

Michael Hill International Limited

ABN 25 610 937 598

Appendix 4E

Results for announcement to the market

Year ended 28 June 2020

Reporting period

Reporting period:	12 months ending 28 June 2020
Previous reporting period:	12 months ending 30 June 2019

Results for announcement to the market

				\$'000
Revenue from contracts with customers	Down	13.6%	to	492,060
Earnings before interest and taxation (EBIT)*	Down	33.3%	to	14,079
Net profit after tax for the period attributable to members	Down	81.5%	to	3,059

* EBIT is Non-IFRS Information and is unaudited. Please refer to Non-IFRS Information on page 8 of the Directors Report for an explanation of Non-IFRS information and a reconciliation of 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)*	1.50	-

*Interim dividend for the year ended 28 June 2020 of AU 1.5c was declared. Subsequent to the shares trading ex dividend, but prior to payment date, the interim dividend payment was deferred to 30 September 2021.

No final dividend has been declared by the Directors for the year ended 28 June 2020.

	2020	2019
Net tangible assets		
Net tangible asset backing per ordinary security	\$0.01	\$0.42

For FY20, net tangible assets were calculated excluding the Group's right-of-use assets relating to leases under AASB 16 Leases. The calculation did include the leasing liabilities.



Emma Hill
Chair
Brisbane
18 August 2020

Webcast scheduled to take place at 10.15am (AEST) on Wednesday 19 August 2020. Please use the following link to register.

<https://edge.media-server.com/mmc/p/pfk9gkpo>.

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Michael Hill International Limited

ABN 25 610 937 598

Directors' report and annual financial report for the year ended 28 June 2020

Michael Hill International Limited

ABN 25 610 937 598

Directors' report and annual financial report - 28 June 2020

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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. Accordingly, you are cautioned not to place undue reliance on any forward-looking statements, particularly in light of the current economic climate and the significant volatility, uncertainty and disruption caused by the COVID-19 pandemic.

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.

Michael Hill International Limited
Corporate directory

Directors

E J Hill B.Com., M.B.A. *Chair*
Sir R M Hill K.N.Z.M.
G W Smith B.Com., F.C.A., F.A.I.C.D.
R I Fyfe B.Eng, FENZ
J S Allis
J E Naylor (appointed 15 July 2020)

Company Secretaries

A Lowe BCom, LLB (Hons), MAppFin, CA, CTA
E Bird LLB (Hons), BA (Psych), GradDipLegalPrac,
GradDipAppCorpGov

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Share registrar

Computershare Investor Services Pty Ltd
Level 1
200 Mary Street
Brisbane QLD 4000
1300 552 270 (within Australia)
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Auditor

Ernst & Young
Level 51
111 Eagle Street
Brisbane QLD 4000

Solicitors

Allens
Level 26
480 Queen Street
Brisbane QLD 4000

Bankers

Australia and New Zealand Banking Group Limited
ANZ Banking Group (New Zealand) Limited
Bank of Montreal
Bank of America N.A.

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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 28 June 2020.

Principal activities

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

There were no 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:

	2020	2019
	\$'000	\$'000
Final ordinary dividend for the year ended 30 June 2019 of AU 1.5 cents (2019: AU 2.5 cents) per fully paid share paid on 27 September 2019 (2019: 28 September 2018)	5,817	9,679
Interim ordinary dividend for the year ended 28 June 2020 of AU 1.5 cents (2019: AU 2.5 cents) per fully paid share deferred for payment (2019: 29 March 2019)*	5,816	9,686
No final dividend has been declared by the Directors for the year ended 28 June 2020 (2019: AU 1.5 cents).	-	5,816

* Interim dividend for the year ended 28 June 2020 of AU 1.5 cents was declared. Subsequent to the shares trading ex-dividend, but prior to payment date, the interim dividend payment was deferred to 30 September 2021.

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 of \$492.1m (2019: \$569.5m) for the 2020 financial year, producing a net profit after tax (NPAT) of \$3.1m (2019: \$16.5m). The Group reported an earnings before interest and tax (EBIT) of \$14.1m (2019: \$21.1m) for the 2020 financial year. Underlying EBIT adjusted for non-cash items and AASB 16 Leases (Underlying Trading EBIT) (per the Non-IFRS Information note on page 8 for the Group was \$25.7m (2019: \$34.6m) for the year.

Review of operations (continued)

Operational Review

The Group achieved the following key outcomes for the 2020 financial year:

Key Financial Results

- Statutory net profit after tax of \$3.1m (FY19: \$16.5m), noting new AASB 16 *Leases* applies for FY20 only.
- Earnings before interest and tax (EBIT)* of \$14.1m (FY19: \$21.1m).
- Underlying EBIT* adjusted for non-cash items and AASB 16 *Leases* of \$25.7m (FY19: \$34.6m).
- Group operating revenues of \$492.1m (FY19: \$569.5m), largely attributable to COVID-19 store closures.
- Group adjusted same store sales* were up 2.7% at \$469.3m (FY19: \$457.1m).
- Group gross margin 60.6% (FY19: 62.0%), predominantly impacted by foreign exchange.
- Controlled inventory management, resulting in stock holdings of \$178.7m (FY19: \$179.5m).
- Strong working capital management.
- No final dividend declared. Interim dividend payment of AU 1.5 cents per share deferred to 30 September 2021.

Operational Performance

- Digital sales increased by 54.7% to a record \$24.7m (FY19: \$16.0m), representing 5.0% of total sales (FY19: 2.8%).
- Branded collection sales represented 37.3% of total sales for the full year (FY19: 32.5%).
- Delivery of cloud enabled ERP platform in June 2020, to optimise inventory allocation and store profiling.
- Decisive cash preservation and cost management throughout the year.
- Loyalty program *Brilliance* launched online and in-store during the year, with over 200,000 members to date.
- Stores were temporarily closed due to COVID-19 for a period of five to thirteen weeks, opening progressively in accordance with Government health guidelines.
- One new store opened and seventeen under-performing stores were closed during the year, giving a network total of 290 stores across all markets (FY19: 306).

* EBIT, Underlying EBIT and Adjusted Same Store Sales are Non-IFRS Information and are unaudited. Please refer to Non-IFRS Information on page 8 of the Directors Report for an explanation of Non-IFRS information and a reconciliation of EBIT, Underlying EBIT and Adjusted Same Store Sales.

The Group reported statutory earnings before interest and tax (EBIT) of \$14.1m for the year ended 28 June 2020 (FY19: \$21.1m). Underlying EBIT adjusted for non-cash items and AASB 16 *Leases* for the year decreased to \$25.7m (FY19: \$34.6m).

Prior to COVID-19, the Company had been gaining positive momentum with increasing same store sales growth and margin improvement. Adjusted same store sales were up 2.7% for the full year to \$469.3m (FY19: \$457.1m), as the Company focused on enhancing the retail fundamentals and implemented the new retail operating model. This was particularly evident in the first half, when same store sales returned to positive growth with an increase of 6.3%.

The second half erosion of EBIT was a result of the temporary closure of all stores for a period between five to thirteen weeks, due to the COVID-19 pandemic. The Company reduced the financial impact by implementing a lean operating model, ceasing all discretionary spend, and seeking rent abatements from landlords. In addition, wage subsidies were received in each market which partially offset the employee benefits paid out during this period.

Review of operations (continued)

Operational Review (continued)

The surge in the Company's online business resulted in record digital sales of \$24.7m for the full year (up 54.7% on FY19). The online business delivered some of the highest weeks in the Company's history during the COVID-19 period as customers embraced online purchasing whilst stores were closed. Digital sales now represent 5.0% of total sales. During the year, the Company accelerated the delivery of a number of digital first initiatives including enhanced website and user experience, direct selling from social media platforms and digital catalogues, virtual selling, along with the successful launch of our loyalty program (*Brilliance*) which has now reached over 200,000 members globally.

A continued focus on re-imagining our branded collections saw them represent 37.3% of total product sales for the year (FY19: 32.5%). A key milestone was reached with the delivery and go-live of the cloud enabled ERP platform. This platform will optimise inventory management, enhance store profiling and stock allocation, and facilitate multiple initiatives to deliver a true omni-channel customer experience.

During the second half of the year (COVID-19 lockdown period), the Company took decisive action to preserve cash, reduce expenditure, and actively monitor inventory. Cash management initiatives included the cancellation or deferral of capital expenditure, renegotiation of vendor payment terms, engaging with landlords to obtain rental assistance packages including deferrals, and a reduction in the cost of doing business through leaner labour models.

Furthermore, during the COVID-19 temporary store closure period, the Company worked closely with its long standing lending partner ANZ. Given a nil net debt position at year end, the existing \$70m facility limit is considered appropriate to meet the Company's inventory and working capital requirements.

Sales from the Group's Professional Care Plan (PCP) declined to \$24.0m (FY19: \$28.5m) with an amount of \$27.5m (FY19: \$32.9m) recognised as revenue for the full year. At 28 June 2020, a deferred amount of \$73.8m remained on the balance sheet (FY19: \$77.8m).

The Company opened one new store and closed seventeen under-performing stores, resulting in 290 stores at year end.

Segment Results

The operational segments below reflect the performance of the Group's retail operations in each geographic segment. The segments include trading activity from our online channels presence and our Canadian in-house credit function. The segments exclude revenue and expenses that do not relate directly to the relevant 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 results below are expressed in local currency.

Australian Retail Performance

OPERATING RESULTS (AU \$000)	2020	2019	2018	2017	2016
Revenue from continuing operations	266,610	313,587	325,709	321,981	309,457
Gross margin	161,030	194,052	206,303	201,707	194,152
Gross margin as a % of revenue	60.4%	61.9%	63.3%	62.6%	62.7%
EBIT	27,410	32,917	48,621	51,688	49,975
As a % of revenue	10.3%	10.5%	14.9%	16.1%	16.1%
Number of stores	155	168	171	166	168

Review of operations (continued)

In Australia, adjusted same store sales marginally improved by 0.1%, and all stores revenue declined by 15.0% to \$266.6m (FY19: \$313.6m) for the year. Gross margin for the year was 60.4% (FY19: 61.9%), largely due to FX impacts on cost of goods. While the majority of the revenue decline is attributable to the COVID-19 temporary store closure period, a portion is also due to the closure of thirteen underperforming stores during the year. Due to COVID-19 health restrictions, all stores in Australia were closed on 24 March 2020 and progressively reopened from May 2020, and as such, stores were closed for a period of between five and ten weeks.

Thirteen underperforming stores permanently closed during the period, resulting in 155 stores trading at 28 June 2020.

New Zealand Retail Performance

OPERATING RESULTS (NZ \$000)	2020	2019	2018	2017	2016
Revenue	106,696	120,064	125,239	121,970	122,903
Gross margin	63,641	73,011	77,673	75,204	75,895
Gross margin as a % of revenue	59.6%	60.8%	62.0%	61.7%	61.8%
EBIT	21,067	24,125	27,800	27,836	27,136
As a % of revenue	19.7%	20.1%	22.2%	22.8%	22.1%
Number of stores	49	52	52	52	52
FX rate for profit translation	1.05	1.06	1.09	1.06	1.09

In New Zealand, adjusted same store sales increased by 2.4% to NZ\$103.9m (FY19: NZ\$101.4m) and all store revenue declined by 11.1% to NZ\$106.7m (FY19: NZ\$120.1m) for the year. Gross margin for the year was 59.6% (FY19: 60.8%). The decline in revenue was attributable to the COVID-19 temporary store closure period. The New Zealand Government mandated store closures from 24 March 2020, with stores reopening on either 16 May 2020 or 23 May 2020. Stores were closed for a period of eight to nine weeks.

Three underperforming stores permanently closed during the period, resulting in 49 stores trading at 28 June 2020.

Canadian Retail Performance

OPERATING RESULTS (CA \$000)	2020	2019	2018	2017	2016
Revenue	110,799	133,146	130,762	112,721	95,423
Gross margin	63,991	80,726	81,576	69,078	59,252
Gross margin as a % of revenue	57.8%	60.6%	62.4%	61.3%	62.1%
EBIT	(2,412)	9,797	14,605	12,386	8,929
As a % of revenue	(2.2)%	7.4%	11.2%	11.0%	9.4%
Number of stores	86	86	83	76	67
FX rate for profit translation	0.90	0.95	0.98	1.00	0.97

In Canada, adjusted same store sales increased by 2.3% to CA\$102.8m (FY19: CA\$100.5m) and all store revenue declined by 16.8% to CA\$110.8m (FY19: CA\$133.1m) for the year. Gross margin declined to 57.8% (FY19: 60.6%), largely due to FX impacts. The decline in revenue was largely attributable to the COVID-19 temporary store closure period. All stores in Canada were temporarily closed on 20 March 2020 and progressively reopened across the provinces from June 2020, and as such stores were closed for a period of between ten and thirteen weeks.

One store was opened in Canada during the period as follows:

- McArthur Glen, British Columbia

One underperforming store permanently closed during the period. There were 70 of the 86 stores trading at 28 June 2020.

Review of operations (continued)

Cash, Cash flow and Dividends

Net operating cash inflows were \$80.9m compared to \$39.0m the previous year. Due to the adoption of AASB 16 Leases, \$32.7m was classified as principal portion of lease payments within cash flow from financing activities for FY2020, previously rent payments that were reported in cash flows from operating activities.

Despite the impact to profit over FY2020, \$13.2m related to non-cash impairments (refer to page 8 of the Directors' Report). Through further disciplined inventory and working capital management, the Group's debt levels reduced. The Group remains in a resilient financial position with \$0.5m in net cash (FY19: net debt of \$24.8m) to continue to invest in improvements to its systems, infrastructure, and capabilities. At balance date, \$13.1m of rental costs were accrued.

Dividends

On 23 March 2020, the Company announced that its FY20 interim dividend had been deferred until 30 September 2020 and was subject to review again before that date. Given the impact of COVID-19 and the uncertain economic environment, in order to protect the Company's balance sheet and liquidity in the interests of shareholders, the Board has decided to further defer payment of the FY20 interim dividend until 30 September 2021. The Board will continue to monitor economic conditions and the Company's performance and may revisit and change the date for payment of the FY20 interim dividend if considered necessary or desirable in the circumstances. The Board has also decided not to declare a final dividend for FY20. The Company's objective is to restore a regular pattern of dividend payments as performance improves and earnings stabilise. Decisions on future dividends will continue to be made in line with the Company's financial framework and dividend policy.

Key initiatives for FY21 - Emphasis on Growth

Strong retail fundamentals embedded within a disciplined framework providing a robust platform to enable a true omni-channel customer experience and maximise growth opportunities:

1. **Omni-channel** - leveraging the recent investment in our new ERP platform, the business will embark on multiple digital and physical initiatives to meet the demands of a modern-day customer, including "click and collect/reserve", "ship from store", as well as "drop ship" and marketplace opportunities.
2. **Digital** - building on the successes of FY20 including positive launches of virtual try-on and virtual selling, further enhancements will be delivered across loyalty, new sales platforms and customer communication channels. August 2020 launch of a pure play digital brand - medleyjewellery.com.au - an aspirational and attainable on-trend jewellery offering.
3. **Retail Fundamentals** - continue to deliver improved gross profit and sales performance by embedding multiple initiatives and reinvigorating the retail store culture and customer experience. Additionally, an increased focus on space planning to optimise store productivity and efficiencies.
4. **Canadian Opportunities** - maintaining focus on increased productivity targets while delivering a new supply chain solution, exploring new growth channels, and maximising commercial opportunities of the in-house credit program including a potential divestment of the credit book.
5. **Product Evolution** - undertake range and assortment rationalisation strategy aligned to refreshed product newness calendar and higher inventory turns. A focus on optimising margin through product mix and continuing to enhance higher margin product offerings (eg. laboratory created diamonds) and branded collections.
6. **Cost Conscious Culture** - embedding an absolute focus on cost disciplines, inventory and capital management across all aspects of the Company.

Risk Management

The Board believe that a strong Corporate Governance framework will underpin the Group's growth and success. The Company regularly reviews its risk management framework and has identified the following at risk areas and mitigating strategies:

Risk	Strategies and mitigation
External factors are not appropriately recognised or responded to appropriately	The Group has a crisis management framework and nominated crisis management team in place. Internal resources are designated to identify and coordinate responses to factors affecting the ongoing operations of the Group. This framework was utilised to manage events including bushfire and COVID-19 this year.
Disruption to supply chain and inefficiencies in replenishment strategies	The Group is exploring and investing in better in-market strategies as well as revamping its ranging and increasing emphasis on sourcing and mix of product.
Inadequate business continuity program and/or disaster recovery strategies	As part of the COVID-19 pandemic the Group has executed business continuity plans as well as invested in increased IT disaster recovery initiatives. Both business continuity and disaster recovery processes will continue to evolve to meet the needs of the business. External consultants continue to be used to help with penetration testing and to provide other technical assessments.
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 increase 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 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	The Group continues to have an intense focus on digital channels and initiatives to meet consumer demand. Following the completion of our ERP upgrade, planning is now underway for further omni-channel enhancements.

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 the Group 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 users of financial information, and minimise the possibility of those users being misled by such information.

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:

- Adjusted same store sales reflect sales through store and online channels on a comparable trading day basis
- Earnings before interest, tax, depreciation and amortisation (EBITDA)
- Earnings before interest and tax (EBIT)
- Underlying EBIT and Underlying Trading EBIT
- Significant item

Calculation of Underlying EBIT and Underlying Trading EBIT

Underlying EBIT and Underlying Trading EBIT has been calculated as follows:

	2020	2019
	\$000's	\$000's
Statutory EBIT	14,079	21,115
<i>Add back costs relating to:</i>		
Employee restructure costs	2,170	1,987
Direct, incremental costs relating to COVID-19	1,755	-
Emma & Roe closure costs	-	258
CEO transition costs	-	758
Remediation of employee benefits	-	4,536
Impairment of aged inventory	-	5,954
Underlying EBIT	18,004	34,608
<i>Non-cash items included above in underlying EBIT:</i>		
Impairment of stores and fixed assets	6,796	-
Impairment of inventory	6,437	-
Underlying EBIT adjusted for non-cash items	31,237	34,608
Less: Impact of AASB 16 Leases	(5,551)	-
Underlying trading EBIT	25,686	34,608

Environmental regulation

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

Information on Directors

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

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 of listed entities	None
Former directorships in last 3 years of listed entities	None
Responsibilities	Chair Non-Executive Director Member People Development and Remuneration Committee
Interests in shares and options	167,487,526 Ordinary Shares

Information on Directors (continued)

Sir Richard Michael Hill K.N.Z.M.	
Experience and expertise	<p>Sir Michael was appointed a Director of the Company on 9 June 2016.</p> <p>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.</p> <p>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.</p> <p>Sir Michael led the Group as Chairman from 1987 until December 2015.</p>
Other current directorships of listed entities	None
Former directorships in last 3 years of listed entities	None
Responsibilities	Non-Executive Director
Interests in shares and options	148,330,600 Ordinary Shares

Gary Warwick Smith B.Com, F.C.A., F.A.I.C.D.	
Experience and expertise	<p>Gary was appointed a Director of the Company upon incorporation on 24 February 2016.</p> <p>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.</p>
Other current directorships of listed entities	Flight Centre Travel Group Limited
Former directorships in last 3 years of listed entities	None
Responsibilities	<p>Non-Executive and Independent Director</p> <p>Chair Audit and Risk Management Committee</p> <p>Member People Development and Remuneration Committee</p>
Interests in shares and options	80,000 Ordinary Shares

Information on Directors (continued)

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 of listed entities	Air Canada
Former directorships in last 3 years of listed entities	None
Responsibilities	Non-Executive and Independent Director Chair People Development and Remuneration Committee Member Audit and Risk Management Committee
Interests in shares and options	1,513,640 Ordinary Shares

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.
Other current directorships of listed entities	None
Former directorships in last 3 years of listed entities	None
Responsibilities	Non-Executive and Independent Director Member Audit and Risk Management Committee
Interests in shares and options	651,745 Ordinary Shares

Information on Directors (continued)

Jacqueline Elizabeth Naylor	
Experience and expertise	Jacqueline was appointed a Director of the Company on 15 July 2020. Jacqueline has over thirty years' executive and board experience in retail, fashion and eCommerce. She has been instrumental in driving performance, organisational renewal and strategy in both ASX listed and privately held companies. In the digital space, Jacqueline has been a strategic advisor to Practicology, a retail commerce consultancy that focuses on digital acceleration and marketplace growth. She has also been a strategic consultant to household brands such as Billabong International, Bras N Things, and Apparel Group, helping them deliver improved financial and customer outcomes. As a retail specialist, Jacqueline has consulted for Ferrier Hodgson Restructuring and continues to consult to various private equity firms. Jacqueline was with the Just Group for fifteen years. She had responsibility for a P&L of over \$600m. She oversaw merchandising, marketing and brand strategies across an 800 retail store portfolio where key brands comprised Just Jeans, Jay Jays, Portmans, Jacqui E and Dotti. Jacqueline was appointed to the board of Just Group as an Executive Director following the company's acquisition by the Catalyst Group. Jacqueline is currently a board member of Myer and Cambridge Clothing and was previously a director of PAS Group Macpac, and the Virgin Australia Melbourne Fashion Festival.
Other current directorships	Myer Holdings Limited
Former directorships in last 3 years	None
Special responsibilities	Non-Executive and Independent Director
Interests in shares and options	Nil

Company secretaries

The Company has appointed two company secretaries, Andrew Lowe and Emily Bird.

Andrew Lowe, who is also the Chief Financial Officer of the Group, was appointed to the position of Company Secretary on 1 March 2019, having held that position previously (15 December 2017 to 22 January 2018). Andrew holds a Bachelor of Commerce, a Bachelor of Laws (Hons) and a Masters of Applied Finance, and is a qualified Chartered Accountant and a Chartered Taxation Adviser of the Taxation Institute of Australia. Andrew has extensive experience in finance and leadership roles across a range of listed corporate groups with Australian and offshore operations.

Emily Bird, who is also the General Counsel of the Group, was appointed to the position of Company Secretary on 31 July 2020. Emily joined Michael Hill in September 2019 as Senior Legal Counsel, and was appointed General Counsel & Company Secretary in July 2020. She holds a Bachelor of Laws, Bachelor of Arts (Psychology), Graduate Diploma in Legal Practice and Graduate Diploma in Applied Corporate Governance and Risk. Emily has broad legal experience with in-house roles at Lactalis Australia (formerly Parmalat Australia), Virgin Blue (now Virgin Australia) and a secondment at Tarong Energy (now Stanwell Corporation), having started her legal career at top-tier firm Clayton Utz.

Prior to Emily's appointment, Richard Amos was Company Secretary from 25 February 2020 to 31 July 2020.

Meetings of directors

The numbers of meetings of the Company's Board of Directors and of each Board committee held during the year ended 28 June 2020, 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	16	16	-	-	5	5
Sir R M Hill	16	16	-	-	-	-
G W Smith	16	16	4	4	5	5
R I Fyfe	15	16	4	4	5	5
J S Allis	16	16	4	4	-	-

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 2020 Michael Hill International Limited remuneration report, outlining key aspects of our remuneration policy and framework, and remuneration awarded during the 2020 financial year. The information provided in this remuneration report has been audited as required by section 308(3C) of the *Corporations Act 2001*.

Remuneration framework

Remuneration policy and link to performance

Our People Development and Remuneration Committee (the Committee) is a Committee of the Board and is made up of two independent non-executive Directors 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 obtains independent advice every three years on the appropriateness of remuneration practices of the Group given trends in comparative companies both locally and internationally, and the objectives of the Group's remuneration strategy.

Remuneration report (audited) (continued)

Remuneration policy and link to performance (continued)

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 senior executives, including key performance indicators and performance hurdles
- remuneration levels of executives, and
- non-executive Director fees.

The Committee is responsible for assessing performance against key performance indicators ('KPIs') and determining the short-term incentive ('STI') and long-term incentive ('LTI') to be paid. In the event of serious misconduct or a material misstatement in the Company's financial statements, the Committee can cancel or defer performance-based remuneration.

The Committee's objective is to ensure that remuneration policies and structures are fair and competitive and aligned with the long-term interests of the Company. The role of the Committee is set out in more detail in the Corporate Governance Statement (available on the Company's Investor Relations Centre website at investor.michaelhill.com).

Remuneration objectives

The following objectives inform the determination of remuneration related decisions:

Attract, Motivate and Retain Executive Talent	Reward the achievement of strategic objectives	Alignment to shareholder value creation
---	--	---

Key management personnel

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 2020 financial year, it was determined that the KMPs of Michael Hill International were:

- Chief Executive Officer (CEO) - Daniel Bracken
- Chief Financial Officer (CFO) - Andrew Lowe
- Chief Operating Officer (COO) - Andrea Slingsby

Vanessa Brennan (Chief Brand & Strategy Officer) became a KMP on 11 August 2020.

Executive remuneration framework

The executive remuneration structure has three components: Total Fixed Remuneration (TFR), STI and LTI.

Compensation levels are reviewed annually by the 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. Further details in relation to the review process including the most recent review, please refer to the Services from remuneration consultants section below.

Remuneration report (audited) (continued)

Executive remuneration framework (continued)

	TFR	STI	LTI
Determination	TFR is set based on relevant market relativities, reflecting responsibilities, performance, qualifications, experience and geographic location	On target performance is determined as a percentage of TFR and paid as cash	An issue of share rights is made to participants of the scheme, the quantum being a % of the STI earned
Delivery	Base salary plus any fixed elements including superannuation and leave entitlements	70% is directly aligned to achieving a Group EBIT target and other related items. 30% is based on achievement of individual performance and development plans	Alignment of executive incentives with the long term performance is achieved by way of a deferred remuneration component
Strategic Intent	TFR will generally be positioned at the median compared to relevant market based data. Expertise and performance in the role are also considerations	Performance incentive is directed to achieving Board approved targets, reflective of market circumstances	LTI is intended to reward executive KMP for sustainable long-term growth aligned to shareholders' interests

The weighting and potential of STI and LTI for KMP is:

	CEO	CFO	COO	Other KMP
Short Term Incentive Potential Value	70% of TFR	50% of TFR	50% of TFR	50% of TFR
Long Term Incentive Potential Value	50% of STI earned	30% of STI earned	30% of STI earned	30% of TFR

Remuneration levels are reviewed annually by the Committee through a process that considers individual, segment and overall performance of the Group.

During the 2019-2020 financial year, the performance linked components of compensation for KMP comprised approximately 11.1% of total payments to senior executives (FY19: 10.5%).

Temporary suspension of STI and LTI awards for senior executives including KMP

The Company was significantly impacted by the COVID-19 global pandemic, resulting in the closure of the entire store network for a period during March to June 2020, and standing down a large portion of our team members during that time. In response to those market conditions, the STI and LTI incentive programs for all senior executives, including KMP, were suspended from 1 April 2020 for the financial year. Senior executives including KMPs had already been awarded an STI payment in relation to the first half of the financial year in February 2020 prior to the COVID-19 related impacts being experienced by the Company and will receive the resulting LTI award in relation to that first half; however they will not receive any STI or LTI award for the second half of the financial year. The STI and LTI framework described below is expected to recommence for the 2021 financial year but this will remain subject to Committee and Board determination.

Remuneration report (audited) (continued)

Temporary reduction of base salary for senior executives including KMP

In addition to the temporary suspension of STI and LTI awards described above, each senior executive of the Company, including KMPs, voluntarily reduced their salaries by 20% for the period inclusive of April to June 2020.

Short-term incentive scheme

The short term incentive scheme is detailed in Performance and Development Plans ('PDPs') that are agreed at the start of the reporting period. The KPIs are in the form of a balanced scorecard, where performance against key deliverables across financial, strategy, business improvement, customer and people areas are measured.

The scheme is supported by 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. Performance against KPIs is formally measured on a biannual basis and informally in regular meetings. The 70% STI component is paid on an annual basis if the Group financial performance target and performance hurdle/s are met. The 30% STI for the individual KPI component is paid biannually post the performance review. The Committee review the PDPs of each Senior Executive to determine achievement, entitlement and eligibility for payment.

The policy and framework cascades from the CEO to Senior Executives and 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.

Long-term incentive scheme

The Company introduced a deferred compensation plan ('LTI') involving the grant of share rights to eligible participants in the 2015-16 financial year. This was approved by shareholders at the Company's Annual General Meeting held on 31 October 2016 and subsequently on 24 October 2019. Prior to that, 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 and share rights is conditional on continuing employment with the Group. No options were issued during the reporting period. Options previously issued are detailed in this report.

Under the LTI 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, except for KMPs whose relevant percentage rate of the STI payment earned is greater as detailed earlier in this report. 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. No exercise price is payable upon the exercise of any share right.

Feature	Description
Opportunity/ Allocation	30% of respective STI which is issued to the executive (or a different percentage rate for KMP as detailed earlier in this report) by way of share rights which are granted. Each share 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)

Consequences of performance on shareholder wealth

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

	2020	2019	2018	2017	2016
	\$'000	\$'000	\$'000	\$'000	\$'000
NPAT	3,059	16,498	1,557	29,654	16,771
NPAT from continuing operations	3,059	16,498	31,765	41,138	23,524
EBIT*	14,079	21,115	8,854	43,840	43,050
EBIT from continuing operations*	14,079	21,115	45,787	58,055	50,416
Underlying EBIT*	18,004	34,608	40,106	48,117	47,058
Dividends payments [^]	5,817	19,365	19,371	19,264	17,490
Share price at year end (NZ\$ 2016)	\$0.32	\$0.54	\$0.97	\$1.11	\$1.14
Return on shareholders equity	1.9%	9.4%	17.4%	20.9%	12.9%
Return on average total assets	0.7%	4.3%	8.2%	10.5%	6.3%

* EBIT and Underlying EBIT are Non-IFRS Information and are unaudited. Please refer to Non-IFRS Information on page 8 of the Directors Report for an explanation of Non-IFRS information and a reconciliation of EBIT and Underlying EBIT.

[^] The 2020 dividend payment relates to the FY19 final dividend.

EBIT is considered the primary financial performance target in setting the STI. Profit amounts for 2016 to 2020 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 IFRS as issued by the International Accounting Standards Board.

The overall level of remuneration takes into consideration 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, except as detailed below for the CEO.

Loans to key management personnel

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

Service contracts

It is the Group's policy that service contracts for KMP are unlimited in term but capable of termination on three months' notice (six months in the case of the CEO) and that the Group retains the right to terminate the contract immediately, by making payment equal to three months' pay in lieu of notice (or six months' in the case of the CEO). KMP 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 service contracts with all KMP (including the CEO) outline the components of remuneration but does not prescribe how remuneration levels are modified year to year. The Committee reviews remuneration levels each year to take into consideration 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 the remuneration policy.

Remuneration report (audited) (continued)

Services from remuneration consultants

The Committee engaged a remuneration consultant during the 2016 financial year to review the amount and elements of KMP remuneration and provide recommendations in relation thereto.

During the 2019 financial year, there was an internal review completed and the Committee were satisfied with the results of this review. The Company did not engage a remuneration consultant during the 2020 financial year.

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 for the 2019-20 year were \$100,419 per annum. Where a Director serves as Chair on the People Development and Remuneration Committee they are entitled to an additional payment of \$20,747 per annum. Where a Director serves as Chair on the Audit and Risk Committee they are entitled to an additional payment of \$31,120 per annum. It is the Company's policy to increase directors' fees annually at the commencement of each financial year of the Company, in accordance with the consumer price index. 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.

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

Temporary reduction in remuneration for non-executive Directors

In response to the COVID-19 global pandemic market conditions impacting the Company in the 2020 financial year, all non-executive director fees were reduced by 50% for the period from 1 April 2020 to 30 June 2020.

Director and KMP 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)

Director and KMP remuneration (continued)

	Short-term			Total	Long-term	Post-employment	Share-based payments			Total	Proportion of remuneration performance related %	Value of options as proportion of remuneration %
	Salary & fees \$	STI cash bonus \$	Non-monetary benefits (relocation) \$		Long service leave \$	Superannuation benefits \$	Termination benefits \$	Options and share rights \$				
Non-executive Directors												
Emma Jane Hill												
2020	170,849	-	-	170,849	-	-	-	-	170,849	-%	-%	
2019	197,047	-	-	197,047	-	-	-	-	197,047	-%	-%	
Sir Richard Michael Hill												
2020	97,989	-	-	97,989	-	-	-	-	97,989	-%	-%	
2019	98,523	-	-	98,523	-	-	-	-	98,523	-%	-%	
Gary Warwick Smith												
2020	104,327	-	-	104,327	-	9,911	-	-	114,238	-%	-%	
2019	117,628	-	-	117,628	-	11,175	-	-	128,803	-%	-%	
Robert Ian Fyfe												
2020	105,545	-	-	105,545	-	-	-	-	105,545	-%	-%	
2019	118,878	-	-	118,878	-	-	-	-	118,878	-%	-%	
Janine Suzanne Allis												
2020	78,594	-	-	78,594	-	7,467	-	-	86,061	-%	-%	
2019	89,799	-	-	89,799	-	8,533	-	-	98,332	-%	-%	
Total Director remuneration												
2020	557,304	-	-	557,304	-	17,378	-	-	574,682	-%	-%	
2019	621,875	-	-	621,875	-	19,708	-	-	641,583	-%	-%	
KMPs												
Daniel Bracken, CEO												
2020	905,142	134,092	-	1,039,234	10,980	25,481	-	15,324	1,091,019	12.29%	1.40%	
2019	594,726	69,300	19,970	683,996	9,327	15,385	-	-	708,708	9.78%	-%	
Phil Taylor, CEO (ceased 21 September 2018)												

Remuneration report (audited) (continued)

Director and KMP remuneration (continued)

	Short-term		Non-monetary benefits (relocation)	Total	Long-term	Post-employment	Share-based payments		Total	Proportion of remuneration performance related %	Value of options as proportion of remuneration %
	Salary & fees	STI cash bonus			Long service leave	Superannuation benefits	Termination benefits	Options and share rights			
	\$	\$	\$	\$	\$	\$	\$	\$	\$	%	%
2019 Andrew Lowe, CFO	192,680	58,508	-	251,188	8,830	6,731	-	71,794	338,543	17.28%	21.21%
2020	429,075	40,021	-	469,096	3,790	25,481	-	9,728	508,095	7.88%	1.91%
2019 Andrea Slingsby, COO	403,807	42,273	-	446,080	8,107	24,355	-	5,067	483,609	8.74%	1.05%
2020	456,372	32,681	-	489,053	5,862	25,481	-	2,688	523,084	6.25%	.51%
2019 Vanessa Brennan, CB&CO (ceased 9 January 2019)	217,708	25,900	-	243,608	3,597	11,538	-	-	258,743	10.01%	-%
2019 Matt Keays, CIO (ceased 9 January 2019)	236,298	37,014	-	273,312	3,637	12,981	-	3,963	293,893	12.59%	1.35%
2019 Galina Hirtzel, GESG (ceased 6 August 2018)	174,788	13,372	-	188,160	3,128	12,981	-	8,154	212,423	6.30%	3.84%
2019 Stewart Silk, GEHR (ceased 3 September 2018)	30,160	2,982	-	33,142	445	2,885	-	1,908	38,380	7.77%	4.97%
2019	44,962	-	-	44,962	625	4,327	-	2,714	52,628	-%	5.16%
Total KMP remuneration											
2020	1,790,589	206,794	-	1,997,383	20,632	76,443	-	27,740	2,122,198	9.74%	1.31%
2019	1,895,129	249,349	19,970	2,164,448	37,696	91,183	-	93,600	2,386,927	10.45%	3.92%
Total Director and KMP remuneration											
2020	2,347,893	206,794	-	2,554,687	20,632	93,821	-	27,740	2,696,880	7.67%	1.03%
2019	2,517,004	249,349	19,970	2,786,323	37,696	110,891	-	93,600	3,028,510	8.23%	3.09%

Remuneration report (audited) (continued)

Analysis of bonuses included in remuneration

Details of the short-term incentive cash bonuses awarded as remuneration to each KMP are detailed below.

KMP	Target bonus available	Included in remuneration \$	Amounts forfeited \$
Daniel Bracken	438,984	134,092	304,892
Andrew Lowe	148,460	40,021	108,439
Andrea Slingsby	164,970	32,681	132,289

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

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.

Unissued shares

As at the date of this report, there were 1,400,000 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

No options were granted to KMPs as compensation for the financial year.

Share rights

The number of share rights issued to KMP and senior executives during the last financial year was 286,294 share rights. Of these, share rights issued to KMP are set out below.

KMP	No. of share rights issued	Fair value per share right \$
Daniel Bracken	110,018	0.57
Andrew Lowe	33,463	0.57
Andrea Slingsby	19,301	0.57

Reconciliation of options and share rights held by KMP

No options are held by KMP.

Remuneration report (audited) (continued)

Additional statutory information (continued)

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

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 Number	Issued during year Number	Vested Number	Forfeited Number	Balance at end of year (unvested) Number
Daniel Bracken	-	110,018	-	-	110,018
Andrew Lowe	17,298	33,463	-	-	50,761
Andrea Slingsby	-	19,301	-	-	19,301
TOTAL	17,298	162,782	-	-	180,080

* Share rights relating to the current reporting period are anticipated to be granted in late 2020. The number of shares will depend on the Michael Hill International Limited's share price over the five days prior to the grant date.

Voting of shareholders at last year's annual general meeting

The Company received 99.2% of "For" votes on its remuneration report for the 2019 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.

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:

	2020 \$	2019 \$
Ernst & Young firm:		
Advisory fees	10,050	127,512
Total remuneration for non-audit services	10,050	127,512

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 24.

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 18 August 2020 in accordance with a resolution of Directors as required by section 298 of the *Corporations Act 2001*.

A handwritten signature in black ink that reads "E J Hill". The signature is written in a cursive, flowing style.

E J Hill
Chair

Brisbane
18 August 2020



**Building a better
working world**

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

As lead auditor for the audit of the financial report of Michael Hill International Limited for the financial year ended 28 June 2020, 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.

A handwritten signature in black ink that reads 'Ernst & Young' in a cursive, stylized font.

Ernst & Young

A handwritten signature in black ink that reads 'Alison de Groot' in a cursive, stylized font.

Alison de Groot
Partner
18 August 2020

The Directors present the consolidated financial statements of Michael Hill International Limited for the year ended 28 June 2020.

Michael Hill International Limited

ABN 25 610 937 598

Annual financial report - 28 June 2020

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Michael Hill International Limited
Consolidated statement of comprehensive income
For the year ended 28 June 2020

	Notes	2020 \$'000	2019 \$'000
Revenue from contracts with customers	5	492,060	569,500
Other income	6(a)	20,574	1,555
Cost of goods sold		(193,855)	(216,468)
Employee benefits expense	6(b)	(149,173)	(163,177)
Occupancy costs		(14,390)	(60,587)
Marketing expenses		(28,918)	(33,732)
Selling expenses		(18,701)	(24,636)
Impairment of property, plant and equipment	9(b)	(6,473)	(289)
Impairment of other assets		(1,582)	(1,823)
Depreciation and amortisation expense	6(b)	(55,611)	(19,366)
Loss on disposal of property, plant and equipment		(499)	(619)
Other expenses		(29,349)	(29,083)
Finance costs	6(b)	(9,598)	(2,464)
Profit before income tax		4,485	18,811
Income tax expense	7	(1,426)	(2,313)
Profit for the year		3,059	16,498
Other comprehensive income			
<i>Items that may be reclassified subsequently to profit or loss</i>			
Gains/(losses) on cash flow hedges	11(b)	434	(323)
Currency translation differences arising during the year	11(b)	(1,716)	4,911
Other comprehensive income for the year, net of tax		(1,282)	4,588
Total comprehensive income for the year		1,777	21,086
Total comprehensive income for the year is attributable to:			
Owners of Michael Hill International Limited		1,777	21,086
		Cents	Cents
Earnings per share for profit attributable to the ordinary equity holders of the Company:			
Basic earnings per share	21	0.79	4.26
Diluted earnings per share	21	0.79	4.25

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

Michael Hill International Limited
Consolidated statement of financial position
As at 28 June 2020

	Notes	2020 \$'000	2019 \$'000
ASSETS			
Current assets			
Cash and cash equivalents	8(a)	11,204	7,923
Trade and other receivables	8(b)	25,006	29,656
Contract assets	5(b)	625	701
Right of return assets	5(b)	108	291
Inventories	9(a)	178,742	179,503
Current tax receivables	9(e)	3,165	2,295
Other current assets		2,103	2,935
Total current assets		220,953	223,304
Non-current assets			
Trade and other receivables	8(b)	10,727	6,985
Property, plant and equipment	9(b)	45,405	63,213
Right-of-use assets	10(a)	123,911	-
Deferred tax assets	9(d)	74,468	67,708
Intangible assets	9(c)	24,429	15,439
Contract assets	5(b)	1,048	1,438
Other non-current assets		677	1,106
Total non-current assets		280,665	155,889
Total assets		501,618	379,193
LIABILITIES			
Current liabilities			
Trade and other payables	8(d)	64,472	44,548
Contract liabilities	5(b)	25,974	26,054
Derivative financial instruments	8(f)	34	468
Current tax liabilities	9(f)	1,445	1,367
Provisions	9(g)	24,949	31,441
Deferred revenue	9(h)	367	1,252
Lease liabilities	10(b)	42,164	-
Total current liabilities		159,405	105,130
Non-current liabilities			
Contract liabilities	5(b)	53,539	55,813
Borrowings	8(e)	10,681	32,704
Provisions	9(g)	8,339	6,947
Deferred revenue	9(h)	-	1,847
Lease liabilities	10(b)	115,848	-
Total non-current liabilities		188,407	97,311
Total liabilities		347,812	202,441
Net assets		153,806	176,752

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

Michael Hill International Limited
Consolidated statement of financial position
As at 28 June 2020
(continued)

	Notes	2020 \$'000	2019 \$'000
EQUITY			
Contributed equity	11(a)	11,016	10,984
Reserves	11(b)	4,420	5,805
Retained profits	11(b)	<u>138,370</u>	<u>159,963</u>
Total equity		<u>153,806</u>	<u>176,752</u>

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

Michael Hill International Limited
Consolidated statement of changes in equity
For the year ended 28 June 2020

Attributable to owners of Michael Hill International Limited						
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
Balance at 1 July 2018	10,266	1,369	605	(145)	162,830	174,925
Profit for the year	-	-	-	-	16,498	16,498
Currency translation differences	-	-	4,911	-	-	4,911
Currency forward contracts	8(f) -	-	-	(390)	-	(390)
Interest rate swaps	8(f) -	-	-	67	-	67
Total comprehensive income for the year	-	-	4,911	(323)	16,498	21,086
Transactions with members in their capacity as owners:						
Dividends paid	14(b)(i) -	-	-	-	(19,365)	(19,365)
Option expense through share based payments reserve	19(c) -	11	-	-	-	11
Issue of share capital on vesting of share rights	490	(490)	-	-	-	-
Transfer option reserve to retained earnings on forfeiture of options	11(a) 228	(228)	-	-	-	-
Share rights expense through share based payments reserve	19(c) -	95	-	-	-	95
	718	(612)	-	-	(19,365)	(19,259)
Balance at 30 June 2019	10,984	757	5,516	(468)	159,963	176,752

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

Michael Hill International Limited
Consolidated statement of changes in equity
For the year ended 28 June 2020
(continued)

Notes	Attributable to owners of Michael Hill International Limited					Total \$'000
	Contributed equity \$'000	Share based payments reserve \$'000	Foreign currency translation reserve \$'000	Cash flow hedge reserve \$'000	Retained profits \$'000	
Balance at 1 July 2019	10,984	757	5,516	(468)	159,963	176,752
Adjustment on adoption of AASB 16 (net of tax)	-	-	(43)	-	(13,019)	(13,062)
Restated total equity at the beginning of the financial year	10,984	757	5,473	(468)	146,944	163,690
Profit for the year	-	-	-	-	3,059	3,059
Currency translation differences	-	-	(1,716)	-	-	(1,716)
Currency forward contracts	-	-	-	145	-	145
Interest rate swaps	-	-	-	289	-	289
Total comprehensive income for the year	-	-	(1,716)	434	3,059	1,777
Transactions with members in their capacity as owners:						
Dividends paid/provided	-	-	-	-	(11,633)	(11,633)
Issue of share capital on vesting of share rights	32	(32)	-	-	-	-
Transfer option reserve to retained earnings on forfeiture of options	-	(166)	-	-	-	(166)
Share rights expense through share based payments reserve	-	166	-	-	-	166
Share rights forfeited	-	(28)	-	-	-	(28)
	32	(60)	-	-	(11,633)	(11,661)
Balance at 28 June 2020	11,016	697	3,757	(34)	138,370	153,806

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

Michael Hill International Limited
Consolidated cash flow statement
For the year ended 28 June 2020

	2020	2019
Notes	\$'000	\$'000
Cash flows from operating activities		
Receipts from customers (inclusive of GST and sales taxes)	547,258	618,416
Payments to suppliers and employees (inclusive of GST and sales taxes)	<u>(451,577)</u>	<u>(536,855)</u>
	95,681	81,561
Interest received	4	160
Other revenue	13,193	1,303
Interest paid	(2,261)	(2,474)
Income tax paid	(3,974)	(5,245)
Net GST and sales taxes paid	<u>(18,944)</u>	<u>(36,336)</u>
Net cash inflow from operating activities	<u>12(a) 83,699</u>	<u>38,969</u>
Cash flows from investing activities		
Proceeds from sale of property, plant and equipment	146	432
Payments for property, plant and equipment	9(b) (6,112)	(10,753)
Payments for intangible assets	9(c) (11,241)	(5,381)
Net cash (outflow) from investing activities	<u>(17,207)</u>	<u>(15,702)</u>
Cash flows from financing activities		
Proceeds from borrowings	70,500	128,800
Repayment of borrowings	(92,300)	(132,000)
Principal portion of lease payments	(35,520)	-
Dividends paid to Company's shareholders	14(b) (5,817)	(19,365)
Net cash (outflow) from financing activities	<u>(63,137)</u>	<u>(22,565)</u>
Net increase in cash and cash equivalents		
	3,355	702
Cash and cash equivalents at the beginning of the financial year	7,923	7,220
Effects of exchange rate changes on cash and cash equivalents	(74)	1
Cash and cash equivalents at the end of the financial year	<u>8(a) 11,204</u>	<u>7,923</u>

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 28 June 2020 were authorised for issue in accordance with a resolution of the Directors on 18 August 2020. Michael Hill International Limited (the Company or Parent) is a for profit company limited by shares incorporated in Australia. The Company is listed on the Australian Securities Exchange ('ASX') 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.

For the financial year the Group adopted a weekly 'retail calendar' closing each Sunday. This resulted in a change in reporting dates with a 52 week period ending on 28 June 2020.

(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.

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) Current versus non-current classification

The Group presents assets and liabilities in the statement of financial position based on current/non-current classification.

An asset is current when it is:

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

All other assets are classified as non-current.

A liability is current when it is:

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

The Group classifies all other liabilities as non-current.

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

2 Summary of significant accounting policies (continued)

(f) Other income

(i) Interest income

Interest income is recognised using the effective interest method.

(g) 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 where there is a legally enforceable right to offset current tax assets and liabilities and where 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 form a tax consolidation group. As a consequence, one income tax return is completed for the Australian tax group and is 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.

2 Summary of significant accounting policies (continued)

(h) 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.

(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, 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. Right-of-use assets are also incorporated into the calculation. Subsequent to an impairment occurring, if the recoverable amount from assets exceeds the carrying value, the impairment loss is reversed to the extent that it has been recognised.

The pre-tax discount rates used in determining the recoverable amount ranged between 9.4% and 12.8%, depending on the geographical segment of the assets.

(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) 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. Management review stock holdings based on recoverability at a product level and impair as appropriate.

(l) Financial instruments - initial recognition and subsequent measurement

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

2 Summary of significant accounting policies (continued)

(I) Financial instruments - initial recognition and subsequent measurement (continued)

(i) Financial assets

Initial recognition and measurement

Financial assets are classified, at initial recognition, as subsequently measured at amortised cost, fair value through Other Comprehensive Income (OCI), and fair value through profit or loss.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Group's business model for managing them. With the exception of trade receivables that do not contain a significant financing component, the Group initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs. Trade receivables that do not contain a significant financing component are measured at the transaction price determined under AASB 15. Refer to the accounting policies in section 5(c).

In order for a financial asset to be classified and measured at amortised cost or fair value through OCI, it needs to give rise to cash flows that are 'Solely Payments of Principal and Interest (SPPI)' on the principal amount outstanding. This assessment is referred to as the SPPI test and is performed at an instrument level.

The Group's business model for managing financial assets refers to how it manages its financial assets in order to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both.

Subsequent measurement

Whilst there are four categories, two are relevant in the current reporting period for the Group, being:

- Financial assets at amortised cost (debt instruments)
- Financial assets at fair value through profit or loss

Financial assets at amortised cost (debt instruments)

This category is the most relevant to the Group. The Group measures financial assets at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets at amortised cost are subsequently measured using the Effective Interest Rate (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

The Group's financial assets at amortised cost include trade receivables included under current and non-current financial assets.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading, financial assets designated upon initial recognition at fair value through profit or loss, or financial assets mandatorily required to be measured at fair value. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets with cash flows that are not solely payments of principal and interest are classified and measured at fair value through profit or loss, irrespective of the business model. Notwithstanding the criteria for debt instruments to be classified at amortised cost or at fair value through OCI, as described above, debt instruments may be designated at fair value through profit or loss on initial recognition if doing so eliminates, or significantly reduces, an accounting mismatch.

2 Summary of significant accounting policies (continued)

(I) Financial instruments - initial recognition and subsequent measurement (continued)

(i) Financial assets (continued)

Subsequent measurement (continued)

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

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in the statement of profit or loss.

This category includes derivative instruments which the Group had not irrevocably elected to classify at fair value through OCI.

Derecognition

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e. removed from the Group's consolidated statement of financial position) when:

- The rights to receive cash flows from the asset have expired; or
- The Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if, and to what extent, it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, nor transferred control of the asset, the Group continues to recognise the transferred asset to the extent of its continuing involvement. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Impairment of financial assets

Further disclosures relating to impairment of financial assets are also provided in the following notes:

- Changes in accounting policies and disclosures: Note 2(x)
- Trade receivables including contract assets: Note 8

The Group recognises an allowance for Expected Credit Losses (ECLs) for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive, discounted at an approximation of the original effective interest rate.

For trade receivables and contract assets, the Group applies a simplified approach in calculating ECLs. Therefore, the Group does not track changes in credit risk, but instead recognises a loss allowance based on lifetime ECLs at each reporting date. The Group has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment.

The Group considers a financial asset in default when contractual payments are past due. However, in certain cases, the Group may also consider a financial asset to be in default when internal or external information indicates that the Group is unlikely to receive the outstanding contractual amounts in full before taking into account any credit enhancements held by the Group. A financial asset is written off when there is no reasonable expectation of recovering the contractual cash flows.

2 Summary of significant accounting policies (continued)

(I) Financial instruments - initial recognition and subsequent measurement (continued)

(ii) Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, payables, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs.

The Group's financial liabilities include trade and other payables, loans and borrowings including bank overdrafts, and derivative financial instruments.

Subsequent measurement

The measurement of financial liabilities depends on their classification, as described below.

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are incurred for the purpose of repurchasing in the near term. This category also includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by AASB 9. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments.

Gains or losses on liabilities held for trading are recognised in the statement of profit or loss.

Financial liabilities designated upon initial recognition at fair value through profit or loss are designated at the initial date of recognition, and only if the criteria in AASB 9 are satisfied. The Group has not designated any financial liability as at fair value through profit or loss.

Loans and borrowings at amortised cost

This is the category most relevant to the Group. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the Effective Interest Rate (EIR) method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in the statement of profit or loss.

This category generally applies to interest-bearing loans and borrowings. For more information, refer to Note 8.

Derecognition

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the statement of profit or loss.

(iii) Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

2 Summary of significant accounting policies (continued)

(m) Derivatives and hedging activities

Initial recognition and subsequent measurement

The Group uses derivative financial instruments, such as forward currency contracts and interest rate swaps, to hedge its foreign currency risks and interest rate risks, respectively. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

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

- Fair value hedges when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment
- Cash flow hedges when hedging the exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction or the foreign currency risk in an unrecognised firm commitment
- Hedges of a net investment in a foreign operation

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which it wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge.

The documentation includes identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the Group will assess whether the hedging relationship meets the hedge effectiveness requirements (including the analysis of sources of hedge ineffectiveness and how the hedge ratio is determined). A hedging relationship qualifies for hedge accounting if it meets all of the following effectiveness requirements:

- There is 'an economic relationship' between the hedged item and the hedging instrument.
- The effect of credit risk does not 'dominate the value changes' that result from that economic relationship.
- The hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Group actually hedges and the quantity of the hedging instrument that the Group actually uses to hedge that quantity of hedged item.

Hedges that meet all the qualifying criteria for hedge accounting are accounted for, as described below.

Fair value hedge

The change in the fair value of a hedging instrument is recognised in the statement of profit or loss as other expense. The change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item and is also recognised in the statement of profit or loss as other expense.

If the hedged item is derecognised, the unamortised fair value is recognised immediately in profit or loss.

When an unrecognised firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognised as an asset or liability with a corresponding gain or loss recognised in profit or loss.

Cash flow hedge

The effective portion of the gain or loss on the hedging instrument is recognised in OCI in the cash flow hedge reserve, while any ineffective portion is recognised immediately in the statement of profit or loss. The cash flow hedge reserve is adjusted to the lower of the cumulative gain or loss on the hedging instrument and the cumulative change in fair value of the hedged item.

2 Summary of significant accounting policies (continued)

(m) Derivatives and hedging activities (continued)

Cash flow hedge (continued)

The Group uses forward currency contracts as hedges of its exposure to foreign currency risk in forecast transactions and firm commitments, as well as interest rate swaps for its exposure to volatility in interest rates. The ineffective portion relating to foreign currency contracts is recognised as other expense and the ineffective portion relating to interest rate swaps is recognised in other operating income or expenses. Refer to Note 13 for more details.

When forward contracts are used to hedge forecast transactions, the group designates the change in fair value of the forward contract related to the spot component as the hedging instrument. Gains or losses relating to the effective portion of the change in the spot component of the forward contracts are recognised in the cash flow hedge reserve within equity. The change in the forward element of the contract that relates to the hedged item ('aligned forward element') is recognised within OCI in the cash flow hedge reserve within equity. In some cases, the entity may designate the full change in fair value of the forward contract (including forward points) as the hedging instrument. In such cases, the gains or losses relating to the effective portion of the change in fair value of the entire forward contract are recognised in the cash flow hedge reserve within equity.

The amounts accumulated in OCI are accounted for, depending on the nature of the underlying hedged transaction. If the hedged transaction subsequently results in the recognition of a non-financial item, the amount accumulated in equity is removed from the separate component of equity and included in the initial cost or other carrying amount of the hedged asset or liability. This is not a reclassification adjustment and will not be recognised in OCI for the period. This also applies where the hedged forecast transaction of a non-financial asset or non-financial liability subsequently becomes a firm commitment for which fair value hedge accounting is applied.

For any other cash flow hedges, the amount accumulated in OCI is reclassified to profit or loss as a reclassification adjustment in the same period or periods during which the hedged cash flows affect profit or loss.

If cash flow hedge accounting is discontinued, the amount that has been accumulated in OCI must remain in accumulated OCI if the hedged future cash flows are still expected to occur. Otherwise, the amount will be immediately reclassified to profit or loss as a reclassification adjustment. After discontinuation, once the hedged cash flow occurs, any amount remaining in accumulated OCI must be accounted for depending on the nature of the underlying transaction as described above.

(n) Property, plant and equipment

All property, plant and equipment is stated at historical cost less depreciation and impairment. 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 9(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.

2 Summary of significant accounting policies (continued)

(o) Leases

The Group assesses at contract inception whether a contract is, or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

Group as a lessee

The Group applies a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets which are recognised in the profit or loss. The Group recognises lease liabilities to make lease payments and right-of-use assets representing the right to use the underlying assets.

(i) Right-of-use assets

The Group recognises right-of-use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Right-of-use assets are depreciated on a straight-line basis over the lease term.

The right-of-use assets are also subject to impairment. Refer to the accounting policies in Note 2(i).

If ownership of the leased asset transfers to the Group at the end of the lease term or the cost reflects the exercise of a purchase option, depreciation is calculated using the estimated useful life of the asset.

(ii) Lease liabilities

At commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Group and payments of penalties for terminating the lease, if the lease term reflects the Group exercising the option to terminate. Variable lease payments that do not depend on an index or a rate are recognised as expenses (unless they are incurred to produce inventories) in the period in which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Group uses its incremental borrowing rate at the lease commencement date because the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the lease payment (e.g., changes to future payments resulting from a change in an index or rate used to determine such lease payments) or a change in the assessment of an option to purchase the underlying asset.

The Group's lease liabilities are included at Note 10(b).

(iii) Short-term leases and leases of low-value assets

The Group applies the short-term lease recognition exemption to its short-term leases of machinery and equipment (i.e., those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). It also applies the lease of low-value assets recognition exemption to leases of office equipment that are considered to be low value. Lease payments on short-term leases and leases of low-value assets are recognised as expense on a straight-line basis over the lease term.

The Group adopted AASB 16 using the modified retrospective method of adoption from 1 July 2019. As a result, the results for the comparative period have been prepared on the basis of AASB 117 Leases.

2 Summary of significant accounting policies (continued)

(o) Leases (continued)

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. 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.

(p) 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.

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

(q) Government grants

Where government grants have been approved or received, the Group releases to 'Other income' as any prerequisite to the grant is met. This includes recognition and timing of expenses as required. During the year, the Group received grants in relation to wage subsidies in all three regions. These grants were recognised as income upon recognition of the corresponding employee benefit expense.

(r) Provisions

Provisions 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.

2 Summary of significant accounting policies (continued)

(r) Provisions (continued)

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.

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.

(s) 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.

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 have previously been issued to Executives of Michael Hill International Limited in accordance with the Company's constitution. The Board of Directors passed resolutions approving the issue of the options. The fair value of options granted was recognised as an employee benefit expense with a corresponding increase in equity.

The fair value was measured at grant date and is recognised over the period during which the employees become unconditionally entitled to the options. The fair value at grant date for options issued during prior financial years was 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. No options were granted during the 2020 financial year.

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)

2 Summary of significant accounting policies (continued)

(s) Employee benefits (continued)

(iii) Share-based payments (continued)

Employee options (continued)

- 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 period), and
- including the impact of any non-vesting conditions (eg the requirement for employees to save or holdings shares for a specific period 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-market 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.

Share rights

Share rights are granted to eligible senior executives in accordance with the Company's deferred compensation plan ('LTI'). The fair value of rights granted is recognised as an employee benefit expense with a corresponding increase in equity.

The fair value was measured at grant date and is recognised over the period during which the employees become unconditionally entitled to the rights. The valuation methodology to calculate fair value is detailed in Note 19(b).

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 share rights that are expected to vest based on the non-market 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 the share rights, the balance of the share-based payments reserve relating to those rights 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.

(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.

(t) 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.

2 Summary of significant accounting policies (continued)

(t) Contributed equity (continued)

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.

(u) 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.

(v) 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 (Note 21(d)).

(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.

(w) 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.

(x) Changes in accounting policies and disclosures

The Group applied AASB 16 *Leases* for the first time. The nature and effect of the changes as a result of adoption of these new accounting standards are described below.

Several other amendments and interpretations apply for the first time in 2020, but do not have an impact on the consolidated financial statements of the Group. The Group has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective.

2 Summary of significant accounting policies (continued)

(x) Changes in accounting policies and disclosures (continued)

AASB 16 Leases

The Group adopted AASB 16 using the modified retrospective method of adoption with the date of initial application of 1 July 2019. Under this method, the standard is applied retrospectively with the cumulative effect of initially applying the standard recognised at the date of initial application. The Group elected to use the transition practical expedient to not reassess whether a contract is, or contains a lease at 1 July 2019. Instead, the Group applied the standard only to contracts that were previously identified as leases applying AASB 117 and IFRIC 4 at the date of initial application.

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) SIC-27 Evaluating the Substance of Transactions involving the Legal Form of a Lease.

The effect of adoption of AASB 16 on the statement of financial position (increase/(decrease)) as at 1 July 2019:

	\$000
Assets	
Right-of-use assets	144,326
Property, plant and equipment	(3,060)
Trade and other receivables	963
Deferred tax assets	5,375
Total assets	147,604
Liabilities	
Trade and other payables	25
Deferred revenue	(2,810)
Lease liability	168,054
Provisions	(4,603)
Total liabilities	160,666
Equity	
Foreign currency translation	(43)
Retained earnings	(13,019)
Total equity	(13,062)

- Right-of-use assets of \$144,326 were recognised and presented separately in the statement of financial position.
- Property, plant and equipment reduced by \$3,060 in relation to fit out contributions received from landlords previously recognised as deferred revenue and recalculation of the make good asset.
- Deferred tax assets increased by \$5,375 due to the deferred tax impact of the changes in assets and liabilities.
- Lease liabilities of \$168,054 were recognised, with \$34,017 as a current liability and \$134,037 as a non-current liability.
- Deferred revenue of \$2,810 relating to lease incentive revenue was derecognised.
- Provisions of \$4,603 related to straight line leasing adjustments for previous operating leases were derecognised.
- The net effect of these adjustments had been adjusted to retained earnings (\$13,019).

Upon adoption of AASB 16, the Group applied a single recognition and measurement approach for all leases except for short-term leases and leases of low-value assets. The standard provided specific transition requirements and practical expedients, which have been applied by the Group.

2 Summary of significant accounting policies (continued)

(x) Changes in accounting policies and disclosures (continued)

Leases previously classified as finance leases

The Group did not change the initial carrying amounts of recognised assets and liabilities at the date of initial application for leases previously classified as finance leases (i.e., the right-of-use assets and lease liabilities equal the lease assets and liabilities recognised under AASB 17). The requirements of AASB 16 were applied to these leases from 1 July 2019.

Leases previously accounted for as operating leases

The Group recognised right-of-use assets and lease liabilities for those leases previously classified as operating leases, except for short-term leases and leases of low-value assets. The right-of-use assets for most leases were recognised based on the carrying amount as if the standard had always been applied, apart from the use of incremental borrowing rate at the date of initial application. In some leases, the right-of-use assets were recognised based on the amount equal to the lease liabilities, adjusted for any related prepaid and accrued lease payments previously recognised. Lease liabilities were recognised based on the present value of the remaining lease payments, discounted using the incremental borrowing rate at the date of initial application.

The Group also applied the available practical expedients wherein it:

- Used a single discount rate to a portfolio of leases with reasonably similar characteristics
- Relied on its assessment of whether leases are onerous immediately before the date of initial application
- Applied the short-term leases exemptions to leases with lease term that ends within 12 months of the date of initial application
- Excluded the initial direct costs from the measurement of the right-of-use asset at the date of initial application
- Used hindsight in determining the lease term where the contract contained options to extend or terminate the lease

COVID-19 related rent concessions

The Group has adopted the practical expedient for rent concessions negotiated as a consequence of COVID-19. This allows the company to elect not to account for changes in lease payments as a lease modification where a change in lease payments to the revised consideration are substantially the same or less than the consideration for the lease preceding the change, the reductions only affects payments which fall due before 30 June 2021 and there has been no substantive change in terms and conditions. Where the practical expedient has been applied, rent concessions are accounted for as a reduction in the right-of-use asset.

The lease liabilities as at 1 July 2019 can be reconciled to the operating lease commitments as of 30 June 2019, as follows:

	2020
	\$'000
Operating lease commitments disclosed as at 30 June 2019	155,070
Discounted using the group's incremental borrowing rate applicable to leases	121,642
Add: payments in optional renewal periods not included in lease commitments as at 30 June 2019	46,412
Lease liability recognised as at 1 July 2019	<u>168,054</u>

IFRIC Interpretation 23 Uncertainty over Income Tax Treatment

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of AASB 12 *Income Taxes*. It does not apply to taxes or levies outside the scope of AASB 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The Interpretation specifically addresses the following:

2 Summary of significant accounting policies (continued)

(x) Changes in accounting policies and disclosures (continued)

- Whether an entity considers uncertain tax treatments separately.
- The assumptions an entity makes about the examination of tax treatments by taxation authorities.
How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates.
- How an entity considers changes in facts and circumstances.

The Group determines whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments and uses the approach that better predicts the resolution of the uncertainty. The Group determined, based on its current tax position that it is probable that its tax treatments will be accepted by the taxation authorities.

The Interpretation did not have an impact on the consolidated financial statements of the Group.

3 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.

Impact of COVID-19

During the second half of the financial year, the Group was impacted by COVID-19. All bricks-and-mortar stores were temporarily closed in order to maintain the safety of our staff and customers or in response to government regulation. The Group also took the opportunity to assess how the stores would reopen. Safety initiatives were subsequently implemented and stores commenced reopening about five weeks after the initial temporary closures.

The uncertainty surrounding the trading environment for the Group has impacted management's approach of forecasting, modelling cash flows and supporting the recoverability of the Group's assets (see Note 2(i)). Further additional sensitivities were overlayed into provisions, such as Expected Credit Losses (ECL) on the Group's receivables (see Note 2(l)) and impairment assessment property, plant and equipment and right of use assets (see Note 9(b)(i)). Partially offsetting the closure of stores and subsequent loss of revenue, the Group received certain government grants (see Note 2(q)) and rental assistance from landlords with further rental negotiations continuing into FY21.

The Group continues to monitor the situation throughout the geographies in which it operates. Uncertainty remains as to the future impact of a 'second-wave' and the ability to operate bricks-and-mortar stores during this period. The Group continues to adhere to provincial and federal government guidance in relation to any future impacts which would temporarily close stores.

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 Black Scholes model. The related assumptions are detailed in Note 19. 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.

3 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 and office premises. The provision includes future cost estimates associated with dismantling and closure of stores and offices. The calculation of this provision requires assumptions such as discount rates, lease exit 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 9(g) Provisions.

Lease term of contracts with renewable options

The Group determines the lease term to be the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain that the option will be exercised. In assessing the likelihood of a lease option being exercised, the Group considers the costs of termination, the extent of any leasehold improvements, the strategic importance of the lease location and the current market rent for the stores.

Holdover leases

At any given point in time, there will be a number of property leases in holdover. These leases are accounted for under AASB 16 *Leases* when it is reasonably certain that the lease will be renewed or a new lease signed, and the terms and conditions of the lease are mutually agreed with the lessor.

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 (PCP) 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. The accounting policies and significant judgements are disclosed in Note 5c(iii) Revenue.

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

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.

3 Significant estimates, judgements and errors (continued)

(a) Significant estimates and judgements (continued)

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.

Provision for expected credit losses of trade receivables

The Group uses a provision matrix to calculate ECLs for trade receivables and contract assets. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by geography and customer rating).

The provision matrix is initially based on the Group's historical observed default rates. The Group will calibrate the matrix to adjust the historical credit loss experience with forward-looking information. For instance, if forecast economic conditions (i.e., gross domestic product) are expected to deteriorate over the next year. At every reporting date, the historical observed default rates are updated and changes in the forward-looking estimates are analysed.

The assessment of the correlation between historical observed default rates, forecast economic conditions and ECLs is a significant estimate. The amount of ECLs is sensitive to changes in circumstances and of forecast economic conditions. The Group's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future. The information about the ECLs on the Group's trade receivables is disclosed in Note 8(b).

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.

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4 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 Management team that are used to make strategic decisions. The Board and Executive Management team consider, organise and manage the business primarily from a geographic perspective, being the country of origin where the sale and service was performed.

The operating segments exclude the adjustments required under AASB 16 Leases and therefore operating lease expenses are included at a segment level.

The amounts provided to the Board and Executive Management 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 operations are 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 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.

4 Segment information (continued)

The Group report regional segments as set out in the table below. These results are prepared on a pre-AASB 16 Leases basis. An adjustment column representing the Group's entries due to AASB 16 Leases has been included for the purposes of comparability.

	Australia \$'000	New Zealand \$'000	Canada \$'000	Corporate & Other \$'000	Michael Hill Proforma \$'000	Adjustment [^] \$'000	Michael Hill \$'000
Segment information 2020							
Operating revenue	266,610	101,276	123,038	1,136	492,060	-	492,060
Gross profit	161,030	60,412	71,075	5,687	298,204	-	298,204
Gross profit %	60.4%	59.7%	57.8%		60.6%		60.6%
EBITDA*	35,102	22,554	3,471	(33,971)	27,156	42,534	69,690
Depreciation and Amortisation	(7,692)	(2,550)	(6,031)	(2,355)	(18,628)	(36,983)	(55,611)
Segment EBIT*	27,410	20,004	(2,560)	(36,326)	8,528	5,551	14,079
EBIT as a % of revenue	10.3%	19.8%	(2.1)%		1.7%		2.9%
Interest income	-	-	-	4	4	-	4
Finance costs	145	16	-	(2,131)	(1,970)	(7,628)	(9,598)
Net profit before tax	27,555	20,020	(2,560)	(38,453)	6,562	(2,077)	4,485
Income tax expense							(1,426)
Net profit after tax	27,555	20,020	(2,560)	(38,453)	6,562	(2,077)	3,059

	Australia \$'000	New Zealand \$'000	Canada \$'000	Corporate & Other \$'000	Michael Hill \$'000
Segment information 2019					
Operating revenue	313,587	112,964	140,402	2,547	569,500
Gross profit	194,052	68,655	85,131	5,194	353,032
Gross profit %	61.9%	60.8%	61.0%		62.0%
EBITDA*	41,421	25,159	16,001	(42,100)	40,481
Depreciation and Amortisation	(8,504)	(2,446)	(5,759)	(2,657)	(19,366)
Segment EBIT*	32,917	22,713	10,242	(44,757)	21,115
EBIT as a % of revenue	10.5%	20.1%	7.0%		3.7%
Interest income	-	1	-	159	160
Finance costs	42	(5)	-	(2,501)	(2,464)
Net profit before tax	32,959	22,709	10,242	(47,099)	18,811
Income tax expense					(2,313)
Net profit after tax	32,959	22,709	10,242	(47,099)	16,498

* EBIT and EBITDA are Non-IFRS Information and are unaudited. Please refer to Non-IFRS Information on page 8 of the Directors' Report for an explanation of Non-IFRS information and a reconciliation of EBIT from continuing operations and Normalised EBIT.

[^] This represents the impact of AASB 16 Leases on the Group.

The totals for the year ended 28 June 2020 include the impacts of AASB 16 Leases and cannot be compared directly to the totals for the year ended 30 June 2019.

5 Revenue

2020
\$'000 2019
\$'000

From contracts with customers:

Sales revenue

Revenue from sale of goods and repair services	460,393	533,282
Revenue from professional care plans	27,478	32,923
Interest and other revenue from in-house customer finance program	3,958	3,293
Lifetime Diamond Warranty	231	2
	492,060	569,500

(a) Disaggregation of revenue from contracts with customers

The Group derives revenue from the transfer of goods and services over time and at a point in time in the following major product lines and geographical regions:

2020	Australia \$'000	New Zealand \$'000	Canada \$'000	Corporate & other \$'000	Total \$'000
Timing of revenue recognition					
At a point in time	249,852	95,770	114,145	626	460,393
Over time	16,758	5,506	8,893	510	31,667
	266,610	101,276	123,038	1,136	492,060

2019	Australia \$'000	New Zealand \$'000	Canada \$'000	Corporate & other \$'000	Total \$'000
Timing of revenue recognition					
At a point in time	295,480	107,064	130,132	606	533,282
Over time	18,107	5,900	10,270	1,941	36,218
	313,587	112,964	140,402	2,547	569,500

(b) Assets and liabilities related to contracts with customers

	2020	2019
	\$'000	\$'000
Right of return assets	Notes 5(b)(i) 108	291
Deferred expenditure	5(b)(ii) 1,673	2,139
Total contract assets	1,781	2,430
Deferred service revenue	5(c)(i) 73,856	77,803
Deferred interest free revenue	5(c)(iv) 2,918	2,247
Rights of return liabilities	5(c)(v) 250	682
Lifetime Diamond Warranty	5(c)(vi) 2,489	1,135
Total contract liabilities	79,513	81,867

5 Revenue (continued)

(b) Assets and liabilities related to contracts with customers (continued)

(i) Revenue recognised in relation to contract liabilities

The following table shows how much of the revenue recognised in the current reporting year relates to carried-forward contract liabilities and how much relates to performance obligations that were satisfied in a prior year:

	2020	2019
	\$'000	\$'000
Revenue recognised that was included in the contract liability balance at the beginning of the year	22,300	26,229
Revenue recognised from performance obligations satisfied in previous years	-	1,770

(ii) Right of return assets

The following table shows contract assets recorded under our change of mind returns policy.

	2020	2019
	\$'000	\$'000
Carrying amount at the start of the year	291	424
Additional amounts recognised	114	270
Amounts incurred and charged	(291)	(424)
Exchange differences	(6)	21
Closing right of return asset	108	291

(iii) Assets recognised from costs to fulfil a contract

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. This is presented within other assets in the consolidated statement of financial position. For further information on the basis of calculation refer to Note 5c(iii).

	2020	2019
	\$'000	\$'000
Carrying amount at the start of the year	2,139	2,494
Additional amounts recognised	435	588
Amounts incurred and charged	(834)	(986)
Exchange differences	(67)	43
Total deferred expenditure	1,673	2,139

(c) Accounting policies and significant judgements

(i) Sale of goods

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.

(ii) Repair services

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

5 Revenue (continued)

(c) Accounting policies and significant judgements (continued)

(iii) *Deferred service revenue*

The Group offers a 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 based on expected services under the plans is used as a basis to establish the amount of service revenue to recognise in the consolidated statement of comprehensive income. During the financial year ended 28 June 2020, the Group did not recognise revenue for PCP services in Canada from 2 March 2020 to 28 June 2020 due to the inability to service customers from closure of stores. An amount of \$1.8m would have otherwise been attributed to this period.

(iv) *Deferred interest free revenue*

Deferred interest free 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) *Rights of return assets and liabilities*

Rights of return recognises the estimated returned sales under the Group's return policy, being 30 day change of mind in Australia and New Zealand and 60 day change of mind in Canada. Management estimates the returned sales based on historical sale return information and any recent trends that may suggest future claims could differ from historical amounts. For sales that are expected to be returned, the Group recognises a right of return liability. The associated inventory value for sales that are expected to be returned is recognised as a right of return asset.

(vi) *Lifetime Diamond Warranty*

LTDW is a warranty provided to customers with the purchase of jewellery items set with a diamond (excluding watches). This has been deemed a service-type warranty and is calculated with reference to the estimated value of service provided to customers and the stand-alone value of customers obtaining the service independently. Income in relation to the LTDW is recognised in line with the estimated pattern of customers utilising this service-type warranty.

6 Other income and expense items

(a) Other income

	Notes	2020 \$'000	2019 \$'000
Insurance recoveries		11	7
Net foreign exchange gains		2,382	92
Government grants		17,678	-
Other items		503	1,456
		20,574	1,555

6 Other income and expense items (continued)

(b) Breakdown of expenses by nature

		2020 \$'000	2019 \$'000
<i>Depreciation and amortisation</i>			
Depreciation on property, plant and equipment	9(b)	15,484	16,932
Depreciation on right-of-use assets		37,876	-
Total depreciation		53,360	16,932
 Total amortisation	 9(c)	 2,251	 2,434
 Total depreciation and amortisation		 55,611	 19,366

		2020 \$'000	2019 \$'000
<i>Finance costs</i>			
Interest on lease liabilities		7,628	-
Bank and interest charges		2,198	2,472
Interest on make good provision	9(g)	(228)	(8)
Total finance costs		9,598	2,464

Employee benefits expense

Employee wages		134,377	142,463
Employee wage on costs and post-retirement benefits		14,796	16,295
Provision for employee remediation		-	4,419
Total employee benefits expense		149,173	163,177

7 Income tax expense

(a) Income tax expense

		2020 \$'000	2019 \$'000
<i>Current tax</i>			
Current tax on profits for the year	Notes	2,488	5,265
Unrecognised tax losses utilised during the year		-	(468)
Adjustments for current tax of prior periods		650	(3,363)
Foreign income tax offsets not recognised		-	154
Total current tax expense		3,138	1,588

7 Income tax expense (continued)

(a) Income tax expense (continued)

	Notes	2020 \$'000	2019 \$'000
<i>Deferred income tax</i>			
(Increase) / Decrease in deferred tax assets	9(d)	(957)	356
Adjustments for deferred tax of prior periods		(755)	369
Total deferred tax expense/(benefit)		(1,712)	725
Income tax expense		1,426	2,313

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

	2020 \$'000	2019 \$'000
Profit from continuing operations before income tax expense	4,486	18,811
Tax at the Australian tax rate of 30.0% (2019 - 30.0%)	1,346	5,643
Tax effect of amounts which are not deductible (taxable) in calculating taxable income:		
Non deductible expenditure	279	269
Non-assessable intragroup markups	-	4
Sundry items	(211)	68
	1,414	5,984
Difference in overseas tax rates	208	(338)
Adjustments for current tax of prior periods	650	(3,363)
Adjustments for deferred tax of prior periods	(755)	369
Utilisation of tax losses not recognised	(91)	-
Unrecognised tax losses utilised during the year	-	(468)
Foreign income tax offset not recognised	-	154
Change in tax rate on deferred tax balance	-	(25)
Income tax expense	1,426	2,313
Income tax expense is attributable to:		
Profit from continuing operations	1,426	2,313

(c) Tax losses

	2020 \$'000	2019 \$'000
Unused United States tax losses for which no deferred tax asset has been recognised	35,745	33,647
Potential tax benefit @ 25.0%	8,936	10,094
Unused New Zealand tax losses for which no deferred tax asset has been recognised	2,651	2,708
Potential tax benefit @ 28.0%	742	758

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.

8 Financial assets and financial liabilities

The Group holds the following financial instruments:

	Notes	2020 \$'000	2019 \$'000
Financial assets			
Financial assets at amortised cost			
Cash and cash equivalents	8(a)	11,204	7,923
Trade receivables	8(b)	35,733	36,641
		46,937	44,564
Total current financial assets		36,210	37,579
Total non current financial assets		10,727	6,985
		46,937	44,564
Financial liabilities			
Liabilities at amortised cost			
Trade and other payables	8(d)	64,472	44,548
Borrowings	8(e)	10,681	32,704
Lease liabilities	10(b)	158,012	-
Derivative financial instruments			
Used for hedging	13(a)	34	468
		233,199	77,720
Total current financial liabilities		106,670	45,016
Total non current financial liabilities		126,529	32,704
		233,199	77,720

The Group's exposure to various risks associated with the financial instruments is discussed in Note 13. 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.

Derivatives not designated as hedging instruments reflect the change in fair value of those foreign exchange forward contracts that are not designated in hedge relationships, but are, nevertheless, intended to reduce the level of foreign currency risk for expected sales and purchases.

Derivatives designated as hedging instruments reflect the change in fair value of foreign exchange forward contracts, designated as cash flow hedges to hedge highly probable forecast purchases in US dollars (USD).

Debt instruments at amortised cost include trade receivables, trade payables and borrowings.

(a) Cash and cash equivalents

		2020 \$'000	2019 \$'000
Current assets			
Cash at bank and on hand		11,204	7,923

Interest rates for the bank accounts have been between 0.00% and 0.75% during the year (2019: between 0.00% and 1.15%).

8 Financial assets and financial liabilities (continued)

(b) Trade and other receivables

	Notes	2020 Current \$'000	2020 Non- current \$'000	Total \$'000	2019 Current \$'000	2019 Non- current \$'000	Total \$'000
Trade receivables		3,432	-	3,432	4,822	-	4,822
Provision for expected credit loss		(340)	-	(340)	(409)	-	(409)
	13(c)(ii)	<u>3,092</u>	<u>-</u>	<u>3,092</u>	<u>4,413</u>	<u>-</u>	<u>4,413</u>
In-house customer finance		14,576	11,021	25,597	20,145	7,337	27,482
Provision for expected credit loss		(1,143)	(294)	(1,437)	(928)	(352)	(1,280)
	13(c)(i)	<u>13,433</u>	<u>10,727</u>	<u>24,160</u>	<u>19,217</u>	<u>6,985</u>	<u>26,202</u>
Sundry debtors		8,481	-	8,481	6,026	-	6,026
		<u>25,006</u>	<u>10,727</u>	<u>35,733</u>	<u>29,656</u>	<u>6,985</u>	<u>36,641</u>

Further information relating to loans to related parties and key management personnel is set out in Note 18.

(i) Trade receivables

Trade receivables from sales made to customers through third party credit providers are non-interest bearing and are generally on 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 40 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. See Note 2(l)(i) for the accounting policy regarding the provision for expected credit losses.

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. In-house customer finance receivables are recognised net of significant financing components.

(iii) Impairment and risk exposure

Information about the impairment of trade receivables and the Group's exposure to credit risk and foreign currency risk can be found in Note 13(b) and 13(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.

8 Financial assets and financial liabilities (continued)

(c) Changes in liabilities arising from financing activities

(i) Movements

Non-current interest-bearing loans and liabilities 2020	Total \$'000
Carrying amount at start of year	32,704
Outwards cash flows	(92,300)
Inwards cash flows	70,500
Foreign exchange movements	(223)
Carrying amount at end of year	10,681
2019	Total \$'000
Carrying amount at start of year	35,213
Outwards cash flows	(132,000)
Inwards cash flows	128,800
Foreign exchange movements	691
Carrying amount at end of year	32,704

(d) Trade and other payables

	2020 \$'000	2019 \$'000
Current liabilities		
Trade payables	28,982	22,592
Annual leave liability	7,758	8,480
Accrued expenses	1,131	3,102
Other payables	26,601	10,374
	64,472	44,548

Trade payables and other payables are unsecured and are usually paid within 45 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.

(e) Borrowings

	2020			2019		
	Current \$'000	Non- current \$'000	Total \$'000	Current \$'000	Non- current \$'000	Total \$'000
Bank loans	-	10,681	10,681	-	32,704	32,704
Total secured borrowings	-	10,681	10,681	-	32,704	32,704

8 Financial assets and financial liabilities (continued)

(e) Borrowings (continued)

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. The agreement with ANZ on 26 June 2018 was updated to provide a \$70,000,000 multi option borrowing facility in line with the business requirements of the Group. At balance date, \$46,248,000 was available (2019: \$70,000,000), and of that, \$10,681,000 was utilised (2019: \$32,704,000).

The Group also has access to various uncommitted credit facility lines serving working capital needs that, at balance date, totalled \$1,935,000 (2019: \$1,955,000). No amounts were drawn under these credit facility lines as at balance date.

(f) 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.

Recurring fair value measurements		Level 1	Level 2	Level 3	Total
At 28 June 2020		\$'000	\$'000	\$'000	\$'000
	Notes				
Financial assets					
Total financial assets		-	-	-	-
Financial Liabilities					
Derivatives used for hedging					
Interest rate swaps	13(a)	-	34	-	34
Total financial liabilities		-	34	-	34
Recurring fair value measurements		Level 1	Level 2	Level 3	Total
At 30 June 2019		\$'000	\$'000	\$'000	\$'000
	Notes				
Financial assets					
Total financial assets		-	-	-	-
Financial Liabilities					
Derivatives designated as hedging instruments					
Foreign exchange contracts	13(a)	-	145	-	145
Interest rate swaps	13(a)	-	323	-	323
Total financial liabilities		-	468	-	468

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

8 Financial assets and financial liabilities (continued)

(f) Recognised fair value measurements (continued)

(i) Fair value hierarchy (continued)

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.

9 Non-financial assets and liabilities

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

(a) Inventories

	2020 \$'000	2019 \$'000
Raw materials	6,313	6,732
Finished goods	174,758	176,670
Packaging and other consumables	3,335	2,033
Provision for impairment	(5,664)	(5,932)
	178,742	179,503

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 2018						
Cost or fair value	38,744	34,667	569	81,642	13,958	169,580
Accumulated depreciation	(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
Year ended 30 June 2019						
Opening net book amount	12,893	11,567	253	35,219	6,734	66,666
Exchange differences	284	256	5	1,373	214	2,132
Additions	2,618	1,695	-	4,952	1,488	10,753
Additions - make good	-	-	-	1,794	-	1,794
Disposals	(762)	(24)	(59)	(20)	(46)	(911)
Transfers	13	-	-	(13)	-	-
Depreciation charge	(3,929)	(3,500)	(110)	(7,429)	(1,964)	(16,932)
Impairment loss (i)	(211)	(12)	-	(64)	(2)	(289)
Closing net book amount	10,906	9,982	89	35,812	6,424	63,213

9 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 2019						
Cost or fair value	32,867	33,153	366	85,774	15,449	167,609
Accumulated depreciation	(21,961)	(23,171)	(277)	(49,962)	(9,025)	(104,396)
Net book amount	10,906	9,982	89	35,812	6,424	63,213
Year ended 28 June 2020						
Opening net book amount	10,906	9,982	89	35,812	6,424	63,213
Adjustment for change in accounting policy	-	-	-	(2,653)	-	(2,653)
Exchange differences	(48)	(52)	-	(265)	19	(346)
Additions	1,852	1,819	-	1,376	1,065	6,112
Additions - make good	-	-	-	1,757	-	1,757
Disposals	(190)	(119)	(38)	(240)	(131)	(718)
Transfers	90	253	-	(346)	-	(3)
Depreciation charge	(3,617)	(3,373)	(35)	(6,540)	(1,919)	(15,484)
Impairment loss (i)	(738)	(404)	-	(2,016)	(3,315)	(6,473)
Closing net book amount	8,255	8,106	16	26,885	2,143	45,405
At 28 June 2020						
Cost	32,831	34,431	47	78,164	15,197	160,670
Accumulated depreciation and impairment	(24,576)	(26,325)	(31)	(51,279)	(13,054)	(115,265)
Net book amount	8,255	8,106	16	26,885	2,143	45,405

(i) Impairment loss

As per the Group's accounting policies, the Group impairs assets where the recoverable amount is less than the carrying amount. This also includes assets held at stores facing closure. Any assets held at an impaired store that are able to redeployed throughout the Group are not impaired.

Impairment indicators were identified due to the impact of COVID-19 which resulted in temporary store closures and reduction in sales. The Group treats each store as a separate cash-generating unit for impairment testing of property, plant and equipment and right of use assets. Key assumptions used in calculating the Value in Use for impairment assessment purposes factor in any immediately visible impact on store sales and performance from COVID-19 as disclosed in Note 3(a).

(ii) Depreciation methods and useful lives

Depreciation is calculated using the straight-line method to allocate the cost or revalued amounts of the assets, 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

9 Non-financial assets and liabilities (continued)

(c) Intangible assets

	Patents, trademarks and other rights \$'000	Computer software \$'000	Total \$'000
At 1 July 2018			
Cost	79	28,941	29,020
Accumulated amortisation	-	(16,394)	(16,394)
Net book amount	79	12,547	12,626
Year ended 30 June 2019			
Opening net book amount	79	12,547	12,626
Exchange differences	-	6	6
Additions	-	5,381	5,381
Disposals	-	(140)	(140)
Amortisation charge	-	(2,434)	(2,434)
Closing net book amount	79	15,360	15,439
At 30 June 2019			
Cost	79	30,852	30,931
Accumulated amortisation	-	(15,492)	(15,492)
Net book amount	79	15,360	15,439
Year ended 28 June 2020			
Opening net book amount	79	15,360	15,439
Additions	-	11,241	11,241
Category transfers	-	3	3
Impairment charge	-	(3)	(3)
Amortisation charge	-	(2,251)	(2,251)
Closing net book amount	79	24,350	24,429
At 28 June 2020			
Cost	79	39,383	39,462
Accumulated amortisation	-	(15,033)	(15,033)
Net book amount	79	24,350	24,429

9 Non-financial assets and liabilities (continued)

(d) Deferred tax balances

(i) Deferred tax assets

	2020 \$'000	2019 \$'000
The balance comprises temporary differences attributable to:		
Doubtful debts	485	450
Fixed assets and intangibles	8,190	5,655
Intangible assets from intellectual property transfer	22,723	24,593
Deferred expenditure	(478)	(601)
Prepayments	(19)	(21)
Deferred service revenue	235	4,223
Unearned income	-	1,738
Leases	7,487	-
Provisions	20,757	16,926
Unrealised foreign exchange losses	(317)	(156)
Sundry items	(511)	989
Inventories	15,916	13,912
Net deferred tax assets	74,468	67,708
Expected settlement:		
Deferred tax assets expected to be recovered within 12 months	39,585	31,180
Deferred tax assets expected to be recovered after more than 12 months	34,883	36,528
	74,468	67,708
Movements:		
Opening balance at 1 July	67,708	68,022
Credited / (charged) to the income statement	957	(356)
Adjustment on adoption of AASB 16	5,375	-
Prior year adjustment	755	(369)
Foreign exchange differences	(327)	411
Closing balance at 30 June	74,468	67,708

(e) Current tax receivables

	2020 \$'000	2019 \$'000
Current tax receivables	3,165	2,295

(f) Current tax liabilities

	2020 \$'000	2019 \$'000
Current tax liabilities	1,445	1,367

9 Non-financial assets and liabilities (continued)

(f) Current tax liabilities (continued)

(g) Provisions

	2020			2019		
	Current \$'000	Non- current \$'000	Total \$'000	Current \$'000 Restated	Non- current \$'000	Total \$'000
Employee benefits (i)	20,599	1,776	22,375	28,140	2,069	30,209
Assurance-type warranties (i)	1,405	-	1,405	1,674	-	1,674
Make good provision (i)	260	6,563	6,823	133	4,878	5,011
Restructuring costs (i)	2,325	-	2,325	1,014	-	1,014
Diamond warranty (i)	360	-	360	480	-	480
	24,949	8,339	33,288	31,441	6,947	38,388

(i) Information about individual provisions and significant estimates

Employee benefits

Employee benefits includes provision for long service leave, revaluation of employee benefits in New Zealand and the provision for remediation. 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 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.

Assurance-type warranties

Provision is made for the estimated sale returns for the Group's return policies, being 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.

9 Non-financial assets and liabilities (continued)

(g) Provisions (continued)

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

(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 staffing exit costs from business structure changes.

Restructuring provisions are recognised only when the Group has a constructive obligation, which is when:

- there is a detailed formal plan that identifies the business or part of the business concerned, the location and number of employees affected, the detailed estimate of the associated costs, and the timeline; and
- the employees affected have been notified of the plan's main features.

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.

(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	Total \$'000
Carrying amount at start of year	30,209	1,014	1,674	5,011	480	38,388
Additional provisions recognised	1,940	1,995	1,405	2,280	-	7,620
Amounts incurred and charged	(9,773)	(682)	(1,663)	(441)	(120)	(12,679)
Exchange differences	(1)	(2)	(11)	(27)	-	(41)
Carrying amount at end of year	<u>22,375</u>	<u>2,325</u>	<u>1,405</u>	<u>6,823</u>	<u>360</u>	<u>33,288</u>

(h) Deferred revenue

	Current \$'000	2020 Non- current \$'000	Total \$'000	Current \$'000	2019 Non- current \$'000	Total \$'000
Lease incentive income	-	-	-	962	1,847	2,809
Sundry Deferred Revenue	367	-	367	290	-	290
	<u>367</u>	<u>-</u>	<u>367</u>	<u>1,252</u>	<u>1,847</u>	<u>3,099</u>

10 Leases

This note provides information for leases where the Group is a lessee.

(a) Right-of-use assets

	2020 \$'000
Right-of-use assets	
Right-of-use assets	162,380
Less: Accumulated impairment	(815)
Less: Accumulated depreciation	(37,654)
	123,911

Reconciliation of right-of-use assets

	2020 \$'000
Opening right-of-use asset on adoption of AASB 16 on 1 July 2019	142,833
Additional right-of-use assets relating to leases entered into during the year	21,702
Lease modifications agreed during the year	(126)
Depreciation	(37,876)
Reduction in right-of-use assets as a consequence of COVID-19 on rent concessions	(2,033)
Impairment of right-of-use assets	(815)
Foreign currency translation	226
Balance at 28 June 2020	123,911

(b) Lease liabilities

Lease liabilities	
Current	42,164
Non-current	115,848
	158,012

Reconciliation of lease liabilities

	2020 \$'000
Opening lease liabilities recognised on adoption of AASB 16 on 1 July 2019	166,322
Additional leases entered into during the year	21,671
Lease modifications during the year	14
Net reduction in future lease payments agreed as a consequence of COVID-19 on rent concessions	(2,033)
Interest accrued	7,628
Lease repayments	(35,520)
Foreign currency translation	(70)
Balance at 28 June 2020	158,012

The incremental borrowing rate used in determining the lease liability ranged between 1.85% and 6.95%.

10 Leases (continued)

(c) Impairment loss

As per the Group's accounting policies, the Group impairs assets where the recoverable amount is less than the carrying amount.

11 Contributed equity

(a) Share capital

	2020 Shares	2019 Shares	2020 \$'000	2019 \$'000
Ordinary shares - fully paid	387,769,105	387,750,000	11,016	10,984
Total share capital	387,769,105	387,750,000	11,016	10,984

(i) Movements in ordinary shares:

Details	Notes	Number of shares	Total \$'000
Opening balance 1 July 2018		387,438,513	10,266
Options forfeited	11(a)(ii)	-	228
Rights converted	11(a)(iii)	311,487	490
Balance 30 June 2019		387,750,000	10,984
Rights converted	11(a)(iii)	19,105	32
Balance 28 June 2020		387,769,105	11,016

(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 on 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 19(a).

(iv) Rights issue

Information relating to share rights issued under the Company's deferred compensation plan, including details of rights issued, exercised and lapsed during the financial year and rights outstanding at the end of the financial year, is set out in Note 19(b).

(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(m). Amounts are reclassified to profit or loss when the associated hedged transaction affects profit or loss.

11 Contributed equity (continued)

(b) Reserves and retained profits (continued)

(i) Nature and purpose of other reserves (continued)

Share-based payments

The share-based payments reserve is used to recognise the value of equity-settled share-based payments provided to employees, including key management personnel, as part of their remunerations. Refer to Note 19 for further details of these plans.

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.

12 Cash flow information

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

	Notes	2020 \$'000	2019 \$'000
Profit for the year		3,059	16,498
Adjustment for			
Depreciation of property, plant and equipment	6(b)	15,484	16,932
Depreciation of right-of-use asset		37,876	-
Amortisation	6(b)	2,251	2,434
Impairment - property, plant and equipment		6,473	289
Impairment - other assets		1,579	1,823
Impairment - intangibles		3	-
Non-cash employee benefits expense - share-based payments		(25)	106
Make good interest		(228)	(8)
Net loss on sale of non-current assets		442	619
Net exchange differences		1,143	(9)
Change in operating assets and liabilities:			
(Increase) / decrease in trade and other receivables		1,490	(8,419)
(Increase) / decrease in inventories		(206)	12,102
(Increase) / decrease in deferred tax assets		(1,430)	227
(Increase) / decrease in other non current assets		2,324	(309)
(Increase) / decrease in other current assets		89	896
(Decrease) / increase in trade and other payables		12,987	(485)
(Decrease) / increase in current tax liabilities		8,509	(3,517)
(Decrease) / increase in provisions		(6,121)	(110)
(Decrease) / increase in deferred revenue		(2,000)	(100)
Net cash inflow from operating activities		83,699	38,969

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.

13	Financial risk management	72
14	Capital management	78

13 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

The Group is exposed to certain risks relating to its ongoing business operations. The primary risks managed using derivative instruments are foreign currency risk and interest rate risk.

The Group's risk management strategy and how it is applied to manage risk are explained below.

(i) Classification of derivatives

Derivatives are only used for economic hedging purposes and not as speculative investments. However, where derivatives do not meet the hedge accounting criteria, they are classified as 'held for trading' for accounting purposes and are accounted for at fair value through profit or loss. They are presented as current assets or liabilities to the extent 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(m). Further information about the derivatives used by the Group is provided in Note 13(b) below.

13 Financial risk management (continued)

(a) Derivatives (continued)

Derivatives not designated as hedging instruments

The Group uses foreign currency-denominated borrowings and foreign exchange forward contracts to manage some of its transaction exposures. The foreign exchange forward contracts are not designated as cash flow hedges and are entered into for periods consistent with foreign currency exposure of the underlying transactions, generally from one to six months.

(ii) Fair value measurements

For information about the methods and assumptions used in determining the fair value of derivatives please refer to Note 8(f).

(iii) Hedging reserves

The Group's hedging reserves are disclosed in the statement of changes in equity.

There were no reclassifications from the cash flow hedge reserve to profit or loss during the year in relation to the foreign currency forwards and options.

(iv) Amounts recognised in profit or loss

In addition to the amounts disclosed in the reconciliation of hedging reserves above, the following amounts were recognised in profit or loss in relation to derivatives:

	2020	2019
	\$'000	\$'000
Net foreign exchange gain/(loss) included in other gains/(losses)	69	92

Hedge ineffectiveness

Hedge effectiveness is determined at the inception of the hedge relationship, and through periodic prospective effectiveness assessments to ensure that an economic relationship exists between the hedged item and hedging instrument.

For hedges of interest rate risk, the Group enters into hedge relationships where the critical terms of the hedging instrument match exactly with the terms of the hedged item. The Group therefore performs a qualitative assessment of effectiveness. If changes in circumstances affect the terms of the hedged item such that the critical terms no longer match exactly with the critical terms of the hedging instrument, the Group uses the hypothetical derivative method to assess effectiveness. It may occur due to:

- the credit value/debit value adjustment on the interest rate swaps which is not matched by the loan, and
- differences in critical terms between the interest rate swaps and loans.

There was no recognised ineffectiveness during 2020 or 2019 in relation to the interest rate swaps.

(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.

13 Financial risk management (continued)

(b) Market risk (continued)

(i) Foreign exchange risk (continued)

Exposure

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

	28 June 2020			30 June 2019		
	USD \$'000	NZD \$'000	CAD \$'000	USD \$'000	NZD \$'000	CAD \$'000
Cash and cash equivalents	36	64	43	16	33	28
Trade receivables	500	-	-	1,590	2	-
Trade payables	7,539	-	2	1,567	-	113
Forward exchange contracts:						
Buy foreign currency (cash flow hedges)	-	-	-	12,000	-	-

Sensitivity

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

Most trade payables are repaid within 45 days so there is minimal equity impact arising from foreign currency exposures. The below calculations are the impact on the Mark to Market (MTM) for the Foreign Exchange Contracts (FEC) hedged. These are not designated as cash flow hedges, therefore the impact will be on pre-tax profit.

	Impact on pre-tax profit		Impact on other components of equity	
	2020 \$'000	2019 \$'000	2020 \$'000	2019 \$'000
USD Trade payables				
US/\$ exchange rate - increase 10%*	1,680	-	-	1,697
US/\$ exchange rate - decrease 10%*	(2,205)	-	-	(1,752)

(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 borrowings to interest rate changes and the contractual re-pricing dates of the borrowings at the end of the reporting year are as follows:

13 Financial risk management (continued)

(b) Market risk (continued)

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

	2020	% of total	2019	% of total
	\$'000	loans	\$'000	loans
Variable rate borrowings	10,681	100.0%	32,704	100.0%
	10,681	100.0%	32,704	100.0%

An analysis by maturities is provided in Note 13(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.

Instruments used by the group

Swaps in place cover approximately 46.8% (2019: 76.4%) of the variable rate principal outstanding.

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

	28 June 2020		30 June 2019	
	Weighted average interest rate	Balance	Weighted average interest rate	Balance
	%	\$'000	%	\$'000
Bank overdrafts and bank loans	1.88%	10,681	2.54%	32,704
Interest rate swaps (notional principal amount)	4.63%	5,000	3.91%	25,000
Net exposure to cash flow interest rate risk		5,681		7,704

An analysis by maturities is provided in note 13(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	
	2020	2019	2020	2019
	\$'000	\$'000	\$'000	\$'000
Interest rates - increase by 100 basis points (100 bps) *	(107)	(109)	(15)	(2)
Interest rates - decrease by 100 basis points (100 bps) *	107	109	(36)	2

* 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%

13 Financial risk management (continued)

(b) Market risk (continued)

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

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

In-house customer finance was established in Canada 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 8(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:

	2020	2019
	\$'000	\$'000
Performing:		
Current, aged 0 - 30 days	24,651	26,511
Past due, 31 - 90 days	491	508
Non performing:		
Past due, aged more than 90 days	455	463
	25,597	27,482

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

	2020	2019
	\$'000	\$'000
Opening balance	1,280	1,430
Amounts written off	(2,093)	(2,263)
Additional provisions recognised	2,270	2,028
Exchange differences	(20)	85
	1,437	1,280

(ii) *Impaired trade receivables*

The ageing of these receivables is as follows:

	2020	2019
	\$'000	\$'000
0 - 30 days	3,027	3,677
31 - 60 days	199	574
61 - 90 days	(2)	171
91 + days	208	400
	3,432	4,822

13 Financial risk management (continued)

(c) Credit risk (continued)

(ii) Impaired trade receivables (continued)

The amount written off during the period amounted to \$193,000 (2019: \$615,000).

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

	2020	2019
	\$'000	\$'000
At 1 July	409	819
Amounts written off	(193)	(615)
Additional provisions recognised	125	201
Exchange differences	(1)	4
At 28 June	340	409

(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. The agreement with ANZ on 26 June 2018 was updated to provide a \$70,000,000 multi option borrowing facility in line with the business requirements of the Group and the facility limit available was reduced in line with rents unpaid. At balance date, \$46,248,000 was available. The Group had access to the following undrawn borrowing facilities at the end of the reporting year:

	2020	2019
	\$'000	\$'000
Floating rate		
- Expiring beyond one year (bank overdrafts)	1,935	1,955
- Expiring beyond one year (bank loans)	46,248	32,704
	48,183	34,659

(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.

13 Financial risk management (continued)

(d) Liquidity risk (continued)

(ii) Maturities of financial liabilities (continued)

Contractual maturities of financial liabilities	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
At 28 June 2020						
Non-derivatives						
Lease liabilities	10,065	1,168	9,954	59,411	77,414	158,012
Trade payables	64,964	-	-	-	-	64,964
Borrowings	-	-	10,681	-	-	10,681
Total non-derivatives	75,029	1,168	20,635	59,411	77,414	233,657
Derivatives						
Gross settled (forward foreign exchange contracts)	69	-	-	-	-	69
Net Settled (Interest rate swaps)	34	-	-	-	-	34
	103	-	-	-	-	103
At 30 June 2019						
Non-derivatives						
Trade payables	44,548	-	-	-	-	44,548
Borrowings	-	-	32,704	-	-	32,704
Total non-derivatives	44,548	-	32,704	-	-	77,252
Derivatives						
Gross settled (forward foreign exchange contracts)	145	-	-	-	-	145
Net Settled (Interest rate swaps)	52	158	113	-	-	323
	197	158	113	-	-	468

14 Capital management

(a) Risk management

The Group's objectives when managing capital are to:

- safeguard its ability to continue as a going concern, so that it 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 EBIT fixed cover charge ratio, consolidated debt to EBITDA, consolidated debt to capitalisation, and consolidated debt to inventory. There have been no breaches of these covenants and the Group continues to collaborate with the external financing partners as required.

14 Capital management (continued)

(b) Dividends

(i) Ordinary shares

	2020	2019
	\$'000	\$'000
Final dividend for the year ended 30 June 2019 of 1.5 cents (2018: 2.5 cents) per fully paid share paid on 27 September 2019 (2019: 28 September 2018).	5,817	9,679
Interim dividend for the year ended 28 June 2020 of 1.5 cents (2019: 2.5 cents) deferred for payment (2019: 27 March 2019)*.	5,816	9,686
	11,633	19,365

*Interim dividend for the year ended 28 June 2020 of 1.5c was declared. Subsequent to the shares trading ex dividend, but prior to payment date, the interim dividend payment was deferred to 30 September 2021.

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

	2020	2019
	\$'000	\$'000
No final dividend has been declared by the Directors for the year ended 28 June 2020 (2019: AU 1.5 cents).	-	5,816

(iii) Franking and imputation credits

	Consolidated entity	
	2020	2019
	\$'000	\$'000
Franking credits available for subsequent reporting periods based on a tax rate of 30.0% (2019: 30.0%)	2,174	1,487
Imputation credits (NZ\$) available for subsequent reporting periods based on the New Zealand tax rate of 28.0% (2019: 28.0%)	18,474	17,885

The dividend paid during the current financial period and corresponding previous financial period were fully imputed and not franked.

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.

The declared interim dividend, which has been deferred, was unfranked and therefore will not reduce the franking account.

The impact on the imputation credit account of the interim dividend declared but deferred is estimated to be a reduction in the imputation credit account of NZ\$2,418,000 (2019: NZ\$2,381,000). The amount of imputation credits is dependant on the NZD exchange rate at the time of the dividend.

15 Interests in other entities

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	
		2020 %	2019 %
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
Medley Jewellery Pty Ltd (formally Emma & Roe Online Pty Ltd)	Australia	100	100
Durante Holdings Pty Limited	Australia	100	100
Michael Hill New Zealand 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 the New Zealand stock exchange at 28 June 2020 of \$33,000 (30 June 2019: \$137,000).

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 over and above already provided in the financial statements 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 Events occurring after the reporting period

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.

18 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.

(b) Key management personnel compensation

	2020	2019
	\$	\$
Short-term employee benefits	1,997,383	2,164,448
Long-term benefits	20,632	37,696
Post-employment benefits	76,443	91,183
Share-based payments	27,740	93,600
	<u>2,122,198</u>	<u>2,386,927</u>

Detailed remuneration disclosures are provided in the remuneration report on pages 13 to 22.

(c) Transactions with other related parties

The following transactions occurred with related parties:

	2020	2019
	\$	\$
<i>Sales and purchases of goods and services</i>		
Services rendered for graphic design of the annual and half year reports by a related party of board members	13,945	13,225

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.

19 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.

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

19 Share-based payments (continued)

(a) Employee Option Plan (continued)

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

	2020		2019	
	Average exercise price per share option	Number of options	Average exercise price per share option	Number of options
As at 1 July NZD options	1.58	1,900,000	1.56	3,400,000
Forfeited during the year	1.60	<u>(800,000)</u>	1.53	<u>(1,500,000)</u>
As at 28 June NZD options	1.56	<u>1,100,000</u>	1.58	<u>1,900,000</u>
As at 1 July AUD options	1.56	600,000	1.78	400,000
Granted during the year	-	-	1.11	200,000
Forfeited during the year	1.56	<u>(300,000)</u>	-	-
As at 28 June AUD options	1.56	<u>300,000</u>	1.56	<u>600,000</u>

Share options outstanding at the end of the year have the following expiry dates and exercise prices:

Grant date	Expiry date	Exercise price	Share options 28 June 2020	Share options 30 June 2019
22 September 2009	30 September 2019	NZ\$0.94	-	100,000
17 September 2010	30 September 2020	NZ\$0.88	100,000	100,000
16 November 2011	30 September 2021	NZ\$1.16	100,000	100,000
19 September 2012	30 September 2022	NZ\$1.41	100,000	100,000
18 September 2013	30 September 2023	NZ\$1.82	100,000	100,000
29 November 2013	30 September 2023	NZ\$1.82	500,000	1,000,000
10 November 2014	30 September 2024	NZ\$1.63	100,000	200,000
5 October 2017	30 September 2027	AU\$1.44	100,000	200,000
22 September 2016	30 September 2026	AU\$2.12	100,000	200,000
22 January 2016	30 September 2025	NZ\$1.14	100,000	200,000
22 September 2018	30 September 2028	AU\$1.11	100,000	200,000
Total			<u>1,400,000</u>	<u>2,500,000</u>

The weighted average remaining contractual life of share options outstanding at the end of the period was 3.9 years (2019: 5.1 years).

The range of exercise prices for options outstanding at the end of the year was NZ\$0.88 - NZ\$1.82 and AU\$1.11 - 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.

(i) Fair value of options granted

The fair value at grant date for the options issued during the 2020 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.

19 Share-based payments (continued)

(a) Employee Option Plan (continued)

(i) Fair value of options granted (continued)

No options were granted during the year ended 28 June 2020 (2019: 200,000).

(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 286,294 share rights to eligible participants of the deferred compensation plan.

All share rights were issued on the basis that they are divided into three tranches and vest over 3, 4 and 5 years, respectively.

	2020		2019	
	Average fair value per share right	Number of rights	Average fair value per share right	Number of rights
Outstanding as at 1 July	0.54	521,609	1.30	919,102
Granted	0.57	286,294	0.54	224,670
Vested	1.66	(19,105)	1.57	(311,487)
Forfeited	-	-	1.05	(310,676)
Outstanding at 28 June	0.81	788,798	0.54	521,609

In prior financial years, 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.

Share rights issued during the 2020 financial year used the Black-Scholes model to determine the fair value of share rights using the following inputs as at 28 June 2020:

	2020	2019
	27 Feb 2020	9 May 2019
Number of rights	286,294	224,670
Share price	\$0.68	\$0.67
Annualised volatility	40%	40%
Expected dividend yield	6.50%	6.50%
Risk free rate	0.75%	1.50%
Fair value of share right	\$0.57	\$0.54

19 Share-based payments (continued)

(c) Expenses arising from share-based payment transactions

	2020 \$'000	2019 \$'000
Options issued under employee option plan	-	11
Share rights issued under LTI plan	166	95
	166	106

20 Remuneration of auditors

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

(a) Ernst & Young

(i) Audit and other assurance services

	2020 \$	2019 \$
Audit and review of financial statements	535,506	477,223
Total remuneration for audit and other assurance services	535,506	477,223

(ii) Other services

Advisory fees	10,050	127,512
Total remuneration for other services	10,050	127,512

Total remuneration of Ernst & Young Australia	545,556	604,735
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Total auditors' remuneration	545,556	604,735
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21 Earnings per share

(a) Basic earnings per share

	2020 Cents	2019 Cents
Earnings per share for profit attributable to the ordinary equity holders of the Company	0.79	4.26

(b) Diluted earnings per share

	2020 Cents	2019 Cents
Diluted earnings per share for profit attributable to the ordinary equity holders of the Company	0.79	4.25

21 Earnings per share (continued)

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

	2020 \$'000	2019 \$'000
<i>Basic earnings per share</i>		
Profit attributable to the ordinary equity holders of the Company used in calculating basic earnings per share:	3,059	16,498
<i>Diluted earnings per share</i>		
Profit from continuing operations attributable to the ordinary equity holders of the Company	3,059	16,498

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

	2020 Number	2019 Number
Weighted average number of ordinary shares used as the denominator in calculating basic earnings per share	387,766,481	387,483,743
Adjustments for calculation of diluted earnings per share:		
Share rights	574,013	854,613
Weighted average number of ordinary and potential ordinary shares used as the denominator in calculating diluted earnings per share	388,340,494	388,338,356

(e) Information concerning the classification of securities

Options and share rights

Options and share rights 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 and share rights have not been included in the determination of basic earnings per share. Details are set out in Note 19(a).

22 Parent entity financial information

(a) Summary financial information

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

	2020 \$'000	2019 \$'000
<i>Balance sheet</i>		
Current assets	1,495	41,146
Non-current assets	464,727	338,180
Total assets	466,222	379,326
Current liabilities	6,153	243
Total liabilities	6,153	243
<i>Shareholders' equity</i>		
Issued capital	291,158	291,126
Reserves		
Acquisition reserve	40,907	40,907
Option and share rights reserve	697	757
Retained earnings	127,307	46,293
	460,069	379,083
Profit or loss for the year	92,647	43,578
Total comprehensive income	92,647	43,578

(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.
- (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, Medley Jewellery 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 at 28 June 2020 of \$33,000 (2019: \$72,000).

23 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, Medley Jewellery 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.

23 Deed of cross guarantee (continued)

(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 28 June 2020 of the closed group consisting of Michael Hill International Limited and the entities noted above.

	2020	2019
	\$'000	\$'000
<i>Consolidated statement of profit or loss</i>		
Revenue from sales of goods and services	370,986	430,052
Sales to Group companies not in Closed Group	30,941	48,004
Other income	15,703	988
Cost of goods sold	(175,412)	(206,255)
Employee benefits expense	(117,063)	(125,720)
Occupancy costs	(9,193)	(45,645)
Marketing expenses	(20,684)	(24,133)
Selling expenses	(15,223)	(21,333)
Depreciation and amortisation expense	(40,988)	(13,714)
Loss in disposal of property, plant and equipment	(454)	(498)
Other expenses	(17,588)	(15,468)
Finance costs	(6,949)	(2,574)
Profit before income tax	14,076	23,704
Income tax expense	(3,801)	(4,203)
Profit for the year	10,275	19,501
	2020	2019
	\$'000	\$'000
Other comprehensive income		
<i>Items that may be reclassified to profit or loss</i>		
Exchange differences on translation of foreign operations	(23,808)	11,336
Other comprehensive income for the period, net of tax	(23,808)	11,336
Total comprehensive income for the year	(13,533)	30,837
	2020	2019
	\$'000	\$'000
<i>Statement of changes in equity</i>		
Equity at the beginning of the financial year	474,874	463,296
Change in accounting policy – adoption of AASB 16	(23,574)	-
Total comprehensive income / (loss)	(13,533)	30,837
Share rights through share based payments reserve	-	95
Option expense through share based payment reserve	(28)	11
Dividends paid	(11,633)	(19,365)
Total equity at the end of the financial year	426,106	474,874

23 Deed of cross guarantee (continued)

(b) Consolidated statement of financial position

Set out below is a consolidated statement of financial position as at 28 June 2020 of the Closed Group consisting of Michael Hill International Limited and the entities noted above.

	2020 \$'000	2019 \$'000
Current assets		
Cash and cash equivalents	6,915	3,704
Trade receivables	8,953	9,004
Inventories	144,719	137,750
Current tax receivables	-	(358)
Loans to related parties	231,628	244,716
Other current assets	1,980	2,904
Total current assets	394,195	397,720
Non-current assets		
Property, plant and equipment	26,004	34,617
Right-of-use assets	81,372	-
Investments in subsidiaries	87,834	87,834
Other non-current assets	1,465	2,062
Intangible assets	24,419	15,386
Deferred tax assets	64,952	55,713
Total non-current assets	286,046	195,612
Total assets	680,241	593,332
Current liabilities		
Trade and other payables	56,575	20,488
Lease liabilities	23,732	-
Current tax liabilities	8,260	-
Deferred revenue	17,456	19,597
Provisions	24,505	25,824
Total current liabilities	130,528	65,909
Non-current liabilities		
Lease liabilities	73,776	-
Provisions	8,339	6,947
Deferred revenue	41,492	45,602
Total non-current liabilities	123,607	52,549
Total liabilities	254,135	118,458
Net assets	426,106	474,874
Equity		
Contributed equity	310,006	309,975
Reserves	(24,633)	(750)
Retained profits	140,733	165,649
Total equity	426,106	474,874

Directors' declaration

In the directors opinion:

- (a) 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) the financial statements and notes of the Group for the financial year ended 28 June 2020, 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 28 June 2020 and of its performance for the financial year ended on that date;
- (c) 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.

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

The directors have been given the declarations by the chief executive officer and chief financial officer required by section 295A of the Corporations Act 2001.

This declaration is made in accordance with a resolution of the directors.



E J Hill
Director

Brisbane
18 August 2020



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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 28 June 2020, 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 statements, including a summary of significant accounting policies, and the directors declaration.

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

- a) giving a true and fair view of the consolidated financial position of the Group as at 28 June 2020 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* (including Independence Standards) (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 Inventory

Why significant

The existence of inventories was a key audit matter due to the size of the recorded asset (28 June 2020: \$178,472,000) which represents 36% (2019:47%) 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 distribution centre and manufacturing warehouse. Inventories comprise a significant number of physically small but high value items. Moreover, a significant portion of stock was returned to the distribution centre due to the temporary store closures due to COVID-19 and then returned to stores once they re-opened.

The Group accounts for inventories in accordance with the policy disclosed in Note 2(k) and further disclosure is included in Note 9(a) of the financial report.

How our audit addressed the key audit matter

Our audit procedures included the following:

Retail Stores and Manufacturing

- Assessed the effectiveness of controls relevant to the conduct of physical stocktaking for a sample of the Group's retail stores and the manufacturing warehouse to assess whether inventories had been appropriately counted at each location and whether movements in to and out of each location prior to and subsequent to the counts had been appropriately recorded.
- We reviewed the summary of stock variances and results prepared by Internal audit across the sample of stores and considered the impact of their findings in our audit approach.
- Selected samples of stock receipts prior to and after the stock count including transfers to stores, to assess whether these were appropriately recorded in the correct period.

Distribution Centre

- We performed sample counts of the Distribution Centre at year-end to assess the existence of stock and corroborate the findings of the Group's full stock count.
- Selected samples of stock receipts prior to and after the stock count including transfers to stores, to assess whether these were appropriately recorded in the correct period.
- Tested a sample of transfers back to the stores in Canada as a result of the temporary store closures during the period. We subsequently attended a number of stores in Canada to physically observe transferred product had been received.
- We performed inventory analysis for the stores and tested any unusual fluctuations, outside of our set expectations of the year-end balance, compared to the stock take. We also compared the movement in stock balances at a country level from the stock take date to year-end.
- We reviewed the implementation of the new Enterprise Resource Planning Inventory system from June 2020 and assessed the proper cut-over of stock balances to the new system.

Professional Care Plan (PCP) Revenue Recognition

Why significant

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 3(a) of the financial report, the Group's performance obligation for its PCPs are satisfied over time. In measuring the progress toward complete satisfaction of the performance obligation, the Group uses customer usage history and industry information. As such, the determination of the pattern of revenue recognition is judgmental.

The pattern of recognising revenue, is disclosed in Note 5(c)(iii) of the financial report and is based on an input method to measure progress towards complete satisfaction of the service, because the customer simultaneously receives and consumes the benefits provided by the Group. As circumstances change over time, the Group updates its measure of progress to reflect any changes in the outcome of the performance obligation. In accordance with Australian Accounting Standards such changes are reflected in the current year results.

This change in estimate has been disclosed in Note 5(c)(iii) to the financial report.

How our audit addressed the key audit matter

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.
- Assessed the appropriateness of the balance of the PCP revenue recognised during the year and the closing deferred PCP contract liability at year end based on the usage pattern.
- Assessed the Group's calculation supporting the change in estimate relating to revenue recognition, which included agreeing assumptions to samples of the underlying PCP repairs usage data.
- Considered the changes in the PCP revenue recognition as a result of the temporary store closures during the COVID-19 lockdowns.

Adoption of Australian Accounting Standard AASB 16 - Leases

Why significant

The 28 June 2020 financial year was the first year of adoption of Australian Accounting Standard AASB 16 – *Leases*. The Group has entered into a significant volume of leases by number and value through its store network and head office as a lessee.

Given the financial significance to the Group of its leasing arrangements, the complexity and judgements involved in the application of AASB 16, the transition requirements of the standard and the subsequent amendment to consider the impact on rent concessions due to COVID-19, this was considered to be a key audit matter.

In addition, the complexity in the modelling of the accounting for the leases, including the calculation of the incremental borrowing rate and the judgement involved in the treatment of renewal options is significant.

Upon transition, a lease liability of \$168.0 million, right of use asset of \$144.3 million including the deferred tax effect and a restatement to opening retained earnings of \$13.0 million was recorded on the statement of financial position as outlined in Note 2(x).

How our audit addressed the key audit matter

Our audit procedures assessed the existence, completeness and valuation of AASB 16 lease balances and the related financial report disclosures. These procedures included the following:

- Assessed the appropriateness of the accounting policies, transition and new disclosures as set out in Notes 2(o) and 2(x) for compliance with the requirements of AASB 16 including the adoption of any practical expedients selected by the Group as part of the transition process.
- Assessed the integrity of the Group's AASB 16 lease calculation model used, including the mathematical accuracy of the underlying calculation formulas of the accounting module utilised by the Group.
- For a sample of leases, we agreed the key inputs in the lease accounting module to the relevant terms of the underlying signed lease agreements.
- We considered the Group's assumptions in relation to the treatment of lease renewal options.
- Assessed completeness of the leases included in transition including the reconciliation of the operating lease commitments disclosure in the prior year financial report to the transition disclosures and new leases entered during the year.
- Assessed the internal borrowing rate used to discount future lease payments to present value for reasonableness by performing sensitivities using published interest rates and terms of the Group's existing debt facilities.
- Tested a sample of rent concessions agreed to contracts and other supporting documentation.

Cashflow forecasts and the impact of COVID-19

Why significant

During the second half of the financial year, the Group was impacted by COVID-19. All bricks-and-mortar stores were temporarily closed in order to maintain the safety of the Group's staff and customers and as also required by local Government regulations.

The cashflow forecasts are used in the Group's impairment review of its cash generating units (CGUs) and used to prepare forecast debt covenant calculations to assess associated compliance. The Group's cash flow forecasts involve a number of assumptions and uncertainty around the short and medium term impact of COVID-19 to the Group. Sensitivity to changes in key assumptions could affect the Group's assessment of the recoverable amount of its CGUs at balance date or forecast debt covenant compliance. Accordingly, this was considered a key audit matter.

The significant judgement and estimates associated with the Group's measurement of its forecast cash flows are disclosed in Note 3(a) of the financial report.

How our audit addressed the key audit matter

Our audit procedures included the following:

- Assessed the cash flow forecasts approved by the Board taking into account our knowledge of the business and relevant external information as at 28 June 2020.
- Considered the reasonableness of the assumptions used in the cash flow forecasts based on historical results, growth rates and a range of possible scenarios resulting from the ongoing uncertainty associated with COVID-19.
- Assessed the Group's sensitivity analysis on its CGUs in three main areas being the cash flows, discount rate and terminal growth rate assumptions.
- In conjunction with our Valuation Specialists, we assessed the appropriateness of the discount rate applied to the cash flows of each CGU to assess whether the rate reflects the risks, including COVID-19 risks, associated with the respective cash flow forecasts for impairment testing.
- Assessed the Group's sensitivity analysis on forecast debt covenant compliance at the future reporting points to the external financier for a period of 12 months from signing the financial statements and the related appropriateness of management's consideration on the going concern assumption.
- Assessed the appropriateness of the disclosures around significant judgments and estimates as required by the relevant Accounting Standards.



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

The directors are responsible for the other information. The other information comprises the information included in the Group's 2020 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, actions taken to eliminate threats or safeguards applied.

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



Report on the Audit of the Remuneration Report

Opinion on the Remuneration Report

We have audited the Remuneration Report included in the directors' report for the year ended 28 June 2020.

In our opinion, the Remuneration Report of Michael Hill International Limited for the year ended 28 June 2020 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.

A handwritten signature in black ink that reads 'Ernst & Young' in a cursive, stylized font.

Ernst & Young

A handwritten signature in black ink that reads 'Alison de Groot' in a cursive, stylized font.

Alison de Groot
Partner
Brisbane
18 August 2020