$ 2016 to 2014)	$.97	$1.11	$1.14	$1.06	$1.24
Return on shareholders equity	17.8%	22.7%	14.1%	18.0%	15.9%
Return on average total assets	9.1%	11.4%	7.2%	9.6%	8.9%

* EBIT and Normalised EBIT are Non-IFRS Information and are unaudited. Please refer to Non-IFRS Information on page 10 of the Directors Report for an explanation of Non-IFRS information and a reconciliation of EBIT from continuing operations and Normalised EBIT.

EBIT and ROA hurdles are considered the primary financial performance targets in setting the STI. Profit amounts for 2014 to 2018 have been prepared in accordance with the requirements of the Corporations Act 2001, Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board. This also complies with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

The overall level of compensation takes into account the performance of the Group over a number of years.

Other benefits

Key management personnel do not receive additional benefits, such as non-cash benefits, other than statutory superannuation, as part of the terms and conditions of their appointment.

Loans to key management personnel

The Company does not provide loans to KMP's or other senior executives.

Service contracts

It is the Group's policy that service contracts for KMPs, excluding the chief executive officer, are unlimited in term but capable of termination on three months' notice and that the Group retains the right to terminate the contract immediately, by making payment equal to three months' pay in lieu of notice.

Remuneration report (audited) (continued)

Service contracts (continued)

The Group has entered into a service contract with four KMPs that are capable of termination on three months' notice. The Group retains the right to terminate a contract immediately by making payment equal to three months' pay in lieu of notice. The KMPs are also entitled to receive on termination of employment their statutory entitlements of accrued annual and long service leave, together with any superannuation benefits.

The Group has entered into a service contract with two KMPs that are capable of termination on six month's notice. The Group retains the right to terminate a contract immediately by making payment equal to six months' pay in lieu of notice. The KMP is also entitled to receive on termination of employment their statutory entitlements of accrued annual and long service leave, together with any superannuation benefits.

CEO Contract

The Group has entered into a service contract with the CEO, Phil Taylor who was appointed CEO on 6 March 2017 after a period as Interim CEO following the resignation of the former CEO, Mike Parsell on 8 August 2016. The service contract does not contain any probationary period or fixed term.

The remuneration payable to Mr Taylor is as follows:

(a) Annual base salary - $707,594 (inclusive of the statutory superannuation contributions but excluding leave provisions).

(b) Short terms incentives (STI) - 75% of base salary payable in cash on performance of agreed Group profit targets based on a return on asset formula (70% of STI) and other agreed annual key indicators (30% of STI).

(c) Deferred compensation plan (LTI) - an allocation of share rights on an annual basis to a value of 30% of the STI payment earned in the preceding year[1]. The share rights progressively vest[2] over a 3 to 5 year period from the date of issue and are retained on exiting the business in the event that Mr Taylor is deemed a 'Good Leaver' pursuant to the LTI plan rules.

(d) Interim CEO engagement package - an allocation of share rights equal to 75% of 2016 TFR ($325,500) per annum for 3 years from 1 September 2016. Each tranche of share rights will vest at a date which is 3 years from the date of issue and are retained provided Mr Taylor is employed by the Group at the commencement of the financial year in which the share right vesting is scheduled to occur. Termination of employment prior to each corresponding 3 year period will result in all unvested share rights being forfeited[3].

Either party may terminate the engagement on six months' notice. Otherwise, the Group may terminate Mr Taylor's position for serious misconduct or professional negligence.

Mr Taylor will be restrained for up to 18 months following the cessation of his engagement with the Group from soliciting business, customers, suppliers or employees of the Group.

The service contract outlines the components of compensation but does not prescribe how compensation levels are modified year to year. The People Development and Remuneration Committee reviews compensation levels each year to take into account cost-of-living changes, any change in the scope of the role performed by the senior executive and any changes required to meet the principles of compensation policy.

1 The number of share rights in each tranche is based on the prescribed dollar value for each tranche divided by the volume weighted average share price of Michael Hill International shares over 5 trading days following the Michael Hill International shares trading on an ex-dividend basis.
2 On vesting, each share right represents a right to receive one (1) ordinary share in the capital of the Company. No exercise price is payable upon the exercise of any share right.
3 The additional share rights component of Mr Taylor's remuneration package is a continuation of the existing plan agreed to upon Mr Taylor's appointment as interim CEO. As a consequence, the deemed issue date for the second tranche of share rights is 18 October 2017 and the corresponding vesting date is 1 September 2020.

Remuneration report (audited) (continued)

Service contracts (continued)

Director consulting agreement

Michael Hill Group Services Pty Limited ACN 134 562 440, a subsidiary of Michael Hill International Limited (MHIL), has entered into a consultancy agreement (Consultancy Agreement) with Robert Ian Fyfe. Mr Fyfe is a non-executive Director of MHIL. Details of the Consultancy Agreement were disclosed to the ASX and NZX on 31 August 2017. The Board (with Rob abstaining) formed the view that the Consultancy Agreement is on arm's length commercial terms.

Under the Consultancy Agreement, Mr Fyfe provides mentoring support to the CEO, Phil Taylor. Mr Taylor was appointed to the role of CEO following a long and successful career with Michael Hill, as CFO leading the global finance team. The Board identified an opportunity to expand Mr Taylor's leadership capability to ensure that Mr Taylor is well equipped for the significant leadership responsibilities and challenges as CEO.

Mr Fyfe is a very well regarded business leader, with deep CEO and leadership experience including having successfully led Air New Zealand with over 11,000 employees. Over many years during Mr Fyfe's tenure, Air New Zealand was recognised globally for, its brand, marketing, service culture and overall business performance. Combined with Mr Fyfe's understanding of the Michael Hill business, the Board recognised that he is well positioned to provide Mr Taylor with tailored leadership mentoring.

Mr Fyfe typically spends one to two days with Mr Taylor every six weeks where he observes Mr Taylor's management practices and provides Mr Taylor with feedback and suggested techniques and styles that Mr Taylor may adopt to enhance the effectiveness of his management and leadership.

The mentoring also enables the Board to gain greater insight into the leadership culture, strengths and challenges.

Mr Fyfe's mentoring is non-prescriptive and Mr Fyfe does not participate in management decisions. Mr Fyfe and the Board consider that Mr Fyfe maintains an ability to bring independent and critical assessment of Mr Taylor's performance as CEO.

The income derived by Mr Fyfe (or entities Mr Fyfe controls) under the Consultancy Agreement accounts for less than 10% of Mr Fyfe's aggregate annual income for FY18. For FY18, a total amount of $84,000 was paid pursuant to the Consultancy Agreement; this comprised an amount of $64,000 paid to Rob Fyfe and an amount of $20,000 paid to The People Shop Ltd. The Board anticipates that less than $100,000 will be paid pursuant to the Consultancy Agreement for FY19 and will be paid to The People Shop Ltd.

Services from remuneration consultants

The People Development and Remuneration Committee engaged a remuneration consultant during the 2016 financial year to review the amount and elements of the key management personnel remuneration and provide recommendations in relation thereto. It is the committee's intention to engage consultants every 3 years to review and advise on executive remuneration.

Non-executive Directors

Total compensation for all non-executive Directors, last voted upon by shareholders on 29 June 2016, is not to exceed $840,000 per annum and is set based on advice from external advisors with reference to fees paid to other non-executive Directors of comparable companies. Directors' base fees are presently $96,805 per annum. Where a Director serves as Chair on the People Development and Remuneration Committee they are entitled to an additional payment of $20,000 per annum. Where a Director serves as Chair on the Audit and Risk Committee they are entitled to an additional payment of $30,000 per annum. All non-executive Directors enter into a service agreement with the Company in the form of a letter of appointment. The letter summarises the board policies and terms, including remuneration, relevant to the office of Director.

The Board Chair receives up to twice the base fee. Non-executive Directors do not receive performance-related compensation. Directors' fees cover all main board activities and membership of committees.

Remuneration report (audited) (continued)

Non-executive Directors (continued)

Non-executive directors are not provided with retirement benefits apart from statutory superannuation.

Directors and KMPs remuneration

Details of the nature and amount of each major element of remuneration of each Director of the Company, and other key management personnel of the consolidated entity are:

Remuneration report (audited) (continued)

Directors and KMPs remuneration (continued)

	Short-term				Long-term	Post-employment		Share-based payments			
	Salary & fees $	STI cash bonus $	Other[(a)] $	Total $	Long service leave $	Superannuation benefits $	Termination benefits $	Options and rights $	Total $	Proportion of remuneration performance related %	Value of options as proportion of remuneration %
Non-executive Directors											
Emma Jane Hill											
2018	193,610	-	-	193,610	-	-	-	-	193,610	-%	-%
2017	190,000	-	-	190,000	-	-	-	-	190,000	-%	-%
Sir Richard Michael Hill											
2018	96,805	-	-	96,805	-	-	-	-	96,805	-%	-%
2017	95,000	-	-	95,000	-	-	-	-	95,000	-%	-%
Gary Warwick Smith											
2018	115,804	-	-	115,804	-	11,001	-	-	126,805	-%	-%
2017	104,072	-	-	104,072	-	10,928	-	-	115,000	-%	-%
Robert Ian Fyfe											
2018	116,805	-	84,000	200,805	-	-	-	-	200,805	-%	-%
2017	115,000	-	-	115,000	-	-	-	-	115,000	-%	-%
Janine Suzanne Allis											
2018	96,805	-	-	96,805	-	-	-	-	96,805	-%	-%
2017	95,000	-	-	95,000	-	-	-	-	95,000	-%	-%
Total Directors' remuneration											
2018	619,829	-	84,000	703,829	-	11,001	-	-	714,830	-%	-%
2017	599,072	-	-	599,072	-	10,928	-	-	610,000	-%	-%
KMPs											
Phil Taylor, CEO (Formerly Interim CEO and CFO)											
2018	720,306	119,407	-	839,713	20,625	19,427	-	313,940	1,193,705	10.00%	26.30%
2017	691,733	167,267	-	859,000	112,205	30,627	-	227,332	1,229,164	13.61%	18.49%

Remuneration report (audited) (continued)

Directors and KMPs remuneration (continued)

	Short-term				Long-term	Post-employment		Share-based payments			
	Salary & fees $	STI cash bonus $	Other[(a)] $	Total $	Long service leave $	Superannuation benefits $	Termination benefits $	Options and rights $	Total $	Proportion of remuneration performance related %	Value of options as proportion of remuneration %
Andrew Lowe, CFO (Appointed 4 December 2017)											
2018	180,200	47,320	-	227,520	2,890	15,981	-	2,979	249,370	18.98%	1.19%
Vanessa Brennan, CCO (Appointed 15 January 2018)											
2018	192,980	70,000	-	262,980	2,976	17,018	-	4,113	287,087	24.38%	1.43%
Matt Keays, CIO											
2018	324,316	30,802	-	355,118	5,596	25,000	-	14,461	400,175	7.70%	3.61%
2017	311,000	39,150	-	350,150	5,764	29,760	-	12,122	397,796	9.84%	3.05%
Galina Hirtzel, GESC											
2018	281,606	24,609	-	306,215	6,243	23,355	-	34,682	370,495	6.64%	9.36%
2017	274,083	29,321	-	303,404	7,818	28,235	-	37,956	377,413	7.77%	10.06%
Stewart Silk, GEHR											
2018	216,018	6,830	-	222,848	5,462	22,443	-	32,689	283,442	2.41%	11.53%
2017	216,847	24,023	-	240,870	4,114	27,640	-	36,281	308,905	7.78%	11.75%
Mike Parsell, CEO (Resigned 8 August 2016)											
2018	-	-	-	-	-	-	-	-	-	-%	-%
2017	61,037	-	-	61,037	(3,984)	38,623	1,603,742	-	1,699,418	-%	-%
Anna Shaw, CMO (Resigned 22 March 2017)											
2018	-	-	-	-	-	-	-	-	-	-%	-%
2017	304,022	68,000	-	372,022	-	29,498	-	-	401,520	16.94%	-%
Total KMPs' remuneration											
2018	1,915,426	298,968	-	2,214,394	43,792	123,224	-	402,864	2,784,274	10.74%	14.47%
2017	1,858,722	327,761	-	2,186,483	125,917	184,383	1,603,742	313,691	4,414,216	7.43%	7.11%

Remuneration report (audited) (continued)

Directors and KMPs remuneration (continued)

	Short-term				Long-term	Post-employment		Share-based payments			
	Salary & fees $	STI cash bonus $	Other[(a)] $	Total $	Long service leave $	Superannuation benefits $	Termination benefits $	Options and rights $	Total $	Proportion of remuneration performance related %	Value of options as proportion of remuneration %
Total Directors' and KMPs' remuneration											
2018	2,535,255	298,968	84,000	2,918,223	43,792	134,225	-	402,864	3,499,104	8.75%	11.80%
2017	2,457,794	327,761	-	2,785,555	125,917	195,311	1,603,742	313,691	5,024,216	6.52%	6.24%

Notes in relation to the table of Directors' and KMPs' remuneration:
a. The amount of $200,805 in respect of Robert Ian Fyfe's salary & fees comprises an amount of $116,805 in respect of director fees and an amount of $84,000 in respect of services provided pursuant to a consultancy agreement (Consultancy Fees); the Consultancy Fees comprised an amount of $64,000 paid to Rob Fyfe and an amount of $20,000 paid to The People Shop Ltd. Further details regarding the consulting agreement are set out in the Service contracts section above on page 22.
b. The short-term incentive bonus is for performance during the respective financial year using the criteria set out on page 17 of the Remuneration report. The amount was determined on 24 August 2018 after performance reviews were completed and approved by the People Development and Remuneration Committee.
c. The fair value of options is calculated at the date of grant using the Binomial option-pricing model and allocated to each reporting period evenly over the period from grant date to vesting date. The value disclosed is the portion of the fair value of the options recognised as an expense in each reporting period.
d. Mike Parsell's termination benefits were approved by shareholders and the Board on 31 October 2016.

Remuneration report (audited) (continued)

Analysis of bonuses included in remuneration

Details of the vesting profile of the short-term incentive cash bonuses awarded as remuneration to each Director of the Company, and other key management personnel are detailed below.

Short-term incentive bonus	Target bonus available	Included in remuneration **$(a)**	Amounts forfeited **$(b)**	Vested in year **%**
KMPs				
Phil Taylor	530,595	159,209	371,386	100
Andrew Lowe	169,000	50,700	118,300	100
Vanessa Brennan	150,500	70,000	80,500	100
Matt Keays	118,470	35,541	82,929	100
Galina Hirtzel	106,995	32,099	74,896	100
Stewart Silk	85,371	25,611	59,760	100

(a) Amounts included in remuneration for the financial year represent the amount related to the financial year based on achievement of personal goals and satisfaction of specified performance criteria. The People Development and Remuneration Committee approved these amounts on 23 August 2018.
(b) The amounts forfeited due to the performance or service criteria not being met in relation to the current financial year.

Additional statutory information

Equity instruments

All options refer to options over ordinary shares of Michael Hill International Limited, which are exercisable on a one-for-one basis under the Executive Incentive Plan.

Options and rights over equity instruments issued as compensation

Details of tranches issued over ordinary shares in the Company that were issued as compensation to each key management person during the reporting period under previously granted options and details on options that vested during the reporting period are as follows:

	Number of options issued during 2018	**Option issue date**	**Fair value at grant date per option**	**Exercise price per option**	**Expiry date**	**Number of options vested during 2018**
KMPs						
Galina Hirtzel	100,000	5 Oct 2017	NZ$0.148	AU$1.44	30 Sep 2027	-
Stewart Silk	100,000	5 Oct 2017	NZ$0.148	AU$1.44	30 Sep 2027	-

All options expire on their expiry date or within 3 months of termination of the individual's employment. The options are exercisable 5 years from release date. The options are conditional on continuing service. For options issued in the current year, the earliest exercise date is 30/9/2022.

Modification of terms of equity-settled share-based payment transactions

No terms of equity-settled share-based payment transactions (including options and rights granted as compensation to a key management person) have been altered or modified by the issuing entity during the reporting period or the prior period. The exercise price of any future option grants will be set by using the same method, with reference to the Australian Securities Exchange ('ASX'). Upon exercise of any option previously granted with a NZ$ exercise price, the $ exercise price will be converted to AU$ with reference to the Reserve Bank of Australian foreign exchange rate on that date.

Remuneration report (audited) (continued)

Additional statutory information (continued)

Equity instruments (continued)

Unissued shares

As at the date of this report, there were 3,800,000 unissued ordinary shares under options. Option holders do not have any right, by virtue of the option, to participate in any share issue of the Company or any related body corporate.

Analysis of options and rights over equity instruments granted as compensation

Details of vesting profiles of the options issued as remuneration to each key management person of the Group are detailed below. When exercisable, each option is convertible into one ordinary share of Michael Hill International Limited. The vesting conditions are set out in note 20(a).

Options issued	Number	Issue date*	Exercise price $	% expired in year**	% exercisable in year	Financial years in which option vests	Financial years in which option exercisable
KMPs							
Phil Taylor	750,000	Nov 2007	NZ$1.25	100%	100%	2008-2012	2013-2018
	150,000	Nov 2009	NZ$0.94	-	100%	2010-2014	2015-2020
	150,000	Sep 2010	NZ$0.88	-	100%	2011-2015	2016-2021
	150,000	Sep 2011	NZ$1.16	-	100%	2012-2016	2017-2022
	150,000	Sep 2012	NZ$1.41	-	100%	2013-2017	2018-2023
	150,000	Sep 2013	NZ$1.82	-	-	2014-2018	2019-2024
	750,000	Dec 2013	NZ$1.82	-	-	2014-2018	2019-2024
Total	2,250,000						
Galina Hirtzel	500,000	Dec 2013	NZ$1.82	-	-	2014-2018	2019-2024
	100,000	Sep 2014	NZ$1.63	-	-	2015-2019	2020-2025
	100,000	Sep 2015	NZ$1.14	-	-	2016-2020	2021-2026
	100,000	Sep 2016	AU$2.12	-	-	2017-2021	2022-2027
	100,000	Oct 2017	AU$1.44			2018-2022	2023-2028
Total	900,000						
Stewart Silk	500,000	Dec 2013	NZ$1.82	-	-	2014-2018	2019-2024
	100,000	Sep 2014	NZ$1.63	-	-	2015-2019	2020-2025
	100,000	Sep 2015	NZ$1.14	-	-	2016-2020	2021-2026
	100,000	Sep 2016	AU$2.12	-	-	2017-2021	2022-2027
	100,000	Oct 2017	AU$1.44	-	-	2018-2022	2023-2028
Total	900,000						

* The issue date refers to the date of the tranches prescribed in the options agreement.
** The percentage forfeited in the year represents the reduction from the maximum number of options available to vest due to performance criteria not being achieved.

Analysis of movements in options

The movement during the reporting period, by value, of options over ordinary shares in the Company held by each key management person is detailed below.

Remuneration report (audited) (continued)

Additional statutory information (continued)

Equity instruments (continued)

Analysis of movements in options (continued)

	Value of options issued in the year	Value of options exercised in year
Phil Taylor	-	-
Andrew Lowe	-	-
Vanessa Brennan	-	-
Matt Keays	-	-
Galina Hirtzel	NZ$14,790	-
Stewart Silk	NZ$14,790	-

Share rights

The number of share rights issued to KMPs and senior executives during the last financial year (including the interim CEO engagement package) was 536,551 share rights. Of these, share rights issued to KMPs are set out below (including the CEO engagement package).

KMP	No. of share rights issued	Fair value per share right $
Phil Taylor	358,570	1.05
Andrew Lowe	-	-
Vanessa Brennan	-	-
Matt Keays	11,210	1.05
Galina Hirtzel	8,395	1.05
Stewart Silk	6,878	1.05

Reconciliation of options and share rights held by KMP

The table below shows a reconciliation of options held by each KMP during the 2018 financial year. All vested options were exercisable.

2018	Balance at the start of the year						Balance at the end of the year	
KMP	Vested	Unvested	Issued as compen-sation	Vested	Exercised	Forfeited	Vested and exercisable	Un-vested
P Taylor	2,250,000	-	-	-	-	(750,000)	1,500,000	-
G Hirtzel	-	800,000	100,000	-	-	-	-	900,000
S Silk	-	800,000	100,000	-	-	-	-	900,000
	-	-	-	-	-	-	-	-
TOTAL	2,250,000	1,600,000	200,000	-	-	(750,000)	1,500,000	1,600,000

No options were exercised during the period.

No amounts are unpaid on any shares issued on the exercise of options.

Remuneration report (audited) (continued)

Additional statutory information (continued)

Reconciliation of options and share rights held by KMP (continued)

Figure 11: Share rights

This table below details share rights that were issued, vested and forfeited during the year for each KMP.

Name	Balance at start of the year	Issued during year	Vested	Forfeited	Balance at end of year (unvested)
	Number	Number	Number	Number	Number
P Taylor	263,593	358,570	-	-	622,163
M Keays	24,051	11,210	-	-	35,261
G Hirtzel	21,824	8,395	-	-	30,219
S Silk	18,484	6,878	-	-	25,362
TOTAL	327,952	385,053	-	-	713,005

* Share rights relating to the current reporting period are anticipated to be granted in late 2018. The number of shares will depend on the Michael Hill International Limited's share price over the five days prior to the grant date.

(i) Voting of shareholders at last year's annual general meeting

Michael Hill International Limited received more than 99.92% of "yes" votes on its remuneration report for the 2017 financial year. The Company did not receive any specific feedback at the AGM or throughout the year on its remuneration practices.

Insurance of officers and indemnities

Insurance of officers

The Company's Constitution provides that it may indemnify any person who is, or has been, an officer of the Group, including the Directors, the Secretaries and other officers, against liabilities incurred whilst acting as such officers to the extent permitted by law. The Company has entered into a Deed of Indemnity, Insurance and Access with each of the Company's Directors, Company Secretary and certain other officers. No Director or officer of the Company has received benefits under an indemnity from the Company during or since the end of the year.

The Company has paid a premium for insurance for officers of the Group. This insurance is against a liability for costs and expenses incurred by officers in defending civil or criminal proceedings involving them as such officers, with some exceptions. The contract of insurance prohibits disclosure of the nature of the liability insured against and the amount of the premium paid.

Indemnity of auditors

To the extent permitted by law, the Company has agreed to indemnify its auditor, 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.

Non-audit services

The following non-audit services were provided by the entity's auditor, Ernst & Young Australia. 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 2001. The nature and scope of each type of non-audit service provided means that auditor independence was not compromised.

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

	2018	2017
	$	$
Ernst & Young firm:		
Advisory fees	**170,231**	7,416
Total remuneration for non-audit services	**170,231**	7,416

Auditor's independence declaration

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 34.

Rounding of amounts

The Company is of a kind referred to in ASIC Legislative Instrument 2016/191, relating to the 'rounding off' of amounts in the Directors' report. Amounts in the Directors' report have been rounded off in accordance with the instrument to the nearest thousand dollars, or in certain cases, to the nearest dollar.

This report is made on 24 August 2018 in accordance with a resolution of Directors as required by section 298 of the Corporations Act 2001.

E J Hill
Chair

Brisbane
24 August 2018

Ernst & Young
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Auditor's Independence Declaration to the Directors of Michael Hill International Limited

As lead auditor for the audit of Michael Hill International 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 Michael Hill International Limited and the entities it controlled during the financial year.

Ernst & Young

Ernst & Young

Alison de Groot
Partner
24 August 2018

Michael Hill International Limited

ABN 25 610 937 598

Annual financial report - 30 June 2018

The Directors present the financial statements of Michael Hill International Limited for the year ended 30 June 2018.

Michael Hill International Limited
Consolidated statement of comprehensive income
For the year ended 30 June 2018

	Notes	2018 $'000	2017 $'000
Revenue from continuing operations	4	**575,549**	551,099
Other income	5(a)	**1,064**	1,640
Cost of goods sold		**(208,657)**	(200,093)
Employee benefits expense		**(151,939)**	(141,755)
Occupancy costs		**(58,074)**	(53,900)
Marketing expenses		**(31,433)**	(26,081)
Selling expenses		**(26,708)**	(24,647)
Impairment of property, plant and equipment		**(348)**	(36)
Impairment of other assets	8(c)	**(134)**	-
Onerous lease provision		**(6)**	-
Depreciation and amortisation expense	5(b)	**(18,694)**	(17,427)
Loss on disposal of property, plant and equipment		**(522)**	(557)
Other expenses		**(29,941)**	(25,896)
Finance costs	5(b)	**(2,690)**	(3,164)
Profit before income tax		**47,467**	59,183
Income tax expense	6	**(12,649)**	(15,051)
Profit from continuing operations		**34,818**	44,132
Profit/(loss) from discontinued operations	14	**(30,208)**	(11,485)
Profit for the year		**4,610**	32,647
Other comprehensive income			
Item that may be reclassified subsequently to profit or loss			
Cash flow hedges	9(b)	**996**	(256)
Currency translation differences arising during the year	9(b)	**320**	(2,542)
Other comprehensive income for the year, net of tax		**1,316**	(2,798)
Total comprehensive income for the year		**5,926**	29,849
Total comprehensive income for the year is attributable to:			
Owners of Michael Hill International Limited		**5,926**	29,849
Total comprehensive income for the year attributable to owners of Michael Hill International Limited arises from:			
Continuing operations		**36,134**	41,334
Discontinued operations		**(30,208)**	(11,485)
		5,926	29,849
		Cents	Cents
Earnings per share for profit attributable to the ordinary equity holders of the Company, attributable to continuing operations:			
Basic earnings per share	22	**8.99**	11.43
Diluted earnings per share	22	**8.98**	11.42
Earnings per share for profit attributable to the ordinary equity holders of the Company:			
Basic earnings per share	22	**1.19**	8.46
Diluted earnings per share	22	**1.19**	8.45

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

	Notes	**2018 $'000**	2017 $'000
ASSETS			
Current assets			
Cash and cash equivalents	7(a)	**7,220**	5,676
Trade and other receivables	7(b)	**25,381**	24,219
Inventories	8(a)	**192,074**	203,853
Derivative financial instruments	11(a)	**245**	-
Current tax receivables	8(e)	**-**	888
Other current assets	8(f)	**3,688**	3,945
Total current assets		**228,608**	238,581
Non-current assets			
Trade and other receivables	7(b)	**2,665**	2,371
Property, plant and equipment	8(b)	**66,666**	79,436
Deferred tax assets	8(d)	**61,895**	57,893
Intangible assets	8(c)	**12,626**	8,784
Other non-current assets	8(f)	**2,888**	2,057
Total non-current assets		**146,740**	150,541
Total assets		**375,348**	389,122
LIABILITIES			
Current liabilities			
Trade and other payables	7(c)	**49,339**	47,918
Derivative financial instruments	11(a)	**390**	1,141
Current tax liabilities	8(g)	**2,696**	-
Provisions	8(h)	**9,386**	4,670
Deferred revenue	8(i)	**26,476**	25,924
Total current liabilities		**88,287**	79,653
Non-current liabilities			
Borrowings	7(d)	**35,213**	45,034
Provisions	8(h)	**4,907**	6,235
Deferred revenue	8(i)	**57,720**	56,017
Total non-current liabilities		**97,840**	107,286
Total liabilities		**186,127**	186,939
Net assets		**189,221**	202,183
EQUITY			
Contributed equity	9(a)	**10,266**	10,015
Reserves	9(b)	**1,829**	281
Retained profits	9(b)	**177,126**	191,887
Total equity		**189,221**	202,183

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

	Notes	Contributed equity $'000	Share based payments reserve $'000	Foreign currency translation reserve $'000	Cash flow hedge reserve $'000	Retained profits $'000	Total equity $'000
		Attributable to owners of Michael Hill International Limited					
Balance at 1 July 2016		3,767	2,188	2,827	(884)	178,503	**186,401**
Profit for the year		-	-	-	-	32,648	**32,648**
Currency translation differences		-	-	(2,542)	-	-	**(2,542)**
Currency forward contracts		-	-	-	(834)	-	**(834)**
Interest rate swaps		-	-	-	578	-	**578**
Total comprehensive income for the year		**-**	**-**	**(2,542)**	**(256)**	**32,648**	**29,850**
Transactions with members in their capacity as owners:							
Dividends paid	13(b)(i)	-	-	-	-	(19,264)	**(19,264)**
Option expense through share based payments reserve	9(b)	-	55	-	-	-	**55**
Issue of shares to employees on exercise of options		4,825	-	-	-	-	**4,825**
Transfer option reserve to contributed equity on exercise of options		712	(712)	-	-	-	**-**
Transfer option reserve to contributed equity on forfeiture of options		711	(711)	-	-	-	**-**
Share rights expense through share based payments reserve		-	316	-	-	-	**316**
		6,248	(1,052)	-	-	(19,264)	**(14,068)**
Balance at 30 June 2017		**10,015**	**1,136**	**285**	**(1,140)**	**191,887**	**202,183**
Profit for the year		-	-	-	-	4,610	4,610
Currency translation differences		-	-	320	-	-	320
Currency forward contracts		-	-	-	336	-	336
Interest rate swaps		-	-	-	659	-	659
Total comprehensive income for the year		**-**	**-**	**320**	**995**	**4,610**	**5,925**
Transactions with members in their capacity as owners:							
Dividends paid	13(b)(i)	-	-	-	-	(19,371)	(19,371)
Option expense through share based payments reserve	9(b)	-	42	-	-	-	42
Share rights expense through share based payments reserve		-	442	-	-	-	442
Transfer option reserve to contributed equity on expiration of options		251	(251)	-	-	-	-
		251	233	-	-	(19,371)	(18,887)
Balance at 30 June 2018		**10,266**	**1,369**	**605**	**(145)**	**177,126**	**189,221**

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

	Notes	**2018 $'000**	2017 $'000
Cash flows from operating activities			
Receipts from customers (inclusive of GST and sales taxes)		**671,165**	649,041
Payments to suppliers and employees (inclusive of GST and sales taxes)		**(570,280)**	(534,444)
		100,885	114,597
Interest received		**10**	16
Other revenue		**1,078**	791
Interest paid		**(2,794)**	(3,106)
Income tax paid		**(6,448)**	(9,179)
Inland revenue tax settlement		**-**	(21,842)
Net GST and sales taxes paid		**(37,838)**	(41,525)
Net cash inflow from operating activities	10(a)	**54,893**	39,752
Cash flows from investing activities			
Proceeds from sale of property, plant and equipment		**549**	289
Payments for property, plant and equipment	8(b)	**(17,890)**	(27,294)
Payments for intangible assets	8(c)	**(6,665)**	(5,851)
Net cash (outflow) from investing activities		**(24,006)**	(32,856)
Cash flows from financing activities			
Proceeds from issues of shares on exercise of options	9(a)	**-**	4,825
Proceeds from borrowings		**116,500**	136,750
Repayment of borrowings		**(126,500)**	(132,250)
Dividends paid to Company's shareholders	13(b)	**(19,371)**	(19,264)
Net cash (outflow) from financing activities		**(29,371)**	(9,939)
Net increase (decrease) in cash and cash equivalents		**1,516**	(3,043)
Cash and cash equivalents at the beginning of the financial year		**5,676**	8,853
Effects of exchange rate changes on cash and cash equivalents		**28**	(134)
Cash and cash equivalents at the end of the financial year	7(a)	**7,220**	5,676

The above consolidated cash flow statement should be read in conjunction with the accompanying notes.

1 Corporate Information

The consolidated financial statements of Michael Hill International Limited and its subsidiaries (collectively, the Group) for the year ended 30 June 2018 were authorised for issue in accordance with a resolution of the directors on 24 August 2018. Michael Hill International Limited (the Company or Parent) is a for profit company limited by shares incorporated in Australia. The Company listed on the Australian Securities Exchange ('ASX') on 7 July 2016 as its primary listing, and maintains a secondary listing on the New Zealand Stock Exchange ('NZX').

2 Summary of significant accounting policies

(a) Basis of preparation

The financial report is a general purpose financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001, Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand ($'000), except when otherwise indicated.

The financial statements have been prepared on a historical cost basis, except for derivative financial instruments that have been measured at fair value. The consolidated financial statements provide comparative information in respect of the previous period.

(i) Compliance with IFRS

The consolidated financial statements of the Group comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

(b) Principles of consolidation and equity accounting

Subsidiaries

Subsidiaries are all entities (including special purpose) over which the Group has control. 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 to direct the activities of the investee. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the statement of comprehensive income. Investments in subsidiaries are accounted for at cost in the individual financial statements of Michael Hill International Limited. Refer to note 15(a).

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated on consolidation. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the transferred asset. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(c) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision makers. The chief operating decision makers, who are responsible for allocating resources and assessing performance of the operating segments, have been identified as the Executive Management team.

2 Summary of significant accounting policies (continued)

(d) Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The Group financial statements are presented in Australian dollars, which is the Group's presentation currency.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges and qualifying net investment hedges or are attributable to part of the net investment in a foreign operation.

(iii) Group companies

The results and financial position of all the Group entities (none of which have the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of the statement of financial position;
- income and expenses for each statement of profit or loss and statement of comprehensive income are translated at average exchange rates, unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions; and
- all resulting exchange differences are recognised in other comprehensive income.

On consolidation, exchange differences arising from the translation of any net investment in foreign entities, and of borrowings and other financial instruments designated as hedges of such investments, are recognised in other comprehensive income.

(e) Revenue recognition

(i) Sales of goods - retail

Sales of goods are recognised when a Group entity delivers a product to the customer. Retail sales are usually by cash, payment plan or credit card. The recorded revenue is the gross amount of sale (excluding taxes), including any fees payable for the transaction.

It is the Group's policy to sell its products to the end customer with a right of return. Accumulated experience is used to estimate and provide for such returns at the time of sale, recognising a Returns provision and corresponding Returns Inventory.

(ii) Rendering of services - deferred service revenue

The Group offers a professional care plan ('PCP') product which is considered deferred revenue until such time that service has been provided. A PCP is a plan under which the Group offers future services to customers based on the type of plan purchased. The Group subsequently recognises the income in revenue in the statement of comprehensive income once these services are performed. An estimate is used as a basis to establish the amount of service revenue to recognise in the consolidated statement of comprehensive income.

(iii) Rendering of services - repairs

Sales of services for repair work performed is recognised in the accounting period in which the services are rendered.

2 Summary of significant accounting policies (continued)

(e) Revenue recognition (continued)

(iv) Interest revenue from in-house customer finance program

Interest revenue is recognised on the in-house customer finance program when consideration is deferred. It is calculated as the difference between the nominal cash and cash equivalents received from customers and the discounted cashflows, on both interest and non-interest bearing products. Interest revenue is brought to account over the term of the finance agreement, and the rate used for non-interest bearing products is in line with current, comparable market rates.

(v) Interest income

Interest income is recognised using the effective interest method.

(f) Taxes

Current income tax

The income tax expense or credit for the year is the tax payable on the current year's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences and to unused tax losses.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting year in the countries where the Group operates and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Current tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred tax liabilities and assets are not recognised for temporary differences between the carrying amount and tax bases of investments in controlled entities where the Parent Entity is able to control the timing of the reversal of the temporary differences and it is probable that the differences will not reverse in the foreseeable future.

Deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Tax consolidation group

Michael Hill International Limited and its wholly-owned Australian controlled entities formed a tax consolidation group on 29 June 2016. As a consequence, one income tax return is completed for the Australian tax group and is treated for income tax purposes as one taxpayer.

2 Summary of significant accounting policies (continued)

(f) Taxes (continued)

Formerly, Michael Hill Jeweller (Australia) Pty Ltd and all wholly-owned Australian controlled entities formed the Australian tax consolidation group which completed one income tax return and was treated for income tax purposes as one taxpayer.

The tax balances have been attributed for reporting purposes to each of the entities on the basis of their individual results. Amounts of tax due to and receivable from the Australian Taxation Office are made by Michael Hill International Limited as nominated member of the Australian tax consolidated group. The current tax balance for the Australian tax group has been allocated between the members based on each entity’s current tax movement for the period. Where tax losses are incurred by Australian tax group members, these are offset within the group.

(g) Goods and Services Tax (GST)

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

- When the GST incurred on a sale or purchase of assets or services is not payable to or recoverable from the taxation authority, in which case the GST is recognised as part of the revenue or the expense item or as part of the cost of acquisition of the asset, as applicable; or
- When 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 statement of financial position. Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

Cash flows are included in the statement of cash flows on a gross basis and the GST components of cash flows arising from investing or financing activities which are recoverable from, or payable to, the taxation authority, are presented as operating cash flows.

(h) Leases

Leases of property, plant and equipment where the Group, as lessee, has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's inception at the fair value of the leased property or, if lower, the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included in other short-term and long-term payables. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to the consolidated statement of comprehensive income over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each year. The property, plant and equipment acquired under finance leases is depreciated over the asset's useful life or over the shorter of the asset's useful life and the lease term.

Leases in which a significant portion of the risks and rewards of ownership are not transferred to the Group as lessee are classified as operating leases (note 17). Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the year of the lease.

(i) Impairment of assets

At each annual reporting date (or more frequently if events or changes in circumstances indicate that they might be impaired), the Group assesses whether there is any indication that an asset may be impaired. Where such an indication is identified, the Group estimates the recoverable amount of the asset and recognises an impairment loss where the recoverable amount is less than the carrying amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value-in-use.

In addition, at least annually, goodwill and intangible assets with indefinite useful lives are tested for impairment by comparing their estimated recoverable amounts with their carrying amounts. Where the recoverable amount exceeds the carrying amount of an asset, an impairment loss is recognised.

The pre-tax discount rates used in determining the recoverable amount ranged between 10.5% and 11.5% (2017: 11.1% and 14.6%), depending on the geographical segment of the assets.

2 Summary of significant accounting policies (continued)

(j) Cash and cash equivalents

Cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the statement of financial position when utilised.

(k) Trade and other receivables

Trade receivables are amounts due from customers for goods sold or services rendered in the ordinary course of business. If collection is expected in one year or less (or in the normal operating cycle of the business if longer), they are classified as current assets. If not, they are presented as non-current assets.

Collectibility of trade receivables is reviewed on an ongoing basis. Trade receivables which are known to be uncollectible are written off. A provision for impaired receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. Cash flows relating to short-term receivables are not discounted if the effect of discounting is immaterial. The amount of the provision is recognised in the statement of comprehensive income.

(l) Deferred expenditure

Direct and incremental bonuses associated with the sale of PCPs are deferred and amortised in proportion to the PCP revenue recognised. Management reviews trends in current and estimated future services provided under the plan to assess whether changes are required to the cost recognition rates used.

(m) Inventories

Raw materials and finished goods are stated at the lower of cost and net realisable value. Cost comprises direct materials, direct labour and an appropriate proportion of variable and fixed overhead expenditure, the latter being allocated on the basis of normal operating capacity. Costs are assigned to individual items of inventory on the basis of weighted average costs. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

(n) 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 co-ordinated 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 in the statement of profit or loss.

(o) Investments and other financial assets

Classification

The Group classifies its financial assets in the following categories:

- financial assets at fair value through profit or loss,
- loans and receivables,
- held-to-maturity investments, and
- available-for-sale financial assets.

2 Summary of significant accounting policies (continued)

(o) Investments and other financial assets (continued)

Classification (continued)

The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition and, in the case of assets classified as held-to-maturity, re-evaluates this designation at the end of each reporting year. See note 7 for details about each type of financial asset.

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

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Derivatives are classified as held for trading unless they are designated as hedges. Assets in this category are classified as current assets if they are expected to be settled within 12 months; otherwise they are classified as non-current.

(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. They are included in current assets, except for those with maturities greater than 12 months after the reporting period which are classified as non-current assets. Loans and receivables are included in trade and other receivables in the statement of financial position (note 7(b)).

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. If the Group were to sell other than an insignificant amount of held-to-maturity financial assets, the whole category would be tainted and reclassified as available-for-sale. Held-to-maturity financial assets are included in non-current assets, except for those with maturities less than 12 months from the end of the reporting period, which are classified as current assets.

Available-for-sale financial assets

Available-for-sale financial assets, comprising principally marketable equity securities, are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless the investment matures or management intends to dispose of the investment within 12 months of the end of the reporting period. Investments are designated as available-for-sale if they do not have fixed maturities and fixed or determinable payments and management intends to hold them for the medium to long-term.

Impairment

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or a Group of financial assets is impaired. A financial asset or a Group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or Group of financial assets that can be reliably estimated. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered an indicator that the assets are impaired.

(p) Derivatives and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value at the end of each reporting year. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either:

- hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedges)
- hedges of a particular risk associated with the cash flows of recognised assets and liabilities and highly probable forecast transactions (cash flow hedges), or
- hedges of a net investment in a foreign operation (net investment hedges).

2 Summary of significant accounting policies (continued)

(p) Derivatives and hedging activities (continued)

The Group documents at the inception of the hedging transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions have been and will continue to be highly effective in offsetting changes in fair values or cash flows of hedged items.

The fair values of various derivative financial instruments used for hedging purposes are disclosed in note 7(e). Movements in the hedging reserve in shareholder's equity are shown in note 9(b). The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months; it is classified as a current asset or liability when the remaining maturity of the hedged item is less than 12 months. Trading derivatives are classified as a current asset or liability.

(a) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The gain or loss relating to the effective portion of interest rate swaps hedging fixed rate borrowings is recognised in profit or loss within finance costs, together with changes in the fair value of the hedged fixed rate borrowings attributable to interest rate risk. The gain or loss relating to the ineffective portion is recognised in profit or loss within other income or other expenses.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to profit or loss over the period to maturity using a recalculated effective interest rate.

(ii) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and accumulated in reserves in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss within other income or other expense.

Amounts accumulated in equity are reclassified to profit or loss in the years when the hedged item affects profit or loss (for instance when the forecast sale that is hedged takes place). The gain or loss relating to the effective portion of interest rate swaps hedging variable rate borrowings is recognised in profit or loss within 'finance costs'. The gain or loss relating to the effective portion of forward foreign exchange contracts hedging export sales is recognised in profit or loss within 'sales'. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory or fixed assets) the gains and losses previously deferred in equity are reclassified from equity and included in the initial measurement of the cost of the asset. The deferred amounts are ultimately recognised in profit or loss as cost of goods sold in the case of inventory, or as depreciation or impairment in the case of fixed assets.

When a hedging instrument expires or is sold or terminated, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately reclassified to profit or loss.

(iii) Net investment hedges

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges.

Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in other comprehensive income and accumulated in reserves in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss within other income or other expenses.

Gains and losses accumulated in equity are reclassified to profit or loss when the foreign operation is partially disposed of or sold.

2 Summary of significant accounting policies (continued)

(p) Derivatives and hedging activities (continued)

(iv) Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in profit or loss and are included in other income or other expenses.

(q) Property, plant and equipment

All property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to profit or loss during the reporting year in which they are incurred.

Depreciation on other assets is calculated using the straight line method to allocate their cost or revalued amounts, net of their residual values, over their estimated useful lives (see Note 8(b)).

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting year.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (note 2(i)).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in profit or loss. When revalued assets are sold, it is Group policy to transfer any amounts included in other reserves in respect of those assets to retained earnings.

(r) Intangible assets

Software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over their estimated useful lives (three to five years).

Costs associated with developing or maintaining software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Group are recognised as intangible assets when the following criteria are met:

- it is technically feasible to complete the software so that it will be available for use
- management intends to complete the software and use or sell it
- there is an ability to use or sell the software
- it can be demonstrated how the software will generate probable future economic benefits
- adequate technical, financial and other resources to complete the development and to use or sell the software are available, and
- the expenditure attributable to the software during its development can be reliably measured.

Directly attributable costs that are capitalised as part of the software include employee costs and an appropriate portion of relevant overheads.

Capitalised development costs are recorded as intangible assets and amortised from the point at which the asset is ready for use.

2 Summary of significant accounting policies (continued)

(r) Intangible assets (continued)

Software (continued)

Computer software development costs recognised as assets are amortised over their estimated useful lives (not exceeding ten years).

(s) Trade and other payables

These amounts represent liabilities for goods and services provided to the Group prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition. Trade and other payables are presented as current liabilities unless payment is not due within 12 months after the reporting year. They are recognised initially at their fair value and subsequently measured at amortised cost using the effective interest method.

Deferred revenue represents lease incentives for entering new lease agreements and revenue from PCPs. The accounting policy used to recognise the revenue is detailed in note 2(e)(ii).

(t) Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in profit or loss over the year of the borrowings using the effective interest method.

Borrowings are removed from the balance sheet when the obligation specified in the contract is discharged, cancelled or expired. The difference between the carrying amount of a financial liability that has been extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in profit or loss as other income or finance costs.

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

(u) Provisions

Provisions for are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Present obligations arising from onerous contracts are required to be recognised and measured as a provision. An onerous contract is considered to exist where the unavoidable cost of meeting the obligations under the contract exceed the economic benefits expected to be received from the contract. The Group has recognised a provision in relation to one contract at our Maryborough location in Australia that was identified as onerous during the reporting period.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the end of the reporting year. The discount rate used to determine the present value is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The increase in the provision due to the passage of time is recognised as interest expense.

(v) Employee benefits

(i) Short-term obligations

Liabilities for wages and salaries, including non-monetary benefits and accumulating sick leave that are expected to be settled wholly within 12 months after the end of the year in which the employees render the related service are recognised in respect of employees' services up to the end of the reporting year and are measured at the amounts expected to be paid when the liabilities are settled.

2 Summary of significant accounting policies (continued)

(v) Employee benefits (continued)

(i) Short-term obligations (continued)

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

(ii) Other long-term employee benefit obligations

The liabilities for long service leave and annual leave that are not expected to be settled wholly within 12 months after the end of the year in which the employees render the related service are measured as the present value of expected future payments to be made in respect of services provided by employees up to the end of the reporting year using the projected unit credit method. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service. Expected future payments are discounted using the Milliman G100 discount rates at the end of the reporting period. Remeasurements as a result of experience adjustments and changes in actuarial assumptions are recognised in profit or loss.

The obligations are presented as current liabilities in the statement of financial position if the entity does not have an unconditional right to defer settlement for at least twelve months after the reporting year, regardless of when the actual settlement is expected to occur.

(iii) Share-based payments

Employee options

Options are issued to Executives of Michael Hill International Limited in accordance with the Company's constitution. The Board of Directors pass a resolution approving the issue of the options. The fair value of options granted is recognised as an employee benefit expense with a corresponding increase in equity.

The fair value is measured at grant date and recognised over the period during which the employees become unconditionally entitled to the options. The fair value at grant date for options issued during 2018 were independently determined using a Binomial option pricing model, which is an iterative model for options that can be exercised at times prior to expiry. The model takes into account the grant date, exercise price, the vesting and performance criteria, the impact of dilution, the non-tradeable nature of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option. It also assumes the options will be exercised at the mid-point of the exercise period.

The fair value of options granted is recognised as an employee benefits expense with a corresponding increase in equity. The total amount to be expensed is determined by reference to the fair value of the options granted:

- including any market performance conditions (eg the entity's share price)
- excluding the impact of any service and non-market performance vesting conditions (eg profitability, sales growth targets and remaining an employee of the entity over a specified time year), and
- including the impact of any non-vesting conditions (eg the requirement for employees to save or holdings shares for a specific year of time).

The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each year, the entity revises its estimates of the number of options that are expected to vest based on the non-marketing vesting and service conditions. It recognises the impact of the revision to original estimates, if any, in profit or loss, with a corresponding adjustment to equity.

Upon the exercise of options, the balance of the share-based payments reserve relating to those options is transferred to share capital.

(iv) Profit-sharing and bonus plans

The Group recognises a liability and an expense for bonuses and profit-sharing based on a formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The Group recognises a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

2 Summary of significant accounting policies (continued)

(v) Employee benefits (continued)

(v) Retirement benefit obligations

All Australian and Canadian employees of the Group are entitled to benefits from the Group's superannuation plan on retirement, disability or death or can direct the group to make contributions to a defined contribution plan of their choice. The Group’s superannuation plan has a defined benefit section which receives fixed contributions from Group companies and the Group's legal or constructive obligation is limited to these contributions.

(w) 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.

Where any Group company purchases the Company's equity instruments, for example as the result of a share buy-back or a share-based payment plan, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the owners of Michael Hill International Limited as treasury shares until the shares are cancelled or reissued. Where such ordinary shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the owners of Michael Hill International Limited.

(x) Dividends

Provision is made for the amount of any dividend declared, being appropriately authorised and no longer at the discretion of the entity, on or before the end of the reporting year but not distributed at the end of the reporting year.

(y) Earnings per share

(i) Basic earnings per share

Basic earnings per share is calculated by dividing:

- the profit attributable to owners of the Company, excluding any costs of servicing equity other than ordinary shares
- by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year and excluding treasury shares.

(ii) Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account:

- the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares, and
- the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

(z) Rounding of amounts

The Company is of a kind referred to in ASIC Legislative Instrument 2016/191, relating to the 'rounding off' of amounts in the financial statements. Amounts in the financial statements have been rounded off in accordance with the instrument to the nearest thousand dollars, or in certain cases, the nearest dollar.

2 Summary of significant accounting policies (continued)

(aa) New accounting standards and interpretations

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2018 reporting periods and have not been early adopted by the group. The Group's assessment of the financial impact of these new standards and interpretations is set out below.

(i) AASB 9 Financial Instruments: Classification and measurement

AASB 9 *Financial Instruments* addresses the classification, measurement and derecognition of financial assets and financial liabilities. The standard is applicable to financial years commencing on or after 1 January 2018, and the Group will be adopting the new standard from 1 July 2018. The impairment model under the new Standard is based on expected credit losses rather than incurred losses under AASB 139. The expected credit loss model results in early recognition of impairment allowances and likely larger amount of the allowances. The level of allowances will also be more volatile in the future, as forecasts change. Adopting the expected credit loss model requires changes in current systems and processes and the use of judgement. Preliminary assessments indicate that the impact of the standard is not expected to be significant on the consolidated financial position, cash flow and results of operations. This standard will require additional assessment and disclosure of financial assets and liabilities held by the Group. The Group will continue to apply the provisions of AASB 139 in relation to open hedges until they are settled.

(ii) AASB 15 Revenue from Contracts with Customers

AASB 15 *Revenue* deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. AASB 15 supersedes:

(a) AASB 111 Construction Contracts;
(b) AASB 118 Revenue;
(c) Interpretation 13 Customer Loyalty Programmes;
(d) Interpretation 15 Agreements for the Construction of Real Estate;
(e) Interpretation 18 Transfers of Assets from Customers;
(f) Interpretation 131 Revenue - Barter Transactions Involving Advertising Services; and
(g) Interpretation 1042 Subscriber acquisition costs in the Telecommunications Industry.

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 the entity expects to be entitled in exchange for those goods or services. This is largely in line with the current accounting policies adopted for recognition of revenue, as described in note 2(e).

The standard is applicable for financial years commencing on or after 1 January 2018, and the Group will be adopting the new standard from 1 July 2018. Substantial work has been completed reviewing the Group's different revenue streams. The revenue from the sale of goods will be recognised at a point in time while the revenue from sale of PCP will be recognised over time consistent with the current accounting treatment. The impact of the new revenue standard is not expected to be significant. The new standard will require certain disclosure related changes to the 2019 financial statements.

(iii) AASB 16 Leases

AASB 16 *Leases* addresses the recognition and measurement of assets and liabilities for all leases with a term of more than 12 months, unless they are of low value. It also contains the disclosure requirements for lessees and lessors. AASB 16 supersedes:

(a) AASB 117 Leases;
(b) Interpretation 4 Determining whether an Arrangement contains a Lease;
(c) SIC-15 Operating Leases - Incentives; and
(d) SEC - 27 Evaluating the Substance of Transactions involving the Legal Form of a Lease.

2 Summary of significant accounting policies (continued)

(aa) New accounting standards and interpretations (continued)

(iii) AASB 16 Leases (continued)

The standard is not applicable until financial years commencing on or after 1 January 2019 but is available for early adoption provided the new revenue standard, AASB 15 Revenue from Contracts with Customers, has been applied or is applied at the same date as AASB 16. The Group has not yet determined the timing of adopting AASB 16 Leases.

The Group will use a modified retrospective adoption approach and expect to elect the package of practical expedients, including the use of hindsight to determine the lease term. As the Group continues to evaluate this standard and the effect on related disclosures, the primary effect of adoption will be to record right-of-use assets and corresponding lease obligations for current operating leases. The adoption is expected to have a material impact on the Group's consolidated balance sheet, consolidated cash flow statement and statement of comprehensive income.

Management is currently evaluating the anticipated impact on the Group’s consolidated financial position and results of operations, the quantitative and qualitative factors that will impact the Group as part of the adoption of this standard, as well as any changes to its leasing strategy that may occur because of the changes to the accounting and recognition of leases.

The ultimate impact of adopting the new standard will depend on the Group's lease portfolio as of the adoption date and the final discount rates used.

Additional Information

This section provides additional information about those individual line items in the financial statements that the Directors consider most relevant in the context of the operations of the entity, including:

(a) accounting policies that are relevant for an understanding of the items recognised in the financial statements.
(b) analysis and sub-totals, including segment information
(c) information about estimates and judgements made in relation to particular items.

3 Segment information

(a) Description of segments and principal activities

Management have determined the operating segments based on the reports reviewed by the Board and Executive team that are used to make strategic decisions. The Board and executive team consider, organise and manage the business primarily from a brand perspective. For the Michael Hill brand, they also consider, organise and manage the business from a geographic perspective, being the country of origin where the sale and service was performed.

During the year, the Company announced the closure of the Emma & Roe brand and the Michael Hill United States segment. These segments have been substantially closed and consequently these segments have been classified as a discontinued operation and are therefore not presented in the segment disclosures for 2018 and 2017.

The amounts provided to the Board and executive team in respect of total assets and liabilities are measured in a manner consistent with the financial statements. These reports do not allocate total assets or total liabilities based on the operations of each segment or by geographical location.

The Group's continuing operations operate in three geographical segments: Australia, New Zealand and Canada.

The corporate and other segment includes revenue and expenses that do not relate directly to the relevant Michael Hill retail segments. These predominately relate to corporate costs and Australian based support costs, but also include manufacturing activities, warehouse and distribution, interest and company tax. Inter-segment pricing is at arm's length or market value.

Types of products and services

Michael Hill International Limited and its controlled entities operate predominately in the sale of jewellery and related services. As indicated above, the Group is organised and managed globally by brand and geographic areas.

Major customers

Michael Hill International Limited and its controlled entities sell goods and provide services to a number of customers from which revenue is derived. There is no single customer from which the Group derives more than 10% of total consolidated revenue.

Accounting policies and inter-segment transactions

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.

3 Segment information (continued)

(b) Segment results

Segment information 2018	**MH Australia $'000**	**MH New Zealand $'000**	**MH Canada** $'000	**Corporate & other $'000**	**Group $'000**
Operating revenue	325,709	115,376	133,000	1,464	575,549
Gross profit	206,303	71,560	82,967	6,063	366,893
Gross profit %	63.3%	62.0%	62.0%	-%	63.7%
EBITDA*	56,935	28,063	19,986	(36,143)	68,841
Depreciation and amortisation	(8,314)	(2,464)	(5,077)	(2,839)	(18,694)
EBIT*	**48,621**	**25,599**	**14,909**	**(38,982)**	**50,147**
EBIT as a % of revenue	14.9%	22.2%	11.0%	-%	8.7%
Interest income	2	1	-	7	10
Finance costs	59	10	-	(2,759)	(2,690)
Net profit before tax	**48,682**	**25,609**	**14,909**	**(41,733)**	**47,467**
Income tax expense	-	-	-	-	(12,649)
Net profit after tax	**48,682**	**25,609**	**14,909**	**(41,733)**	**34,818**

Segment information 2017	**MH Australia $'000**	**MH New Zealand $'000**	**MH Canada** $'000	**Corporate & other $'000**	**Group $'000**
Operating revenue	321,981	115,518	112,930	670	551,099
Gross profit	201,707	71,237	69,210	8,853	351,007
Gross profit %	62.6%	61.7%	61.0%	-%	63.7%
EBITDA*	59,454	29,048	16,643	(25,386)	79,759
Depreciation and amortisation	(7,766)	(2,651)	(4,195)	(2,815)	(17,427)
EBIT*	**51,688**	**26,397**	**12,448**	**(28,201)**	**62,332**
EBIT as a % of revenue	16.1%	22.9%	11.0%	-%	11.3%
Interest income	-	1	-	15	16
Finance costs	(17)	(41)	-	(3,106)	(3,164)
Net profit before tax	**51,671**	**26,356**	**12,448**	**(31,292)**	**59,183**
Income tax expense	-	-	-	-	(15,051)
Net profit after tax	**51,671**	**26,356**	**12,448**	**(31,292)**	**44,132**

* EBIT and EBITDA are Non-IFRS Information and are unaudited. Please refer to Non-IFRS Information on page 10 of the Directors Report for an explanation of Non-IFRS information and a reconciliation of EBIT from continuing operations and Normalised EBIT.

4 Revenue

	2018 $'000	2017 $'000
From continuing operations:		
Sales revenue		
Revenue from sale of goods and repair services	**541,349**	517,222
Revenue from professional care plans	**31,929**	32,131
Interest and other revenue from in-house customer finance program	**2,261**	1,730
	575,539	551,083
Other revenue		
Interest income	**10**	16
Total revenue from continuing operations	**575,549**	551,099

5 Other income and expense items

(a) Other income

	Notes	**2018 $'000**	2017 $'000
Insurance recoveries		**-**	2
Net foreign exchange gains	11(b)	**-**	863
Other items		**1,064**	775
		1,064	1,640

(b) Breakdown of expenses by nature

		2018 $'000	2017 $'000
Depreciation			
Plant and equipment		**4,153**	3,386
Furniture and fittings		**3,619**	69
Motor vehicles		**145**	166
Leasehold improvements		**6,668**	9,677
Display materials		**1,681**	1,724
Total depreciation	8(b)	**16,266**	15,022
Amortisation			
Software		**2,428**	2,405
Total depreciation and amortisation		**18,694**	17,427

5 Other income and expense items (continued)

(b) Breakdown of expenses by nature (continued)

		2018 $'000	2017 $'000
Finance costs			
Bank and interest charges		**2,762**	3,105
Interest expense - make good provision	8(h)	**(72)**	59
Total finance costs		**2,690**	3,164
Net foreign exchange losses included in other expenses		**1,029**	-

6 Income tax expense

(a) Income tax expense

	Notes	2018 $'000	2017 $'000
Current tax			
Current tax on profits for the year		**5,723**	6,402
Derecognised tax losses		**3,651**	461
Adjustments for current tax of prior periods		**3,908**	947
Foreign income tax offsets not recognised		**(1,055)**	1,055
Total current tax expense		**12,227**	8,865
Deferred income tax			
(Increase) / Decrease in deferred tax assets	8(d)	**(2,659)**	8,125
Tax consolidation cost base adjustments		**-**	(4,389)
Derecognised tax losses		**66**	-
Adjustments for deferred tax of prior periods		**(3,708)**	(291)
Total deferred tax expense/(benefit)		**(6,301)**	3,445
Income tax expense		**5,926**	12,310

(b) Numerical reconciliation of income tax expense to prima facie tax payable

	Notes	2018 $'000	2017 $'000
Profit from continuing operations before income tax expense		**47,467**	59,183
Profit from discontinuing operations before income tax expense		**(36,934)**	(14,226)
		10,533	44,957
Tax at the Australian tax rate of 30.0% (2017 - 30.0%)		**3,160**	13,487
Tax effect of amounts which are not deductible (taxable) in calculating taxable income:			
Non deductible expenditure		**163**	178
Non-assessable intragroup markups		**(551)**	(653)
Sundry items		**10**	89
Tax consolidation cost base adjustments		**-**	(4,389)
		2,782	8,712

6 Income tax expense (continued)

(b) Numerical reconciliation of income tax expense to prima facie tax payable (continued)

	Notes	2018 $'000	2017 $'000
Difference in overseas tax rates		**288**	(321)
Adjustments for current tax of prior periods		**3,908**	947
Adjustments for deferred tax of prior periods		**(3,644)**	(291)
Tax losses not recognised		**3,651**	2,208
Foreign income tax offset not recognised		**(1,055)**	1,055
Change in tax rate on deferred tax balance		**(4)**	-
Income tax expense		**5,926**	12,310
Income tax expense is attributable to:			
Profit from continuing operations		**12,649**	15,051
Profit from discontinuing operations		**(6,723)**	(2,741)
		5,926	12,310

(c) Tax losses

	2018 $'000	2017 $'000
Unused United States tax losses for which no deferred tax asset has been recognised	**32,203**	19,524
Potential tax benefit @ 25.0% (2017 @ 40.0%)	**8,051**	7,810
Unused New Zealand tax losses for which no deferred tax asset has been recognised	**2,623**	1,645
Potential tax benefit @ 28.0%	**735**	461

The unused tax losses incurred in the United States and New Zealand are available indefinitely for offsetting against future taxable profits of the countries in which the losses arose. Deferred tax assets have not been recognised in respect of these losses as it is unknown when the New Zealand losses may be used to offset taxable profits and the United States losses are not expected to be used.

7 Financial assets and financial liabilities

	Notes	Derivatives used for hedging $'000	Financial assets at amortised cost $'000	Total $'000
Financial assets				
2018				
Cash and cash equivalents	7(a)	**-**	**7,220**	**7,220**
Trade and other receivables	7(b)	**-**	**28,046**	**28,046**
Derivative financial instruments	11(a)	**245**	**-**	**245**
		245	**35,266**	**35,511**

7 Financial assets and financial liabilities (continued)

		Derivatives used for hedging $'000	Financial assets at amortised cost $'000	Total $'000
2017				
Cash and cash equivalents	7(a)	-	5,676	5,676
Trade and other receivables	7(b)	-	26,590	26,590
		-	32,266	32,266

	Notes			
Financial liabilities				
2018				
Trade and other payables	7(c)	**-**	**49,339**	**49,339**
Borrowings	7(d)	**-**	**35,213**	**35,213**
Derivative financial instruments	11(a)	**390**	**-**	**390**
		390	**84,552**	**84,942**
2017				
Trade and other payables	7(c)	-	47,918	47,918
Borrowings	7(d)	-	45,034	45,034
Derivative financial instruments	11(a)	1,141	-	1,141
		1,141	92,952	94,093

The Group’s exposure to various risks associated with the financial instruments is discussed in note 11. The maximum exposure to credit risk at the end of the reporting year is the carrying amount of each class of financial assets mentioned above.

(a) Cash and cash equivalents

	2018 $'000	2017 $'000
Current assets		
Cash at bank and on hand	**7,220**	5,676

Interest rates for the bank accounts have been between 0.00% and 1.15% during the year (2017: between 0.00% and 1.15%).

(b) Trade and other receivables

		2018			2017		
	Notes	**Current $'000**	**Non-current $'000**	**Total $'000**	Current $'000	Non-current $'000	Total $'000
Trade receivables		**4,912**	**-**	**4,912**	4,752	-	4,752
Provision for impairment of receivables		**(819)**	**-**	**(819)**	(502)	-	(502)
	11(c)(i)	**4,093**	**-**	**4,093**	4,250	-	4,250

7 Financial assets and financial liabilities (continued)

(b) Trade and other receivables (continued)

	Notes	**2018** Current $'000	**2018** Non-current $'000	**2018** Total $'000	2017 Current $'000	2017 Non-current $'000	2017 Total $'000
In-house customer finance		**17,681**	**2,864**	**20,545**	15,157	2,533	17,690
Provision for impairment of receivables		**(1,231)**	**(199)**	**(1,430)**	(956)	(162)	(1,118)
	11(c)(ii)	**16,450**	**2,665**	**19,115**	14,201	2,371	16,572
Sundry debtors		**4,838**	**-**	**4,838**	5,768	-	5,768
		25,381	**2,665**	**28,046**	24,219	2,371	26,590

Further information relating to loans to related parties and key management personnel is set out in note 19.

(i) Trade receivables

Trade receivables from sales made to customers through third party credit providers are non-interest bearing and are generally on a 0-30 day terms.

(ii) In-house customer finance

In October 2012, Michael Hill launched an in-house customer finance program in the Canadian and United States markets. The terms available to customers range from an interest bearing revolving line of credit through to interest free terms of between 6 and 24 months, although 12 to 18 months is the typical financing period.

The receivables from the in-house customer finance program are comprised of a large number of transactions with no one customer representing a significant balance. The finance portfolio consists of contracts of similar characteristics that are evaluated collectively for impairment. The allowance is an estimate of the losses as of the balance date, and is calculated using such factors as delinquency and recovery rates.

Sundry debtors

Sundry debtors relates to supplier credits, security deposits and other sundry receivables.

Effective interest rates

Other than in-house customer finance, all receivables are non-interest bearing. The majority of in-house customer finance receivables are also non-interest bearing.

(iii) Impairment and risk exposure

Information about the impairment of trade and other receivables, their credit quality and the Group's exposure to credit risk, foreign currency risk and interest rate risk can be found in note 11(b) and 11(c).

Only trade receivables and in-house customer finance contain impaired assets. The remaining classes within trade and other receivables do not contain impaired assets and are not past due. Based on the credit history of these other classes, it is expected that these amounts will be received when due.

7 Financial assets and financial liabilities (continued)

(c) Trade and other payables

	2018 $'000	2017 $'000
Current liabilities		
Trade payables	**24,686**	27,649
Annual leave liability	**8,938**	8,571
Accrued expenses	**7,154**	6,442
Other payables	**8,561**	5,256
	49,339	47,918

Trade payables are unsecured and are usually paid within 30 days of recognition.

The carrying amounts of trade and other payables are considered to be the same as their fair values, due to their short-term nature.

(d) Borrowings

		2018			2017		
	Notes	**Current $'000**	**Non-current $'000**	**Total $'000**	Current $'000	Non-current $'000	Total $'000
Bank loans		**-**	**35,213**	**35,213**	-	45,034	45,034
Total secured borrowings		**-**	**35,213**	**35,213**	-	45,034	45,034

The Group’s objectives when managing capital are to ensure sufficient liquidity to support its financial obligations and execute the Group's operational and strategic plans. The Group continually assesses its capital structure and makes adjustments to it with reference to changes in economic conditions and risk characteristics associated with its underlying assets. Accordingly, the Group entered into a three year agreement with ANZ on 26 June 2018 that provides for a $110,000,000 multi option borrowing facility, the availability of which is adjusted throughout the year in line with business requirements. At balance date, $70,000,000 was available, and of that, $35,213,000 was utilised.

The Group also has access to various uncommitted credit facility lines serving working capital needs that, at balance date, totalled $1,924,000. No amounts were drawn under these credit facility lines as at balance date.

(e) Recognised fair value measurements

(i) Fair value hierarchy

This section explains the judgements and estimates made in determining the fair values of the financial instruments that are recognised and measured at fair value in the financial statements. To provide an indication about the reliability of the inputs used in determining fair value, the Group has classified its financial instruments into the three levels prescribed under the accounting standards. An explanation of each level follows underneath the table.

7 Financial assets and financial liabilities (continued)

(e) Recognised fair value measurements (continued)

(i) Fair value hierarchy (continued)

Recurring fair value measurements **At 30 June 2018**	**Notes**	**Level 1 $'000**	**Level 2 $'000**	**Level 3 $'000**	**Total $'000**
Financial assets					
Derivatives used for hedging					
Foreign exchange contracts	11(a)	**-**	**245**	**-**	**245**
Total financial assets		**-**	**245**	**-**	**245**
Financial Liabilities					
Derivatives used for hedging					
Interest rate swaps	11(a)	**-**	**390**	**-**	**390**
Total financial liabilities		**-**	**390**	**-**	**390**

Recurring fair value measurements At 30 June 2017	**Notes**	**Level 1 $'000**	**Level 2 $'000**	**Level 3 $'000**	**Total $'000**
Financial assets					
Total financial assets		-	-	-	-
Financial Liabilities					
Derivatives used for hedging					
Foreign exchange contracts	11(a)	-	414	-	414
Interest rate swaps	11(a)	-	727	-	727
Total financial liabilities		-	1,141	-	1,141

There were no transfers between levels during the year.

The Group's policy is to recognise transfers into and transfers out of fair value hierarchy levels as at the end of the reporting period

Level 1: The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the Group is the current bid price. These instruments are included in level 1.

Level 2: The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined using valuation techniques which maximise the use of observable market data and rely as little as possible on entity-specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2.

Level 3: If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3. This is the case for unlisted equity securities.

7 Financial assets and financial liabilities (continued)

(f) Changes in liabilities arising from financing activities

(i) Movements

	Non-current interest-bearing loans and liabilities $'000	**Total $'000**
Carrying amount at start of year	45,034	45,034
Inwards cash flows	116,500	116,500
Outwards cash flows	(126,500)	(126,500)
Foreign exchange movements	179	179
Carrying amount at end of year	35,213	35,213

8 Non-financial assets and liabilities

This note provides information about the Group's non-financial assets and liabilities, including:

(a) Inventories

	2018 $'000	2017 $'000
Raw materials	**10,243**	7,870
Finished goods	**178,944**	191,768
Packaging and other consumables	**2,887**	4,215
	192,074	203,853

All inventories are held at the lower of cost or net realisable value.

(b) Property, plant and equipment

	Plant and equipment $'000	**Fixtures and fittings $'000**	**Motor vehicles $'000**	**Leasehold improvements $'000**	**Display materials $'000**	**Total $'000**
At 1 July 2016						
Cost or fair value	33,203	30,206	930	72,926	12,767	150,032
Accumulated depreciation	(20,331)	(15,443)	(396)	(36,933)	(4,996)	(78,099)
Net book amount	12,872	14,763	534	35,993	7,771	71,933
Year ended 30 June 2017						
Opening net book amount	12,872	14,763	534	35,993	7,771	71,933
Exchange differences	(124)	(119)	(6)	(525)	(93)	(867)
Additions	6,868	5,034	153	13,193	2,046	27,294
Additions - make good	-	-	-	773	-	773
Disposals	(427)	(118)	(55)	(791)	(64)	(1,455)
Depreciation charge	(4,229)	(3,956)	(194)	(7,089)	(1,947)	(17,415)
Impairment loss (iii)	(26)	(5)	-	(796)	-	(827)
Closing net book amount	14,934	15,599	432	40,758	7,713	79,436

8 Non-financial assets and liabilities (continued)

(b) Property, plant and equipment (continued)

	Plant and equipment $'000	Fixtures and fittings $'000	Motor vehicles $'000	Leasehold improvements $'000	Display materials $'000	Total $'000
At 30 June 2017						
Cost or fair value	37,944	34,169	796	82,602	13,816	169,327
Accumulated depreciation	(23,010)	(18,570)	(364)	(41,844)	(6,103)	(89,891)
Net book amount	14,934	15,599	432	40,758	7,713	79,436
Year ended 30 June 2018						
Opening net book amount	14,934	15,599	432	40,758	7,713	79,436
Exchange differences	(70)	(27)	(4)	84	17	-
Additions	4,339	3,146	45	8,196	2,164	17,890
Additions - make good	-	-	-	(1,154)	-	(1,154)
Disposals	(391)	(216)	(72)	(392)	(71)	(1,142)
Depreciation charge	(4,429)	(3,925)	(148)	(7,257)	(1,806)	(17,565)
Impairment loss (iii)	(1,490)	(3,010)	-	(5,016)	(1,283)	(10,799)
Closing net book amount	12,893	11,567	253	35,219	6,734	66,666
At 30 June 2018						
Cost	38,744	34,667	569	81,642	13,958	169,580
Accumulated depreciation and impairment	(25,851)	(23,100)	(316)	(46,423)	(7,224)	(102,914)
Net book amount	12,893	11,567	253	35,219	6,734	66,666

(i) Impairment loss

As per the Group's accounting policies, the Group impairs assets where the recoverable amount is less than the carrying amount. The Group has impaired the assets of all Emma & Roe assets, four Michael Hill Australia stores and two Michael Hill Canada stores. Any assets held at an impaired Emma & Roe store that are able to redeployed throughout the Group are not impaired. This cost has reported in Other expenses in the statement of comprehensive income. The segment breakdown of impairment losses recognised during the year is reported at note 3.

(ii) Revaluation, depreciation methods and useful lives

Depreciation is calculated using the straight-line method to allocate their cost or revalued amounts, net of their residual values, over their estimated useful lives or, in the case of leasehold improvements and certain leased plant and equipment, the shorter lease term as follows:

- Plant and equipment 5 - 6 years
- Motor vehicles 3 - 5 years
- Fixtures and fittings 6 - 10 years
- Leasehold improvements 6 - 10 years
- Display material 6 - 10 years

8 Non-financial assets and liabilities (continued)

(c) Intangible assets

	Patents, trademarks and other rights $'000	Computer software $'000	Total $'000
At 1 July 2016			
Cost	79	16,675	16,754
Accumulation amortisation	-	(11,193)	(11,193)
Net book amount	79	5,482	5,561
Year ended 30 June 2017			
Opening net book amount	79	5,482	5,561
Exchange differences	-	(27)	(27)
Additions	-	5,851	5,851
Amortisation charge *	-	(2,601)	(2,601)
Closing net book amount	79	8,705	8,784
At 30 June 2017			
Cost	79	22,472	22,551
Accumulation amortisation	-	(13,767)	(13,767)
Net book amount	79	8,705	8,784
Year ended 30 June 2018			
Opening net book amount	79	8,705	8,784
Exchange differences	-	2	2
Additions	-	6,665	6,665
Impairment charge	-	(228)	(228)
Amortisation charge *	-	(2,597)	(2,597)
Closing net book amount	79	12,547	12,626
At 30 June 2018			
Cost	79	28,941	29,020
Accumulated amortisation	-	(16,394)	(16,394)
Net book amount	79	12,547	12,626

* Amortisation of $2,428,000 (2017: $2,405,000) is included in depreciation and amortisation expense in the statement of comprehensive income. The amount above also includes amortisation for discontinued operations (see note Discontinued operations).

8 Non-financial assets and liabilities (continued)

(d) Deferred tax balances

(i) Deferred tax assets

	2018 $'000	2017 $'000
The balance comprises temporary differences attributable to:		
Doubtful debts	**555**	397
Fixed assets and intangibles	**10,508**	14,855
Intangible assets from intellectual property transfer	**26,438**	28,101
Deferred expenditure	**(697)**	(764)
Prepayments	**(6)**	(55)
Deferred service revenue	**3,850**	4,322
Unearned income	**1,653**	1,201
Provisions	**8,628**	7,309
Unrealised foreign exchange losses	**117**	(15)
Sundry items	**1,481**	200
Inventories	**9,368**	-
Tax losses recognised	**-**	2,342
Net deferred tax assets	**61,895**	57,893
Expected settlement:		
Deferred tax assets expected to be recovered within 12 months	**23,758**	11,846
Deferred tax assets expected to be recovered after more than 12 months	**38,137**	46,047
	61,895	57,893
Movements:		
Opening balance at 1 July	**57,893**	64,074
Credited / (charged) to the income statement	**2,660**	(8,125)
Tax losses recognised	**(2,342)**	2,342
Prior year adjustment	**3,707**	(291)
Foreign exchange differences	**(23)**	(107)
Closing balance at 30 June	**61,895**	57,893

(e) Current tax receivables

	2018 $'000	2017 $'000
Current assets		
Current tax receivables	**-**	888

8 Non-financial assets and liabilities (continued)

(f) Other assets

	2018			2017		
	Current $'000	**Non - current $'000**	**Total $'000**	Current $'000	Non - current $'000	Total $'000
Prepayments	**2,889**	**1,193**	**4,082**	3,089	178	3,267
Deferred expenditure	**799**	**1,695**	**2,494**	856	1,879	2,735
	3,688	**2,888**	**6,576**	3,945	2,057	6,002

(g) Current tax liabilities

	2018 $'000	2017 $'000
Current tax liabilities	**2,696**	-

(h) Provisions

	2018			2017		
	Current $'000	**Non- current $'000**	**Total $'000**	Current $'000	Non- current $'000	Total $'000
Employee benefits (i)	**3,555**	**2,063**	**5,618**	1,894	1,931	3,825
Returns provision (i)	**2,972**	**-**	**2,972**	2,518	-	2,518
Make good provision (i)	**356**	**2,844**	**3,200**	223	4,246	4,469
Restructuring costs (i)	**1,897**	**-**	**1,897**	-	-	-
Diamond warranty (i)	**600**	**-**	**600**	-	-	-
Other provisions (i)	**6**	**-**	**6**	35	58	93
	9,386	**4,907**	**14,293**	4,670	6,235	10,905

(i) Information about individual provisions and significant estimates

Employee benefits

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

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

Returns provision

Provision is made for the estimated sale returns for the Group's return policies, being 30 day change of mind, 12 month guarantee on the quality of workmanship and the 3 year watch guarantee. In addition, all Michael Hill watches sold before 30 June 2018 included a lifetime battery replacement guarantee. Management estimates the provision based on historical sale return information and any recent trends that may suggest future claims could differ from historical amounts.

8 Non-financial assets and liabilities (continued)

(h) Provisions (continued)

(i) Information about individual provisions and significant estimates (continued)

Employee benefits - long service leave (continued)

Make good provision

The Group has an obligation to restore certain leasehold sites to their original condition upon store closure or relocation. This provision represents the present value of the expected future make good commitment. Amounts charged to the provision represent both the cost of make good costs incurred and the costs incurred which mitigate the final liability prior to the closure or relocation.

Restructuring

A provision has been raised for the estimated lease surrender and staffing exit costs associated with the six Emma & Roe stores trading at the end of the year.

Diamond warranty

Provision is made for the estimated costs for the Group's diamond warranty offered with the purchase of selected diamond jewellery lines. Management estimates the provision based on costs incurred in recent years and will review the adequacy of the provision each reporting date as more data becomes available.

Other provisions

Other provisions relate to a provision for an onerous lease.

(ii) Movements in provisions

Movements in each class of provision during the financial year are set out below:

	Employee benefits $'000	**Restructuring obligations $'000**	**Returns provision $'000**	**Make good provision $'000**	**Diamond warranty $'000**	**Other provisions $'000**	**Total $'000**
Carrying amount at the start of the year	3,825	-	2,518	4,469	-	93	10,905
Additional provisions recognised	2,142	1,897	2,971	(857)	600	6	6,759
Amounts incurred and charged	(346)	-	(2,517)	(378)	-	(93)	(3,334)
Exchange differences	(3)	-	-	(34)	-	-	(37)
Carrying amount at end of year	5,618	1,897	2,972	3,200	600	6	14,293

(i) Deferred revenue

	2018			2017		
	Current $'000	**Non-current $'000**	**Total $'000**	Current $'000	Non-current $'000	Total $'000
Deferred service revenue	**24,686**	**55,276**	**79,962**	24,121	52,989	77,110
Lease incentive income	**782**	**2,230**	**3,012**	1,211	2,827	4,038
Deferred interest free revenue	**1,008**	**214**	**1,222**	592	201	793
	26,476	**57,720**	**84,196**	25,924	56,017	81,941

9 Contributed equity

(a) Share capital

	2018 Shares	2017 Shares	**2018 $'000**	2017 $'000
Ordinary shares - fully paid	**387,438,513**	387,438,513	**10,266**	10,015
Total share capital	**387,438,513**	**387,438,513**	**10,266**	**10,015**

(i) Movements in ordinary shares:

Details	**Notes**	**Number of shares**	**Total $'000**
Opening balance 1 July 2016		383,138,513	3,767
Exercise of options - proceeds received	9(a)(iii)	4,300,000	4,825
Transfer option reserve to contributed equity		-	1,423
Balance 30 June 2017		387,438,513	10,015
Options expired	9(a)(ii)	-	251
Balance 30 June 2018		387,438,513	10,266

(ii) Ordinary shares

Ordinary shares entitle the holder to participate in dividends, and to share in the proceeds of winding up the Company in proportion to the number of and amounts paid on the shares held.

On a show of hands every holder of ordinary shares present at a meeting in person or by proxy, is entitled to one vote, and upon a poll each share is entitled to one vote.

(iii) Options

Information relating to the Michael Hill International Employee Option Plan, including details of options issued, exercised and lapsed during the financial year and options outstanding at the end of the financial year, is set out in note 20(a).

(b) Reserves and retained profits

(i) Nature and purpose of other reserves

Cash flow hedges

The hedging reserve is used to record gains or losses on derivatives that are designated and qualify as cash flow hedges and that are recognised in other comprehensive income, as described in note 2(p). Amounts are reclassified to profit or loss when the associated hedged transaction affects profit or loss.

Share-based payments

The share-based payments reserve is used to recognise:

- the grant date fair value of options issued to employees but not exercised
- the grant date fair value of shares issued to employees
- the grant date fair value of deferred shares granted to employees but not yet vested

Foreign currency translation

Exchange differences arising on translation of the foreign controlled entity are recognised in other comprehensive income as described in note 2(d) and accumulated in a separate reserve within equity. The cumulative amount is reclassified to profit or loss when the net investment is disposed of.

10 Cash flow information

(a) Reconciliation of profit after income tax to net cash inflow from operating activities

	Notes	**2018 $'000**	2017 $'000
Profit for the year		**4,610**	32,647
Adjustment for			
Depreciation	5(b)	**17,565**	17,415
Amortisation	5(b)	**2,597**	2,601
Impairment - property, plant and equipment		**11,029**	-
Impairment - other assets		**563**	-
Non-cash employee benefits expense - share-based payments		**484**	371
Other non-cash expenses		**(78)**	897
Net loss on sale of non-current assets		**450**	1,166
Net exchange differences		**966**	(908)
Change in operating assets and liabilities:			
(Increase) / decrease in trade and other receivables		**(1,348)**	(579)
(Increase) / decrease in inventories		**12,169**	(6,073)
(Increase) / decrease in deferred tax assets		**(3,968)**	6,043
(Increase) / decrease in other current assets		**273**	1,085
(Increase) / decrease in other non current assets		**(826)**	118
(Decrease) / increase in trade and other payables		**2,258**	3,050
(Decrease) / increase in current tax liabilities		**3,665**	(26,110)
(Decrease) / increase in provisions		**2,030**	830
(Decrease) / increase in deferred revenue		**2,454**	7,199
Net cash inflow from operating activities		**54,893**	39,752

Risk

This section of the notes discusses the Group's exposure to various risks and shows how these could affect the Group's financial position and performance.

11 Financial risk management

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, interest rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Group. The Group uses derivative financial instruments such as foreign exchange contracts and interest rate swaps to hedge certain risk exposures. Derivatives are exclusively used for hedging purposes, i.e. not as trading or other speculative instruments. The Group uses different methods to measure different types of risk to which it is exposed. These methods include sensitivity analysis in the case of interest rate and foreign exchange risks and aging analysis for credit risk.

Risk	Exposure arising from	Measurement	Management
Market risk - foreign exchange	Future commercial transactions Recognised financial assets and liabilities not denominated in AUD	Cash flow forecasting Sensitivity analysis	Forward foreign exchange contracts
Market risk – interest rate	Long-term borrowings at variable rates	Sensitivity analysis	Interest rate swaps
Credit risk	Cash and cash equivalents and trade receivables	Aging analysis	Diversification of bank deposits, credit limits and letters of credit
Liquidity risk	Borrowings and other liabilities	Rolling cash flow forecasts	Availability of committed credit lines and borrowing facilities

The Group's overall risk management program includes a focus on financial risk including the unpredictability of financial markets and foreign exchange risk.

The policies are implemented by the central finance function that undertakes regular reviews to enable prompt identification of financial risks so that appropriate actions may be taken.

(a) Derivatives

Derivatives are only used for economic hedging purposes and not as speculative investments. However, where derivatives do not meet the hedging criteria, they are classified as 'held for trading' for accounting purposes. The Group has the following derivative financial instruments:

	2018 $'000	2017 $'000
Current assets		
Forward foreign exchange contracts - cash flow hedges ((b)(i))	**245**	-
Total current derivative financial instrument assets	**245**	-
Current liabilities		
Interest rate swap contracts - cash flow hedges ((b)(ii))	**390**	727
Forward foreign exchange contracts - cash flow hedges ((b)(i))	**-**	414
Total current derivative financial instrument liabilities	**390**	1,141

11 Financial risk management (continued)

(a) Derivatives (continued)

(i) Classification of derivatives

Derivatives are classified as held for trading and accounted for at fair value through profit or loss unless they are designated as hedges. They are presented as current assets or liabilities if they are expected to be settled within 12 months after the end of the reporting year.

The Group's accounting policy for its cash flow hedges is set out in note 2(p). For hedged forecast transactions that result in the recognition of a non-financial asset, the Group has elected to include related hedging gains and losses in the initial measurement of the cost of the asset.

(ii) Fair value measurements

For information about the methods and assumptions used in determining the fair value of derivatives please refer to note 7(e).

(b) Market risk

(i) Foreign exchange risk

Foreign exchange risk arises from future commercial transactions and recognised assets and liabilities that are denominated in a currency that is not the entity's functional currency and net investments in foreign operations.

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures. Where it considers appropriate, the Group enters into forward foreign exchange contracts to buy specified amounts of various foreign currencies in the future at a pre-determined exchange rate.

Foreign exchange forward contracts measured through Other comprehensive income are designated as hedging instruments in cash flow hedges of forecast purchases in USD. These forecast transactions are highly probable.

The cash flow hedges of the expected future purchases were assessed to be highly effective and a net unrealised gain of $337,000 (2017: $834,000 loss) is included in Other comprehensive income. Fair value adjustments are included in Derivative financial instruments.

Exposure

The Group's exposure to foreign currency risk at the end of the reporting year, expressed in transactional currency, was as follows:

	30 June 2018			30 June 2017		
	USD $'000	**NZD $'000**	**CAD $'000**	USD $'000	NZD $'000	CAD $'000
Cash and cash equivalents	**6**	**52**	**48**	25	40	45
Trade receivables	**266**	**-**	**-**	882	-	-
Trade payables	**5,811**	**53**	**101**	3,696	228	57
Forward exchange contracts						
Buy foreign currency (cash flow hedges)	**7,000**	**-**	**-**	17,000	-	-

Sensitivity

The Group's principal foreign currency exposures arise from trade payables and receivables outstanding at year end.

Most trade payables are repaid within 30 days so there is minimal equity impact arising from foreign currency exposures.

11 Financial risk management (continued)

(b) Market risk (continued)

(i) Foreign exchange risk (continued)

Sensitivity (continued)

	Impact on pre-tax profit		Impact on other components of equity	
	2018	2017	**2018**	2017
	$'000	$'000	**$'000**	$'000
USD Trade payables				
US/$ exchange rate - increase 10%*	**-**	-	**372**	2,011
US/$ exchange rate - decrease 10%*	**-**	-	**(1,542)**	(2,458)

* Holding all other variables constant, this represents the impact of the forward exchange contracts held at the end of the reporting period if the USD exchange rate was to increase or decrease by 10%

(ii) Cash flow and fair value interest rate risk

The Group's main interest rate risk arises from long-term borrowings and cash. Borrowings issued at variable rates expose the Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value interest rate risk. Group policy is to maintain fixed interest cover of between 50% and 100% of core debt up to 12 months, between 50% and 75% of core debt between 1 and 3 years, and between 25% and 50% of core debt between 3 and 5 years.

To manage variable interest rate borrowings risk, the Group enters into interest rate swaps in which the Group agrees to exchange, at specified intervals, the difference between fixed and variable rate interest amounts calculated by reference to an agreed-upon notional principal amount.

The interest rate derivatives require settlement of net interest receivable or payable each 30 days and are settled on a net basis.

The exposure of the Group's borrowing to interest rate changes and the contractual re-pricing dates of the fixed interest rate borrowings at the end of the reporting year are as follows:

	2018	2017
	$'000	$'000
Variable rate borrowings	**35,213**	45,034
	35,213	45,034

Instruments used by the group

The cash flow hedges were assessed to be highly effective and a net realised gain of $659,000 (2017: $578,000 gain) is included in Other comprehensive income. Fair value adjustments are included in Derivative financial instruments.

The interest rate swaps are designated as cash flow hedging instruments. Changes in the interest paid on the variable rate fully drawn down advance facility are measured at fair value through Other comprehensive income.

Swaps in place cover approximately 71.0% (2017: 77.7%) of the variable rate principal outstanding.

11 Financial risk management (continued)

(b) Market risk (continued)

(ii) Cash flow and fair value interest rate risk (continued)

Instruments used by the group (continued)

As at the end of the reporting year, the Group had the following variable rate borrowings and interest rate swap contracts outstanding:

	30 June 2018		30 June 2017	
	Weighted average interest rate %	**Balance $'000**	Weighted average interest rate %	Balance $'000
Bank overdrafts and bank loans	**2.97%**	**35,213**	2.50%	45,034
Interest rate swaps (notional principal amount)	**3.91%**	**25,000**	3.85%	35,000
Net exposure to cash flow interest rate risk		**10,213**		10,034

An analysis by maturities is provided in note 11(d) below. The percentage of total loans shows the proportion of loans that are currently at variable rates in relation to the total amount of borrowings.

Amounts recognised in profit or loss and other comprehensive income

The cash flow hedges were assessed to be highly effective. Fair value adjustments are included in Derivative financial instruments.

Sensitivity

Profit or loss is sensitive to higher/lower interest income from cash and cash equivalents as a result of changes in interest rates. Other components of equity change as a result of an increase/decrease in the fair value of the cash flow hedges of borrowings. All other non-derivative financial liabilities have a contractual maturity of less than 6 months.

	Impact on post-tax profit		**Impact on other components of equity**	
	2018 $'000	2017 $'000	**2018 $'000**	2017 $'000
Interest rates - increase by 100 basis points (100 bps) *	**(102)**	(100)	**(9)**	(16)
Interest rates - decrease by 100 basis points (100 bps) *	**102**	100	**8**	16

* Holding all other variables constant, this represents the impact of the interest rate swaps held at the end of the reporting period and variable borrowings if the interest rate was to increase or decrease by 10%

(c) Credit risk

Credit risk is managed on a Group basis and refers to the risk of a counterparty failing to discharge an obligation. In the normal course of business, the Group incurs credit risk from trade receivables and transactions with financial institutions. The Group places its cash and short term deposits with only high credit quality financial institutions. Sales to retail customers are required to be settled via cash, major credit cards or passed onto various credit providers in each country.

(i) Impaired trade receivables

A provision for impairment loss is recognised when there is objective evidence that an individual trade receivable is impaired. An impairment loss of $415,000 (2017: $313,000) has been recognised by the Group. All trade receivables related to third party credit providers past 90 days have been impaired. Receivables past due but not impaired were $343,000 (2017: $273,000).

11 Financial risk management (continued)

(c) Credit risk (continued)

(i) Impaired trade receivables (continued)

The ageing of these receivables is as follows:

	2018 $'000	2017 $'000
0 - 30 days	**3,749**	3,977
31 - 60 days	**375**	295
61 - 90 days	**201**	73
91 + days	**586**	407
	4,911	4,752

Movements in the provision for impairment of trade receivables that are assessed for impairment collectively are as follows:

	2018 $'000	2017 $'000
At 1 July	**502**	675
Amounts written off	**(415)**	(313)
Additional provisions recognised	**733**	141
Exchange differences	**(1)**	(1)
At 30 June	**819**	502

(ii) Credit quality and impaired in-house customer finance

In-house customer finance was established in Canada and the United States in October 2012. Customer credit risk is managed subject to the Group's established policy, procedures and control relating to customer credit risk management. Credit quality of a customer is assessed based on an extensive credit rating scorecard and individual credit limits are defined in accordance with this assessment.

An impairment analysis is performed at each reporting date. The maximum exposure to credit risk is the carrying value of in-house customer finance program as disclosed in note 7(b)(ii). The Group does not hold collateral as security. The Group evaluates the concentration of risk with respect to trade receivables as low.

The credit quality and ageing of these receivables is as follows:

	2018 $'000	2017 $'000
Performing:		
Current, aged 0 - 30 days	**19,566**	16,786
Past due, 31 - 90 days	**460**	402
Non performing:		
Past due, aged more than 90 days	**519**	502
	20,545	17,690

Movements in the provision for in-house customer finance receivables impairment loss were as follows:

11 Financial risk management (continued)

(c) Credit risk (continued)

(ii) Credit quality and impaired in-house customer finance (continued)

	2018 $'000	2017 $'000
Opening balance	**1,118**	901
Amounts written off	**(2,162)**	(2,051)
Additional provisions recognised	**2,451**	2,299
Exchange differences	**23**	(31)
	1,430	1,118

(d) Liquidity risk

The Group maintains prudent liquidity risk management with sufficient cash and marketable securities and the availability of funding through an adequate amount of committed credit facilities.

(i) Financing arrangements

The Group’s objectives when managing capital are to ensure sufficient liquidity to support its financial obligations and execute the Group's operational and strategic plans. The Group continually assesses its capital structure and makes adjustments to it with reference to changes in economic conditions and risk characteristics associated with its underlying assets. Accordingly, the Group entered into an agreement with ANZ on 26 June 2018 that provides for a $110,000,000 multi option borrowing facility, the availability of which is adjusted throughout the year in line with business requirements. At balance date, $70,000,000 was available. The Group had access to the following undrawn borrowing facilities at the end of the reporting year:

	2018 $'000	2017 $'000
Floating rate		
- Expiring beyond one year (bank overdrafts)	**1,924**	1,957
- Expiring beyond one year (bank loans)	**34,787**	24,966
	36,711	26,923

(ii) Maturities of financial liabilities

The tables below analyse the Group's financial liabilities into relevant maturity groupings based on their contractual maturities for:

(a) all non-derivative financial liabilities, and

(b) net and gross settled derivative financial instruments for which the contractual maturities are essential for an understanding of the timing of the cash flows.

The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant. For interest rate swaps the cash flows have been estimated using forward interest rates applicable at the end of the reporting year.

11 Financial risk management (continued)

(d) Liquidity risk (continued)

(ii) Maturities of financial liabilities (continued)

Contractual maturities of financial liabilities **At 30 June 2018**	**Less than 6 months $'000**	**6 - 12 months $'000**	**Between 1 and 2 years $'000**	**Between 2 and 5 years $'000**	**Over 5 years $'000**	**Total contractual cash flows $'000**
Non-derivatives						
Trade payables	**49,339**	**-**	**-**	**-**	**-**	**49,339**
Borrowings	**-**	**-**	**35,213**	**-**	**-**	**35,213**
Total non-derivatives	**49,339**	**-**	**35,213**	**-**	**-**	**84,552**
Derivatives						
Net Settled (Interest rate swaps)	**-**	**-**	**302**	**88**	**-**	**390**
	-	**-**	**302**	**88**	**-**	**390**
At 30 June 2017						
Non-derivatives						
Trade payables	47,918	-	-	-	-	47,918
Borrowings	-	-	45,034	-	-	45,034
Total non-derivatives	47,918	-	45,034	-	-	92,952
Derivatives						
Gross settled (forward foreign exchange contracts)	-	414	-	-	-	414
Net Settled (Interest rate swaps)	22	-	190	515	-	727
	22	414	190	515	-	1,141

12 Significant estimates, judgements and errors

(a) Significant estimates and judgements

The preparation of financial statements requires the use of accounting estimates which, by definition, will seldom equal the actual results. Management also needs to exercise judgement in applying the Group's accounting policies. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

Share-based payment transactions

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined with the assistance of an external valuer using the Binomial model. The related assumptions are detailed in note Share-based payments. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liabilities within the next annual reporting period but may impact expenses and equity.

12 Significant estimates, judgements and errors (continued)

(a) Significant estimates and judgements (continued)

Make good provisions

A provision has been made for the present value of anticipated costs of future restoration of leased store premises. The provision includes future cost estimates associated with dismantling and closure of stores. The calculation of this provision requires assumptions such as discount rates, store closure dates and lease terms. These uncertainties may result in future actual expenditure differing from the amounts currently provided. The provision recognised is periodically reviewed and updated based on the facts and circumstances available at the time. Changes for the estimated future costs for sites are recognised in the statement of financial position by adjusting both the expense or asset (if applicable) and provision. The related carrying amounts are disclosed in note 8(h) Provisions.

Estimation of useful lives of assets

The estimation of the useful lives of assets has been based on historical experience, lease terms (for display assets) and policies (for motor vehicles). In addition, the condition of the assets is assessed at least once per year and considered against the remaining useful life. Adjustments to useful lives are made when considered necessary.

Revenue recognition

Professional care plan revenue is recognised as sales revenue in the statement of comprehensive income. Management judgement is required to determine the amount of service revenue that can be recognised based on the usage pattern of PCPs and general information obtained on the operation of service plans in other markets. Those direct and incremental bonuses associated with the sale of these plans are deferred and amortised in proportion to the revenue recognised. Management reviews trends in current and estimated future services provided under the plan to assess whether changes are required to the revenue and cost recognition rates used.

Due to management reviews conducted during the year, an adjustment to the revenue recognition pattern has been deemed necessary. As a result of this, an additional $532,000 has been recognised as revenue in the current financial year. Of this, $59,000 relates to the current financial year, and $473,000 relates to prior financial years. The change in estimate will result in lower revenue in future periods by the corresponding amount.

Taxation and recovery of deferred tax assets

The Group is subject to income taxes in Australia and jurisdictions where it has foreign operations. Significant judgement is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business.

Deferred tax assets are recognised for deductible temporary differences as management considers that it is probable that future taxable profits will be available to utilise those temporary differences. Management judgement is required to determine the amount of deferred tax assets that can be recognised.

Impairment of non-financial assets other than goodwill and indefinite life intangibles

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 store performance, product and manufacturing performance, technology and economic environments and future product expectations. If an impairment trigger exists the recoverable amount of the asset is determined.

Employee benefits

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

13 Capital management

(a) Risk management

The Group's objectives when managing capital are to

- safeguard their ability to continue as a going concern, so that they can continue to provide returns for shareholders and benefits for other stakeholders, and
- maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

There are a number of external bank covenants in place relating to debt facilities. These covenants are calculated and reported to the bank quarterly. The principal covenants relating to capital management are the earnings before interest and taxation (EBIT) fixed cover charge ratio, the consolidated debt to earnings before interest, taxation, depreciation and amortisation (EBITDA) and consolidated debt to capitalisation. There have been no breaches of these covenants or events of review for the current or prior period.

(b) Dividends

(i) Ordinary shares

	2018 $'000	2017 $'000
Final dividend for the year ended 30 June 2017 of 2.5 cents (2016 - 2.5 cents) per fully paid share paid on 29 September 2017 (2016 - 6 October 2016).	**9,685**	9,578
Interim dividend for the year ended 30 June 2018 of 2.5 cents (2017 - 2.5 cents) per fully paid share paid on 29 March 2018 (2017 - 31 March 2017).	**9,686**	9,686
	19,371	19,264

(ii) Dividends not recognised at the end of the reporting period

	2018 $'000	2017 $'000
Since year end the Directors have declared the payment of a final dividend of AU 2.5 cents per fully paid ordinary share* (2017 - AU 2.5 cents). The final dividend will be unfranked and fully imputed. The aggregate amount of the dividend expected to be paid on 28 September 2018 out of retained earnings, but not recognised as a liability at year end, is	**9,686**	9,686

* This will not be declared as conduit foreign income, therefore Australian withholding tax will be deducted from the dividend payment for foreign (non-Australian tax resident) shareholders.

(iii) Franking and imputation credits

	Consolidated entity	
	2018 $'000	2017 $'000
Franking credits available for subsequent reporting periods based on a tax rate of 30.0% (2017 - 30.0%)	**1,822**	(2,148)
Imputation credits available for subsequent reporting periods based on the New Zealand tax rate of 28.0% (2017 - 28.0%)	**23,893**	28,424

13 Capital management (continued)

(b) Dividends (continued)

(iii) Franking and imputation credits (continued)

The dividends paid during the current financial period and corresponding previous financial period were partly franked or imputed.

The above franking credit amounts represent the balance of the franking account as at the end of the financial year, adjusted for franking credits that will arise from the payment and refund of income tax payable.

The above imputation credit amounts represent the balance of the imputation account as at the end of the financial year, adjusted for imputation credits that will arise from the payment and refund of income tax payable.

As the dividend recommended by the Directors since year end, but not recognised as a liability at year end, will be unfranked, there will be no reduction in the franking account.

The impact on the imputation credit account of the dividend recommended by the Directors since year end, but not recognised as a liability at year end, is estimated to be a reduction in the imputation credit account of NZ$4,075,000 (2017: NZ$4,051,000). The amount of imputation credits is dependant on the NZD exchange rate at the time of the dividend.

14 Discontinued operations

(a) Financial performance and cash flow information

Emma & Roe	**2018 $'000**	2017 $'000
Revenue	**16,935**	15,448
Expenses	**(26,939)**	(23,859)
Impairment of other assets	**(429)**	-
Impairment of property, plant and equipment	**(7,038)**	-
Store exit costs	**(6,038)**	-
(Loss) before income tax	**(23,509)**	(8,411)
Income tax expense	**6,737**	2,758
(Loss) after income tax of discontinued operation	**(16,772)**	(5,653)
(Loss) from discontinued operation	**(16,772)**	(5,653)
Net cash (outflow) from operating activities	**(12,656)**	(12,092)
Net cash (outflow) from investing activities	**(3)**	(318)
Net cash inflow from financing activities	**12,675**	12,411
Net increase in cash generated by the subsidiary	**16**	1

14 Discontinued operations (continued)

(a) Financial performance and cash flow information (continued)

Michael Hill United States	**2018** **$'000**	2017 $'000
Revenue	**11,845**	16,427
Expenses	**(16,309)**	(21,467)
Impairment of property, plant and equipment	**(3,641)**	(790)
Store exit costs	**(5,333)**	-
Other income	**13**	14
(Loss) before income tax	**(13,425)**	(5,816)
Income tax expense	**(11)**	(17)
(Loss) from discontinued operation	**(13,436)**	(5,833)
Total profit/(loss) from discontinued operations	**(30,208)**	(11,485)
Net cash (outflow) from operating activities	**(1,521)**	(858)
Net cash (outflow) from investing activities	**(65)**	(318)
Net cash inflow / (outflow) from financing activities	**987**	(470)
Net decrease in cash generated by the subsidiary	**(599)**	(1,646)

15 Interests in other entities

(a) Subsidiaries

The consolidated financial statements incorporate the assets, liabilities and results of the following subsidiaries in accordance with the accounting policy described in note 2(b):

Name of entity	Country of incorporation	Ownership interest held by the group	
		2018	2017
		%	%
Michael Hill Jeweller (Australia) Pty Limited	Australia	**100**	100
Michael Hill Wholesale Pty Limited	Australia	**100**	100
Michael Hill Manufacturing Pty Limited	Australia	**100**	100
Michael Hill Franchise Pty Limited	Australia	**100**	100
Michael Hill Franchise Services Pty Limited	Australia	**100**	100
Michael Hill Finance (Limited Partnership)	Australia	**100**	100
Michael Hill Group Services Pty Limited	Australia	**100**	100
Michael Hill Charms Pty Limited	Australia	**100**	100
Michael Hill Online Pty Limited	Australia	**100**	100
Emma & Roe Pty Limited	Australia	**100**	100
Emma & Roe Online Pty Ltd	Australia	**100**	100
Durante Holdings Pty Limited	Australia	**100**	100
Michael Hill New Zealand Limited (formerly known as Michael Hill International Limited)	New Zealand	**100**	100
Michael Hill Jeweller Limited	New Zealand	**100**	100
Michael Hill Finance (NZ) Limited	New Zealand	**100**	100
Michael Hill Franchise Holdings Limited	New Zealand	**100**	100
MHJ (US) Limited	New Zealand	**100**	100
Emma & Roe NZ Limited	New Zealand	**100**	100
Michael Hill Online Holdings Limited	New Zealand	**100**	100
Michael Hill Jeweller (Canada) Limited	Canada	**100**	100
Michael Hill LLC	United States	**100**	100

16 Contingent liabilities and contingent assets

(a) Contingent liabilities

The Group had contingent liabilities in respect of guarantees to bankers and other financial institutions in respect of store occupancy agreements and the New Zealand stock exchange at 30 June 2018 of $472,000 (30 June 2017 - $461,000).

From time to time, Companies within the Group are party to various legal actions as well as inquiries from regulators and government bodies that have arisen in the normal course of business. The Directors have given consideration to such matters which are or may be subject to claims or litigation at year end and are of the opinion that that any liabilities arising from such action would not have a material effect on the Group's financial performance.

The Group is not aware of any significant events occurring subsequent to balance date that have not been disclosed.

(b) Contingent assets

The Group has no material contingent assets existing as at balance date.

17 Commitments

(a) Operating leases

The Group leases all shops and in addition, various offices and warehouses under non-cancellable operating leases expiring within various periods of up to fifteen years. The leases have varying terms, escalation clauses and renewal rights. On renewal, the terms of the leases are renegotiated.

The Group also leases various plant and machinery under cancellable operating leases. The Group is required to give six months notice for termination of these leases.

	2018 **$'000**	2017 $'000
Commitments for minimum lease payments in relation to non-cancellable operating leases are payable as follows:*		
Within one year	**40,752**	42,784
Later than one year but not later than five years	**88,701**	95,788
Later than five years	**24,407**	20,195
	153,860	158,767

** Includes lease commitments for Emma & Roe stores where store closure is still in progress via negotiated outcomes with the respective landlords.*

18 Events occurring after the reporting period

Dividends

On 24 August 2018, the Directors have declared the payment of a final dividend for the year ended 30 June 2018. Refer to note 13(b)(ii) for details.

No other matters or circumstances have occurred subsequent to year end that has significantly affected, or may significantly affect, the operations of the Group, the results of those operations or the state of affairs of the Group or economic entity in subsequent financial years.

19 Related party transactions

(a) Subsidiaries

The ultimate parent and controlling entity of the Group is Michael Hill International Limited. Interests in subsidiaries are set out in note 15(a).

(b) Key management personnel compensation

	2018 **$**	2017 $
Short-term employee benefits	**2,214,394**	2,186,483
Long-term benefits	**43,792**	125,917
Post-employment benefits	**123,224**	184,383
Termination benefits	**-**	1,603,742
Share-based payments	**402,864**	313,691
	2,784,274	4,414,216

Detailed remuneration disclosures are provided in the remuneration report on pages 15 to 32.

(c) Transactions with other related parties

The following transactions occurred with related parties:

	2018 **$**	2017 $
Sales and purchases of goods and services		
Services rendered for graphic design of the annual and half year reports by a related party of board members	**12,447**	12,676
Consulting Agreement with a Director (Robert Ian Fyfe)	**84,000**	-

All transactions with related parties were in the normal course of business and provided on commercial terms. Further details regarding the Consulting Agreement with a Director is included within the Director's Report Service contracts.

20 Share-based payments

(a) Employee Option Plan

Options are granted from time to time at the discretion of Directors to senior executives within the Group. Motions to issue options to related parties of Michael Hill International Limited are subject to the approval of shareholders at the Annual General Meeting in accordance with the Company's constitution.

Options are granted under the plan for no consideration. Options are granted for a ten year period and are exercisable at any time during the final five years.

Options granted under the plan carry no dividend or voting rights. When exercisable, each option is convertible into one ordinary share.

The exercise price of the options previously granted was set at 30% above the weighted average price at which the Company's shares were traded on the New Zealand Stock Exchange for the calendar month following the announcement by the Group to the New Zealand Stock Exchange of its annual results.

20 Share-based payments (continued)

(a) Employee Option Plan (continued)

The exercise price of any future option grants will be set using the same method, with reference to the Australian Securities Exchange.

Set out below are summaries of options granted under the plan:

	2018 Average exercise price per share option	**2018** Number of options	2017 Average exercise price per share option	2017 Number of options
As at 1 July NZD options	**1.47**	**4,650,000**	1.47	12,550,000
Exercised during the year *	**-**	**-**	1.19	(4,300,000)
Forfeited during the year	**-**	**-**	1.81	(3,600,000)
Expired during the year	**1.25**	**(1,250,000)**	-	-
As at 30 June NZD options	**1.56**	**3,400,000**	1.47	4,650,000
As at 1 July AUD options	**2.12**	**200,000**	-	-
Granted during the year	**1.44**	**200,000**	2.12	200,000
As at 30 June AUD options	**1.78**	**400,000**	2.12	20,000

A total of 1,250,000 options expired during the year ended 30 June 2018.

Share options outstanding at the end of the year have the following expiry date and exercise prices.

Grant date	Expiry date	Exercise price	Share options 30 June 2018	Share options 30 June 2017
9 November 2007	30 September 2017	NZ$1.25	-	1,250,000
22 September 2009	30 September 2019	NZ$0.94	100,000	100,000
5 November 2009	30 September 2019	NZ$0.94	150,000	150,000
17 September 2010	30 September 2020	NZ$0.88	250,000	250,000
16 November 2011	30 September 2021	NZ$1.16	250,000	250,000
19 September 2012	30 September 2022	NZ$1.41	250,000	250,000
18 September 2013	30 September 2023	NZ$1.82	250,000	250,000
29 November 2013	30 September 2023	NZ$1.82	1,750,000	1,750,000
10 November 2014	30 September 2024	NZ$1.63	200,000	200,000
22 January 2016	30 September 2025	NZ$1.14	200,000	200,000
22 September 2016	30 September 2026	AU$2.12	200,000	200,000
5 October 2017	30 September 2027	AU$1.44	200,000	-
Total			3,800,000	4,850,000

The weighted average remaining contractual life of share options outstanding at the end of the period was 5.1 years (2017: 4.4 years).

The range of exercise prices for options outstanding at the end of the year was NZ$0.88 - NZ$1.82 and AU$1.44 - AU$2.12. Refer to the table above for detailed information on each issue.

The exercise price will be converted to Australian dollars using the Reserve Bank of Australia exchange rate on the day the option is exercised.

20 Share-based payments (continued)

(a) Employee Option Plan (continued)

(i) Fair value of options granted

The fair value at grant date for the options issued during the 2018 financial year were independently determined using a Binomial option pricing model, which is an iterative model for options that can be exercised at times prior to expiry. The model takes into account the grant date, exercise price, the expected life, the expiry date, the share price at grant date, expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option. The expected life assumes the option is exercised at the mid-point of the exercise period, and reflects the ability to exercise early and the non-transferability of the option.

The expected price volatility is based on the historic volatility (based on the remaining life of the options), adjusted for any expected changes to future volatility due to publicly available information.

The model inputs for options granted during the year ended 30 June 2018 and 30 June 2017 included:

	June 2018 5 October 2017	June 2017 22 September 2016
Number of options	200,000	200,000
Dividend yield	5.00%	5.00%
Expected volatility	25%	25%
Risk-free interest rate	4.78%	4.78%
Expected life of options (years)	7.5	7.5
Option exercise price	AU$1.44	AU$2.12
Share price at grant date	AU$1.09	AU$1.74
Weighted average fair value per option	NZ14.8c	NZ15.6c

(b) Share rights

The Company introduced a deferred compensation plan ("LTI") involving the granting of share rights to eligible participants in 2016 and was approved by shareholders at the Company's Annual General Meeting held on 31 October 2016.

Under the plan, a senior executive may be granted share rights by the Company. Each share right represents a right to receive one ordinary share in the Company, subject to the terms and conditions of the rules of the plan. An allocation of share rights is made to each eligible participant on an annual basis to a value of 30% of the STI payment earned in the preceding year. The share rights progressively vest over a 3, 4 and 5 year period from the date of issue and are only retained on exiting the business in the event that the participant is deemed a 'Good Leaver' pursuant to the LTI plan rules.

During the year, the Board agreed to grant 536,551 share rights to eligible participants of the deferred compensation plan.

225,875 of the share rights were issued on the basis that they are divided into three tranches and vest over 3, 4 and 5 years, respectively. 310,676 of the share rights were issued on the basis that 100% will vest if the participant has been continuously engaged under an engagement arrangement with the Company at grant date, which is in three years time.

The number of share rights in each tranche is based on the prescribed dollar value for each tranche divided by the volume weighted average share price ('VWAP') of Michael Hill International shares over 5 trading days following the Michael Hill International shares trading on an ex-dividend basis.

20 Share-based payments (continued)

(b) Share rights (continued)

	2018		2017	
	Average exercise price per share right $	**Number of options**	**Average exercise price per share right $**	**Number of options**
Outstanding as at 1 July	1.66	382,551		-
Granted	1.05	536,551	1.66	382,551
Exercised	-	-	-	-
Forfeited	-	-	-	-
Outstanding at 30 June	1.30	919,102	1.66	382,551

(c) Expenses arising from share-based payment transactions

Total expenses arising from share-based payment transactions recognised during the year as part of employee benefit expense were as follows:

	2018 $'000	2017 $'000
Options issued under employee option plan	**42**	55
Share rights issued under CEO and LTI plan	**442**	316
	484	371

21 Remuneration of auditors

During the year the following fees were paid or payable for services provided by the auditor of the parent entity, its related practices and non-related audit firms:

(a) Ernst & Young

(i) Audit and other assurance services

	2018 $	2017 $
Audit and review of financial statements	**411,910**	342,651
Total remuneration for audit and other assurance services	**411,910**	342,651

(ii) Other services

Advisory fees	**170,231**	7,416
Total remuneration for other services	**170,231**	7,416

Total remuneration of Ernst & Young Australia	**582,141**	350,067

Total auditors' remuneration	**582**	350

22 Earnings per share

(a) Basic earnings per share

	2018 Cents	2017 Cents
From continuing operations	**8.99**	11.43
From discontinued operation	**(7.80)**	(2.97)
Total basic earnings per share attributable to the ordinary equity holders of the Company	**1.19**	8.46

(b) Diluted earnings per share

	2018 Cents	2017 Cents
From continuing operations	**8.98**	11.42
From discontinued operation	**(7.79)**	(2.97)
Total diluted earnings per share attributable to the ordinary equity holders of the Company	**1.19**	8.45

(c) Reconciliation of earnings used in calculating earnings per share

	2018 $'000	2017 $'000
Basic earnings per share		
Profit attributable to the ordinary equity holders of the Company used in calculating basic earnings per share:		
From continuing operations	**34,818**	44,132
From discontinued operations	**(30,208)**	(11,485)
	4,610	32,647
Diluted earnings per share		
Profit from continuing operations attributable to the ordinary equity holders of the Company		
From continuing operations	**34,818**	44,132
From discontinued operations	**(30,208)**	(11,485)
Used in calculating diluted earnings per share	**4,610**	32,647

(d) Weighted average number of shares used as the denominator

	2018 Number	2017 Number
Weighted average number of ordinary shares used as the denominator in calculating basic earnings per share	**387,438,513**	385,963,992
Adjustments for calculation of diluted earnings per share:		
Options	**500,000**	500,000
Weighted average number of ordinary and potential ordinary shares used as the denominator in calculating diluted earnings per share	**387,938,513**	386,463,992

22 Earnings per share (continued)

(e) Information concerning the classification of securities

(i) Options

Options granted to employees under the Michael Hill International Limited Employee Option Plan are considered to be potential ordinary shares and have been included in the determination of diluted earnings per share to the extent to which they are dilutive. The options have not been included in the determination of basic earnings per share. Details relating to the options are set out in note 20(a).

23 Parent entity financial information

(a) Summary financial information

The individual financial statements for Michael Hill International Limited (the parent) show the following aggregate amounts:

	2018 $'000	2017 $'000
Balance sheet		
Current assets	**39**	4,605
Non-current assets	**338,473**	329,278
Total assets	**338,512**	333,883
Current liabilities	**3,517**	-
Total liabilities	**3,517**	-
Shareholders' equity		
Issued capital	**290,408**	290,157
Reserves		
Acquisition reserve	**40,907**	40,907
Option reserve	**1,370**	1,136
Retained earnings	**2,310**	1,683
	334,995	333,883
Profit or loss for the year	**20,000**	19,275
Total comprehensive income	**20,000**	19,275

(b) Guarantees entered into by the parent entity

The Parent has issued the following guarantees in relation to the debts of its subsidiaries:

(i) Pursuant to Class Order 2016/785, Michael Hill International Limited and the subsidiaries listed below entered into a deed of cross guarantee on 30 June 2016. The effect of the deed is that Michael Hill International Limited has guaranteed to pay any deficiency in the event of winding up of any controlled entity or if they do not meet their obligations under the terms of overdrafts, loans, leases or other liabilities subject to the guarantee. The controlled entities have also given a similar guarantee in the event that Michael Hill International Limited is wound up or if it does not meet its obligations under the terms of overdrafts, loans, leases or other liabilities subject to the guarantee.

23 Parent entity financial information (continued)

(b) Guarantees entered into by the parent entity (continued)

(ii) The subsidiaries subject to the deed are: Durante Holdings Pty Ltd, Michael Hill Group Services Pty Ltd, Michael Hill Jeweller (Australia) Pty Ltd, Michael Hill Manufacturing Pty Ltd, Michael Hill Wholesale Pty Ltd, Michael Hill Franchise Services Pty Ltd, Michael Hill Franchise Pty Ltd, Michael Hill New Zealand Ltd, Michael Hill Jeweller Ltd, Michael Hill Franchise Holdings Ltd, Michael Hill Finance (NZ) Ltd, Michael Hill Online Pty Ltd, Michael Hill Charms Pty Ltd, Emma & Roe Pty Ltd, Emma & Roe Online Pty Ltd, Michael Hill Online Holdings Ltd and Emma & Roe NZ Ltd

(c) Contingent liabilities of the parent entity

The Parent entity had contingent liabilities in respect of guarantees to bankers and other financial institutions in respect of overdraft facilities and fixed assets at 30 June 2018 of $72,000 (2016: $72,000).

24 Deed of cross guarantee

Pursuant to ASIC Class Order 2016/785, the Australian wholly-owned subsidiaries listed below are relieved from the Corporations Act 2001 requirements for preparation, audit and lodgement of financial reports and directors' report in Australia.

The subsidiaries subject to the deed are: Durante Holdings Pty Ltd, Michael Hill Group Services Pty Ltd, Michael Hill Jeweller (Australia) Pty Ltd, Michael Hill Manufacturing Pty Ltd, Michael Hill Wholesale Pty Ltd, Michael Hill Franchise Services Pty Ltd, Michael Hill Franchise Pty Ltd, Michael Hill New Zealand Ltd, Michael Hill Jeweller Ltd, Michael Hill Franchise Holdings Ltd, Michael Hill Finance (NZ) Ltd, Michael Hill Online Pty Ltd, Michael Hill Charms Pty Ltd, Emma & Roe Pty Ltd, Emma & Roe Online Pty Ltd, Michael Hill Online Holdings Ltd and Emma & Roe NZ Ltd.

The Class Order requires the Parent Company and each of the subsidiaries to enter into a Deed of Cross Guarantee. The effect of the deed is that the Company guarantees each creditor payment in full of any debt in the event of winding up of any of the subsidiaries under certain provisions of the Corporations Act 2001. If a winding up occurs under other provisions of the Corporations Act 2001, the Company will only be liable in the event that after six months any creditor has not been paid in full. The subsidiaries have also given similar guarantees in the event that the Company is wound up.

The above companies represent a Closed Group for the purposes of the Class Order and, as there are no other parties to the Deed of Cross Guarantee that are controlled by Michael Hill International Limited, they also represent the Extended Closed Group.

(a) Consolidated statement of profit or loss, statement of comprehensive income and summary of movements in consolidated retained earnings

Set out below is a consolidated statement of profit or loss, a consolidated statement of comprehensive income and a summary of movements in consolidated retained earnings for the year ended 30 June 2018 of the closed group consisting of Michael Hill International Limited and the entities noted above.

	2018 **$'000**	2017 $'000
Consolidated statement of profit or loss		

24 Deed of cross guarantee (continued)

(a) Consolidated statement of profit or loss, statement of comprehensive income and summary of movements in consolidated retained earnings (continued)

	2018 $'000	2017 $'000
Revenue from sales of goods and services	**461,319**	455,114
Sales to Group companies not in Closed Group	**34,803**	43,527
Other income	**231**	1,164
Cost of goods sold	**(200,608)**	(205,916)
Employee benefits expense	**(133,899)**	(126,861)
Occupancy costs	**(53,293)**	(45,394)
Marketing expenses	**(26,647)**	(22,537)
Selling expenses	**(23,788)**	(22,454)
Impairment of investment	**(14,361)**	-
Depreciation and amortisation expense	**(14,535)**	(14,554)
Loss in disposal of property, plant and equipment	**(377)**	(322)
Other expenses	**(21,854)**	(11,767)
Finance costs	**(3,003)**	(3,550)
Profit before income tax	**3,988**	46,450
Income tax expense	**(4,289)**	(11,022)
Profit for the year	**(301)**	35,428

	2018 $'000	2017 $'000
Other comprehensive income		
Items that may be reclassified to profit or loss		
Exchange differences on translation of foreign operations	**(4,412)**	(4)
Other comprehensive income for the period, net of tax	**(4,412)**	(4)
Total comprehensive income for the year	**(4,713)**	35,424

	2018 $'000	2017 $'000
Statement of changes in equity		
Equity at the beginning of the financial year	**501,191**	479,835
Total comprehensive income / (loss)	**(4,713)**	35,424
Issue of share capital - exercise of options	**-**	4,825
Share rights through share based payments reserve	**440**	316
Option expense through share based payment reserve	**45**	55
Dividends paid	**(19,371)**	(19,264)
Total equity at the end of the financial year	**477,592**	501,191

(b) Consolidated statement of financial position

Set out below is a consolidated statement of financial position as at 30 June 2018 of the Closed Group consisting of Michael Hill International Limited and the entities noted above.

24 Deed of cross guarantee (continued)

(b) Consolidated statement of financial position (continued)

	2018 $'000	2017 $'000
Current assets		
Cash and cash equivalents	**2,977**	1,600
Trade and other receivables	**8,070**	8,982
Inventories	**153,164**	152,907
Current tax receivables	**(2,095)**	1,008
Loans to related parties	**237,783**	234,510
Other current assets	**2,641**	2,542
Total current assets	**402,540**	401,549
Non-current assets		
Property, plant and equipment	**38,214**	47,713
Deferred tax assets	**56,776**	53,485
Intangible assets	**12,525**	8,613
Investments in subsidiaries	**85,727**	102,991
Other non-current assets	**2,310**	1,634
Total non-current assets	**195,552**	214,436
Total assets	**598,092**	615,985
Current liabilities		
Trade and other payables	**42,557**	39,278
Provisions	**7,498**	4,336
Deferred revenue	**19,804**	20,135
Total current liabilities	**69,859**	63,749
Non-current liabilities		
Provisions	**4,908**	6,177
Deferred revenue	**45,733**	44,868
Total non-current liabilities	**50,641**	51,045
Total liabilities	**120,500**	114,794
Net assets	**477,592**	501,191
Equity		
Contributed equity	**309,256**	309,004
Reserves	**(3,651)**	528
Retained profits	**171,987**	191,659
Total equity	**477,592**	501,191

Directors' declaration

The Directors declare that:

(a) in the Directors' opinion there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable;

(b) note 2(a) confirms that the financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board;

(c) the financial statements and notes of the Group for the financial year ended 30 June 2018, are in accordance with the Corporations Act 2001, including:

    (i) complying with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and

    (ii) giving a true and fair view of the consolidated entity's financial position as at 30 June 2018 and of its performance for the financial year ended on that date;

(d) the Directors have been give the declarations by the chief executive officer and chief financial officer required by section 295A of the Corporations Act 2001; and

(d) as at the date of this declaration, there are reasonable grounds to believe that the members of the extended closed group identified in note 24 will be able to meet any obligations or liabilities to which they are, or may become, subject to by virtue of the deed of cross guarantee described in note 24.

This declaration is made on 24 August 2018 in accordance with a resolution of Directors in accordance with section 295 Corporations Act 2001.

E J Hill
Chair
Brisbane
24 August 2018

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Independent Auditor's Report to the Members of Michael Hill International Limited

Report on the Audit of the Financial Report

Opinion

We have audited the financial report of Michael Hill International 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, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, notes to the financial report, including a summary of significant accounting policies, and the directors' declaration.

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

a) giving a true and fair view of the consolidated financial position of the Group as at 30 June 2018 and of its consolidated financial performance for the year ended on that date; and

b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

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

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

Key Audit Matters

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

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

Existence of Inventories

Why significant	How our audit addressed the key audit matter
The existence of inventories was a key audit matter due to the size of the recorded asset (30 June 2018: $192,074,000) which represents more than 50% of the Group's total assets, the nature of the inventory and its location. Inventories are primarily kept in the Group's retail stores situated in three countries and the dispatch and manufacturing warehouses. Inventories comprise a significant number of physically small but high value items. The Group accounts for inventories in accordance with the policy disclosed in Note 2(m) and further disclosure is included in Note 8(a) of the financial report.	Our audit procedures included the following: · Assessed the effectiveness of controls relevant to the conduct of physical stocktaking. · Attended full stock counts at the dispatch and manufacturing warehouse and at a sample of retail stores across all countries to assess whether inventories had been appropriately counted at each location and whether movements into and out of each location prior to and subsequent to the counts had been appropriately recorded. · Considered the work performed by the Group's Internal Audit function in relation to stock counts performed at the retail stores and considered the impact of their findings in our audit approach. We assessed whether their work could be used for the purpose of our audit which included an assessment of the competence of the Internal Audit function. · For the dispatch and manufacturing warehouse stock counts we selected samples or stock receipts prior to and after the stock count including transfers to stores, to assess whether these were appropriately recorded in the correct period. · We performed store-by-store inventory analyses of any unusual fluctuations outside of our set expectations of the year-end balance compared to prior year.

Professional Care Plan Revenue Recognition

Why significant	How our audit addressed the key audit matter
The recognition of professional care plan (PCP) revenue was considered a key audit matter due to the significant degree of estimation involved in determining the appropriate revenue recognition pattern for both the lifetime and 3 year plans offered to the Group's customers. The estimation is based on a combination of comparative market data and an analysis of services (through historical repairs data) made under these plans since inception in October 2010. The estimation is reviewed by the Group at least on an annual basis. As disclosed in Note 12(a) of the financial report, in respect of the lifetime plans, given	Our audit procedures included the following: · Considered the Group's PCP revenue recognition accounting policies and assessed compliance with the requirements of Australian Accounting Standards. · Assessed the effectiveness of controls relating to PCP revenue recognition. · We assessed the appropriateness of the balance of the PCP revenue recognised during the year and the closing deferred PCP at year end based on the change in usage pattern. · Assessed the Group's calculation supporting the change in estimate relating to revenue recognition,

Why significant	How our audit addressed the key audit matter
the infancy of the PCP product, there is limited customer usage history to reference and industry information is also utilised. As such, the determination of the optimal revenue recognition pattern is judgmental. The pattern of recognising revenue is disclosed in Note 2(e)(ii) of the financial report under *rendering of service which is based on percentage of completion*. A change in estimate in the current year has resulted from new information that meets the criteria of a revision in an estimate in accordance with Australian Accounting Standards has been reflected in the current year results. This change in estimate has been disclosed in Note 12(a) to the financial report.	which included agreeing assumptions to samples of the underlying PCP repairs usage data.

Michael Hill US and Emma & Roe Brand Closure

Why significant	How our audit addressed the key audit matter
During the year, the Group made the decision to completely exit its retail operations in the United States. As part of the Group's reprioritising its resources and strategic focus on the core Michael Hill brand, a decision was made to close all Emma & Roe stores and its associated online presence. These decisions had a significant impact on the current year operating results of the Group. The Group has accounted for the discontinued operations in accordance with the policy disclosed in Note 2 and further disclosure is included in Note 14 to the financial report.	Our audit procedures included the following: · Agreed the closure costs incurred such as impairment loss recognised on fixed assets, employee related costs, lease exit costs and other expenses to appropriate supporting evidence. Where the costs have been paid during and subsequent to year end, we have agreed the costs recorded to the cash payments. · Assessed whether any remaining Michael Hill US and Emma & Roe brand inventory was carried at the lower of cost and net realisable value. · Assessed whether the discontinued operations were accounted for and disclosed in accordance with Australian Accounting Standards.

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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 Group's 2018 Annual Report, other than the financial report and our auditor's report thereon. We obtained the Directors' Report that is to be included in the Annual Report, prior to the date of this auditor's report, and we expect to obtain the remaining sections of the Annual Report after the date of this auditor's report.

Our opinion on the financial report does not cover the other information and accordingly 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 on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Report

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

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

Auditor's Responsibilities for the Audit of the Financial Report

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

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

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

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

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

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

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Report on the Audit of 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 Michael Hill International 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

Ernst & Young

Alison de Groot
Partner
Brisbane
24 August 2018