Dunelm mill

Dunelm Group plc Annual report & accounts 2011

Dunelm Group plc Annual report & accounts 2011

Simply Value...

...for money

Dunelm is a fast growing specialist out-of-town homewares retailer providing a comprehensive range of products to a wide customer base, under the brand name Dunelm Mill

The Group's 'Simply Value for Money' proposition combines market-leading choice, great prices, reliable quality, strong product availability and friendly and knowledgeable service.

Contents

Dunelm mill

Operational highlights

103 superstores at 2 July 2011

10 new superstores opened in the year (including one relocation)

Average superstore selling area of approximately 30,000 square feet

Over 20,000 lines in a superstore – broad and deep ranges

Financial highlights FY11

Revenue increase 9.3%

Operating margin 15.5%

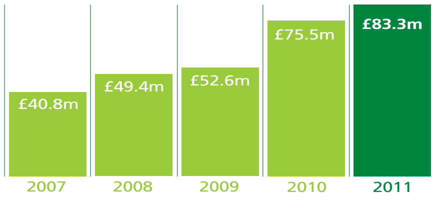
Net cash generated from operations £74.0m

* The 2007 figures for operating profit and profit before tax included non-recurring items in respect of IPO and warehouse relocation as well as a non-recurring gain on a property disposal. The combined effect of these was to reduce operating profit by £3.2m and profit before tax by £3.0m.

† The 2009 figures reflect a 53 week trading period, compared with 52 weeks in all other years.

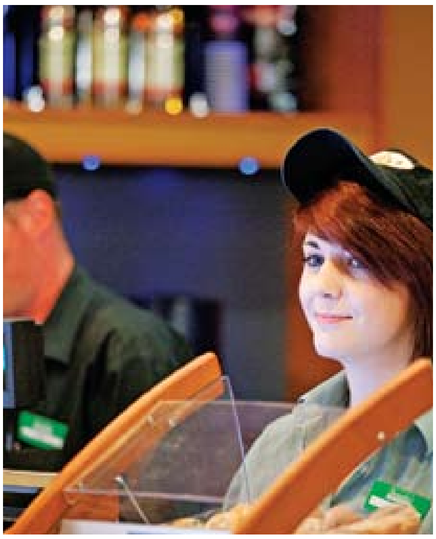
Revenue†

Operating profit*†



Profit before tax*†

Net cash from operations†



Business overview

‘Choice is at the heart of our proposition and allows us to attract a broad cross section of customers’.

How we generate shareholder value

Our markets

The UK 'Homewares' market is estimated to be worth £11bn per annum, comprising 'Textiles & Soft Furnishings' (45%) and 'Household, Hardware and Lighting' (55%). Dunelm competes strongly in all segments.

Customer buying decisions in this market are primarily influenced by range, price and convenience with quality and service also essential attributes to a winning formula.

Our business model

Our offer is based on a 'simply value for money' proposition.

We reach our customers through a UK chain of 112 retail stores and two websites (www.dunelm-mill.com and www.dorma.co.uk) 103 of the stores are in our out-of-town 'superstore' format. Our key sources of competitive advantage are industry-leading choice, everyday low prices and convenient out of town locations.

Our superstores stock over 20,000 different products with a typical store size of approximately 30,000ft².

Our strategy

Our strategy is to develop the business as follows:

1. Develop our specialist proposition.
2. Open more superstores.
3. Grow multi-channel.
4. Develop and exploit infrastructure.

Business overview

Our focus on constantly improving our customer offer has allowed us to gain market share.

Our strategic priorities

1 Develop our specialist proposition

We must continue to evolve our offer so that we maintain and grow our competitive advantage in choice and price, supported by quality, service and availability.

2 Develop the store portfolio

We aim to grow market share and reach more customers by opening more superstores across the UK. We expect to grow our portfolio to 150-200 superstores in the medium term.

3 Grow multi-channel

www.dunelm-mill.com is our No.1 store for revenue. We expect to increase customer engagement, develop new customer touch points, grow revenue and further develop our multi-channel offer through reserve & collect and an improved delivery service.

4 Develop and exploit our infrastructure

We have a well-invested infrastructure. Our aim is to ensure that we continue to develop this ahead of our growth curve, so that it is an enabler and never a constraint.

Our near term objectives

1.
> Continuously evolve product ranges
> Develop knowledge based customer service as a point of differentiation

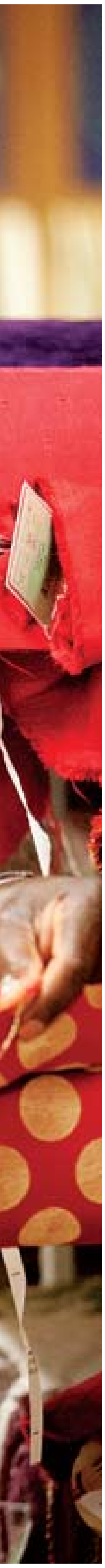
2.
> Continue new store opening programme

3.
> Develop collect in-store service
> Establish social media presence
> Extend the range on-line
> Develop Dunelm At Home

4.
> Exploit core retail systems to improve stock control
> Drive efficiency through new store support and distribution facilities

Business overview

We opened ten new superstores in the year adding over 300,000 square feet of selling space.



Strong superstore roll out plan

Our committed pipeline of stores, which we continue to add to, will provide further growth over the next 12 to 18 months as we expand towards our target for national coverage in the UK of between 150 and 200 superstores.

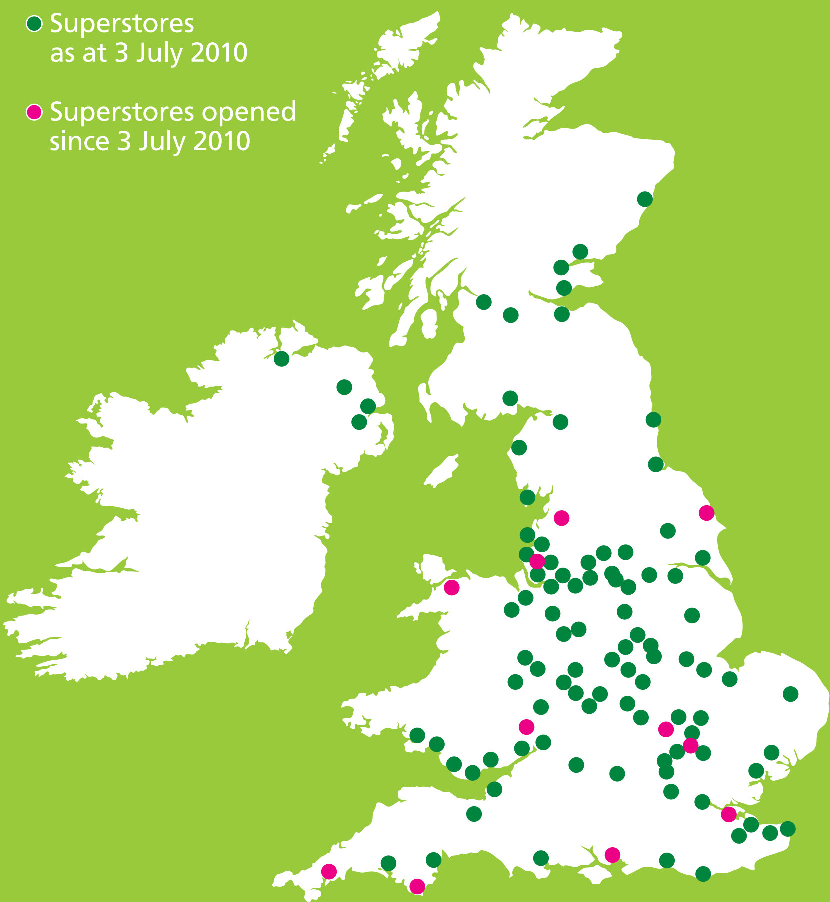
> 10 new stores opened in 2010

> 13 further openings committed

Superstore locations

● Superstores as at 3 July 2010

● Superstores opened since 3 July 2010



Ways to shop at Dunelm

www.dunelm-mill.com

0844 346 0022

Over 110 stores nationwide

Business review

Chairman's statement

Geoff Cooper Chairman

"The Board's confidence in the continuing cash generation of the business is reflected in our proposal to reduce dividend cover to the bottom of our target range at 2.5x."

Our key strengths

- UK's largest specialist homewares retailer
- Portfolio of established out-of-town superstores, average sales area approximately 30,000 square feet
- 'Simply Value for Money' proposition:
  – Good quality products
  – Great prices
  – Industry leading choice
  – Deep availability
  – Friendly knowledgeable service
- On-line store featuring 20,000 products
- Owner of 'Dorma' brand
- Robust, scalable infrastructure
- Experienced management team, entrepreneurial culture
- Highly cash generative
- Strong balance sheet

The most recent financial year has been a challenging period for most non-food retailers. In the context of subdued customer demand for homewares, it was a satisfactory achievement for Dunelm to deliver like-for-like (LFL) sales growth in two of the four quarters, with only a small decline in LFL sales over the year as a whole. With continuing progress on gross margin and good contribution from stores opened in the last 24 months, the Group was able to deliver a highly creditable 9.0% increase in profit before tax.

We have continued to generate very strong operating cash flows. This enabled the Group to fund out of current cash flow a record year of capital investment in the business, including new stores, a larger refit programme and also key infrastructure investments comprising a doubling of space at the central warehouse in Stoke and the creation of a new head office facility.

The Board's confidence in the continuing cash generation of the business is reflected in our proposal to reduce dividend cover to the bottom of our target range at 2.5x, leading to a recommended 60% increase in the final dividend to 8.0p per share (2010 – 5.0p). This would bring full year dividends to 11.5p per share (2010 – 8.0p), an increase of 43.8%.

It is the Board's intention to grow future dividends in line with earnings. In addition, the Board will continue to review the capital structure of the Group, returning excess capital if appropriate.

Since taking over as Chief Executive from Will Adderley in the course of the year, Nick Wharton has assumed full responsibility for running Dunelm. Will continues to provide support to Nick on key trading issues such as managing the effects of cotton price increases, and will be able to allocate his time increasingly to development activities.

Looking ahead, we have a range of exciting development initiatives and attractive network expansion opportunities. Despite seeing no major catalyst for significant short term growth in the homewares market, we are confident in our 'SImply Value for Money' offer and look forward to further growth in profits and returns.

Geoff Cooper
Chairman
15 September 2011

Business review

Chief Executive's review

Nick Wharton Chief Executive

"We have demonstrated through disciplined execution of our strategy and close operational management that our business can make good progress in challenging conditions."

Business highlights

- 10 new superstore openings (including one relocation) and 21 refits of existing stores
- Continued market share growth
- Exciting developments in our customer offer
- www.dunelm-mill.com number one store by turnover following strong revenue growth
- Continuing investment in infrastructure to underpin future growth

Introduction

Having assumed the role of Chief Executive during the year, I want to start by paying tribute to the significant contribution my predecessor Will Adderley has made over the 15 years in which he led Dunelm. Will is a first class retailer and has built on the foundations laid by his father to make Dunelm an outstanding business. As the first externally-appointed Chief Executive of the Group I am delighted to have the opportunity to grow and further develop the Group with the close support of Will in his new role as Executive Deputy Chairman, pursuing our clear strategy that has served Dunelm so well to date.

Trading

In the context of a consumer environment which has continued to be challenging, we are satisfied with our trading performance over the last financial year. Reflecting the opening of 10 new superstores which increased overall retail space by over 300,000 square feet, our total revenue increased by 9.3% over the financial year. Like-for-like sales (calculated by comparing stores which have traded throughout the last two financial years) were marginally lower by 0.6%, but measurably better than the decline of 1.9% for the home textiles market as a whole, as measured by the British Retail Consortium.

The environment across the year was characterised by new levels of uncertainty, both in consumer behaviour and in the rate of commodity price inflation, which in cotton and man-made alternatives was at a level not experienced for a generation.

Against this backdrop we have focused on managing the controllable elements of our business model, with a particular emphasis on operating costs. The growth achieved in gross margins and the progress made in the second half of the year in cost management were particularly pleasing and have led to a 20 basis points expansion in operating margins year on year, after absorbing the costs associated with the expansion of retail space.

Strategy development

We continue to develop the business through a strong focus on our four strategic priorities. These priorities reflect our intention progressively to expand and strengthen our customer offer, while at the same time increasing scale through store and multi-channel expansion.

Priority 1 – develop our specialist proposition

We continue to invest in the development of the Group's 'Simply Value for Money' proposition within the £11bn UK homewares market. This proposition combines great prices, reliable quality, strong product availability and friendly and knowledgeable service, with our core differentiator of offering industry-leading choice.

Business review

Chief Executive's review *continued*

Choice is at the heart of our proposition and allows us to attract a broad cross section of customers. Under the single Dunelm brand we successfully sell entry-level products that compete with those sold by grocery or discount multiples, through mid-range product to premium ranges, that compete directly with offers within department stores or higher end independent retailers. These premium ranges include bedding and bathroom merchandise under our owned Dorma brand.

Our range of choice has been particularly valuable during the past financial year. We have seen customer behaviour changing, with more affluent customers looking for greater value and more value-led customers seeking to trade up within our ranges to provide a low cost, indulgent treat.

We continue to use our Miss it Miss Out ('MIMO') promotions and special buys to emphasise Dunelm's value credentials and provide a seasonally relevant feel to the store.

We have developed a new advertising approach during the financial year which is focused on brand development and on emphasising the Dunelm value proposition. This is part of a migration towards a more consistent presence in the national media.

Friendly, knowledgeable customer service is an increasingly important point of differentiation for Dunelm. In order to make more colleague time available for customer service without increasing overall labour cost, we continue to invest in a number of systems and process enhancements that reduce the level of non-customer facing tasks that are performed within store. For example, the migration from a labour intensive manual process to an automated system for inventory ordering is key. Trials completed during the year have confirmed its potential to reduce activity while maintaining availability and we intend to have ordering of over 50% of our inventory automated by the end of the calendar year.

We are also continuing to invest in training to provide our colleagues with the knowledge and confidence to engage with customers and are using tailored incentives to reward good customer service.

We also see an opportunity to further enhance the Dunelm proposition through the addition of new services. Dunelm At Home is a relatively new service offering a free home consultation which allows customers to choose bespoke, made to measure window treatments in their own homes. Recognising that the initial execution of this proposition was insufficiently scalable without endangering quality of service, we have redesigned our processes to ensure high quality delivery and a second pilot of this service has been launched in three stores since the year end.

Priority 2 – develop the store portfolio

The Group operates from two formats. The vast majority of stores operate as out of town superstores averaging 30,000 square feet, where Dunelm's market leading range, breadth and depth stands out in a sector that is still characterised by small independent retailers and is best delivered to our customers. We also trade from a limited number of smaller high street locations where there are no suitable out of town alternatives.

We opened ten new superstores in the year (one being a relocation), over 300,000 square feet of selling space. As at the year-end, our superstore chain comprised 103 stores providing 3.1m square feet of selling space. The high street chain totalled nine, after we closed one shop during the year upon lease expiry.

Our recent openings continue to trade well and deliver strong returns on invested capital. We estimate that, on a discounted cash flow basis, the average payback period for stores opened in the last three financial years will be approximately 30 months. This performance enables us to acquire further space with confidence that we will continue to deliver our targeted payback period for new stores of 36 months, even allowing for potential cannibalisation of revenue and potentially higher costs associated with operating in the south east.

Despite the lack of fresh retail development across the UK, we have opened a further store since the year-end in Dartford and are contractually committed to 13 more units, two of which are relocations of existing superstores to significantly enhanced trading locations. We also continue to use our strong balance sheet to acquire interests in freeholds where, for example, we wish to secure long term tenure or avoid onerous lease clauses.

Our committed pipeline of stores, which we aim to add to, will provide further growth over the next 12 to 18 months as we expand towards our target for national coverage in the UK of between 150 and 200 superstores.

We continue to invest in a programme of store refits to improve the shopping environment in our existing stores. These refits enhance revenue by introducing new ranges, for example kitchen concept or arts and crafts, and improve the overall shopping experience, for example through better department adjacencies or through the introduction of a Pausa coffee shop.

Through new and refitted stores, we now have Dorma sub-shops in 53 stores; our arts and crafts offer is present in 79 stores; and our extended kitchen offer, now divided between cooking, dining and utility sub-shops, is in 50 stores.

Our Pausa coffee shop, now present in 58 stores, provides both an additional reason to visit for new customers and increases dwell time. Our confidence that Pausa fits with our 'Simply Value for Money' proposition was reinforced during the year when it won the coveted Coffee Shop Sandwich Retailer of the Year at the British Sandwich Association awards.

During the year we developed a lower cost refit alternative, more suitable to newer or smaller footprint stores, and have reviewed the costs associated with all refit activities to ensure that capital is focused on those areas which deliver greatest financial returns. This review has reduced the average cost of a major refit by approximately 25% to around £0.6m, whilst a medium refit requires substantially lower investment (c£0.1m).

We completed eight major refits in the last financial year (2010 – nine) as well as a significant number of 'medium' refits.

Through this ongoing refit programme, 49 stores (almost 50% of the superstore chain) are either new or have benefited from a major refit in the last three financial years.

Priority 3 – grow multi-channel

It is clear from the general increase in multi-channel revenues across UK retail and from our own customer research that enthusiasm for the convenience and value that multi-channel shopping provides continues to grow. Enhancing our on-line offer and extending our multi-channel presence is therefore an investment priority.

This level of enthusiasm is illustrated by the number of visitors to our websites and their average spend which, at over £50, is approximately twice the level achieved through store transactions. Dunelm-mill.com is our biggest shop window allowing the full range to be viewed and researched by existing customers, and providing the opportunity to extend our reach and establish brand awareness with new customers.

During the year our investment included a major refresh of our website to provide a more contemporary, functional and user friendly shopping experience. Responding to customer feedback, this included significant improvements to the key home and landing pages and the streamlining of the checkout process.

Sales from our on-line businesses (www.dunelm-mill.com and www.dorma.co.uk) have continued to grow strongly over the last financial year. As a result of the investment made, the direct channel is now ranked as our number one store in sales terms.

During the year we invested in a dedicated warehouse facility for our top 4,000 selling lines on the web for home delivery. This investment increased on-line availability, particularly for premium delivery options, while eliminating the requirement for expensive store picking activity previously used to service these sales.

Significant development is under way to deliver a further step-change improvement in the convenience of our multi-channel proposition. Such improvements will not only improve customer experience but will also reduce operating costs.

In the first half of the forthcoming financial year we intend to offer increased convenience through a true 'Reserve and Collect' model as well as launching a mobile-friendly website. Through linking individual store stock files to the web, customers will be able to check availability and reserve each of over 20,000 products prior to visiting the store to collect their purchase at a time of their convenience on the same day or beyond.

Chief Executive's review *continued*

"We continue to invest in physical systems and human infrastructure in order to strengthen the current business and provide a sound foundation for our future growth."

Through reducing customer waiting time and eliminating logistics costs, this development will represent a major improvement compared with our existing proposition, where customers currently reserve centrally held stock for delivery to their local store for collection.

The web will also play an increasing part in our overall marketing strategy with digital advertising planned to form a much more significant part of our overall advertising and customer engagement plan. As shown by the 13,000 customer recommendations on our site, of which two-thirds achieve the highest 5 Star rating, our customers are highly engaged with the Dunelm brand and products. Our recent launches on Facebook where 5,000 customers now follow us after only five weeks, and on Twitter, are part of a broader social media strategy which will further deepen this relationship.

Priority 4 – develop and exploit our infrastructure

We continue to invest in our physical, and systems infrastructure and in our people, in order to strengthen the current business and provide a sound foundation for our future growth. Specifically, we continue to extract further benefits from our IT systems, enabling us to improve stock control and make in-store processes more efficient.

The year saw two key developments that have strengthened our logistics infrastructure. We have doubled the space available at our Stoke warehouse, to 500,000 square feet and successfully transitioned to a new third party carrier to operate the delivery of merchandise from UK-based suppliers to our stores. These developments will enable us to accommodate future growth either in new stores or in the proportion of product that we source directly from overseas suppliers.

Development of our new head office near to our existing base in Syston, Leicestershire was completed shortly after the year-end and the new building was officially opened by Bill Adderley (our founder and honorary Life President) together with his wife Jean on 8 September 2011. We will retain our existing head office for a number of operational uses, such as the central stockholding of fabric and a photo studio to enhance product imagery on our websites.

We also continue to enhance our organisational capacity and capability through recruitment into a number of key management roles. The existing Operating Board was strengthened during the year through the addition of a Buying and Merchandise Director, and the first half of the current financial year will see the further addition of a Chief Operating Officer and a dedicated Director of Multi-Channel.

Summary & Outlook

While we anticipate that the consumer environment will remain challenging through the current financial year, we have demonstrated, through disciplined execution of our strategy and close operational management, that our business can make good progress in these conditions.

Our focus on constantly improving our customer offer has allowed us to gain market share while expanding gross margins; at the same time our future growth prospects have been enhanced through strengthening the pipeline of new stores and the continuing development of our multi-channel footprint.

The Group's financial position remains robust and the trading business is strongly cash generative, readily financing the investment required for our envisaged growth. While retaining a preference for capital flexibility, our reduction in dividend cover to 2.5x and our intention to grow future dividends in line with earnings reflect the Board's confidence in the future development of the Group.

Nick Wharton
Chief Executive
15 September 2011

Business overview
Business review
Governance
Financial statements

Business review

Finance Director's review

David Stead Finance Director

"The Group generated £74.0m net cash from operating activities in the last financial year, an increase of 2.8%."

Financial highlights

- 9.3% increase in overall revenues
- Gross margin change +120 bps
- Operating margin 15.5%
- Earnings per share (diluted) 29.3p
- Dividends per share 11.5p (44% increase)

Operating result

Group revenue for the 52 weeks to 2 July 2011 was £538.5m (2010: £492.8m), an increase of 9.3%.

Like-for-like sales declined slightly by 0.6% over the period, however non-comparable space contributed +9.9%. The like-for-like sales performance strengthened in H2 at +0.1%, with H1 having recorded -1.2% against a particularly strong comparative performance in the equivalent period last year (+15.4%).

The Group continued to improve gross margin which, over the year, increased by 120 basis points to 48.0% (2010: 46.8%). Improved life-cycle management and sell through of sale stock (summer 2010 & winter 2011) in particular boosted this result. The market experienced some price inflation over the year as a result of higher commodity prices and an increase in VAT rates but these challenges were met while maintaining our 'Simply Value for Money' price positioning.

Operating costs grew by 12.8% compared with last year, with the increase primarily due to investment in the store portfolio and supporting central infrastructure. Operating costs in like-for-like stores increased by just 2.1%, despite increased investment in multi-channel operations and refits. Non-store costs grew in line with the overall growth of the business, including increased marketing investment and enhanced warehousing and distribution capacity.

Operating profit for the financial year was £83.3m (2010: £75.5m), an increase of £7.8m.

EBITDA

Earnings before interest, tax, depreciation and amortisation were £97.4m. This has been calculated as operating profit (£83.3m) plus depreciation and amortisation (£14.1m) and represents a 12.1% increase on the previous year. The EBITDA margin achieved was 18.1% of sales (2010: 17.6%).

Financial items and PBT

The Group generated £0.4m net financial income for the year ended 2 July 2011 (2010: £1.3m). Financial items include foreign exchange losses of £0.1m (2010: gain of £0.8m) arising in respect of US dollar holdings; as at 2 July 2011 the Group held $1.8m in US dollar cash deposits and had forward contracts covering approximately 35% of the anticipated US dollar spend over the next 12 months. The balance of net financial income, £0.5m (2010: £0.5m), represents interest on surplus cash deposits.

Business overview
Business review
Governance
Financial statements

Business review

Finance Director's review *continued*

"The major investments in the year were in stores, including fit-out costs for 10 new stores and 8 major refits."

After accounting for interest and foreign exchange impacts, profit before tax for the year amounted to £83.6m (2010: £76.8m), an increase of 9.0%.

Tax, PAT and EPS

The tax charge for the year was 28.5% of profit before tax compared with 29.2% in the prior year. The year on year reduction reflects both the lower headline rate of corporation tax and an increase in the level of assets qualifying for capital allowances following a review completed during the year.

Profit after tax was £59.8m (2010: 54.4m) an increase of 9.9%.

Basic EPS for the year ended 2 July 2011 was 29.7p (2010: 27.1p), an increase of 9.6%. Fully diluted EPS increased by 8.9% to 29.3p (2010: 26.9p).

Capital expenditure

Gross capital expenditure in the financial year was £37.2m compared with £24.6m last year. The major investments in the year were in stores, including fit-out costs for 10 new stores and 8 major refits in the period as well as acquisition of two freehold sites.
In addition, central infrastructure was bolstered by the completion of the fit-out of our 250,000ft^2 extension to our central warehouse as well as a £5.8m investment in the build of our new head office.

Working capital

Investment in working capital increased by £4.1m over the financial year, primarily due to expansion of the store chain.

Cash position

The Group generated £74.0m (2010: £72.0m) net cash from operating activities in the last financial year, an increase of 2.8%. At the end of the year net cash resources were £35.1m (2010: £15.4m). The Group cancelled its committed bank facility under a revolving loan agreement with Lloyds Banking Group plc of £40m. In light of the Group's financial strength, the Board concluded that access to external funding would not be required in the near term.

During the next financial year to 1 July 2012 Dunelm will continue to invest in the expansion of the business. This will include opening new superstores (estimated capital cost £1.2m per site), major and medium store refits and development of multi-channel operations. In addition the investment in final fit-out of the new head office will be completed. Further freehold acquisitions will be considered as opportunities arise.

Dividend

An interim dividend of 3.5p was paid in April 2011 (2010: 3.0p). It is proposed to pay a final dividend of 8.0p per share (2010: 5.0p). The total dividend of 11.5p represents a 43.8% increase over last year reflecting the Group's strong financial performance and leaves dividend cover of 2.5x, within our target range of 2.5x–3.0x.

Key performance indicators

In addition to the traditional accounting measures of sales and profits, the Directors review business performance each month using a range of other KPIs. These include those on the table on page 19.

David Stead
Finance Director
15 September 2011

Key performance indicators FY11

Sales growth†

2011	+9.3%
2010	+18.2%
2009	+6.4%

Like-for-like sales growth†

2011	–0.6%
2010	+8.0%
2009	+0.5%

Gross margin change (basis points)

2011	+120bps
2010	+190bps
2009	+120bps

Operating margin

2011	15.5%
2010	15.3%
2009	12.4%

EBITDA £m

2011	£97.4m
2010	£86.9m
2009	£63.2m

Earnings per share (diluted)

2011	29.3p
2010	26.9p
2009	18.6p

Dividend (per share)

2011	11.5p
2010	8.0p
2009	6.0p

New store openings

2011	10
2010	10
2009	6

Major refits

2011	8
2010	9
2009	6

† 2009 is treated as a 52 week period for these measures (53 weeks for the rest).

Business review

Key risks and uncertainties

Dunelm recognises that effective business management requires regular review of business risks to identify, evaluate and prioritise them, to assign management ownership and to ensure appropriate controls are in place in mitigation.

An annual risk identification and assessment workshop is in place to review the risk profile of the organisation and to compile the Group's Risk Register. Quarterly reviews of these risks are undertaken by management and the Board gains assurance through twice yearly reviews, as well as by regular challenge to the executive team to consider 'What keeps us up at night.'

The Board considers that the principal risks to Dunelm's aims of achieving its strategic objectives are as follows:

Strategic objectives

- Develop our specialist proposition
- Develop the store portfolio
- Grow multi-channel
- Develop and exploit our infrastructure

Strategic risks	Mitigation	Strategy
Competition The Group competes with a wide variety of retailers in both store format as well as on-line. Failure to withstand increased competition in the Homewares market on multiple fronts (price, range, quality and service) could materially impact returns and limit opportunities for growth.	The Board continually monitors Group performance within the Homewares market and against specific competitive threats. Various initiatives are in place to continue the enhancement of our specialist proposition.	
Economic uncertainty Uncertainty surrounding the resilience of the UK economy and effectiveness of fiscal and monetary measures will continue to put pressure on consumer expenditure. This is likely to result in difficult trading conditions in the retail sector as a whole limiting profitability and growth opportunities.	The Group mitigates this by reacting quickly to consumer changes and adjusting its offer in response. In addition our focus on maintaining a low cost base helps us to maintain our affordable 'Simply Value for Money' proposition.	
Commodity prices Significant cost price increases and high levels of volatility have been a feature of retailing over recent years particularly freight rates, raw materials, energy and exchange rates. Failure to manage and control these changes will lead to pressure on margins and adversely impact the financial results.	Dunelm uses its scale, buying power and growth to secure supply of key raw materials at competitive prices. Freight rates, energy and currency are bought forward to help mitigate volatility and aid margin management.	
Portfolio expansion Availability of vacant or new retail space is essential to support our growth plans. Inability to secure the required retail trading space either in terms of the number of new locations or at the required size to deliver our format will limit our pace of expansion or force us to compromise our offer.	The Group has a strong pipeline of new space legally committed. The Property team has been strengthened to ensure that the appropriate resource can deliver a flexible approach to property acquisition. In addition the Company's debt-free position provides an attractive covenant to landlords, and the ability to acquire freehold units if appropriate.	
Information technology & systems Dunelm is dependent on the reliability and capability of key information systems and technology. A major incident or sustained performance problems with regard to store, logistics, multi-channel or head office systems could constitute a significant threat to the business, at least in the short term. Trading performance could be adversely impacted by this reliance.	All business critical systems are established, industry leading package solutions. They are supported by a disaster recovery strategy designed to ensure continuity of trade. In addition, a specialist company is responsible for hosting Dunelm's main ERP system off-site and a full backup server facility is in place for all other key systems.	

Strategic risks	Mitigation	Strategy
Infrastructure The Group could suffer the loss of a major facility or supply partner with a consequent impact on short term trading or diversion of focus from longer term strategy and planning. This could materially affect the profitability of the business.	The Group seeks to mitigate this risk by limiting the dependency on individual suppliers and by actively managing key supplier relationships. High stock service levels and a high proportion of direct-to-store deliveries further mitigate supply chain risk. Head office, workroom, multi-channel and distribution centre activities are all subject to disaster recovery plans and could all operate from fall back facilities.	
Key personnel The success of Dunelm is dependent upon senior management closely supervising all aspects of Group performance, growth and development. The business could be vulnerable to the loss of individual key managers.	The Group's remuneration policy detailed on page 40 ensures that high calibre executives are attracted and retained. In addition the Board has ensured that the Company continues to build strength in depth in the operating management team. Lock-in of senior management is supported by awards under the Long-Term Incentive Plan. The Operating Board seeks to develop high calibre individuals through sponsored talent management and succession planning.	
Product & service quality The Group recognises that the quality and safety of our products and services (including coffee shops) is essential to the business. If our specialist proposition fails to deliver this there is a risk that individuals could be harmed and that reputational damage could lead to consumers losing confidence in the brand.	Dunelm operates a full test schedule for all new products and on a sample basis for on-going lines, overseen by our specialist QA team. Food hygiene is maintained through the adoption of clear operating guidelines contained in the company's 'Food Safety Manual'. Staff certification is compulsory and risk assessments, equipment inspections and compliance audits are in constant use to ensure standards are maintained.	
Compliance The Group risks incurring penalties or punitive damages arising from failure to comply with legislative or regulatory requirements across many areas including but not limited to, trading, health & safety, data protection, advertising, ethical standards and the environment.	Dunelm operates a number of company policies and codes of practice outlining mandatory requirements within the business governing behaviours in all key areas. Operational management are also responsible for liaising with external advisors to ensure that potential issues from new legislation are identified and managed.	
Finance & treasury Lack of appropriate levels of cash resources or exposure to significant variations in interest rates or exchange rates could have an impact on the Group's operations and growth plans.	Dunelm has significant cash surpluses and further uncommitted borrowing facilities with partner banks to fund growth plans. In addition, cash flows are monitored weekly against agreed budgets. A Group Treasury Policy is in place to govern cash management strategies and to control foreign exchange exposures.	

Nick Wharton
Chief Executive
15 September 2011

David Stead
Finance Director

Governance

Letter from the Chairman

Dear Shareholder,
Following the practice we adopted last year, I am in this letter introducing the Corporate Governance section in our Annual Report, and have asked Marion Sears to write a separate introduction to the Remuneration section. I hope these letters help your consideration of the various matters we report to you as part of our corporate governance responsibilities.

As ever, this year has been very busy on corporate governance matters, with a number of important developments in governance requirements and in the matters we have considered inside Dunelm. These include the introduction of the Bribery Act, the Davies report on gender diversity, the new stewardship code, the implementation of the UK Corporate Governance Code, and the FRC guidance on board effectiveness and risk. We have also actively followed up and acted upon issues raised with us by shareholders following dialogue during the course of the year.

With the benefit of a relatively small board, the whole Board's participation and engagement in debating these issues has been very high, and the Board has given serious consideration to an appropriate response from the Company – one which we believe both meets our responsibilities and yet adopts practical, non-bureaucratic, common sense solutions.

Of particular note in the course of the Board's deliberations on governance matters this year have been:

- Managing the transition of Nick Wharton from non-executive director to Chief Executive, and the implications of this for Board and committee membership;
- An update to the Group's internal certification exercise, which requires key executives to confirm their adherence to legal, governance and company policies, to include the requirements of the Bribery Act;
- Reviewing Board and committee terms of reference and Board processes in line with the new UK Corporate Governance Code;
- A further annual review of the Board's performance, which involved the whole Board in an active debate including consideration of the progress on matters identified the previous year, the value of the Board in guiding strategy, individual directors' development requirements and external advice on governance issues that have typically caused difficulties elsewhere;
- A new review of the skills, perspectives and experiences provided by current Board members;
- Extensive Board debate about Board composition, including its diversity;
- Consideration by the whole Board of Non-Executive Director candidates;
- A new process for the Executive Director team to present a review of the high level risks emerging from the Group's system of internal control ('Things that are keeping us awake');

The outcome of our discussions on these matters is reported below.

There remains a strong collegiate and respectful relationship between the Executive and Non-Executive Directors. We have retained our approach of all Non-Executive Directors aiming to visit a store once a month, often with a member of the senior management team. This continues to be helpful in fostering our understanding of business issues as well as communicating internally from head office to store teams and vice versa. In addition, Board meetings are often held at store or other Company locations and include presentations from managers within the business.

Our routine activity includes regular monitoring of shareholder feedback, with Non-Executive Directors joining management in a selection of shareholder meetings following our results announcements. We have also consulted shareholders this year on a number of matters raised in response to our annual report and AGM resolutions last year. However, we are conscious that it is becoming ever more difficult for companies and shareholders to sustain an efficient dialogue given the welter of requirements – and even more difficult to recall the nuances of corporate governance when responding to specific proposals. Accordingly, we plan to invite corporate governance representatives of our major institutional shareholders to a presentation next January and from time to time thereafter as appropriate, with the aim of increasing understanding of how we approach our corporate governance duties as a Board. This will be hosted by the Chairman, the Non-Executive Directors and Will Adderley, representing the majority family shareholding.

Geoff Cooper
Chairman
15 September 2011


cookshop
THE Utility ROOM
99p
Change now!
GLASS

Governance

Directors

1. Geoff Cooper

Non-Executive Chairman

Geoff Cooper, joined the Board in November 2004. Geoff is Acting Chairman of the Audit Committee and a member of the Nominations and Remuneration Committees. A qualified accountant, Geoff is currently Chief Executive of Travis Perkins plc. He is a former Director of Gateway (now Somerfield plc) and was Finance Director and then Deputy Chief Executive of Alliance UniChem plc.

2. Nick Wharton

Chief Executive Officer

Nick Wharton, joined the Board in August 2009 as an Independent Non-Executive Director. Nick took over from Will Adderley as Chief Executive of the Group In February 2011. Prior to that he was Chairman of the Audit Committee, and a member of the Remuneration and Nominations Committees; Nick was previously Finance Director of Halfords Group PLC.

3. Will Adderley

Executive Deputy Chairman

Will Adderley, joined the business in 1992. He has worked in and is familiar with all major areas of the business and took over the day-to-day running of the Group from his father in 1996. Will remained as Chief Executive through the Group's IPO in 2006 and until February 2011, when he took the new role of Executive Deputy Chairman. Will is a member of the Nominations Committee.

4. David Stead

Finance Director

David Stead, joined the Group in 2003. Previously he spent 14 years at Boots where he was Finance Director of Boots The Chemists and Finance Director of Boots Healthcare International.

5. Marion Sears

Senior Independent Non-Executive Director

Marion Sears, joined the Board in July 2004. Marion is Chair of the Remuneration and Nominations Committees and a member of the Audit Committee. She is also a Non-Executive Director of both Zetar Plc and Octopus AIM VCT PLC.

6. Simon Emeny

Independent Non-Executive Director

Simon Emeny, joined the Board in June 2007. Member of the Audit, Remuneration and Nominations Committees. Simon is Group Managing Director of Fuller Smith and Turner Plc.

Bill Adderley

Founder and Life President

Bill Adderley founded Dunelm in 1979. He led the development of the business successfully for many years, then took a non-executive role before retiring in February 2008. He and his wife Jean remain passionate Dunelm supporters and major shareholders.

Executive

Non-Executive

▲ Audit Committee Member ● Nomination Committee Member ■ Remuneration Committee Member

Directors' report and business review

The Directors present their report together with the audited financial statements for the year ended 2 July 2011. Together with certain information in the reports from the Chief Executive and the Finance Director on pages 10 to 21 above and the Corporate Social Responsibility review on pages 47 to 50 below, which are incorporated into this report by reference, this report satisfies the requirements of the Companies Act 2006 to produce a Business Review.

The purpose of this Business Review is to provide to shareholders a review of the Group's business over the period, and to describe the principal risks and uncertainties facing the Group.

Principal activity

The principal activity of the Group is that of a specialist UK homewares retailer selling to customers through stores and over the internet.

Review of business and future developments

A review of the business and future developments of the Group is given in the Chief Executive's Review on pages 10 to 14.

Shareholder and voting rights

All members who hold Ordinary Shares are entitled to attend and vote at the Annual General Meeting. On a show of hands at a general meeting every member present in person shall have one vote and on a poll, every member present in person or by proxy shall have one vote for every Ordinary Share held.

On 2 October 2006, Jean Adderley, Bill Adderley and Will Adderley (all shareholders) entered into a Relationship Agreement with the Company, pursuant to which each of Jean Adderley, Bill Adderley and Will Adderley undertook to the Company that, for so long as, individually or together, they are entitled to exercise, or to control the exercise of, 30 per cent or more of the rights to vote at general meetings of the Company or they are able to control the appointment of directors who are able to exercise a majority of votes at Board meetings of the Company, they will:

(a) conduct all transactions and relationships with any member of the Group on arms length terms and on a normal commercial basis;
(b) not take any action which precludes or inhibits any member of the Group from carrying on its business independently of Jean and Bill Adderley and their associates (as defined in the Listing Rules);
(c) not exercise any of their voting rights or other powers to procure any amendment to the Articles of Association of the Company which would be inconsistent with or undermine any of the provisions of the Relationship Agreement;
(d) abstain from voting on any resolution to which LR11.7.R(4) of the Listing Rules applies involving Jean Adderley, Bill Adderley or Will Adderley or any of their associates as the related party;
(e) not carry on (other than through their holding of securities of the Company) or have any financial interest (other than a financial interest in securities which are held for investment purposes only) in any person who carries on a business as a homewares retailer, to the extent that it would be inconsistent with or undermine any provisions of the Relationship Agreement; and
(f) only enter into, amend or terminate any transaction, agreement or relationship between themselves or any of their associates and any member of the Group with the approval of a majority of the independent Non-Executive Directors.

There are no restrictions on the transfer of Ordinary Shares in the Company other than certain restrictions imposed by laws and regulations (such as insider trading and marketing requirements relating to close periods) and requirements of the Listing Rules whereby Directors and certain employees of the Company require Board approval to deal in the Company's securities.

Change of control

The Company is not party to any significant agreements which take effect, alter or terminate solely on a change of control of the Company following a takeover bid.

There are no agreements between the Company and its Directors or employees providing for additional compensation for loss of office or employment (whether through resignation, redundancy or otherwise) that occurs because of a takeover bid.

Results and dividends

The consolidated profit for the year after taxation was £59.8m (2010: £54.4m). The results are discussed in greater detail in the Finance Director's review on pages 16 and 18.

A final dividend of 8.0p per share (2010: 5.0p) is proposed in respect of the year ended 2 July 2011 to add to an interim dividend of 3.5p per share paid on 1 April 2011 (2010: 3.0p per share). The final dividend will be paid on 16 December 2011 to shareholders on the register at 25 November 2011.

Directors

Details of the Directors in office at the year end are set out on page 24.

Directors serving at the year end and their beneficial interests in the shares of the Company were:

	At 2 July 2011 1p ordinary shares	At 3 July 2010 1p ordinary shares
WL Adderley	69,943,939	69,953,809
D Stead	529,338	466,546
G Cooper	181,611	181,611
M Sears	101,313	100,000
N Wharton	30,000	12,500
S Emeny	26,400	24,000

During the period there were the following changes to Will Adderley's shareholding:

14 July 2010	Transfer to Nadine Adderley (his spouse)	–2,000,000
11 October 2010	Exercise of nil cost options under LTIP	190,130
11 October 2010	Transfer to Nadine Adderley (his spouse)	–190,130
30 November 2010	Transfer to the Leicester Foundation	–200,000

All of the shares held by Nadine Adderley are included in the total beneficial interest of Will Adderley in the table above. At the period end Nadine Adderley's shareholding was 2,283,939 Ordinary Shares.

Will Adderley is deemed to retain a legal interest in shares held by two trusts, the Leicester Foundation and the Paddocks Discretionary Trust, by virtue of the fact that he and his wife are trustees , although not beneficiaries, of those trusts. At the period end the shareholdings of these trusts were: Leicester Foundation 167,250 Ordinary Shares (2010: 140,000), Paddocks Trust 172,750 Ordinary Shares (2010: nil). These interests are not included in the table above.

David Stead exercised nil cost options over 127,792 shares under the Long Term Incentive Plan on 12 October 2010. On the same day he sold 65,000 Ordinary Shares at a price of 445.91p per share to cover his income tax and national insurance liability, the balance of 62,792 shares were transferred to his wife Jane Stead. Shares held by David's wife are included in his beneficial interest in the table above.

On 23 February 2011, Donna Wharton, the wife of Nick Wharton purchased 17,500 shares, included in Nick's beneficial holding in the table above, and Marion Sears purchased 1,313 shares. Simon Emeny purchased 2,400 Ordinary Shares on 23 May 2011.

There were no changes in the Directors' shareholdings between the year end and 15 September 2011.

Details of share options held by Directors at the year end are given in the Remuneration Report.

All Directors will be retiring at the 2011 Annual General Meeting and will be offering themselves for re-election. Biographical details of the Directors are set out on page 24 and details of their service contracts are in the Remuneration Report on page 44.

Share capital and treasury shares

The Company has only one class of shares, Ordinary Shares of 1p each.

The issued Ordinary Share capital of the Company has increased by 449,960 Ordinary Shares during the period plus 99,628 shares were issued out of treasury due to the exercise of share options. Details of option exercises by Directors are set out above.

At 2 July 2011 the Company did not hold any Ordinary Shares in treasury. During the period 99,628 Ordinary Shares were transferred out of treasury to employees on the exercise of share options as noted above. There have been no movements of shares in or out of treasury since the period end.

Governance

Directors' report and business review *continued*

Substantial shareholders
At 15 September 2011 the following had notified the Company of a disclosable interest in 3% or more of the nominal value of the Company's Ordinary Shares:

	Ordinary shares	Percentage of share capital
WL Adderley	69,943,939	34.7
W Adderley	48,070,000	23.8

WL Adderley is also deemed to hold a legal interest in 167,250 Ordinary Shares held by The Leicester Foundation and 172,750 Ordinary Shares held by the Paddocks Discretionary Trust, by virtue of the fact that he is a trustee of those trusts.

Powers of directors
Specific powers of the Directors in relation to shares and the Company's Articles of Association are referred to in the Corporate Governance report on page 31.

Treasury and risk management
The Group's approach to treasury and financial risk management is explained in the Key Risks and Uncertainties section on pages 20 to 21.

Going concern
The Directors have made appropriate enquiries and formed a judgement at the time of approving the financial statements that there is a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason the Directors continue to adopt the going concern basis in preparing the financial statements.

Disclosure of information to auditors
The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Group's auditors are unaware; and each Director has taken all the steps that they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Group's auditors are aware of that information.

Disclaimer
This Directors' Report and Business Review and the Financial Statements contain certain forward-looking statements with respect to the financial condition, results, operations and business of Dunelm Group plc. These statements and forecasts involve risk and uncertainty because they relate to events, and depend upon circumstances, that will occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements and forecasts. Nothing in this Directors' Report and Business Review or in these Financial Statements should be construed as a profit forecast.

Annual General Meeting

The Annual General Meeting will be held at 10.30am on Thursday 17 November at Cheshunt Marriott Hotel, Halfhide Lane, Turnford, Hertfordshire, EN10 6NG.

Special business at the Annual General Meeting will be:

- Requesting authority pursuant to section 551 of the Companies Act 2006, to issue shares to the value of one third of the issued Ordinary Share capital of the Company. The nominal amount of shares covered by this authority is £671,637, (67,163,699 Ordinary Shares), 33.3% of the issued share capital at 15 September 2011. This authority will lapse at the 2012 Annual General Meeting or, if earlier, on 31 December 2012. The Directors have no present intention to exercise this authority except to issue shares pursuant to the Group's employee share schemes.
- Requesting authority pursuant to section 561 of the Companies Act 2006 to distribute Ordinary Shares to the value of £100,746 (10,074,555 Ordinary Shares), which constitutes 5% of the Company's issued share capital at 15 September 2011, without offering them to existing shareholders. This authority will lapse at the 2012 Annual General Meeting or, if earlier, on 31 December 2012. The Directors do not intend to issue more than 7.5% of the issued share capital of the Company for cash on a non pre-emptive basis in any rolling three year period without prior consultation with the Investment Committees of the Association of British Insurers and the National Association of Pension Funds.
- Requesting that the Directors be authorised pursuant to section 701 of the Companies Act 2006 to buy up to 5,000,000 Ordinary Shares approximately 2.5% of the issued Ordinary Share capital in the Company. The Directors will only exercise this authority if it is expected to enhance earnings per share and is in the interests of shareholders generally. Shares purchased may be cancelled or held in treasury. If held in treasury and used to satisfy share options, the NAPF's (National Association of Pension Funds) guidelines would be complied with.
- Requesting a waiver of any obligation that could arise on WL Adderley to make a general offer for the entire issued capital of the Company as a result of purchases by the Company of Ordinary Shares; and/or the exercise by WL Adderley of options granted to him under the Company's Long-Term Incentive Plan. Voting on these resolutions will take place on a poll; WL Adderley and persons connected with him will not be eligible to vote.
- Authorising the Board to convene a general meeting other than an Annual General Meeting on at least 14 days' notice. The Companies (Shareholders' Rights) Regulations require that all meetings other than an Annual General Meeting must be held on at least 21 days' notice unless shareholders agree to a shorter period. Under the Companies Act 2006 and the Company's Articles of Association, the Company can call meetings other than an Annual General Meeting on 14 days' notice. This resolution will allow the Company to continue to do so, and will be effective until the next Annual General Meeting when it is intended that a similar resolution will be proposed. The Company will also need to meet the requirements for electronic voting under the Regulations before it can call a meeting on 14 days' notice.
- Adopting new Articles of Association. The amendments are primarily to take account of the coming into force of the Shareholders' Rights Regulations in August 2009, and the implementation of the last parts of the Companies Act 2006. Further details are set out in the Notice of Annual Meeting.
- Amending the rules of the Company's Long-Term Incentive Plan, to increase the maximum annual grant from 120% of base salary to 150% of base salary. Further details are set out in the Notice of Annual Meeting.

The Notice of Annual General Meeting is set out in the separate booklet enclosed with this report.

Auditors

KPMG Audit Plc offer themselves for reappointment as auditors in accordance with section 489 of the Companies Act 2006.

By order of the Board

David Stead
Company Secretary
15 September 2011

Corporate governance report

The Board is committed to high standards of corporate governance. This report explains how the Group has applied the principles of good governance and code of best practice set out in the Corporate Governance Code ('the Corporate Governance Code') published in June 2010.

The Board considers that it has complied with the Corporate Governance Code during the financial year, except in one respect: On 1 December 2010, Nick Wharton, formerly an independent Non-Executive Director of the Company and Chairman of the Audit Committee, was appointed as Chief Executive Designate of the Company, succeeding to the Chief Executive position on 17 February 2011. Therefore, since 1 December 2010, the Board has comprised the Chairman, three Executive Directors and two independent Non-Executive Directors, which means that the required balance is not in place. As a consequence Committee membership has also not been in accordance with the Code; the Chairman has been acting Chairman of the Audit Committee, and he has also sat on the Nominations and Remuneration Committee. As explained in the Chairman's letter above, the Board has been actively seeking an additional Non-Executive Director during the year. The Board is satisfied that it has continued to operate effectively despite the lack of required balance, as demonstrated by the continuing success of the business.

The Board

The Board has overall responsibility for controlling the Group, making decisions relating to the Group's strategic direction and measuring progress towards strategic goals.

The Board held 10 meetings in the course of the year with one meeting extended to include a formal review of strategy. Attendance at meetings was as follows:

Director	Meetings attended
Geoff Cooper	10
Marion Sears	10
Will Adderley	10
Simon Emeny	8
Nick Wharton	10
David Stead	10

There is a schedule of matters reserved to the Board for decision or approval, which was reviewed in 2011 and is available on the Group's website or from the Company Secretary. Examples of such matters include Group strategy and budget, Group capital structure, approval of financial results and report and accounts, significant capital or contractual commitments, maintaining internal control and risk management, and approval of Group-wide policies.

At each meeting, the Chief Executive and the Finance Director report on operational performance (including health and safety) and the Finance Director reports on financial performance and position. Other matters are discussed by the Board as required, supported by a briefing paper where a decision is to be made by the Board.

Minutes of all Board and Committee meetings are taken by the Company Secretary and committee secretaries respectively and circulated for approval. Any unresolved concerns raised by a Director are recorded in the minutes.

The Chairman and the other Non-Executive Directors meet from time to time without Executive Directors being present, and regularly have individual meetings with other senior managers in the business. In addition the Non-Executive Directors have the opportunity to meet at least once a year without the Chairman present as part of the Board effectiveness review process, which includes a formal review of the Chairman's performance.

Directors

The Non-Executive Chairman is Geoff Cooper, the Executive Deputy Chairman is Will Adderley, and the Chief Executive is Nick Wharton. At the beginning of the financial year Will Adderley was the Chief Executive, however it was announced on 16 September 2010 that he would relinquish this role and become Executive Deputy Chairman from 17 February 2011. Nick Wharton was appointed as Chief Executive Designate on 1 December 2010, and became Chief Executive on 17 February 2011.

The Board has adopted written statements setting out the respective responsibilities of the Chairman, Executive Deputy Chairman and the Chief Executive, these are available on the Group's website or from the Company Secretary. In general terms, the Chairman is responsible for running the Board and the Chief Executive is responsible for running the Group's business, supported by the Executive Deputy Chairman who focuses specifically on strategic activities which protect and enhance shareholder value and embed the Company's culture and values.

The other Non-Executive Directors are Marion Sears and Simon Emeny. David Stead is an Executive Director and Company Secretary. David will relinquish his role as Company Secretary in November 2011 when the Company's newly appointed Company Secretary takes up her position.

The Senior Independent Director is Marion Sears.

The Board considers that Geoff Cooper was independent on appointment, and that Marion Sears and Simon Emeny are independent. Overall the Board considers that there is a good balance of Executive and Non-Executive Directors.

In accordance with the Corporate Governance Code, all Directors will retire from the Board and offer themselves for re-election at the Annual General Meeting.

Board committees

The Board has appointed three committees, an Audit Committee, a Nominations Committee and a Remuneration Committee. The terms of reference of each of these committees, which were updated in 2011, can be found on the Group's website at www.dunelm-mill.com and are available from the Company Secretary.

Details of the membership of the committees and of their activities during the past financial year, can be found in the reports from the Chair of each of the committees on pages 34 to 46.

Appointment and removal of Directors

The Articles of Association of the Company provide that a Director may be appointed by ordinary resolution of the Company's shareholders in general meeting, or by the Board so long as the Director stands down and offers himself for election at the next Annual General Meeting of the Company. The Articles also provide that each Director must stand down and offer him or herself for re-election by shareholders at the Annual General Meeting at least every three years. The Board has decided to adopt the requirement of the Corporate Governance Code, that all Directors should stand down and offer themselves for re-election at the Annual General Meeting.

Directors may be removed by a special resolution of shareholders, or by an ordinary resolution of which special notice has been given in accordance with the Companies Act 2006. The Articles also provide that the office of a Director shall be vacated if he is prohibited by law from being a director, or is bankrupt; and that the Board may resolve that his office be vacated if he is of unsound mind or is absent from Board meetings without consent for six months or more. A Director may also resign from the Board.

The Nominations Committee makes recommendations to the Board on the appointment and removal of Directors.

Powers of Directors

In accordance with the Companies Act 2006 and the Articles of Association, the business of the Company is managed by the Board, which may exercise all of the powers of the Company, subject to the requirements of the Companies Acts, the Memorandum and Articles of Association of the Company, and any special resolution of the Company. As stated above, the Board has adopted internal delegations of authority in accordance with the Code, and these set out matters which are reserved to the Board or committees and the powers and duties of the Chairman, the Executive Deputy Chairman and the Chief Executive respectively.

At the Annual General Meetings of the Company in 2007, 2008, 2009 and 2010 the Board sought and was given authority to issue shares and to buy back and re-issue shares, subject to the limits imposed by law and those set out in the text of the resolution. Similar resolutions are being tabled at the 2011 Annual General Meeting, together with a waiver of any obligation of Will Adderley under the City Code on Takeovers and Mergers to make an offer for all of the shares of the Company if the authority to buy back shares is used. For further details see page 29 of the Directors' Report and Business Review, and the Notice of Annual General Meeting which accompanies this report.

Advice and insurance

All Directors have access to the advice and services of the Company Secretary. In addition Directors may seek legal advice at the Group's cost if they consider it necessary in connection with their duties.

The Group purchases Directors' and Officers' Liability insurance cover for its Directors.

Training

Upon joining the Board, any new Director is offered a comprehensive induction programme with visits to key sites and meetings with senior managers and other staff members. As part of each Director's annual review any additional training or development needs are addressed. Throughout the year all Directors have maintained a regular series of visits to stores and meetings with members of the senior management team. The Board has also received presentations from independent advisers on financial policy and on corporate governance trends.

Geoff Cooper and Simon Emeny are considered to have relevant and up-to-date skills and experience for a listed retail business due to their current executive positions in businesses with similar multi-site, consumer-facing business models. Marion Sears has a different perspective of retail from her other Non-Executive role and also brings City and Shareholder experience due to her former executive position in banking. Directors also attend seminars and tutorials provided by independent organisations for NEDs which cover the whole range of governance topics.

Corporate governance report *continued*

Evaluation

The Chairman appraises the performance of the Chief Executive with regard to personal objectives agreed at the start of each financial year. The Chief Executive similarly appraises the performance of other Executive Directors.

There is a formal, rigorous and well established process for evaluating the performance of the Chairman, the other Non-Executive Directors, the Board Committees and the Board as a whole. This takes the form of a Board meeting convened solely for the purpose of such review. During the course of this meeting there is the opportunity for the Chairman or other individual Directors to be asked to leave the discussion whilst their performance is assessed. Separately the Senior Independent Director meets with the other Non-Executive Directors to evaluate the Chairman's performance. Further details are included in the Nominations Committee Report.

Following the review a list of actions is formulated and progress against these is reviewed periodically by the Board.

The Board intends to appoint an external provider to carry out a Board evaluation in 2013.

Conflicts of interest

The Companies Act 2006 allows the Board of public companies to authorise conflicts and potential conflicts of interest of individual directors where the Articles of Association contain a provision to that effect. At the 2008 Annual General Meeting, new Articles of Association were adopted which give the Board this authority subject to the following safeguards:

- Directors who have an interest in matters under discussion at a Board meeting must declare that interest and abstain from voting.
- Only directors who have no interest in the matter being considered are able to approve a conflict of interest, and, in taking that decision the Directors must act in a way they consider, in good faith, would be most likely to promote the success of the Company.
- The Directors are able to impose limits or conditions when giving authorisation if they feel this is appropriate.

These provisions are also in the Articles of Association being put forward for approval at the AGM.

Following the adoption of the Articles of Association, all Directors were requested to disclose any actual or potential conflicts to the Board and the following matters were considered and approved:

- Will Adderley is a major shareholder and connected to other major shareholders. Authorised on the basis that Mr Adderley continues to abide by the terms of the Relationship Agreement entered into between himself, other major shareholders and the Company on flotation of the Company in 2006.
- Geoff Cooper is a director of Travis Perkins plc which potentially competes with the Company for retail property. Authorised on the basis that Mr Cooper is not involved in day to day decisions in relation to the property portfolio in either company.
- Until 30 November 2010, Nick Wharton was a director of Halfords Group PLC which potentially competes with the Company for retail property. Authorised on the basis that Mr Wharton was not involved in day to day decisions in relation to the property portfolio in either company.

There were no other matters disclosed that were considered by the Board to give rise to a conflict of interest.

Any conflicts considered by the Board and any authorisations given are recorded in the Board minutes and reviewed annually by the Board.

The Board considers that its procedures to approve conflicts of interest and potential conflicts of interest are operating effectively.

Significant shareholders

The Group's significant shareholders are listed in the Directors' report on page 28 and voting rights are stated on page 26.

Articles of Association

The Company's Articles of Association may only be amended by a special resolution of shareholders.

Risk management
Throughout the year and up to the date of approval of this Annual Report there has been in place an established, ongoing process for identifying, evaluating and managing the significant risks faced by the Group. The process has been reviewed by the Audit Committee and the Board and is in accordance with the Turnbull Guidance on Internal Control for Directors.

A register of major strategic and operational risks is maintained and reviewed twice per annum by the Board, who also monitor the status of agreed actions to mitigate key risks. Management review the register once a year in a workshop and quarterly after that. During the year the register was expanded and each risk analysed in more detail.

In addition, during the year, the Non-Executive Directors reviewed the risk management process overall and considered how other companies monitor risk. Following this review a series of 'risk' topics were selected for in-depth discussion by the Board through department heads. This will now be an on-going process in which, for each risk topic, the executive staff member responsible prepares a board briefing, presents it to all of the Directors and answers questions. Topics covered up to the date of this Annual Report include IT capacity, key suppliers, ethical sourcing and fraud risk.

Internal control
The Board is ultimately responsible for the Group's system of internal control and for reviewing its effectiveness. However such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can provide only reasonable, and not absolute, assurance against material loss and misstatement.

The Group maintains a well established control framework comprising clear structures and accountabilities, well understood policies and procedures and budgeting and review processes.

Each store manager has clear responsibilities and operates within defined policies and procedures covering such areas as financial targets, human resources management, customer service, health and safety. The Executive Directors monitor compliance with these policies and procedures in the course of regular reviews.

The Audit Committee considers annually whether an internal audit function is required. It does not currently consider that this is necessary in view of the adequacy of internal and risk management controls and reporting in place, the relatively low level of complexity in the business and the close involvement of the Executive Directors in the operation of the business.

Investor relations and understanding shareholder views
There is a formal investor relations programme based around results presentations and trading statements and the Board takes a number of additional steps to ensure that all Directors have a clear understanding of the views of major shareholders about the Company. Analyst/shareholder visits are arranged with the executives and comments are reported back to the Board. The Non-Executive Directors attend the results presentations and are available to attend meetings at shareholder request.

All Directors will be available at the Annual General Meeting to meet with shareholders and answer their questions.

As a further step to promoting communication and shareholder understanding, we plan to invite corporate governance representatives of our major institutional shareholders to a presentation in January 2012, and from time to time thereafter. This will be hosted by the Chairman, the Non-Executive Directors and Will Adderley, the Executive Deputy Chairman, representing the majority family shareholding. The other executives will not be present.

Governance

Audit Committee report

This report provides details of the role of the Audit Committee and the work it has undertaken during the year.

The purpose of the committee is to oversee the integrity of the Group's financial statements and public announcements relating to financial performance, to oversee the audit process, monitor the effectiveness of financial controls and the process for identifying and managing risk throughout the Group. The full terms of reference for the committee can be found on the Company's website, www.dunelm-mill.com.

The following Directors served on the Committee during the year:

Member	Period from:	To:
Geoff Cooper (acting Chair)	1 December 2010	To date
Marion Sears	18 January 2005	To date
Simon Emeny	25 June 2007	To date
Nick Wharton	16 September 2009	30 November 2010

Nick Wharton was the Chairman of the committee as a Non-Executive Director, prior to assuming his executive role on 1 December 2010. Since that date I have been acting Chairman, it being the intention of the Board to appoint an additional Non-Executive Director who will assume this position. Details of this process are in the Nominations Committee report.

The Board considers that I have recent and relevant financial experience by virtue of my professional qualification and my current executive role as Chief Executive of Travis Perkins plc.

Committee activities in 2010/11

Two meetings were held in the year and members' attendance was as shown in the table below. Marion Sears also acts as Secretary to the committee.

Member	Meetings attended:
Geoff Cooper (acting Chair)	2
Marion Sears	2
Simon Emeny	1
Nick Wharton	1

The Finance Director usually attends meetings by invitation, along with representatives from the external auditors.

During the year the activities of the Committee included:

- Approval of the full year results issued in September 2010 and the half year results issued in February 2011;
- Review of the requirement for an internal audit function – we continue to consider that this is not required in view of the adequacy of financial controls in place and the relatively low level of complexity in the business;
- Review and confirmation of the Group's policy for use of external auditors for non-audit work; the committee has approved a policy that the auditors should only be used for non-audit work if they offer demonstrably better capability than alternative providers and there is no potential conflict with the independence of the audit;
- Verification of the independence of the external auditors, and approval of the scope of the audit plan and the audit fee.

During the year management completed a review of risks throughout the Group to refresh the Company's risk register prior to presentation to the Board. Reviews were primarily focused on risk associated with delivery of the Group's growth strategy, key operational risks, governance & legislative risk and financial risk management and control. A summary of the key risks is presented on pages 20 to 21.

The Audit Committee also reviewed the Group's Treasury Policy governing cash management and interest rate optimisation as well as foreign exchange rate risk and associated exposures. The policy was amended to ensure that appropriate consideration was given to exposures under a range of future scenarios and that the effectiveness of treasury instruments was being appropriately considered.

External Auditor

The Group re-appointed KPMG LLP as external auditor for the financial year ended 2 July 2011. The Group paid KPMG £72,000 in relation to the statutory audit of the Group and Company financial statements and the audit of Group subsidiaries pursuant to legislation. The Group also paid KPMG £43,000 in relation to other non-audit services which mainly consists of tax compliance and tax planning initiatives.

The committee met privately with the auditors in the course of each meeting during the period.

The committee has approved a policy which allows employees to raise legitimate concerns in confidence without fear of discrimination.

This report was reviewed and approved by the Board on 15 September 2011.

Geoff Cooper
Acting Chair, Audit Committee

Governance

Nominations Committee report

This report provides details of the role of the Nominations Committee and the work it has undertaken during the year.

The purpose of the committee is to assist the Board by keeping the composition of the Board under review and conducting a rigorous and transparent process when new appointments to the Board are made. The full terms of reference for the committee can be found on the Company's website, www.dunelm-mill.com.

The following Directors served on the committee during the year:

Member	Period from:	To:
Marion Sears (Chair)	18 January 2005	To date
Geoff Cooper	18 January 2005	To date
Simon Emeny	25 June 2007	To date
Nick Wharton	16 September 2009	30 November 2010
Will Adderley	17 February 2011	To date

Six meetings were held in the year and members' attendance was as shown in the table below. Marion Sears also acts as Secretary to the committee.

Member	Meetings attended:
Marion Sears (Chair)	6
Geoff Cooper	6
Simon Emeny	5
Nick Wharton	1
Will Adderley	3

General succession planning

The committee keeps under review the balance of skills on the Board as a whole and the knowledge, experience, length of service and performance of the directors. On at least an annual basis each director's intentions are discussed with regard to serving on the Board and their succession is considered in the context of the shape of the overall Board and the corporate governance guidance on NED tenure. This transparency amongst a small and collegiate Board allows for an open discussion about succession for each individual, both for short term emergency purposes as well as longer term retirement plans.

While all Board appointment processes and succession discussions are led by the Nominations Committee these are viewed as important whole-Board topics and no appointment will be made to the Board without unanimous agreement of all directors.

Committee activities in FY2010/11

Most of the committee's activities during the year have stemmed from the CEO succession during the year as described below:

CEO Succession

During the year the committee finalised the succession of Will Adderley as CEO by Nick Wharton, who was previously a Non-Executive Director of the Company. A search process was conducted, with the aid of an external search firm, in early 2010 which included Nick Wharton in its later stages as a candidate. Nick Wharton did not participate in committee discussions on CEO succession once his candidature was confirmed. As a result of this process we announced in September that Nick would succeed Will as CEO in February 2011, after a handover period.

NED search

Following Nick's appointment as CEO we believe that an appropriate Board structure for the Company is comprised of a Chairman, three Executive and three Non-Executive Directors. We announced last September that we would seek to appoint a new non-executive director to replace Nick. A detailed specification was prepared including the expected time commitment and a very large number of candidates were screened. Following a search during the year we identified two excellent candidates both of whom, ultimately, were unable to accept the position due to existing business commitments. Accordingly, we have restarted our search. We are working with the assistance of an external search firm and the search will be conducted, and any appointment will be made, on merit against the criteria specified having regard to the benefits of diversity on the Board, including gender. We look forward to announcing the appointment of a new Non Executive Director in due course and in the meantime, as a temporary measure, Geoff Cooper acts as Chair of the Audit Committee.

Skills, balance and Directors' Performance Evaluation

The Nominations Committee reviews Board composition and the balance of skills provided by the Directors in a whole Board session each year. A detailed review was conducted during 2010/11 in the light of the search process for a new Non-Executive Director. All the skills that a Company might require were considered and each Director assessed against these. The process enabled the committee to be specific about the operational expertise that we wish to identify in future senior level recruitment.

In addition, the performance of all of the Directors has been assessed individually. The Chairman of the Board led a process of collecting feedback on each Director's performance and provided them with a one-to-one evaluation and discussion of training needs. The Senior Independent Director collected feedback about the Chairman and provided an evaluation of his performance.

Tenure of Non-Executives

The Committee is mindful that both Geoff Cooper and Marion Sears have served on the Board for more than six years, and that the Corporate Governance Code and institutional shareholders expect a careful consideration of their continuing contribution, balanced against the value of refreshing Board membership. The Committee, in consultation with the Board as a whole, considers that each of these individuals continues to offer valuable leadership and challenge to the Board. In the context of the transition of the Chief Executive role and the ongoing search for an additional Non-Executive Director, the Committee and the Board consider that their continued membership of the Board outweighs any benefit that might be obtained by seeking to replace them.

Diversity

In conjunction with whole Board discussions, the committee specifically considered its approach to Board diversity, including gender diversity, following publication of the Davies report in February 2011. These issues were considered in the following context:

- The vast majority of Dunelm customers are female
- The majority of staff members (65%) are female, including over 50% of store management
- 7 of the 24 most senior positions in the business below Board level are held by women
- There has been a female Board member since 2004.

Whilst confirming that the overriding concern is to ensure that the Board comprises outstanding individuals who can lead the Company, the committee also believes that the Company's best interests are served by ensuring that these individuals represent a range of skills, experiences, backgrounds and perspectives, including gender. Accordingly, Dunelm's policy is that the Board should always be of mixed gender. That said, we believe that whilst discussion of quotas may be needed to spur action, quotas are not appropriate as a target for female representation on company boards since they are likely to lead to compromised decisions on board membership, quality and size.

In the three most recent Director searches (one still in progress), specific and directed effort has been made to ensure female candidates can be considered. It should be noted that this approach was adopted prior to the prospect of gender quotas.

In order to ensure a strong supply of female candidates for senior positions in the future, all organisations will have to ensure that women are able to develop their careers. The committee has examined Dunelm's approach to the development of talented individuals of either gender throughout the Group and is satisfied that current practices are 'gender-neutral'. We will continue to ensure that the approach enables talented individuals, both male and female, to enjoy career progression opportunities within Dunelm.

Re-election of Directors

During the year the Board discussed the UK Corporate Governance Code's proposal of annual re-election of directors. Whilst we have reservations as we believe other and better avenues exist to enable shareholders to register any dissatisfaction, we have decided to adopt the guidance. Accordingly all Directors will seek re-election at the 2011 and future AGMs.

This report was reviewed and approved by the Board on 15 September 2011.

Marion Sears
Chair of the Nominations Committee

Letter from the Chair of the Remuneration Committee

Dear Shareholder,
I wrote to shareholders in last year's annual report setting out the principles behind Dunelm's approach to executive remuneration, as well as explaining the thinking behind the most significant remuneration event of last year which was setting the remuneration and incentive targets for our new Chief Executive, Nick Wharton.

There has been no change to our underlying philosophy over the past year. However, as indicated in my previous letter we have taken independent advice on the reward level and performance targets relating to our Long Term Incentive Plan for Executive Directors. Proposed changes have been discussed with major shareholders and are described fully within the Remuneration Report. We will seek shareholder approval for them at the forthcoming AGM.

Other than the above point, there are no plans for significant change to remuneration in the coming year. Base salary increases for Executive Directors will be minimal, with only David Stead receiving an increase. The performance range for awards under the annual bonus scheme will be tightened to 95% – 105% of EPS target (previously 93% – 112%), as we feel this is more appropriate for the size of business which Dunelm has become.

The Remuneration Committee has been actively involved in setting remuneration packages for senior managers below Board level. The principles applying to Executive Director remuneration have also been used in structuring the packages for members of the newly formed operating board, ensuring strong alignment of targets at that next level in the organisation.

As Chair of the Remuneration Committee, I am passionate about extending share ownership as far into the organisation as possible. The Committee has therefore agreed a minimum shareholding requirement for Executive Directors of twice base salary, to be acquired over time. At the operating board level, managers are required to build over time a holding of at least one times their base salary. Last but not least, I am delighted that many members of staff have had the opportunity to share in Dunelm's wealth creation through our approved Sharesave scheme, under which two savings opportunities have now matured.

Yours faithfully,

Marion Sears
Chair of the Remuneration Committee
15 September 2011

Remuneration report

The Directors present their Remuneration Report for the period ended 2 July 2011.

Introduction

The Remuneration Committee has prepared this report in accordance with the requirements of Section 420 Companies Act 2006 and the Listing Rules. The report and the Group's remuneration policy comply with the UK Corporate Governance Code. An ordinary resolution to approve the report through a shareholder vote will be proposed at the Annual General Meeting.

The disclosures that the Group's auditors are required to audit within the Remuneration Report are contained in the section headed 'Audited Information'. The auditors' opinion is included in their report on page 52.

In this report Nick Wharton appears both as a Non-Executive Director and as CEO. This is because he served as Non-Executive Director until 1 December 2010 when he was appointed as CEO designate. Nick succeeded Will Adderley as CEO on 17 February 2011 when Will became Executive Deputy Chairman.

Non-audited information

Remuneration committee membership and advisers

The purpose of the Committee is to assist the Board by:

- Recommending to the Board the specific pay and benefits packages for the Executive Directors, including the remuneration package of Nick Wharton on appointment as Chief Executive;
- Recommending and monitoring the structure and level of pay and benefits for senior management below Board level; and
- Implementing any awards made under share incentive schemes.

The full terms of reference for the Committee can be found on the Company's website, www.dunelm-mill.com.

The following Directors served on the Committee during the year:

Member	Period from:	To:
Marion Sears (Chair)	18 January 2005	To date
Geoff Cooper	18 January 2005	To date
Simon Emeny	25 June 2007	To date
Nick Wharton	16 September 2009	30 November 2010

Marion Sears acts as Secretary to the Committee.

Six meetings were held in the year and members' attendance was as shown in the table below.

Member	Meetings attended:
Marion Sears (Chair)	6
Geoff Cooper	6
Simon Emeny	5
Nick Wharton	1

Prior to his appointment as an Executive Director on 1 December 2010, Nick Wharton was a member of the committee in his role as Non-Executive Director. He did not participate in any decisions concerning his own remuneration. No Director is ever present when their own remuneration is discussed.

During the year, the committee appointed Deloitte to review and benchmark the remuneration of the Executive Directors. Deloitte's only other connection with the Company in the last financial year was to provide advice on certain taxation matters in which they were considered to have particular expertise.

Governance

Remuneration report *continued*

Remuneration committee role, responsibility and meetings

The Board has delegated to the Remuneration Committee responsibility for reviewing and recommending the pay and benefits and contractual arrangements of the Executive Directors and senior managers and for overseeing the operation of the Group's share schemes. The Remuneration Committee is committed to principles of accountability and transparency to ensure that remuneration arrangements demonstrate a clear link between performance and reward. The committee considers fully the principles and provisions of the UK Corporate Governance Code and its terms of reference are available on the Group's website.

Executive remuneration policy and alignment with corporate strategy

The Remuneration Committee's policy is to provide an executive remuneration structure that will pay fairly for the roles and responsibilities of each director, and incentivise strongly for value creation, with an emphasis on the long term. This is in line with our successful strategy to continue to grow and strengthen our business as described in the Chief Executive's review.

The Committee considers alignment between Group strategy and the remuneration of its senior executives to be critical. In view of this required director shareholdings are set at above market levels. The committee also believes that senior executives should be highly rewarded on a market competitive basis for the delivery of stretching goals but should receive reduced rewards if the business performs poorly. The pay and employment conditions of employees of the Group are also taken into account when determining directors' remuneration.

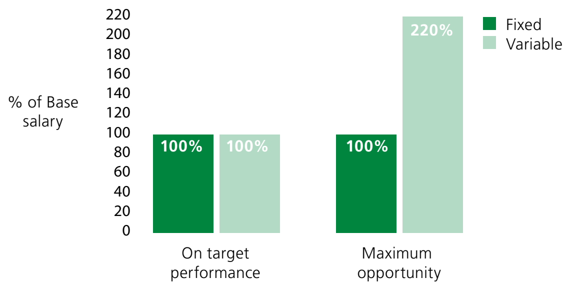
In particular the remuneration policy aims to provide packages for Executive Directors and other senior managers in the Group which:

- Align management's interests with those of shareholders by incentivising management to deliver the Group's long-term strategy and enhance shareholder value;
- Provide management with the opportunity to earn competitive remuneration through variable pay;
- Provide upper quartile rewards compared to other FTSE 250 companies, but only if upper quartile performance is delivered; and
- Enable the Group to attract and retain management of the calibre required to run the business and drive exceptional shareholder value creation.

To strengthen further the alignment between management and long term business success, Executive Directors are required to build up, over time, a shareholding equivalent to at least twice their base salary.

Balance of fixed and variable remuneration

The Remuneration Committee's policy is that a substantial proportion of the Executive Directors' remuneration should be variable and performance related in order to encourage and reward superior business performance and shareholder returns. Through performance criteria and the setting of personal objectives each director's remuneration is individually linked to both personal and Company performance. The following illustrates the balance between fixed and variable remuneration during the year for the Executive Directors:



The breakdown does not include any share price growth or other benefits (e.g. cash car allowance, value of private medical insurance, pension contribution or all employee share ownership plans).

Summary of Remuneration

The Remuneration Committee selects performance measures that it believes are aligned with the Group's strategic goals, that are unambiguous and easy to calculate and that are transparent to Directors and shareholders. Each element of remuneration is designed to support the achievement of different corporate objectives as outlined in the following table:

Element	Purpose and link to remuneration policy	Maximum award	Key features
Base salary	• Reflects at or below median market salary for the individual and their role • Takes account of personal performance and contribution to corporate performance	N/A	• Paid monthly in cash • Based on individual contribution • Reviewed annually – any increase in context of Group wide review
Annual Bonus	• Rewards the achievement of annual EPS targets	100% of base salary	• Paid in cash after year end results are audited • Remuneration Committee discretion linked to achievement of personal objectives
LTIP	• Aligns with shareholder interests through the delivery of shares • Rewards growth in long-term earnings and shareholder value	120% of base salary*	• Based on EPS performance • Vests based on a three year performance period • Shares vesting may contribute to minimum shareholding requirement

* Will increase to 150% of base salary in 2011/12, subject to shareholder approval.

During the year the committee expressly considered whether to introduce provisions that permit the Company to reclaim variable components of remuneration in exceptional circumstances. It was decided that while such provisions are particularly required in other industries, they would be inappropriate at this time at Dunelm.

Further details are provided about each element of remuneration below.

Base salary and benefits

Prior to the beginning of each financial year the Remuneration Committee sets the base salaries of Executive Directors. The committee examines the salaries of Directors in a comparator group of public companies and considers the operational scale and complexity of the role each Director performs. It also reviews published research and surveys, and considers the wage increases across the Group as a whole. The committee aims to set salaries at or below the median level provided by similar companies. In addition to base salary, the Executive Directors are entitled to benefits comprising a car allowance, a contribution to a personal pension, private medical insurance and life insurance.

During the year, Will Adderley received an increase in basic salary of 2%, in line with the pay increase across the Group. Will then took a reduced salary when he assumed his new role as Executive Deputy Chairman. Will's basic salary will be unchanged in 2011/12.

Nick Wharton's base salary and remuneration from date of joining were set out in last year's remuneration report. Nick's basic salary is first due for review from July 2012.

David Stead's role has increased significantly over recent years as a result of the growth of the business and includes additional responsibility, inter alia, for the HR and IT functions. After taking these factors into account and benchmarking David's salary against comparable roles in other companies, the committee awarded a base salary increase in 2010/11 of 13.6% to £255,000. It continues to be below median level for the FTSE 250 and below our closest competitors. In 2011/12 David's base salary has increased in line with the Company wide review by 1.5% to £258,800.

Governance

Remuneration report *continued*

Annual bonus

The Group operates a discretionary annual cash bonus scheme. Any bonus amounts determined to be payable are paid after the year-end results are finalised. The Remuneration Committee has established bonus objectives that are principally financial, based on the level of EPS achieved against target for the relevant financial year, but also include personal objectives for the year relevant to each Director.

In setting the budget EPS target for the year, both market consensus expectations for EPS and individual broker forecasts are considered. As notified in last year's annual report, the potential reward available to Executive Directors under this scheme was increased for the year ended 2 July 2011 as follows (with payment in each case conditional on satisfactory personal performance against job objectives):

	EPS performance (percentage of target)	Bonus payment (percentage of base salary)	
		FY10	FY11
Threshold	93%	3%	5%
Target	100%	24%	40%
Maximum	112%	60%	100%

For the year ended 2 July 2011, EPS was 7% below target. After due consideration of job performance, the committee awarded an annual bonus to Nick Wharton of £11,667 (proportionate to date of joining), to Will Adderley of £15,219 and to David Stead of £12,750.

Long-Term Incentive Plan

Under the LTIP, Executive Directors are awarded nominal cost share options annually. These awards will vest three years after date of grant, to the extent that the applicable performance target is met.

If there is a change of control of the Company, any awards under the LTIP that have not yet vested will be exercisable, at the discretion of the Company, taking into account the period of time that has elapsed since grant of the award, and to the extent that any performance target has been met.

The Remuneration Committee has chosen growth in fully diluted EPS over each three-year performance period as the performance target for the awards under the LTIP. The committee believes that this measure is closely aligned to the drivers of growth of the business, and that in the long term, EPS performance will be reflected in shareholder value. The committee is satisfied that capital expenditure controls exercised by the Board are sufficiently rigorous to avoid EPS accretion by means of ineffective investment of capital, and in any event reserves the right to adjust the target in the event of a major capital transaction.

The LTIP is structured as follows (awards vest on a straight-line basis between the threshold and maximum points):

	Compound Annual Growth in EPS		*Amount of award to vest*
Periods ending	2010	2011, 2012, 2013	
Threshold	RPI + 5%	RPI + 3%	25%
Maximum	RPI + 20%	RPI + 12%	100%

The committee decided after consultation with shareholders, to reduce the performance hurdle in respect of the schemes maturing from 2011, recognising the challenging market conditions expected to result from global recession.

The committee meets after the results for each three-year performance period and are available to determine the extent to which performance conditions have been satisfied. There is no retesting.

Awards cannot be granted to Executive Directors under the LTIP over Ordinary Shares in excess of 5% of the issued Ordinary Share capital in any rolling 10 year period.

Conditional awards of nominal cost options over Ordinary Shares worth 120% of base salary were made to Will Adderley and David Stead in March and September 2007, in September 2008 and in September 2009; and to Nick Wharton (pro rata to service), Will Adderley and David Stead on 1 December 2010. In addition, on 1 December 2010, with the approval of shareholders at the Annual General Meeting, a 'one off' nominal cost option award was made to Nick Wharton under the LTIP over 198,807 Ordinary Shares. The award will vest on 30 November 2015, subject to Nick continuing to be employed by the Company at that date. No other performance conditions apply to this award. The committee approved this award to Nick on his appointment as Chief Executive. It considered that a longer than usual vesting period (five years) would be sufficient without further performance hurdles being applied. The closing share price on the date preceding the options granted on 1 December 2010, which was used to calculate the number of shares covered by the award, was 503p.

The September 2007 award was in respect of the three-year performance period to 3 July 2010, over which the compound annual fully diluted growth in EPS was 30.1% (27.3% above RPI). Accordingly, 100% of the conditional nominal cost options awarded in September 2007 vested in September 2010 and the entitlements were exercised by both Will Adderley (190,130 shares) and David Stead (127,792 shares) on 11 and 12 October 2010. The closing share price on those days were 440p and 449p respectively.

The Remuneration Committee has reviewed the Company's EPS record over the three-year performance period which ended on 2 July 2011. Reported fully diluted EPS grew at a compound annual rate of 20.8%. This is 18.0% above RPI over the same period. Accordingly, 100% of the September 2008 LTIP award will vest in September 2011, representing 259,459 shares in favour of Will Adderley and 178,378 shares in favour of David Stead.

Changes in policy during the year

As noted in last year's report, we increased the maximum annual cash bonus potential for Executive Directors in the year ended 2 July 2011 to 100% of salary (previously 60%). This change was made to bring Dunelm into line with normal market practice.

During the year a requirement was introduced for Executive Directors to build a shareholding over time equivalent to at least twice their basic salary, further reinforcing the alignment of interests between management and shareholders.

There have been no other changes to remuneration policy during the year.

Proposed future changes in policy

From 2011/12 the annual bonus performance range will move to 95% – 105% of budget EPS. This is a narrower range than the 93% – 112% used in the year ended 2 July 2011 but is considered to be more appropriate for a larger company. It also harmonises the bonus structure for Executive Directors with that of the new operating board.

We also indicated in last year's report that we would review the long-term incentive arrangements applicable to Executive Directors. A formal review was carried out in May with the benefit of external advice from Deloitte. In the review we took advice on how Dunelm's Long-Term Incentive Plan (LTIP) compared to equivalent schemes in other FTSE 250 companies, as well as the overall remuneration levels of Dunelm's Executive Directors compared with the median. The conclusion was that Dunelm's overall remuneration levels are restrained. This is because base salaries are at or below median levels and both annual bonus and LTIP are functions of base salary.

Whilst the Remuneration Committee is content with the positioning of Executive Directors' base salaries, we believe that it is important to provide both incentive and reward for strong business performance. Accordingly, taking into account the findings of our review we wish to increase both the maximum reward achievable under the LTIP and the performance target required in order to achieve the maximum reward. Specifically, we propose that the award of conditional nominal cost share options under the LTIP should be increased to 150 per cent of salary (currently 120 per cent), with vesting on a straight-line basis when compound annual growth rate in EPS over the plan period falls between RPI+3 per cent and RPI+15 per cent (currently RPI+3 per cent to RPI+12 per cent).

This proposed change will be put to shareholders for approval at the forthcoming AGM.

Governance

Remuneration report *continued*

Other share options
The Group operates an all-employee SAYE scheme in which Executive Directors are also entitled to participate after having been employed for 3 months.

Pension arrangements
The Remuneration Committee has decided not to use final salary pension plans as a way of remunerating its Executive Directors. Instead the Group contributes to the Executive Directors' personal pension plans. The Remuneration Committee believes this is an efficient way to assist Executives to prepare for retirement. When determining overall remuneration levels for an Executive, the Remuneration Committee takes account of contributions to pension plans.

Share ownership requirements
Executive Directors are required to build a shareholding equal to at least twice their base salary over time and shares vesting under the LTIP must be held for this purpose. Below Board level, members of the Operating Board are required to own shares equal to at least one times their base salary, to be accumulated over time.

Non-Executive remuneration policy
Non-Executive Directors' remuneration is determined by the Executive Directors. The Non-Executive Directors do not receive bonuses or participate in any incentive plans. They are paid annual fees which reflect additional responsibilities taken when chairing a committee of the Board. Fees were reviewed and amended in the light of market practice in July 2010. The next review will be in July 2012.

Service contracts
In accordance with the Group's policy, the service contracts of the Executive Directors have no fixed term, the notice period for termination is 12 months from either party and payments on termination are restricted to a maximum of the value of salary for the notice period. The Remuneration Committee will apply mitigation rigorously in respect of any post remuneration payment.

The Non-Executive Directors have letters of appointment for an initial period of three years with a provision for termination of one month's notice from either party, or three months' notice from either party in the case of Geoff Cooper, the Chairman.

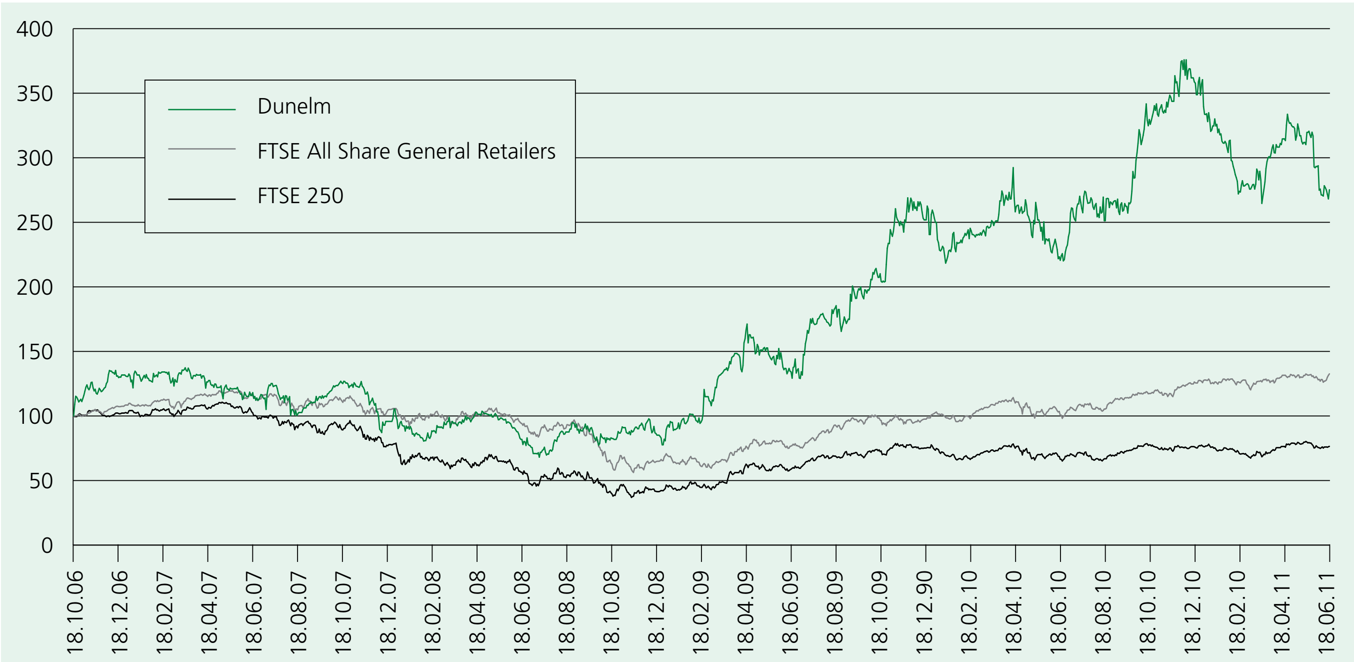
	Date of contract	Unexpired term	Notice period
Nick Wharton	15.09.10	n/a	12 months
Will Adderley	28.09.06	n/a	12 months
David Stead	15.09.03	n/a	12 months
Geoff Cooper	08.10.04	25 months	3 months
Marion Sears	22.07.04	22 months	1 month
Simon Emeny	25.06.07	21 months	1 month

Senior Executive remuneration
The Remuneration Committee provides oversight and guidance on the remuneration structure for below Board management. The package for new appointments is formally presented to the committee for approval. In conducting its assessment of senior executive remuneration the committee pays particular regard to whether any individual is incentivised to take risks inappropriate to their role and responsibilities. In the finance function, managers are not remunerated against individual financial performance, but against corporate performance and personal qualitative objectives.

Share options and dilution
It is Group policy to comply with the provisions of the Association of British Insurers' Guidelines on Executive Remuneration when determining the number of shares over which share scheme incentive awards may be made. At the date of this report options have been granted over 1.23% of the Company's issued share capital.

Performance graph

The graph below shows the Group's performance since flotation, measured by total shareholder return, compared with the FTSE General Retail Index and the FTSE 250. The Remuneration Committee has chosen these indices for comparison because they provide a range of comparator companies which have similar market capitalisation, which are in the same sector and which face similar market and economic challenges in the long term.



The shares traded in the range 326.8p to 550.0p during the year, and stood at 399.3p at 2 July 2011.

Audited information

Details of Directors' remuneration

Details of individual Directors' remuneration in respect of the year ended 2 July 2011 are as follows:

	Base salary or fees £'000	Vehicle allowance £'000	Taxable benefits £'000	Contribution to personal pension £'000	Joining incentive £'000	Annual bonus £'000	2011 Total £'000	Total 2010 £'000
Executive Directors								
Nick Wharton	233	7	1	23	150	15	429	–
Will Adderley	304	12	1	20	–	13	350	533
David Stead	255	12	–	20	–	12	299	389
Non-Executive Directors								
Geoff Cooper	100	–	–	–	–	–	100	86
Marion Sears	40	–	–	–	–	–	40	32
Simon Emeny	30	–	–	–	–	–	30	27
Nick Wharton	15	–	–	–	–	–	15	24
Total	977	31	2	63	150	40	1,263	1,091

Nick Wharton was appointed Chief Executive with effect from 1 December 2010. On taking up his position as an Executive Director on 1 December 2010, Nick Wharton received a cash payment of £150,000 to compensate him for the loss of bonus and other incentives at his previous employment.

Will Adderley's salary as Chief Executive was £332,500 from July to January inclusive, and as Executive Deputy Chairman was £265,000 from February to June inclusive.

David Stead waived taxable benefits totalling approximately £1,000.

Governance

Remuneration report *continued*

Directors' interests in share options

The Directors' beneficial interests in options granted under the Long-Term Incentive Plan, which (unless otherwise noted) will vest only if EPS performance conditions are met, are as follows:

Director	Date of award	Share options at 2 July 2011	End of performance period	Market Price of Shares at date of award
Nick Wharton	Dec 2010	198,807	Nov 2015*	503p
	Dec 2010	55,666	June 2013	503p
Will Adderley	Sept 2008	259,459	June 2011	148p
	Sept 2009	123,949	June 2012	316p
	Dec 2010	72,614	June 2013	503p
David Stead	Sept 2008	178,378	June 2011	148p
	Sept 2009	85,215	June 2012	316p
	Dec 2010	60,835	June 2013	503p

* The nominal cost options over 198,807 shares made to Nick Wharton on 1 December 2010 can only vest if he remains an employee for five years. There is no vesting entitlement if Nick leaves the company, for any reason, before 1 December 2015. This award was made in compensation for LTIP benefits left behind with Nick's previous employer and there are no other performance conditions attached to it.

The Directors' beneficial interests in options granted under other schemes are as follows:

Director	Type of option	Shares under option at 3 July 2010	Shares under option at 2 July 2011	Granted during period	Exercised during period	Lapsed during period	Exercise price per share	Market price of shares at date of exercise	Vesting date	Expiry date
Will Adderley	SAYE	7,710	7,710	–	–	–	124p	–	Jan 2012	Jun 2012
David Stead	SAYE	7,710	7,710	–	–	–	124p	–	Jan 2012	Jun 2012

Approval

This report was approved by the Board of Directors on 15 September 2011 and signed on its behalf by:

Marion Sears
Chair, Remuneration Committee
15 September 2011

Corporate social responsibility

Corporate Social Responsibility ('CSR') is integral to meeting the long-term expectations of our customers and other stakeholders and to ensure the sustainable development of our business.

It is clear that protecting the environment and running our business ethically not only makes good commercial sense but also improves the experience for both staff and customers. The Board places particular emphasis on maintaining good relationships with its customers, employees, suppliers and local communities; on ethical sourcing; on environmental issues; and on charitable contributions.

The Executive Management team reports regularly to the Board on all of these issues.

Our people

Dunelm employs over 6,600 people throughout the Group's 113 stores, distribution, manufacturing and head office locations and the Group places a high priority on maintaining regular communications with all employees. This keeps colleagues engaged in the development of the Group and also keeps them aware of the many career development opportunities that exist.

The Group is a growing business and places an emphasis on the retention and development of its own employees. Our benefits package is competitive. We offer nationally accredited training programmes and ILM (Institute of Leadership and Management) qualifications to support the development of talented individuals at all levels of the business.

The Group is an equal opportunities employer and is committed to recruit, develop, promote and retain skilled and motivated people regardless of disability, race, religion or belief, sex, sexual orientation, gender reassignment, marital status or age.

Our suppliers

Dunelm is clear that committed suppliers are crucial to us achieving our growth ambitions. Our products are sourced from many countries around the world and finding the best manufacturers to meet our high standards for design & innovation, quality and value is essential as we leverage our increased buying scale.

The Group continues to work in collaboration with suppliers to ensure that our products are produced in clean and safe environments, that workers are treated with respect and earn a reasonable wage and that suppliers work within the relevant local laws and legislation. All direct suppliers are required to sign up to our 'Ethical Code of Conduct' enforced by a full program of independent factory audits, based on the Ethical Trading Initiative ('ETI') base code.

Dunelm operates standard terms and conditions ensuring that all suppliers are treated fairly and on a consistent basis. All new suppliers are made aware of the basis of trade with Dunelm and in particular our standard payment terms in advance of commencing trade.

The number of days' purchases outstanding for payment at 2 July 2011 was 36 days (2010: 36 days).

Health and safety

Dunelm is committed to achieving high standards of health and safety in all operations and understands its duty of care to our employees, contractors, customers and any other visitors to our premises.

The business has a Health & Safety Committee which meets quarterly supported by a dedicated Health & Safety manager and senior operational management. This committee ensures that key risks are fully understood and that all mitigating action has been taken to provide a safe environment. Monthly KPI reporting, outlining significant risks and incidents, is also presented to the board.

The Group undertakes a program of risk assessments and audits to identify areas of concern whether it's in workplace transport, safety during store development or a safe shopping environment. Training programs ranging from documented Safe Systems of Work ('SSOW') to web based 'e-learning' and testing modules are also in place to help ensure a safe and clean environment and each site is subject to an annual compliance review.

During the past year the number of reported accidents was 49 (2010: 46).

Governance

Corporate social responsibility *continued*

Environment

Dunelm recognises that good environmental management makes good business sense. The Group is committed to controlling and minimising the impact of our operations both directly and indirectly in the key areas of waste management, energy consumption and carbon emissions.

The Company has established an 'Environment Policy' to determine appropriate business behaviour and has an 'Environment Committee' tasked with delivering the strategy to continually improve these key areas and to achieve high levels of environmental performance.

Our progress over the past financial year and our goals for the forthcoming year are detailed below:

1. Waste recycling

Dunelm is aiming to maximise the volume of waste which is recycled and in so doing reduce the volume going to landfill.

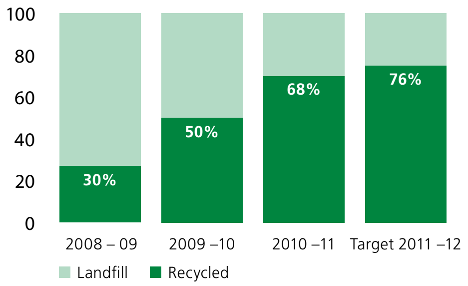
Part of our strategy is to boost recycling capabilities by accelerating our investment in balers. This year we have increased the number of sites with balers to 103 (2010: 43) and at the same time launched our 'Recycle at Work' initiative to engage colleagues in correct treatment of waste. A new position of 'Group Recycling Manager' has been created to oversee this and to deliver more effective waste management strategies.

In the year we have also completed the full roll-out of DMR ('Dry Mixed Recycling') to all Dunelm stores and central support facilities (2010: 12 sites). As a result we now recycle all of our plastics, paper, bottles and cans in addition to cardboard. We have also engaged our suppliers to review the specification of packaging used to maximise recyclable content.

These initiatives, together with enhanced volume, weight and contamination reporting of site by site performance has enabled Dunelm to reduce the proportion of waste to landfill from 50% (2010) to our lowest ever level of 32%.

Our target for the forthcoming year is to reduce the cube volume of waste sent to landfill by a further 25%. In addition we now expect to achieve our target of 'zero waste to landfill' within the next 3 years.

Waste recycled (all stores) – %



2. Energy usage

Energy reduction on a site-by-site basis has been a key focus for the Group in the last financial year.

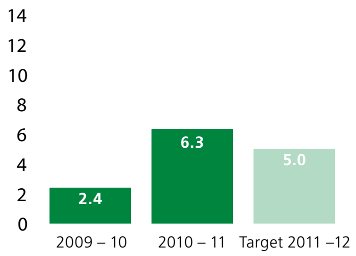
In addition to the AMR ('Automatic Meter Reading') smart meters that are in place for all electricity supplies we have applied the same technology to monitor and control our gas usage. Data on energy consumption is pulsed through on a half-hourly basis allowing us to profile high or unusual patterns, target specific sites and to monitor the success of our energy reduction initiatives.

All investments in new and refitted stores now come with a Building Management System ('BMS') as standard. This BMS is designed to optimise energy usage across the site while maintaining an appropriate shopping environment for our customers and staff. In H2 we commenced the trial of these systems in 3 other existing stores and we expect to roll-out more widely next year. At the end of the year we had 30 BMS stores (2010: 11).

As a result of these actions we have reduced electricity usage by 6.3% and gas usage by 20% in like-for-like stores.

Our target for the forthcoming year is to reduce electricity by 5% and gas usage by 10% in like-for-like stores.

YOY Reduction in electricity consumption (L4L stores) - %



3. Carbon emissions (CO_2)

We have reduced our total CO_2 equivalent emissions (from energy and business mileage) per ft^2 of selling space by 15% over the year. Dunelm's carbon footprint for the period ended 2 July 2010 was 23,280 tonnes of CO_2 (Company's Independent energy advisers).

Over the past year we have continued to source energy from 'Green Energy' supplies such as combined heat and power sources where CO_2 emissions are 30% lower than the national average. In July 2010 we agreed to switch all supplies of electricity to 'Green Energy' and we will continue to monitor this over the coming year.

We have continued to reduce the maximum emissions tolerated within our company car fleet, this is now 135g/km (2010: 155 g/km) and many fuel efficient variants have been added to the scheme.

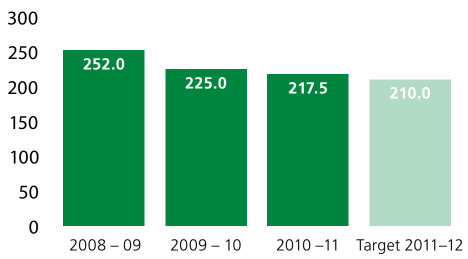
This year we will focus on building design and efficient investments to reduce consumption further. Continued investment in BMS will remain a strategic goal but we will also look to invest in LED lighting solution for stores where possible.

During the year Dunelm achieved the Carbon Trust Standard ('CTS') certification recognising our success in reducing our carbon footprint but also our continuing governance and management in this area. We have also registered for the Carbon Reduction Commitment ('CRC') and have submitted both 'annual' and 'footprint' reports as part of our commitment.

We will continue to partner with an external consultancy to further focus on reducing our carbon emissions.

Our target for the forthcoming year is to reduce relative CO_2 emissions year on year.

Carbon emissions - tonnes per store



Corporate social responsibility *continued*

4. Product packaging

Dunelm continues to work with suppliers to reduce both the absolute level and recyclability of packaging in our products.

In the year we have audited many of our waste streams to divert materials from landfill where possible. Most recently we have identified a particular spec of clear plastic or wrap that should be used by suppliers – LDPE ('Low Density Polyethylene'). This product has the most has a much greater recyclable content. This will be the standard for all suppliers going forward.

The Group is promoting a reduction in the use of 'single-use' carrier bags and we ensure that Eco-bags are offered in all stores.

Charitable donations

The Group's charity of the year in the last financial year was 'Rays of Sunshine' children's charity. Collections are made in stores, specific fund-raising events are organised and the Group makes its own donations, from time to time the Group also makes ad hoc donations to local charities.

The total value of donations made by the Group in the year ended 2 July 2011 was £56,000 (2010: £60,000). Total funds raised for charity by the Group and its staff was £140,000 (2010: £157,000).

Statement of Directors' responsibilities in respect of the Annual Report and the financial statements

The Directors are responsible for preparing the Annual Report and the Group and Parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the European Union ('EU') and applicable law and have elected to prepare the Parent Company financial statements on the same basis.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period. In preparing each of the Group and Parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transaction and disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that complies with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website.

Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility Statement

We confirm that to the best of our knowledge:

(a) The financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and

(b) the management report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

Geoff Cooper
Chairman
15 September 2011

Nick Wharton
Chief Executive

Independent Auditor's report to the members of Dunelm Group plc

We have audited the financial statements of Dunelm Group plc for the financial year ended 2 July 2011 set out on pages 53 to 57. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ('IFRSs') as adopted by the EU and, as regards the Parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Company's members, as a body, in accordance with chapter 3 of part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 51, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's ('APB's') Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at www.frc.org.uk/apb/scope/private.cfm.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 2 July 2011 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU;
- the Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006;
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the information given in the Corporate Governance Statement set out on pages 30 to 33 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- a Corporate Governance Statement has not been prepared by the company.

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 51, in relation to going concern; and
- the part of the Corporate Governance Statement on pages 30 to 33 relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review.
- certain elements of the report to shareholders by the Board on directors' remuneration.

Wayne Cox
(Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
Leicester
15 September 2011

Consolidated income statement
For the 52 weeks ended 2 July 2011

	Note	52 weeks 2011 £'000	52 weeks 2010 £'000
Revenue	1	**538,474**	492,839
Cost of sales		(280,125)	(262,253)
Gross profit		**258,349**	230,586
Operating costs	3	(175,051)	(155,126)
Operating profit	2	**83,298**	75,460
Financial income	5	523	1,361
Financial expenses	5	(172)	(65)
Profit before taxation		**83,649**	76,756
Taxation	6	(23,814)	(22,406)
Profit for the period attributable to equity shareholders of the parent		**59,835**	54,350
Earnings per ordinary share – basic	8	29.7p	27.1p
Earnings per ordinary share – diluted	8	29.3p	26.9p
Dividend proposed per ordinary share	7	8.0p	5.0p
Dividend paid per ordinary share	7	3.5p	3.0p

All activities relate to continuing operations.

Financial statements

Consolidated statement of comprehensive income
For the 52 weeks ended 2 July 2011

	52 weeks 2011 £'000	52 weeks 2010 £'000
Profit for the period	59,835	54,350
Effective portion of movement in fair value of cash flow hedges	147	(545)
Deferred tax on hedging movements	(50)	153
Total comprehensive income for the period	**59,932**	53,958

Consolidated statement of financial position
As at 2 July 2011

	Note	2 July 2011 £'000	3 July 2010 £'000
Non-current assets			
Intangible assets	9	4,692	5,202
Property, plant and equipment	10	125,850	102,599
Total non-current assets		**130,542**	107,801
Current assets			
Inventories	12	76,455	62,583
Trade and other receivables	13	14,566	10,470
Cash and cash equivalents	14	35,139	15,369
Total current assets		**126,160**	88,422
Total assets		**256,702**	196,223
Current liabilities			
Trade and other payables	15	(85,805)	(71,638)
Liability for current tax		(12,636)	(11,200)
Financial instruments	17	(398)	(545)
Total current liabilities		**(98,839)**	(83,383)
Non-current liabilities			
Deferred tax liability	11	(645)	(152)
Total non-current liabilities		(645)	(152)
Total liabilities		**(99,484)**	(83,535)
Net assets		**157,218**	112,688
Equity			
Issued capital	18	2,015	2,010
Share premium		681	580
Capital redemption reserve		43,155	43,155
Hedging reserve		(295)	(392)
Retained earnings		111,662	67,335
Total equity attributable to equity holders of the Parent		**157,218**	112,688

The financial statements on pages 53 to 73 were approved by the Board of Directors on 15 September 2011 and were signed on its behalf by:

Nick Wharton
Chief Executive

Financial statements

Consolidated statement of cash flows
For the 52 weeks ended 2 July 2011

	Note	52 weeks 2011 £'000	52 weeks 2010 £'000
Profit before taxation		83,649	76,756
Adjustment for net financing costs		(351)	(1,296)
Operating profit		83,298	75,460
Depreciation and amortisation		14,079	11,370
Loss on disposal of property, plant and equipment		703	13
Operating cash flows before movements in working capital		98,080	86,843
(Increase) in inventories		(13,872)	(4,688)
(Increase)/decrease in receivables		(4,080)	269
Increase in payables		13,848	6,094
Net movement in working capital		(4,104)	1,675
Share-based payments expense		1,199	1,330
Foreign exchange losses		(115)	516
		95,060	90,364
Interest paid		(29)	(71)
Interest received		507	557
Tax paid		(21,513)	(18,899)
Net cash generated from operating activities		**74,025**	71,951
Cash flows from investing activities			
Proceeds on disposal of property, plant and equipment		–	7
Acquisition of property, plant and equipment		(36,124)	(23,344)
Acquisition of intangible assets		(1,085)	(1,233)
Net cash utilised in investing activities		**(37,209)**	(24,570)
Cash flows from financing activities			
Proceeds from issue of share capital		101	244
Proceeds from issue of treasury shares		–	642
Repayment of bank loan		–	(10,000)
Proceeds from bank loan		–	10,000
Return of capital to shareholders		–	(43,155)
Dividends paid		(17,119)	(14,029)
Net cash flows utilised in financing activities		**(17,018)**	(56,298)
Net increase/(decrease) in cash and cash equivalents		19,798	(8,917)
Foreign exchange revaluations		(28)	288
Cash and cash equivalents at the beginning of the period		15,369	23,998
Cash and cash equivalents at the end of the period	14	**35,139**	15,369

Consolidated statement of changes in equity
For the 52 weeks ended 2 July 2011

	Issued share capital £'000	Share premium £'000	Capital redemption reserve £'000	Hedging reserve £'000	Retained earnings £'000	Total equity £'000
As at 4 July 2009	**2,008**	**345**	**–**	**–**	**110,419**	**112,772**
Profit for the financial year	–	–	–	–	54,350	54,350
Movement in fair value of cash flow hedges	–	–	–	(545)	–	(545)
Deferred tax on hedging movements	–	–	–	153	–	153
Total comprehensive income for the financial year	–	–	–	(392)	54,350	53,958
Issue of share capital	2	235	–	–	–	237
Issue of B shares	43,155	–	–	–	(43,155)	–
Redemption of B shares	(43,155)	–	43,155	–	(43,155)	(43,155)
Treasury shares reissued in respect of share option schemes	–	–	–	–	649	649
Share-based payments	–	–	–	–	1,330	1,330
Deferred tax on share-based payments	–	–	–	–	320	320
Current corporation tax on share options exercised	–	–	–	–	606	606
Dividends	–	–	–	–	(14,029)	(14,029)
Total transactions with owners, recorded directly in equity	2	235	43,155	–	(97,434)	(54,042)
As at 3 July 2010	**2,010**	**580**	**43,155**	**(392)**	**67,335**	**112,688**
Profit for the financial year	–	–	–	–	59,835	59,835
Movement in fair value of cash flow hedges	–	–	–	147	–	147
Deferred tax on hedging movements	–	–	–	(50)	–	(50)
Total comprehensive income for the financial year	–	–	–	97	59,835	59,932
Issue of share capital	5	101	–	–	–	106
Treasury shares reissued in respect of share option schemes	–	–	–	–	(9)	(9)
Share-based payments	–	–	–	–	1,199	1,199
Deferred tax on share-based payments	–	–	–	–	(41)	(41)
Current corporation tax on share options exercised	–	–	–	–	462	462
Dividends	–	–	–	–	(17,119)	(17,119)
Total transactions with owners, recorded directly in equity	5	101	–	–	(15,508)	(15,402)
As at 2 July 2011	**2,015**	**681**	**43,155**	**(295)**	**111,662**	**157,218**

Financial statements

Accounting policies

Basis of preparation

The Group financial statements consolidate those of the Company and its subsidiaries (together referred to as the 'Group'). The Parent Company financial statements present information about the Company as a separate entity and not about its Group.

The Group financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ('Adopted IFRSs') and in accordance with the provisions of the Companies Act 2006 and these are presented on pages 53 to 73.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these Group financial statements.

The annual financial statements are prepared under the historical cost convention except where financial instruments have been stated at fair value. The financial statements are prepared in pounds sterling, rounded to the nearest thousand.

Going concern

The Group has considerable financial resources together with long standing relationships with a number of key suppliers and an established reputation in the retail sector across different geographic areas. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully despite the current economic outlook. The Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and financial statements.

Further information regarding the Group's business activities, together with the factors likely to affect its future development, performance and position is set out in the Directors' Report and Business Review on pages 26 to 29. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Finance Director's review on pages 16 to 18. In addition note 17 to the financial statements includes the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; and its exposures to credit risk and liquidity risk.

Use of estimates and judgements

The presentation of the annual financial statements requires the Directors to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

The key estimates and judgements used in the financial statements are as follows:

Inventory provisions

The Group provides against the carrying value of inventories held, based upon average losses incurred to clear old and discounted lines.

Dilapidations

The Group provides for the full estimated costs of any dilapidations on stores where required.

Taxation

There are transactions whose ultimate tax treatment is uncertain. The Group makes provision for anticipated tax issues based on the likelihood of whether additional taxes may arise. The Group recognises deferred tax assets and liabilities based on estimates of future taxable income and recoverability. If these estimates do not materialise or change, or there are changes in tax rates or to the period over which losses might be recognised, then the value of the deferred tax assets or liability will need to be revised in a future period.

Equity-settled share-based payments

Certain employees and Directors of the Group receive equity-settled remuneration in the form of equity-settled share-based payment transactions, whereby employees render services in exchange for shares or rights over shares. The cost equity-settled transactions with employees is measured by reference to the fair value, determined using an appropriate pricing model, at the date at which they are granted. The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the non-market vesting conditions are expected to be fulfilled, ending on the relevant vesting date. The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period and is adjusted to reflect the Directors' best available estimate of the number of equity instruments that will ultimately vest based upon non-market conditions.

Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Transactions eliminated on consolidation

Intragroup balances, and any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the consolidated financial statements.

Revenue

Revenue represents the proceeds from sales of goods and related services. It excludes sales between Group companies and is after deducting returns, discounts given and VAT. For the majority of sales, revenue is recognised at the point of sale with the exception of make-up charges for custom made products, where revenue is recognised at the point that the goods are collected, and gift vouchers, where revenue is recognised when the vouchers are redeemed.

Foreign currencies

Transactions in foreign currencies are recorded at the prevailing rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currency are translated at the rates ruling at the balance sheet date. Resulting exchange gains or losses are recognised in the income statement for the period.

Intangible assets

These comprise software development and implementation costs and trademarks and are stated at cost less amortisation (see below).

Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful life of the asset. These are as follows:

- software development 3 years
- trademarks 5 years

Property, plant and equipment

Owned assets

Items of property, plant and equipment are stated at cost less accumulated depreciation (see below) and impairment losses.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

Depreciation

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Land is not depreciated. The estimated useful lives are as follows:

- computer equipment 3 years
- freehold buildings 50 years
- fixtures and fittings 4 years
- motor vehicles 4 years
- office equipment 5 years
- plant and machinery 4 years
- leasehold improvements over the period of the lease

The residual value of an asset, if significant, is reassessed annually.

Current assets

Trade and other receivables

Trade and other receivables are initially recognised at fair value and then carried at amortised cost net of impairment provisions.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is derived using the average cost method and includes costs incurred in bringing the inventories to their present location and condition. Net realisable value is the estimated selling price less cost to sell in the ordinary course of business.

Accounting policies *continued*

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

Bank borrowings and borrowing costs

Interest-bearing bank loans and overdrafts are recorded at the proceeds received.

Borrowing costs are recognised as an expense in the financial period in which they are incurred.

Borrowings are classed as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months from the balance sheet date.

Derivative financial instruments

Derivative financial instruments used are forward exchange contracts and are measured at fair value. The fair values are determined by reference to the market prices available from the market on which the instruments involved are traded.

Certain derivative financial instruments are designated as hedges in line with the Group's treasury policy. Cash flow hedges that hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or a liability or a highly probable forecasted transaction.

For cash flow hedges that proportion of the gain or loss on the hedging instrument that is determined to be an effective hedge, as defined by IAS 39 'Financial Instruments: Recognition and Measurement', is recognised in equity, directly in the hedge reserve with any ineffective portion recognised in the income statement. Such hedges are tested, both at inception to ensure they are expected to be effective and periodically throughout their duration to assess continuing effectiveness. When the forecast transaction results in the recognition of a non-financial asset or liability, the associated gains or losses previously recognised in equity are included in the initial measurement of the asset or liability. For all other cash flow hedges, the gains or losses that are recognised in equity are transferred to the income statement in the same period in which the hedge cash flows affect the income statement.

Any gains or losses arising from changes in fair value derivative financial instruments not designated as hedges are recognised in the income statement.

Impairment

The carrying amounts of the Group's assets, other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

The recoverable amount is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time-value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds the recoverable amount. Impairment losses are recognised in the income statement.

Share capital

Where the Company purchases its own equity share capital (treasury shares) the consideration paid, including any directly attributable incremental costs is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued. Where such shares are subsequently sold or reissued, any consideration received net of any directly attributable incremental transactions costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

Provisions

A provision is recognised in the balance sheet when the Group has a current legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. A provision for onerous contracts is recognised when the expected benefit to be derived by the Group from a contract is lower than the unavoidable costs of meeting its obligations under the contract.

Expenses

Property leases

Lease incentives received are recognised in the income statement evenly over the full term of the lease.

Where leases for land and buildings provide for fixed rent review dates and amounts, the Group accounts for such reviews by recognising, on a straight-line basis, the total implicit minimum lease payments over the non-cancellable period of the lease term.

Accounting policies *continued*

Financing income/expense
Financing income/expense comprises interest payable on borrowings calculated using the effective interest rate method, interest receivable on funds invested and foreign exchange gains and losses.

Retirement benefits
The Group operates a defined contribution pension plan using a third-party provider. Obligations for the contributions to this plan are recognised as an expense in the income statement as incurred.

Share-based payment transactions
The Group operates an employee share save scheme open to all employees with over three months' service, enabling them to save money which may be used after three years to acquire shares in the Company at a predetermined price.

The Group also operates other share option schemes enabling certain employees to acquire shares of the Company.

The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. Fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. Fair value is measured using the binomial model, taking into account the terms and conditions applicable to the options.

At each balance sheet date the Group revises its estimates of the number of share incentives that are expected to vest and amends the charge accordingly.

Dividends
Dividends are recognised as a liability in the period in which they are approved such that the Company is obligated to pay the dividend.

Taxation
Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax represents the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, together with any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be recognised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be recognised.

Adopted IFRS and IFRIC not yet applied
At the date of approval of these financial statements, the following standards, amendments and interpretations were in place but not yet effective:

IFRS 9	Revised IFRS 9	– Financial Instruments
IFRS 13	Revised IFRS 13	– Fair value measurement
IAS 12	Revised IAS 12	– Deferred tax

The above will be adopted in the Group and Company's financial statements when they become effective.

When adopted none of the above standards or amendments are expected to have any significant impact on the financial statements of the Group or Company.

IFRS 9 will replace IAS 39 Financial Instruments: Recognition and Measurement. The standard contains two primary measurement categories for financial assets:

- amortised cost; and
- fair value

Financial statements

Notes to the annual financial statements
For the 52 weeks ended 2 July 2011

1 Segmental reporting
The Group has one reportable segment, retail of homewares.

The Chief Operating Decision Maker is the Group's Operating Board. Internal management reports are reviewed by them on a monthly basis. Performance of the segment is assessed based on profit before taxation.

All material operations of the reportable segment are carried out in the UK. The Group's revenue is driven by the consolidation of individual small value transactions and as a result Group revenue is not reliant on a major customer or group of customers.

Management believe that these measures are the most relevant in evaluating the performance of the segment and for making resource allocation decisions.

2 Operating profit
Operating profit is stated after charging the following items:

	2011 £'000	2010 £'000
Inventories		
Cost of inventories included in cost of sales	280,125	262,253
Movement on provisions for write down of inventories	(787)	1,120
Amortisation of intangible assets	1,909	1,876
Depreciation of owned property, plant and equipment	12,170	9,494
Operating lease rentals		
Land and buildings	25,493	22,544
Plant and machinery	1,522	1,351
Loss on disposal of property, plant and equipment and intangible assets	703	13

The analysis of auditors' remuneration is as follows:

	2011 £'000	2010 £'000
Fees payable to the Company's auditors for the audit of the Parent and consolidated annual accounts	16	15
Fees payable to the Company's auditors and their associates for other services to the Group		
– audit of the Company's subsidiaries pursuant to legislation	56	52
– tax compliance	33	30
– other tax services	10	88
– all other services	–	17

3 Operating costs

	2011 £'000	2010 £'000
Selling and Distribution	147,392	130,606
Administrative	26,956	24,507
Loss on disposal of property, plant and equipment and intangible assets	703	13
	175,051	155,126

4 Employee numbers and costs
The average number of people employed by the Group (including Directors) was:

	2011 Number of heads	2011 Full time equivalents	2010 Number of heads	2010 Full time equivalents
Selling	6,135	3,777	5,608	3,493
Distribution	261	252	285	274
Administration	228	223	198	194
	6,624	4,252	6,091	3,961

4 Employee numbers and costs *continued*

The aggregate remuneration of all employees including Directors comprises:

	2011 £'000	2010 £'000
Wages and salaries including bonuses and termination benefits	69,740	61,994
Social security costs	4,715	4,324
Share-based payment expense (note 20)	1,199	1,330
Defined contribution pension costs	282	196
	75,936	67,844

Details of Directors' remuneration, share options, long-term incentive schemes and pension entitlements are disclosed in the Remuneration Report on pages 39 to 46.

5 Financial income and expense

	2011 £'000	2010 £'000
Finance income		
Interest on bank deposits	523	557
Foreign exchange gains	–	804
	523	1,361
Finance expenses		
Interest on bank borrowings and overdraft	(29)	(65)
Foreign exchange losses	(143)	–
	(172)	(65)
Net finance income	351	1,296

6 Taxation

	2011 £'000	2010 £'000
Current taxation		
UK corporation tax charge for the period	24,610	22,146
Adjustments in respect of prior periods	(1,198)	(238)
	23,412	21,908
Deferred taxation		
Origination of temporary differences	(442)	324
Adjustment in respect of prior periods	844	174
	402	498
Total taxation expense in the income statement	23,814	22,406

The tax charge is reconciled with the standard rate of UK corporation tax as follows:

	2011 £'000	2010 £'000
Profit before taxation	83,649	76,756
UK corporation tax at standard rate of 27.5% (2010: 28.0%)	23,002	21,492
Factors affecting the charge in the period:		
Non-deductible expenses	179	128
Ineligible depreciation	1,035	972
Lease incentive deductions	(120)	(122)
Adjustments to tax charge in respect of prior years	(354)	(64)
Effect of standard rate of corporation tax change	(104)	–
Loss on disposal of ineligible assets	176	–
	23,814	22,406

The taxation charge for the period as a percentage of profit before tax is 28.5% (2010: 29.2%).

Financial statements

Notes to the annual financial statements *continued*
For the 52 weeks ended 2 July 2011

7 Dividends
All dividends relate to the 1p Ordinary Shares.

		2011 £'000	2010 £'000
Final for the period ended 4 July 2009	– paid 4.0p	–	(8,008)
Interim for the period ended 3 July 2010	– paid 3.0p	–	(6,021)
Final for the period ended 3 July 2010	– paid 5.0p	(10,067)	–
Interim for the period ended 2 July 2011	– paid 3.5p	(7,052)	–
		(17,119)	(14,029)

The Directors are proposing a final dividend of 8.0p per Ordinary Share for the period ended 2 July 2011 which equates to £16.1m. The dividend will be paid on 16 December 2011 to shareholders on the register at the close of business on 25 November 2011.

8 Earnings per share
Basic earnings per share is calculated by dividing the profit for the period attributable to equity shareholders by the weighted average number of Ordinary Shares in issue during the period.

For diluted earnings per share, the weighted average number of Ordinary Shares in issue is adjusted to assume conversion of all dilutive potential Ordinary Shares. These represent share options granted to employees where the exercise price is less than the average market price of the Company's Ordinary Shares during the period.

Weighted average numbers of shares:

	52 weeks ended 2 July 2011 '000	52 weeks ended 3 July 2010 '000
Weighted average number of shares in issue during the period	201,394	200,264
Impact of share options	2,506	2,047
Number of shares for diluted earnings per share	203,900	202,311

9 Intangible assets

	Software development and licences £'000	Rights to Dorma brand £'000	Total £'000
Cost			
At 4 July 2009	7,738	5,036	12,774
Additions	1,233	–	1,233
Disposals	(5,444)	–	(5,444)
Transfers from property, plant and equipment	2	–	2
At 3 July 2010	3,529	5,036	8,565
Additions	1,399	–	1,399
Disposals	(3)	–	(3)
At 2 July 2011	4,925	5,036	9,961
Amortisation			
At 4 July 2009	6,008	923	6,931
Charge for the financial period	869	1,007	1,876
Disposals	(5,444)	–	(5,444)
At 3 July 2010	1,433	1,930	3,363
Charge for the financial period	902	1,007	1,909
Disposals	(3)	–	(3)
At 2 July 2011	2,332	2,937	5,269
Net book value			
At 4 July 2009	1,730	4,113	5,843
At 3 July 2010	2,096	3,106	5,202
At 2 July 2011	2,593	2,099	4,692

9 Intangible assets *continued*

All additions were acquired and do not include any internal development costs.

Transfers relate to assets which were classified initially as fixtures and fittings and leasehold improvements.

10 Property, plant and equipment

	Land and buildings £'000	Leasehold improvements £'000	Plant and machinery £'000	Motor vehicles £'000	Fixtures and fittings £'000	Total £'000
Cost						
At 4 June 2009	48,738	47,408	195	86	34,338	130,765
Additions	4,144	10,049	281	–	8,870	23,344
Transfers to intangible assets and reclassifications	–	66	–	–	(68)	(2)
Disposals	–	(319)	–	(33)	(13,206)	(13,558)
At 3 July 2010	52,882	57,204	476	53	29,934	140,549
Additions	13,806	12,004	1,166	–	9,148	36,124
Transfers to intangible assets and reclassifications	34	(34)	(14)	–	14	–
Disposals	(515)	(665)	(28)	(8)	(766)	(1,982)
At 2 July 2011	66,207	68,509	1,600	45	38,330	174,691
Depreciation						
At 4 July 2009	2,715	13,272	96	86	25,825	41,994
Charge for financial period	802	3,996	43	–	4,653	9,494
On disposals	–	(314)	–	(33)	(13,191)	(13,538)
At 3 July 2010	3,517	16,954	139	53	17,287	37,950
Charge for financial period	896	5,032	242	–	6,000	12,170
On disposals	(127)	(413)	(2)	(8)	(729)	(1,279)
At 2 July 2011	4,286	21,573	379	45	22,558	48,841
Net book value						
At 4 July 2009	46,023	34,136	99	–	8,513	88,771
At 3 July 2010	49,365	40,250	337	–	12,647	102,599
At 2 July 2011	61,921	46,936	1,221	–	15,772	125,850

11 Deferred tax

Deferred tax is provided in full on temporary differences under the liability method using a taxation rate of 26.0% (2010: 28%).

Deferred taxation assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2011 £'000	2010 £'000	2011 £'000	2010 £'000	2011 £'000	2010 £'000
Property, plant and equipment	–	–	(1,670)	(1,187)	(1,670)	(1,187)
Other temporary differences	103	153	(155)	(169)	(52)	(16)
Share-based payments	1,077	1,051	–	–	1,077	1,051
	1,180	1,204	(1,825)	(1,356)	(645)	(152)

Financial statements

Notes to the annual financial statements *continued*
For the 52 weeks ended 2 July 2011

11 Deferred tax *continued*

The movement in the net deferred tax balance is as follows:

	Balance at 4 July 2009 £'000	Recognised in income £'000	Recognised in equity £'000	Balance at 3 July 2010 £'000
Property, plant and equipment	(634)	(553)	–	(1,187)
Employee benefits	558	173	320	1,051
Short-term temporary differences	(51)	(118)	153	(16)
	(127)	(498)	473	(152)

	Balance at 3 July 2010 £'000	Recognised in income £'000	Recognised in equity £'000	Balance at 2 July 2011 £'000
Property, plant and equipment	(1,187)	(483)	–	(1,670)
Employee benefits	1,051	67	(41)	1,077
Short-term temporary differences	(16)	14	(50)	(52)
	(152)	(402)	(91)	(645)

12 Inventories

	2011 £'000	2010 £'000
Goods for resale	76,455	62,583

13 Trade and other receivables

	2011 £'000	2010 £'000
Trade receivables	454	122
Other receivables	2,159	628
Prepayments and accrued income	11,953	9,720
	14,566	10,470

All amounts fall due within one year. All trade receivables are current. No interest is charged on trade receivables, whilst these remain current.

14 Cash and cash equivalents

	2011 £'000	2010 £'000
Cash at bank and in hand	35,139	15,369

15 Trade and other payables

	2011 £'000	2010 £'000
Trade payables	36,709	32,451
Accruals and deferred income	42,695	35,509
Other taxation and social security	5,163	3,283
Other creditors	1,238	395
	85,805	71,638

16 Interest bearing loans and borrowings

On 26 September 2006 the Group entered into a £50m revolving credit facility, repayable in full on 26 September 2011 and sub-divided into two elements: a £40m facility and a £10m facility. The £10m facility was cancelled on 26 May 2009. The £40m facility was cancelled on 30 December 2010.

Interest was payable on funds utilised under the £40m facility at the rate of LIBOR plus 0.35%. LIBOR is fixed for a given loan at the date of draw down.

The facility was guaranteed by the Parent Company and its subsidiaries.

On 7 February 2011 the Group entered into a £10m overdraft facility. Interest is payable on funds utilised under the facility at the rate of 1.5% above the bank's base rate.

Financial assets at 2 July 2011 consisted of £412,000 (2010: £122,000) trade receivables and £35,139,000 (2010: £15,369,000) cash at bank and on deposit; interest earned is at normal commercial rates.

17 Financial risk management

The Board of Directors has overall responsibility for the oversight of the Group's risk management framework. A formal process for reviewing and managing risk in the business has been developed. A register of strategic and operational risks is maintained and reviewed quarterly by the Board, who also monitor the status of agreed actions to mitigate key risks.

Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Group's receivables from customers. The Group only deals with creditworthy counterparties, and uses publicly available financial information to rate its customers.

As the principal business of the Group is retail related, trade receivables consist of a relatively small number of customers, which tend to be charity or local authority based. The carrying amount of financial assets recorded in the financial statements represents the Group's maximum exposure to credit risk.

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity risk is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and extreme circumstances. The Group manages this risk by continuously monitoring cash flow forecasts. The Group's available facilities can be found in note 16.

Group policy is that surplus funds are placed on deposit with counterparties approved by the Board, with a minimum of 'A' credit rating. Credit limits with approved counterparties are limited to £20m for any individual party.

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the Group's income.

Interest rate risk

The Group's bank borrowings incur variable interest rate charges linked to LIBOR and Barclays Bank Base Rate. The Directors do not consider that future changes in interest rates are likely to cause a material direct impact on profitability. The Group's exposure to interest rates on financial assets and liabilities are detailed in note 16.

Foreign currency risk

The Group is exposed to foreign currency risk on purchases denominated in US dollars. These amounted to approximately 10% of the total stock purchases in the year ended 2 July 2011. The outstanding US dollar liabilities at the year end were $353,000 (2010: $139,000).

During the year the Group entered into exchange rate swaps for $25.5m to sell sterling and buy US dollars. These swaps are accounted for as cash flow hedges. During the year the mark to market profit on foreign currency hedging instruments taken to equity was £0.1m (2010: £0.5m). At the balance sheet date the Group had six swap contracts outstanding with a maximum value of $19.8m.

All of the Group's revenues are in sterling. Purchases of promotional goods are generally in US dollars. Purchase of regular range goods are generally in sterling, although some lines are now being imported directly and paid for in dollars. We will cover exchange rate exposure on expected promotional product purchases up to a maximum of 100% of forecast purchases over a four month horizon. We will cover exchange rate exposure on expected regular range purchases up to a maximum of 50% of forecast purchases over a twelve month horizon. We will use various means to cover the above currency exposures; hold excess funds in US dollars, take out forward contracts for the purchase of US dollars, enter into forward rate options.

Financial statements

Notes to the annual financial statements *continued*
For the 52 weeks ended 2 July 2011

17 Financial risk management *continued*
In the event of a significant adverse movement in the US dollar exchange rate, the Group would seek to minimise the impact on profitability by changing the selling price of goods.

Sensitivity analysis
The Group's principal foreign currency exposure is to the US dollar.

The Directors believe that an increase or decrease of 10% in the US dollar/sterling exchange rates would not have a material effect on the Statement of comprehensive income.

The US dollar year end exchange rate applied in the above analysis is 1.6069 (2010: 1.5186). Strengthening and weakening of sterling may not produce symmetrical results depending on the proportion and nature of foreign exchange derivatives which do not qualify for hedge accounting.

Fair values
The fair value of the Group's financial assets and liabilities is not materially different from their carrying value. The fair value of foreign currency contracts are sums required by the counterparties to cancel the contracts at the end of the year.

Fair value hierarchy
Financial instruments carried at fair value are required to be measured by reference to the following levels:

- Level 1: quoted prices in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

All financial instruments carried at fair value have been measured by a Level 2 valuation method.

Losses on cashflow hedges during the year amounted to £30,000 (2010: gain £313,000).

Capital management
The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business.

From time to time the Group purchases its own shares on the market; the timing of these purchases depends on market prices. The shares are intended to be used for issuing shares under the Group's share option programmes. Buy and sell decisions are made on a specific transaction basis by the Board. The Group does not have a defined share buy-back plan.

The following table is a comparison by category of the carrying amounts and fair values of the Group's financial assets and liabilities at 2 July 2011 and 3 July 2010.

	2011 Carrying value £'000	2011 Fair value £'000	2010 Carrying value £'000	2010 Fair value £'000
Cash and cash equivalents	35,139	35,139	15,369	15,369
Trade receivables	454	454	122	122
Total financial assets	35,593	35,593	15,491	15,491
Trade payables	(36,709)	(36,709)	(32,451)	(32,451)
Forward exchange contracts	(398)	(398)	(545)	(545)
Total financial liabilities	(37,107)	(37,107)	(32,996)	(32,996)
Net financial liabilities	(1,514)	(1,514)	(17,505)	(17,505)

The fair value on trade receivables and trade payables are approximate to the carrying value.

17 Financial risk management *continued*

The currency profile of the Group's cash and cash equivalents is as follows:

	2011 £'000	2010 £'000
Sterling	32,870	14,057
US dollar	1,526	1,209
Euro	743	103
	35,139	15,369

As at 2 July 2011, the analysis of trade receivables that were past due but not impaired is as follows:

	Total £'000	Neither past due nor impaired £'000	Less than 30 days £'000	31–60 days £'000	61–90 days £'000	More than 90 days £'000
2 July 2011	496	112	315	44	–	25
3 July 2010	122	26	49	1	10	36

18 Share capital

	Number of ordinary shares of 1p each 2011	Number of B shares of 21.5p each 2010	Number of ordinary shares of 1p each 2010
In issue at the start of the period	201,040,148	–	200,791,400
B shares issued via a bonus issue	–	200,723,131	–
B shares redeemed in the year	–	(200,723,131)	–
Issued during the period in respect of share option schemes	449,960	–	248,748
In issue at the end of the period	201,490,108	–	201,040,148

Proceeds received in relation to shares issued during the period were £101,000 (2010: £238,000).

	2011 number of shares	2011 £'000	2010 number of shares	2010 £'000
Ordinary shares of 1p each:				
Allotted, called up and fully paid	201,490,108	2,015	201,040,148	2,010

19 Treasury shares

	2011 number of shares	2011 £'000	2010 number of shares	2010 £'000
Outstanding at beginning of year	99,628	128	837,135	1,301
Reissued during the period in respect of share option schemes	(99,628)	(128)	(737,507)	(1,173)
Outstanding at end of year	–	–	99,628	128

In the past the Company has acquired its own shares ('treasury shares') for the purpose of delivery to employees under employee share schemes. No such purchases were made during the financial year.

The Company reissued 99,628 (2010: 737,507) treasury shares for a total consideration of £Nil (2010: £641,843).

The Company has the right to reissue the remaining treasury shares at a later date.

Financial statements

Notes to the annual financial statements *continued*
For the 52 weeks ended 2 July 2011

20 Share-based payments
As at 2 July 2011, the Group operated three share award plans:
a) Dunelm Group Share Option Plan ('GSOP')
b) Dunelm Group Savings Related Share Option Plan ('Sharesave')
c) Long-Term Incentive Plan ('LTIP')

There were 36,495 exercisable options in total under these schemes as at 2 July 2011.

a) Dunelm Group Share Option Plan
The GSOP was established in December 2003. Options have a vesting period of three years from date of grant and a maximum life of 10 years. All options granted prior to October 2006 have an exercise price equal to the market value as agreed with HMRC at date of grant; all subsequent grants have had an exercise price equal to market price at date of grant. There are no performance conditions but there is a requirement that the Group's shares be traded on a public exchange at date of exercise, and the awards are also subject to continued employment with the Group.

The fair value of services received in return for share options granted is measured by reference to the fair value of the options, assessed using a binomial model. The fair value per option granted and the assumptions used in the calculations are as follows:

	October 2010 grant	June 2008 grant
Fair value at measurement date	145.8p	65.6p
Exercise price	420.0p	137.0p
Expected volatility (weighted average volatility used in modelling – based on historical volatility of comparable quoted companies)	36%	35%
Option life (weighted average life used in modelling)	3 years	3 years
Expected dividends	2.5%	8.7%
Risk-free interest rate	1.7%	4.8%

The number and weighted average exercise price of options under the GSOP is as follows:

	Weighted average exercise price 2011	Number of shares under option 2011	Weighted average exercise price 2010	Number of shares under option 2010
Outstanding at beginning of year	203.8p	48,840	60.5p	427,331
Granted during year	420.0p	100,000	405.0p	12,345
Exercised during year	–	–	54.9p	(390,836)
Lapsed during year	405.0p	(12,345)	–	–
Outstanding at end of year	344.3p	136,495	203.8p	48,840

20 Share-based payments *continued*

b) Dunelm Group Savings Related Share Option Plan

The Sharesave scheme was established in 2006 and is open to all staff with eligible length of service. One grant was made under the scheme during the year, in October 2009. Options may be exercised under the scheme on completion of the three year savings contract and must be exercised within six months from that date. There is provision for early exercise in certain circumstances such as death, disability, redundancy and retirement.

The fair value per option granted and the assumptions used in the calculations are as follows:

	October 2010	October 2009	October 2008	October 2007
Fair value at measurement date	192.8p	180.4p	47.0p	70.0p
Share price	497.5p	376.3p	125.0p	212.0p
Exercise price	337.0p	253.0p	124.5p	157.0p
Expected volatility (weighted average volatility used in modelling – based on historical volatility of comparable quoted companies)	43%	57%	58%	30%
Option life (weighted average life used in modelling)	3.5 years	3.5 years	3.5 years	3.5 years
Expected dividends	2.5%	2.5%	2.5%	2.5%
Risk-free interest rate	1.7%	2.8%	3.0%	4.8%
Forfeiture rate	48%	29%	10%	0%

The number and weighted average exercise price of options outstanding under the Sharesave at 2 July 2011 is as follows:

	Weighted average exercise price 2011	Number of shares under option 2011	Weighted average exercise price 2010	Number of shares under option 2010
Outstanding at beginning of year	190.4p	671,772	142.9p	867,972
Granted during year	337.0p	349,142	253.0p	347,376
Exercised during the year	139.2p	(64,207)	153.0p	(440,150)
Forfeited during year	252.4p	(86,095)	161.5p	(103,426)
Outstanding at end of year	245.7p	870,612	190.4p	671,772

The weighted average share price at the time of exercise was 490.8p

c) Long-Term Incentive Plan

The LTIP was approved by the Board in 2006 enabling the Group to award shares to particular individuals, normally in the form of nominal cost options. The LTIP is administered by the Remuneration Committee. Four grants were made in the year, to the Executive Directors, senior management, selected staff and a separate grant to Nick Wharton as part of his joining package. The Executive Directors' and selected staff grants in December 2010 are exercisable in December 2013, the senior management grant in October 2010 is exercisable in Oct 2013 and Nick Wharton's joining grant in December 2010 is exercisable in December 2015. The grant to the Executive Directors is dependent on the level of growth in Group EPS relative to RPI, as well as continuing employment. The grants to senior management and selected staff and the separate grant to Nick Wharton are dependent on continuing employment within the Group. The maximum life of options under the LTIP is 10 years from the date of grant. Full details of this plan are included in the Remuneration Report on pages 39 to 46.

Notes to the annual financial statements *continued*
For the 52 weeks ended 2 July 2011

20 Share-based payments *continued*
c) Long-Term Incentive Plan
The fair value of services received in return for share options granted is measured by reference to the fair value of the options.

This has been calculated as follows:

	December 2010	December 2010	September 2009	September 2008
Share price at date of grant	500.0p	500.0p	316.0p	148.0p
Discount factor, based on dividend yield of 2.5% to vesting date	0.881	0.927	0.913	0.889
Fair value of option	440.6p	463.4p	288.5p	132.5p

The number and weighted average exercise price of options under the LTIP at 2 July 2011 is as follows:

	Weighted average exercise price 2011	Number of shares under option 2011	Weighted average exercise price 2010	Number of shares under option 2010
Outstanding at beginning of year	–	1,326,468	–	1,263,571
Granted during year	–	664,661	–	384,164
Exercised during year	–	(482,482)	–	(155,270)
Forfeited during year	–	(9,381)	–	(165,997)
Outstanding at end of year	–	1,499,266	–	1,326,468

The weighted average share price at the time of exercise was 387.3p

The total expense recognised in the income statement arising from share-based payments is as follows:

	2011 £'000	2010 £'000
GSOP	61	2
Sharesave	240	93
LTIP	898	1,235
	1,199	1,330

21 Commitments
As at 2 July 2011 the Group had entered into capital contracts amounting to £21.8m. The equivalent figure as at 3 July 2010 was £15.4m.

The future minimum lease payments under non-cancellable operating leases were as follows:

	2011 Motor vehicles £'000	2011 Land and buildings £'000	2011 Plant and machinery £'000	2010 Motor vehicles £'000	2010 Land and buildings £'000	2010 Plant and machinery £'000
Within one year	414	27,566	380	428	23,723	292
In the second to fifth year inclusive	92	103,079	651	374	86,794	535
After five years	–	134,408	–	–	115,241	–
	506	265,053	1,031	802	225,758	827

The Group has 101 operating leases in respect of properties. These leases run for periods of up to 20 years, with an option to renew leases on expiry. Lease payments are typically reviewed every five years.

The Group also leases a number of vehicles, shop fittings and items of computer hardware under operating leases. These vary in length.

22 Contingent liabilities
The Group had no contingent liabilities at either period end date.

23 Related parties

Identity of related parties

The Group has related party relationships with its subsidiaries and with its Directors. Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation for the Group.

Key management personnel

The key management personnel of the Group comprise members of the Board of Directors and the executive team.

Directors of the Company and their immediate relatives control 59.1% of the voting shares of the Company.

Disclosures relating to remuneration of Directors are set out in the Remuneration Report on pages 39 to 46. The remuneration of the key management personnel (Executive Committee excluding Directors) of the Group is set out below:

	2011 £'000	2010 £'000
Salaries and other short-term benefits	1,086	1,269
Post-employment benefits	29	22
Share-based payments	186	4
	1,301	1,295

From time to time the Group makes purchases on behalf of a major shareholder, Bill Adderley, and sells fully depreciated vehicles to him that the Group no longer requires. These amounts are billed based on normal market rates for such supplies and payable under normal payment terms. No balances remained unsettled at either period end. The aggregate value of these transactions in the year ended 2 July 2011 was £1,750 (2010: £766).

From time to time Directors of the Group, or their related entities, may purchase goods from the Group. These purchases are on the same terms and conditions as those entered into by other Group employees or customers and values involved are trivial.

24 Ultimate controlling party

The Directors consider that the Adderley family is the ultimate controlling party of Dunelm Group plc by virtue of their combined shareholding.

25 Subsequent events

There are no material post-balance sheet events.

Financial statements

Parent Company statement of financial position
As at 2 July 2011

	Note	2011 £'000	2010 £'000
Non-current assets			
Investment in subsidiaries	4	46,719	46,134
Deferred tax asset	5	655	630
Total non-current assets		47,374	46,764
Current assets			
Trade and other receivables	6	89,886	47,910
Current tax asset		591	–
Total current assets		90,477	47,910
Total assets		137,851	94,674
Current liabilities			
Trade and other payables	7	(286)	(855)
Liability for current tax		–	(102)
Total current liabilities		(286)	(957)
		–	
Total liabilities		(286)	(957)
Net assets		137,565	93,717
Capital and reserves			
Issued capital	10	2,015	2,010
Share premium		681	580
Non-distributable reserves		1,564	979
Capital Redemption Reserve		43,155	43,155
Retained earnings		90,150	46,993
Equity shareholders' funds		137,565	93,717

The financial statements on pages 74 to 83 were approved by the Board of Directors on 15 September 2011 and were signed on its behalf by:

David Stead
Director
15 September 2011

Company number 4708277

Parent Company statement of cash flows
For the 52 weeks ended 2 July 2011

	52 weeks 2011 £'000	52 weeks 2010 £'000
Profit before tax	59,190	38,922
Adjusted for:		
Net financing costs	(2,061)	(2,390)
Operating profit	57,129	36,532
Operating cash flows before movements in working capital		
Decrease in receivables	(41,976)	16,200
(Decrease)/increase in payables	(574)	266
Net movement in working capital	(42,550)	16,466
Investment income	(60,000)	(40,000)
Share-based payments expense	614	935
Cash flows from operating activities	(44,807)	13,933
Dividends received	60,000	40,000
Tax paid	(236)	–
Interest paid	(29)	(71)
Interest received	2,090	2,454
Net cash generated from operating activities	17,018	56,316
Cash flows from financing activities		
Proceeds from issue of share capital	101	244
Proceeds from issue of treasury shares	–	642
Proceeds from bank loan	–	10,000
Repayment of bank loan	–	(10,000)
Return of capital	–	(43,155)
Dividends paid	(17,119)	(14,029)
Net cash flows utilised in financing activities	(17,018)	(56,298)
	–	
Net increase in cash and cash equivalents	–	18
Cash and cash equivalents at the beginning of the period	–	(18)
Cash and cash equivalents at the end of the period	–	–

Financial statements

Parent Company statement of changes in equity
For the 52 weeks ended 2 July 2011

	Issued share capital £'000	Share premium £'000	Merger reserve £'000	Capital redemption reserve £'000	Non-distributable reserve £'000	Retained earnings £'000	Total £'000
As at 4 July 2009	2,008	346	43,155	–	616	63,068	109,193
Profit for the financial year	–	–	–	–	–	39,205	39,205
Issue of share capital	2	234	–	–	–	–	236
Treasury shares reissued in respect of share option schemes	–	–	–	–	–	649	649
Issue of B shares as bonus issue	43,155	–	(43,155)	–	–	–	–
Redemption of B shares for cash	(43,155)	–	–	–	–	–	(43,155)
Creation of capital redemption reserve	–	–	–	43,155	–	(43,155)	–
Share-based payments	–	–	–	–	363	935	1,298
Deferred tax on share-based payments	–	–	–	–	–	284	284
Current corporation tax on share options exercised	–	–	–	–	–	36	36
Dividends	–	–	–	–	–	(14,029)	(14,029)
Total transactions with owners, recorded directly in equity	2	234	(43,155)	43,155	363	(55,280)	(54,681)
As at 3 July 2010	2,010	580	–	43,155	979	46,993	93,717
Profit for the financial year	–	–	–	–	–	59,385	59,385
Total comprehensive income for the financial year	–	–	–	–	–	59,385	59,385
Issue of share capital	5	101	–	–	–	–	106
Treasury shares reissued in respect of share option schemes	–	–	–	–	–	(9)	(9)
Share-based payments	–	–	–	–	585	614	1,199
Deferred tax on share-based payments	–	–	–	–	–	52	52
Current corporation tax on share options exercised	–	–	–	–	–	234	234
Dividends	–	–	–	–	–	(17,119)	(17,119)
Total transactions with owners, recorded directly in equity	5	101	–	–	585	(16,228)	(15,537)
As at 2 July 2011	2,015	681	–	43,155	1,564	90,150	137,565

The non-distributable reserve's purpose is to reflect movements in share-based payments in respect of awards given by the Parent Company to employees of subsidiaries.

Accounting policies

Basis of preparation
The Company financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ('Adopted IFRSs') and as applied in accordance with the provisions of the Companies Act 2006.

The accounts of the Company are prepared under the historical cost convention, in accordance with the Companies Act 2006, applicable accounting standards and specifically in accordance with the accounting policies set out below.

After making enquiries, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Investments
Investments in subsidiary undertakings are stated at the adjusted cost of the investment, IFRIC 8 'Scope of IFRS 2 share-based payments' requires the Parent Company to recognise an increase in the cost of its investment in a subsidiary which has issued share options in the Parent Company's shares to its employees.

Bank borrowings and borrowing costs
Interest bearing bank loans and overdrafts are recorded at the proceeds received.

Borrowing costs are recognised as an expense in the financial period in which they are incurred.

Borrowings are classed as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months from the balance sheet date.

Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

Where a Group Company enters into financial guarantee contracts to guarantee the indebtedness of other Group Companies within the Group, the Company considers these to be insurance arrangements for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable the Company will be required to make a payment under the guarantee.

Share capital
Where the Company purchases its own equity share capital (treasury shares) the consideration paid, including any directly attributable incremental costs is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued. Where such shares are subsequently sold or reissued, any consideration received net of any directly attributable incremental transactions costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

Share-based payments
The Company operates three share option schemes details of which are set out in note 12.

The fair value of options granted is realised as an employee expense with a corresponding increase in equity. Fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. Fair value is measured using the binomial model, taking into account the terms and conditions applicable to the options.

At each balance sheet date the Company revises its estimates of the number of share incentives expected to vest. Any impact of this revision is recognised as an adjustment to equity with a corresponding adjustment to investments.

Dividends
Dividends are recognised as a liability in the period in which they are approved such that the Company is obligated to pay the dividend.

Accounting policies *continued*

Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax represents the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, together with any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be recognised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be recognised.

Adopted IFRS and IFRIC not yet applied

At the date of approval of these financial statements, the following standards, amendments and interpretations were in place but not yet effective:

IFRS 9	Revised IFRS 9	– Financial Instruments
IFRS 13	Revised IFRS 13	– Fair value measurement
IAS 12	Revised IAS 12	– Deferred tax

The above will be adopted in the Group and Company's financial statements when they become effective.

When adopted none of the above standards or amendments are expected to have any significant impact on the financial statements of the Group or Company.

IFRS 9 will replace IAS 39 Financial Instruments: Recognition and Measurement. The Standard contains two primary measurement categories for financial assets:

- amortised cost; and
- fair value

Notes to the Parent Company financial statements
For the 52 weeks ended 2 July 2011

1 Income statement
The Company made a profit after tax of £59,385,000 (2010: £39,205,000). The Directors have taken advantage of the exemption available under section 408 Companies Act 2006 and have not presented an income statement for the Company alone.

The Company is not required to give details of the fees paid to its auditors in accordance with the Companies (Disclosure of Auditor Remuneration) Regulations 2005.

2 Employee costs
The Company has no employees other than the three Executive Directors. Full details of the Directors' remuneration and interest are set out in the Remuneration Report on pages 39 to 46, and share-based payments details in note 20 on pages 70 to 72.

3 Dividends
All dividends relate to the 1p Ordinary Shares.

	2011 £'000	2010 £'000
Final for the period ended 4 July 2009 – paid 4.0p	–	(8,008)
Interim for the period ended 3 July 2010 – paid 3.0p	–	(6,021)
Final for the period ended 3 July 2010 – paid 5.0p	(10,067)	–
Interim for the period ended 2 July 2011 – paid 3.5p	(7,052)	–
	(17,119)	(14,029)

The Directors are proposing a final dividend of 8.0p per Ordinary Share for the period ended 2 July 2011 which equates to £16.1m. The dividend will be paid on 16 December 2011 to shareholders on the register at the close of business on 25 November 2011.

4 Investments
Shares in subsidiary undertakings.

	Restated £'000
As at 4 July 2009	45,771
Share-based payments	363
As at 3 July 2010	46,134
Share-based payments	585
As at 2 July 2011	46,719

Principal subsidiaries
The following are the principal subsidiaries as at the end of the year:

Subsidiary	Proportion of ordinary shares held	Nature of business
Dunelm (Soft Furnishings) Limited	100%	Retailer of soft furnishings
Dunelm Estates Limited	100%	Property holding company

Both of the above subsidiaries and the Parent Company are registered and operate in England and Wales.

5 Deferred tax assets

	Assets	
	2011 £'000	2010 £'000
Employee benefits	655	630

Financial statements

Notes to the Parent Company financial statements *continued*
For the 52 weeks ended 2 July 2011

5 Deferred tax assets *continued*

The movement in deferred tax assets is as follows:

	Balance at 4 July 2009 £'000	Recognised in income £'000	Recognised in equity £'000	Balance at 3 July 2010 £'000
Employee benefits	202	144	284	630

	Balance at 3 July 2010 £'000	Recognised in income £'000	Recognised in equity £'000	Balance at 2 July 2011 £'000
Employee benefits	630	(27)	52	655

Deferred tax assets are recognised for other temporary differences to the extent that the realisation of the related tax benefit through future taxable profits is probable.

6 Trade and other receivables

	2011 £'000	2010 £'000
Amounts owed by subsidiary undertakings	89,848	47,870
Prepayments and accrued income	38	29
Other taxation and social security	–	11
	89,886	47,910

Amounts owed by subsidiary undertakings are immediately repayable. Interest is charged monthly on all intercompany balances at an annual rate of 5.25%.

7 Trade and other payables

	2011 £'000	2010 £'000
Trade payables	39	15
Accruals and deferred income	196	820
Other taxation and social security	31	–
Other creditors	20	20
	286	855

8 Interest bearing loans and borrowings

	2011 £'000	2010 £'000
Bank overdraft	–	–
	–	–

On 26 September 2006 the Company entered into a £50m revolving credit facility which is repayable in full on 26 September 2011. The facility is sub-divided into two elements: a £40m facility and a £10m facility. The £10m facility was cancelled on 26 May 2009. The £40m facility was cancelled on 30 December 2010.

Interest was payable on the £40m facility at the rate of LIBOR plus 0.35%.

The facility was guaranteed by the Company and its subsidiaries.

On 7 February 2011 the Company entered into a £10m overdraft facility. Interest is payable on funds utilised under the facility at the rate of 1.5% above the banks' base rate.

9 Financial risk management

Capital management

The following table is a comparison by category of the carrying amounts and fair values of the Company's financial assets and liabilities at 2 July 2011 and 3 July 2010.

	2011 Carrying value £'000	2011 Fair value £'000	2010 Carrying value £'000	2010 Fair value £'000
Subsidiary loans	89,848	89,848	47,870	47,870
Total financial assets	89,848	89,848	47,870	47,870
Trade payables	(39)	(39)	(15)	(15)
Total financial liabilities	(39)	(39)	(15)	(15)
Net financial assets	89,809	89,809	47,855	47,855

The fair value on subsidiary loans and trade payables are approximate to the carrying value.

The currency profile of the Company's net debt is as follows:

	2011 £m	2010 £m
Sterling	–	–
	–	–

10 Share capital

	Number of ordinary shares of 1p each 2011	Number of B shares of 21.5p each 2010	Number of ordinary shares of 1p each 2010
In issue at the start of the period	201,040,148	–	200,791,400
B shares issued via a bonus issue	–	200,723,131	–
B shares redeemed in the year	–	(200,723,131)	–
Issued during the period in respect of share option schemes	449,960	–	248,748
In issue at the end of the period	201,490,108	–	201,040,148

Proceeds received in relation to shares issued during the period were £101,000 (2010: £238,000).

	2011 number of shares	2011 £'000	2010 number of shares	2010 £'000
Ordinary Shares of 1p each Allotted, called up and fully paid	201,490,108	2,015	201,040,148	2,010

The holders of the Ordinary Shares are entitled to receive dividends as declared and are entitled to one vote per share.

Financial statements

Notes to the Parent Company financial statements *continued*
For the 52 weeks ended 2 July 2011

11 Treasury shares

	2011 number of shares	2011 £'000	2010 number of shares	2010 £'000
Outstanding at beginning of year	99,628	128	837,135	1,301
Reissued during the period in respect of share option schemes	(99,628)	(128)	(737,507)	(1,173)
Outstanding at end of year	–	–	99,628	128

In the past the Company has acquired its own shares ('treasury shares') for the purpose of delivery to employee share schemes. No such purchase was made during the year.

The Company reissued 99,628 (2010: 737,507) treasury shares for a total consideration of £Nil (2010: £641,843).

The Company has the right to reissue the remaining treasury shares at a later date.

12 Share-based payments
As at 2 July 2011, the Company operated two share award plans:
a) Dunelm Group Share Option Plan ('GSOP')
b) Long-Term Incentive Plan ('LTIP')

There were no exercisable options as at 2 July 2011.

a) Dunelm Group Share Option Plan
The GSOP was established in December 2003. Options have a vesting period of three years from date of grant and a maximum life of 10 years. All options granted prior to IPO have an exercise price equal to the market value as agreed with HMRC at date of grant; there have been no further grants since IPO. There are no performance conditions but there is a requirement that the Group's shares be traded on a public exchange at date of exercise, and the awards are also subject to continued employment with the Group.

The fair value of services received in return for share options granted is measured by reference to the fair value of the options, assessed using a binomial model. The fair value per option granted and the assumptions used in the calculations are as follows:

	October 2010 grant	June 2008 grant
Fair value at measurement date	145.8p	65.6p
Exercise price	420.0p	137.0p
Expected volatility (weighted average volatility used in modelling – based on historical volatility of comparable quoted companies)	36%	35%
Option life (weighted average life used in modelling)	3 years	3 years
Expected dividends	2.5%	8.7%
Risk-free interest rate	1.7%	4.8%

The number and weighted average exercise price of options under the GSOP is as follows:

	Weighted average exercise price 2011	Number of shares under option 2011	Weighted average exercise price 2010	Number of shares under option 2010
Outstanding at beginning of year	–	–	–	–
Exercised during year	–	–	–	–
Outstanding at end of year	–	–	–	–

12 Share-based payments *continued*

b) Long-Term Incentive Plan

The LTIP was approved by the Board prior to IPO enabling the Company to award shares to particular individuals, normally in the form of nominal cost options. The LTIP is administered by the Remuneration Committee. Two grants have been made in the year, to the Executive Directors and Nick Wharton, the Executive Director's grant is exercisable in December 2013 depending on the level of growth in Group EPS relative to RPI, the grant awarded to Nick is exercisable in December 2015 and dependent on continuing employment. The maximum life of options under LTIP is 10 years from the date of grant. Full details of this plan are included in the Remuneration Report on pages 39 to 46.

The fair value of services received in return for share options granted is measured by reference to the fair value of the options.

This has been calculated as follows:

	December 2010	December 2010	September 2009	September 2008
Share price at date of grant	500.0p	500.0p	316.0p	149.0p
Discount factor, based on dividend yield of 2.5% to vesting date	0.881	0.927	0.913	0.889
Fair value of option	440.6p	463.4p	288.5p	132.5p

The number and weighted average exercise price of options under the LTIP at 2 July 2011 is:

	Weighted average exercise price 2011	Number of shares under option 2011	Weighted average exercise price 2010	Number of shares under option 2010
Outstanding at beginning of year	–	964,923	–	1,006,193
Granted during year	–	387,922	–	209,164
Exercised during year	–	(317,922)	–	(155,270)
Lapsed during year	–	–	–	(95,164)
Outstanding at end of year	–	1,034,923	–	964,923

The total expense recognised in the income statement arising from share-based payments is as follows:

	2011 £'000	2010 £'000
LTIP	614	935
	614	935

13 Contingent liability

The Company and certain subsidiaries have given joint and several guarantees in connection with all bank facilities provided by the Group's principal bankers.

The Group's banking facilities are subject to a netting facility whereby credit balances may be offset against indebtedness of other Group companies.

14 Related party disclosure

The amount due to the Company from subsidiary undertakings is set out in note 6. Transactions between the Company and its subsidiaries were as follows:

	2011 £'000	2010 £'000
Cash paid to Group undertakings	(20,303)	(69,653)
Cash received from Group undertakings	192	10,997
Dividends received	60,000	40,000
Net interest receivable	2,090	2,454

Advisers

Corporate Brokers and Financial Advisers

UBS Investment Bank
1 Finsbury Avenue
London EC2M 2PP
Tel: 020 7567 8000

Oriel Securities Limited
150 Cheapside
London EC2V 6ET
Tel: 020 7710 7600

Legal Advisers

Allen & Overy LLP
One Bishops Square
London E1 6AO
Tel: 020 3088 0000

Auditors

KPMG Audit Plc
1 Waterloo Way
Leicester LE1 6LP
Tel: 0116 256 6000

Principal Bankers

Barclays Bank plc
Midlands Corporate Banking
PO Box 333
15 Colmore Row
Birmingham B3 2WN
Tel: 0845 755 5555

Registrars

Equiniti
Aspect House
Spencer Road
Lancing
West Sussex BN99 6DA
Tel: 0871 384 2030

Financial Public Relations

MHP Communications
60 Great Portland Street
London W1W 7RT
Tel: 020 3128 8100

FSC
LOGO
HERE

Designed and produced by **Emperor Design Consultants Ltd**
Telephone **+44 (0)121 262 3830 www.emperordesign.co.uk**

www.dunelm-mill.com

Tel: 0116 264 4356
Email: investorrelations@dunelm-mill.co.uk