KATHMANDU HOLDINGS LIMITED

# Annual Report 2018

Kathmandu®
World ready.

Oboz®
FOOTWEAR
TRUE TO THE TRAIL®

**Caroline Bellamy**
Adventurer and artist from
Nelson, New Zealand

Lake Marian, Fiordland
National Park – South Island
New Zealand

# World ready.

We come from New Zealand, home to some of the world's harshest conditions. Since 1987 we've been engineering outdoor gear for adventurers all over the world – preparing all kinds of people for their next adventure.

For us, preparation is more than having the right gear. It's a mindset. It's having curiosity, an open mind, and a hunger to learn.

Whether you're on an epic expedition, volunteering in a remote part of the world, or exploring the best local trails, you can be confident you can take on any destination in any weather conditions with Kathmandu.

**We believe travel and adventure is the ultimate life experience. With product engineering and expert advice, we aim to give you the confidence to discover the world.**

# Highlights 2018

## Sales $

497.4m

↑ 11.7%

## Same store sales growth

4.4%

↑ AU 7.5% ↓ NZ (2.4%)

## Gross margin

63.4%

↑ 140 bps ↑ AU 180 bps ↑ NZ 260 bps

## Operating costs % of sales

45.4%

↓ 0.7% pts better than 2017

## EBIT $

74.6m

↑ 30.9%

## Net profit after tax $

50.5m

↑ 32.9%

## Full year dividend

15cps

↑ 2 cps

## Operating cash flow

75.6m

↑ $8.3m

## Online % of Kathmandu sales

9.4%

↑ 35.9% online sales growth

## Summit club members

1.9m

↑ 0.2m active members


"In Kathmandu and Oboz, we have two great brands with significant growth potential in North America and Europe."

# Contents



## Notice of Annual Meeting 2018

11.00am Friday
23 November 2018
Link Market Services,
Level 11, Deloitte Centre,
80 Queen Street, Auckland

# Chairman and CEO's letter

**David Kirk**
Chairman

**Xavier Simonet**
Managing Director and
Chief Executive Officer

2018 was our most successful year ever. We achieved record sales and profit in our core markets, acquired Oboz footwear, and made significant progress towards our sustainability goals.

We struck a healthy balance between sales and gross margin. Sales growth was supported by the successful launch of innovative new products, inspiring digital content, and an enhanced in-store customer experience. Top line growth combined with continued cost control, resulted in excellent profit growth.

## Oboz acquisition

During the year we were pleased to successfully acquire Oboz, an authentic US based outdoor footwear brand. Oboz was founded in 2007, and has grown significantly, with Kathmandu as a key international customer.

Kathmandu and Oboz are very culturally aligned with core principles of brand development, innovation, quality, customer service, and sustainability. Kathmandu is a successful Australasian retailer, whereas Oboz has strong expertise in building a wholesale footwear brand in North America. The combination of the two businesses enables diversification in complementary markets and product categories, while also assisting to accelerate Kathmandu international wholesale growth. We are excited by the opportunity to develop international wholesale channels for both the Oboz and Kathmandu brands.

## Growth Strategies and Investments

Kathmandu's strategy is focussed on two pillars: continuous improvement initiatives in our core Australasian market, and international growth strategies targeting new markets and channels.

**Continuous improvement initiatives (Australasia):**

- Elevate brand distinctiveness through product design and innovation, with a focus on our expertise in adventure travel;
- Inspire our customers and engage with our Summit Club members with a focus on social media and digital channels;
- Optimise store locations, refine visual merchandising and product presentation, and improve the customer experience to drive sales growth;
- Provide a channel agnostic offer, and increase online site visitation and purchase conversion to deliver online sales growth;

"We are focused on answering the needs of our customers by designing original, sustainable, engineered and adaptive products."

International growth strategies with a focus on driving profitable sales:

- Accelerate Kathmandu's international wholesale growth by leveraging our brand equity, online platform, and Oboz customer relationships;
- Grow Oboz as an authentic outdoor footwear brand internationally;
- Evaluate further new market opportunities using a capital light model.

## Sustainability

Sustainability is a core value for both Kathmandu and Oboz, and is an integral part of how we do business. We have made significant progress toward our goal of industry leadership thanks to the care and dedication of our passionate team.

Key achievements this year include being awarded an A rating in the Ethical Fashion Report[1], and becoming the first company in Australasia to gain accreditation with the Fair Labor Association.

Full details of our progress can be found in our 2018 Sustainability Report, produced in conjunction with our Annual Report and prepared in accordance with the Global Reporting Initiative (GRI).

## People

Two new directors joined the Board of Directors' this year. Philip Bowman and Brent Scrimshaw are a great fit for the next stage of Kathmandu's journey. They have provided key insights and guidance in the areas of retail, brand development and international markets.

The Board would like to thank management and the wider team for their passion and determination to deliver another very successful year.

## Dividend

The Directors have declared a final dividend of 11 cents per share, which with the 4 cents interim dividend makes a record payout of 15 cents per share, an increase of 2 cents per share compared to last year. The final dividend will be fully imputed for New Zealand shareholders and fully franked for Australian shareholders.

## Outlook

Kathmandu and Oboz are both authentic product and customer led brands. We are focused on answering the needs of our customers by designing original, sustainable, engineered and adaptive products.

In the year ahead, we remain committed to continuous improvement in our core markets, elevating our brand and customer engagement against an ever-changing mix of competitors.

Beyond our core markets, we are excited by the opportunity to develop new international wholesale channels for both the Oboz and Kathmandu brands.

**David Kirk**
Chairman

**Xavier Simonet**
Managing Director and Chief Executive Officer

[1]Each year, Baptist World Aid and Tear Fund rate apparel brands in Australia and New Zealand on their supply chain practices.

# Result and Financial Performance

| Key performance indicators | 2018 | 2017 | % Change |
|---|---|---|---|
| **Sales** | $497.4m | $445.3m | ↑ 11.7% |
| *Same store sales growth* | *4.4%* | *5.5%* | |
| **Gross profit** | $315.5m | $276.2m | ↑ 14.2% |
| *Gross margin* | *63.4%* | *62.0%* | |
| **Operating expenses** | ($225.7m) | ($205.4m) | ↑ 9.9% |
| *Operating expenses % of sales* | *45.4%* | *46.1%* | |
| **EBITDA** | $89.8m | $70.8m | ↑ 26.8% |
| *EBITDA margin* | *18.1%* | *15.9%* | |
| **EBIT** | $74.6m | $57.0m | ↑ 30.9% |
| *EBIT margin* | *15.0%* | *12.8%* | |
| **NPAT** | $50.5m | $38.0m | ↑ 32.9% |
| **Earnings per share** | 23.9cps | 18.7cps | ↑ 27.8% |
| **Dividend** | 15.0cps | 13.0cps | ↑ 15.4% |
| **Net Debt** | $31.4m | $6.9m | |
| **Share Price (NZX)** | $3.08 | $2.27 | ↑ 35.7% |
| **Summit club members** | 1.9m | 1.7m | ↑ 12% |
| **Employees** | 1,998 | 1,955 | ↑ 2.2% |
| **Store count** | 167 | 164 | |

# "Group sales increased by 11.7% to $497.4m. Kathmandu same store sales increased by 4.4% measured at constant exchange rates."

**Group sales** increased by 11.7% to $497.4m. Kathmandu same store sales increased by 4.4% measured at constant exchange rates. Oboz sales added a further $15.9m. By country the change in same store sales was:

- Australia +7.5% increase
- New Zealand -2.4% decrease

**Gross profit** increased by 14.2% to $315.5m. Gross margin increased by 140bps to 63.4%, and Kathmandu only gross margin was 64.1%. Improvement came from increased full price sell through, combined with a higher average selling price. By country the change in gross margins were:

- Australia +180bps
- New Zealand +260bps

Our foreign currency forward hedging policy up to a twelve month basis.

**Operating Expenses** excluding depreciation, amortisation and financing costs increased by $20.3m (9.9%), but as a percentage of sales decreased from 46.1% to 45.4%. Efficiencies were achieved through improved sales productivity of store labour and rent, distribution centre labour and targeted promotional spend. Abnormal costs of $4.0m arose from the acqusition of Oboz ($2.0m) and a one-off exceptional team bonus ($2.0m). Operating expenses also include $3.9m in relation to Oboz. Operating cost efficiency remains a key area of focus in 2019.

**Capital expenditure** of $16.7m was $3.4m higher than last year. Retail store spend was $13.8m, primarily in relocations and refurbishments to further optimise the store network. Systems capital investment was $2.9m, focused on online platform and CRM upgrades. Capital expenditure is planned to increase in FY2019 as ongoing investments will be made in existing retails sites, and the three year roadmap for technology projects includes the online platform upgrade, new warehouse management system, an upgraded ERP system.

**Depreciation and amortisation** expense increased by $1.4m (10.1%), from the annualised impact of prior year capital infrastructure expenditure.

**Finance costs** reduced as a result of lower average debt levels throughout the year, and a decline in effective interest rates.

**Inventory** levels increased by $22.7m to $111.9m. This includes $17.9m to support Kathmandu international growth and Oboz inventory on hand.

**Taxation** The effective tax rate of c.31% is higher than prior year. This increase is due to higher non-deductible expenditure, in particular $2.0m acquisition costs in relation to Oboz.

**Oboz's acquisition** was completed during the year, for a purchase price of $103m (net consideration of $97m). This was funded through a mix of debt and capital, with $49m of equity raised. Intangible assets totalling $103m have been recongised for goodwill, brand and customer relationship assets. A deferred consideration balance of $22m has been recognised and will settle during the coming year dependant on acheivement of profit targets being met by Oboz.

## "Our customers have reacted positively to innovative products and engaging brand content."

# Our top 5 sustainability highlights.

At Kathmandu, sustainability isn't a department, it's a way of doing things. Here are some of our highlights from last year.

Fair Labor Association accredited

#2 world ranking by the Textile Exchange for preferred materials

Scored an 'A' in the Ethical Fashion Report

80% towards our zero waste to landfill target

Recycled 6.7 million bottles into our gear

# The Board


**1 David Kirk** Chairman

Mr Kirk is the Chairman of Trade Me Group Ltd, the co-founder and Managing Partner of Bailador Investment Management, and sits on the Board of Bailador portfolio companies. Mr Kirk's Executive Management career has seen him hold Chief Executive Officer roles at Fairfax Media and PMP Limited and the Regional President (Australasia) for Norske Skog.

**2 Xavier Simonet**

Managing Director and Chief Executive Officer

Joined Kathmandu in July 2015 with over 20 years international experience in building brands and developing successful retail businesses in fashion, apparel, accessories and related products.

Prior roles include CEO of Radley (London), VP & GM International of DB Apparel, 11 years at LVMH (primarily Asia-Pacific) and International Director of Seafolly.

**3 Philip Bowman** (appointed 2 October 2018)

Non-executive Director

Mr Bowman has extensive experience in retail including roles as CFO of Bass, CEO of Bass Taverns, Executive Chairman of Liberty PLC, CEO of Allied Domecq, Chairman of Coral Eurobet, CEO of Scottish Power and CEO of Smiths Group. He has held office as an independent director of BSkyB, Scottish & Newcastle and Berry Bros. & Rudd. He currently sits on the boards several entities, including, Ferrovial SA, and is Chairman of Majid al Futtaim Properties.

**4 John Harvey** Non-executive Director

Mr Harvey is a professional director with a background in accounting and professional services, including 23 years as a partner of PricewaterhouseCoopers where he held a number of leadership and governance roles. Mr Harvey has extensive experience in financial reporting, governance, information systems and processes, business evaluation, acquisition, merger and takeover reviews.

**5 Sandra McPhee** Non-executive Director

Ms McPhee is an experienced executive and non-executive Director in consumer facing sectors including aviation, retail, energy and media. She held a range of senior international executive roles in the aviation industry, most recently with Qantas Airways Limited.

**6 Brent Scrimshaw** (appointed 2 October 2018)

Non-executive Director

Mr Scrimshaw has had an 18-year career with Nike Inc across Marketing, Commerce and General Management. He led marketing across Nike Pacific, was the Regional GM for Nike North America, was the Chief Marketing officer for Nike EMEA, and also served as Vice President and Chief Executive of Nike Western Europe. He is currently the CEO and Co-Founder of Unscriptd.com and is a Non-Executive Director of ASX listed Rhinomed (RNO) and Catapult International Limited (CAT).

# Management Team










1 **Xavier Simonet**
Chief Executive Officer

2 **Reuben Casey**
Chief Operating & Financial Officer, Company Secretary

3 **Paul Stern**
General Manager, Marketing, Online & International

4 **Ben Ryan**
General Manager, Product

5 **Rebecca Edwards**
General Manager, Human Resources

6 **Stephen Domancie**
General Manager, Retail Stores & Operations

7 **Caleb Nicolson**
General Manager, Supply Chain

8 **Jolann Van Dyk**
Chief Information Officer

9 **Mark Handy**
General Manager, Merchandising, from 4 September 2017

# Directors' Report

YOUR DIRECTORS PRESENT THEIR REPORT AND THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 JULY 2018.

## Directors

The following persons were Directors of Kathmandu Holdings Limited during the financial year.

### David Kirk

Was re-appointed as a non-Executive Director, Chairman, Member of the Audit and Risk Committee, Member of the Remuneration Committee on 18 November 2016. He continues in these offices at the date of this report.

### Xavier Simonet

Was appointed as Managing Director and Chief Executive Officer on 29 June 2015 and continues in these offices at the date of this report.

### John Harvey

Was re-appointed as a non-Executive Director, Chair of the Audit and Risk Committee, Member of the Remuneration Committee on 21 November 2014. He continues in these offices at the date of this report.

### Sandra McPhee

Was re-appointed as a non-Executive Director, Member of the Audit and Risk Committee, Chair of the Remuneration Committee on 18 November 2016, and continues in these offices at the date of this report.

### Philip Bowman

Was appointed as a non-Executive Director, Member of the Remuneration Committee, Member of the Audit and Risk Committee on 2 October 2017 and continues in these offices at the date of this report.

### Brent Scrimshaw

Was appointed as a non-Executive Director, Member of the Remuneration Committee, Member of the Audit and Risk Committee on 2 October 2017 and continues in these offices at the date of this report.

### Christine Cross

Was re-appointed as a non-Executive Director, Member of the Remuneration Committee, Member of the Audit and Risk Committee on 20 November 2015, and retired as a Director effective 2 October 2017.

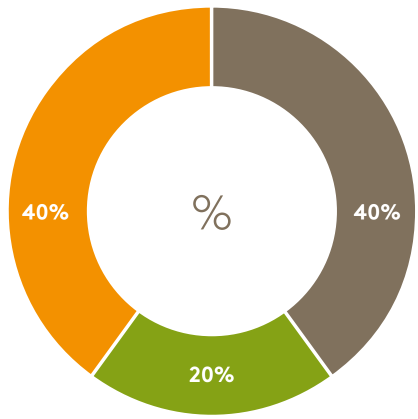
### John Holland

Was re-appointed as a non-Executive Director, Member of the Audit and Risk Committee, Member of the Remuneration Committee on 20 November 2015, and retired as a Director effective 2 October 2017.

Details of the experience and expertise of the Directors are outlined on page 15 of this annual report.

## Board Tenor

The average tenor for non-executive Directors is 6 years 4 months, with the following tenor mix:




- 0 - 3 Years
- 4 - 6 Years
- 7 - 9 Years

## Retirement of Directors

In accordance with the Company's constitution, Mr. David Kirk and Ms. Sandra McPhee will retire as Directors at the annual general meeting and being eligible, offer themselves for re-election.

## Meeting of Directors

The number of meetings of the Board of Directors and Committees held during the year ended 31 July 2018 and the numbers of meetings attended by each Director were:

| | Director Meetings | | Audit and Risk Committee Meetings | | Remuneration and Nominee Committee Meetings | |
|---|---|---|---|---|---|---|
| Director | A | B | A | B | A | B |
| David Kirk | 8 | 8 | 5 | 5 | 5 | 5 |
| Xavier Simonet | 8 | 8 | XX | XX | XX | XX |
| John Harvey | 8 | 8 | 5 | 5 | 5 | 5 |
| Sandra McPhee | 8 | 8 | 5 | 5 | 5 | 5 |
| Brent Scrimshaw | 6 | 6 | 3 | 3 | 3 | 3 |
| Philip Bowman | 6 | 6 | 3 | 3 | 3 | 3 |
| John Holland | 2 | 2 | 1 | 1 | 2 | 2 |
| Christine Cross | 2 | 2 | 1 | 1 | 2 | 2 |

A – Number of meetings attended
B – Number of meetings held during the time the Director held office during the year
XX - Not a member of relevant Committee

## Board Skills Matrix

The Board benefits from the combination of the different skills, experiences and expertise that Directors bring to the Board and the insights that result from this diversity.

The following chart summarises the skills, attributes and experience of the Company's Directors. Percentages are determined as at the date of this report.


**Executive Leadership:** Experienced and successful leadership at a senior executive level of large organisations. Governance: Knowledge and experience of high standards of corporate governance, including ASX/NZX Listing Rules and practices.

**International Business Development:** Experienced in multi-national, complex environments, including multi-channel business development.

**Strategy:** Expertise in the development and implementation of strategic plans and risk management to deliver investor returns over time.

**Capital Projects, Mergers and Acquisitions:** Experience in evaluating and implementing projects involving large-scale financial commitments, investment horizons and major transactions.

**Financial acumen:** Expertise in understanding financial accounting and reporting, corporate finance and internal financial controls, including an ability to probe the adequacies of financial and risk controls.

**Retail and Consumer Experience:** Experienced in retail and consumer sectors, understanding multi-channel retailing and brand development.

**Marketing and product development:** Expertise and senior executive experience in marketing and new media marketing metrics and tools.

**Remuneration:** Experience in remuneration design to drive business success.

**Technology and data:** Expertise and experience in the adoption of new technology and use of data analytics in a consumer environment.

## Principal Activities

The Group's principal activity in the course of the financial year was the design, marketing and retailing of clothing and equipment for outdoor, travel and adventure. It operates through wholly owned subsidiaries in New Zealand, Australia, United States and the United Kingdom.

## Matters Subsequent to the End of the Financial Year

No matters or circumstances have arisen since the end of the financial year which significantly affect or may significantly affect the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in future financial years.

## Likely Developments and Expected Results of Operations

Likely developments in the operations of the consolidated entity and the expected results of those operations in future financial years are contained on pages 38-50 of this annual report.

## Environmental Regulation

The consolidated entity's operations are not regulated by any significant environmental regulation under a law of the Commonwealth or of a State or Territory of Australia, or of New Zealand.

## Dividends

Since the end of the financial year, the Directors have declared the payment of a final ordinary dividend of NZ 11.0 cents per share. Dividends will carry full New Zealand imputation credits and full Australian franking credits. The dividend will be paid on 30 November 2018.

The Company does not currently have a dividend re-investment plan.

## Insurance of Officers

The Company has entered into deeds of indemnity, insurance and access with each Director which confirms each person's right of access to certain books and records of the Company for a period of seven years after the Director ceases to hold office. This seven year period can be extended where certain proceedings or investigations commence before the seven years expires. The deed also requires the Company to provide an indemnity for liability incurred as an officer of the Company, to the maximum extent permitted by law.

Indemnification: Pursuant to the Constitution, the Company is required to indemnify all Directors and employees, past and present against all liabilities allowed under law. The Company has entered into an agreement with each Director to indemnify those parties against all liabilities to another person that may arise from their position as Director or other officer of the Company or its controlled entities to the extent permitted by law. The deed stipulates that the Company will meet the full amount of any such liabilities, including reasonable legal costs and expenses.

Insurance: Pursuant to the Constitution, the Company may arrange and maintain Directors' and officers' insurance during each Director's period of office, and for a period of seven years after a Director ceases to hold office. This seven year period can be extended where certain proceedings or investigations commence before the seven years expires.

## Remuneration Report

### 1. Summary

Kathmandu's financial results for FY2018 reflect a continuation of a return to sustainable long-term profitable growth.

Earnings before interest and tax (EBIT) was $74.6m an increase of 30.9% and Net Profit after Tax was $50.5m, a 32.9% increase over FY2017.

**FY2018 remuneration**

- Non-Executive Directors fees increased by 2.0%.
- Executive base salary increases were limited to 2.0%.
- Short term incentives (cash) were paid to all eligible Executives (including the CEO) for exceeding the Group financial performance target (EBIT).
- Short term incentives (equity) were earned by all eligible Executives (excluding the CEO) and will vest subject to the Executives remaining employed by the Group as at 31 July 2019.

### 2. Key Management Personnel

The following Executives are identified as key management personnel with the authority and responsibility along with the Directors for planning, directing and controlling the activities of the Group, directly or indirectly, during the financial year:

**Currently Employed:**

**Xavier Simonet**
– Chief Executive Officer

**Reuben Casey**
– Chief Operating & Financial Officer, Company Secretary

## Other Management Team (Executive) members:

### Currently Employed:

**Ben Ryan**
– General Manager, Product

**Rebecca Edwards**
– General Manager, Human Resources

**Stephen Domancie**
– General Manager, Retail Stores & Operations

**Caleb Nicolson**
– General Manager, Supply Chain

**Paul Stern**
– General Manager, Marketing, Online & International

**Jolann van Dyk**
– Chief Information Officer

**Mark Handy**
– General Manager, Merchandising, from 4 September 2017

The Group employed all of the above Executives for the full years ended 31 July 2018 and 2017, unless otherwise stated.

Throughout their period of employment, Reuben Casey, Caleb Nicolson, Jolann Van Dyk, Rebecca Edwards and Ben Ryan were employees of Kathmandu Limited (New Zealand) and Xavier Simonet, Paul Stern, and Stephen Domancie were employees of Kathmandu Pty Limited (Australia).

## 3. Principles used to determine the nature and amount of remuneration

The Company's Remuneration and Nomination Committee of the Board, currently comprising all independent non-Executive Directors, determines the quantum and structure of Directors and Executive remuneration. The composition, role and responsibility of the Committee is outlined in the Corporate Governance Statement on page 24 of this annual report. The Committee adopts a series of principles in determining remuneration related decisions. The principles used are:

- The remuneration structure should reward those employees who have the ability to influence the achievement of the Group's strategic objectives and business plans to enhance shareholder value for successful Group performance outcomes and their contribution to these;
- Executive remuneration should be market competitive, and generally account for market practice including consideration of employee place of domicile;
- Executives' remuneration package should have:
    - a substantial portion of their total remuneration that is "at risk" and aligned with reward for creating shareholder value,
    - an appropriate balance between short and long-term performance focus and outcomes,
    - a mix of cash and equity based remuneration;
- The CEO because of his leadership role in establishing and delivering achievement of medium and long term Group strategic objectives and business plans, and increasing shareholder value over that period should, relative to other Executives have
    - a greater proportion of total remuneration (at least 50%) that is "at risk", i.e. contingent upon the achievement of performance hurdles, and
    - a greater proportion of "at risk" remuneration weighted towards equity based rewards rather than cash,
- Non-Executive Directors' remuneration should enable the Company to attract and retain high quality Directors with the relevant experience. In order to maintain independence and impartiality, non-Executive Directors should not receive performance based remuneration;
- The Board uses discretion when setting remuneration levels, taking into account interests of shareholders, the current market environment and Group performance.

## 4. Remuneration framework

The Board, through the Committee undertakes its governance role in establishing Executive remuneration including, where required, use of external independent remuneration consultants and/or available market information.

The Executive remuneration structure has three components:

a) **Base salary and benefits;**

b) **Short term incentives** determined on the basis of achievement of specific targets and outcomes relating to annual Group financial performance and individual value adding performance objectives. The available incentive reward is split between cash and equity.

c) **Long term incentives** via participation in the Company's Long Term Incentive plan.

### a) Base salary and benefits

Base salary for Executives is reviewed annually to assess appropriateness to the position and competitiveness with the market.

**b) Short term incentives (STI)**
Executives are eligible to participate in an annual STI that delivers rewards by way of cash and/or deferred equity. Group Earnings before interest and tax (EBIT), has been determined as the appropriate financial performance target to trigger payment of STI.

The amount of any STI paid in a year is dependent upon:

a. the level of performance achieved against the Group's financial performance target (EBIT) for the year; and

b. the outcome of individual value adding performance, measured by achievement of individual KPI's, subject to a minimum level of performance achieved by the Group relative to the financial performance target (EBIT) for the year.

The weighting of STI between Group financial performance, individual KPI's, cash and deferred equity is:

| Short term incentive weighting: | CEO | | Executives | |
|---|---|---|---|---|
| | Cash | Equity | Cash | Equity |
| Group financial performance target | 70% | - | 29% | 46% |
| Individual KPI achievement | 30% | - | 25% | - |
| **Total** | **100%** | **-** | **54%** | **46%** |

For Executives where a short-term equity incentive is earned, vesting is subject to ongoing employment by the Group for a period of one year following the end of the financial year in which the incentive is earned.

**c) Long Term Incentive Plan (LTI)**
Shareholders reapproved the current LTI at the Company's 2016 Annual General Meeting based on the granting of nil cost performance rights. Rights have been offered each year since the plan was originally approved in 2010.

The plan is intended to focus performance on achievement of key long term performance metrics. The selected performance measures provide an appropriate balance between relative and absolute Company performance. The Board continues to reassess the plan and its structure to ensure it will best support and facilitate the growth in shareholder value over the long term relative to current business plans and strategies. Any grants made to Executive Directors are subject to shareholder approval.

Rights granted are dependent upon the Company achieving Earnings per Share (EPS) and/or relative TSR targets over specified performance periods, with the value of rights allocated between EPS and relative TSR determined each year. EPS is measured on a compound annual growth basis and TSR is measured on a relative basis against a comparator group of ASX listed companies (other than metal and mining stocks) ranked 101 to 200 in the S&P/ASX200 as at the date of the grant.

Performance measurement under either criterion is at the end of each applicable performance period with no ability to re-test. Fifty per cent of the relevant portion of the award vests for achievement of targets and a further fifty per cent vests for the achievement of aspirational targets. A sliding scale operates between target and aspirational performance levels.

"Sales growth was supported by the success of our key product groups, improved promotional execution, inspiring digital content, and an enhanced in-store customer experience."

In FY2018, grants were made to the CEO and COO/CFO. The Board resolved to grant nil cost performance rights that;

- Were measurable for a single specified performance period of three years, and
- Required achievement of relative TSR targets and EPS growth targets over a single specified performance period of three years with the value of rights allocated 50:50 between EPS and relative TSR.
- Performance measurement under either criterion is at the end of the performance period with no ability to re-test.

## 5. CEO Remuneration details:

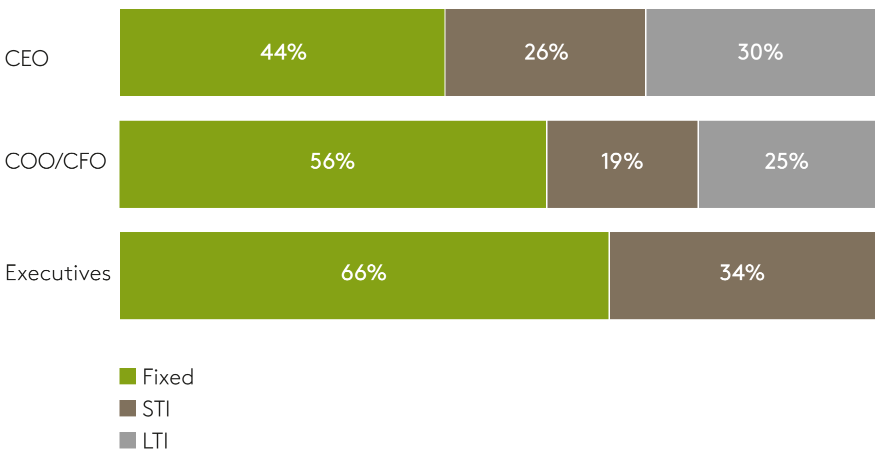
CEO remuneration comprises a mixture of base salary, STI and LTI:

| CEO 2018 Remuneration package | A$'000 |
|---|---|
| Fixed (Base salary, superannuation) | 812 |
| STI (60% of fixed) | 487 |
| LTI (70% of fixed) * | 568 |
| Maximum potential remuneration | 1,867 |

* Vesting dependent on achievement of performance hurdles measured over a three-year period. Vesting date 1 December 2020.

- More than half (56%) the total remuneration for the CEO is at risk:
- Over 85% of the at risk remuneration (all except for the STI KPI's) is solely dependent on outcomes of Group financial performance against short and long term targets, and
- All long term incentive (70% of Fixed Annual Remuneration) will be measured on a single 3-year performance period.

### Remuneration Structure – CEO and Executives:




**FY2018 STI outcomes**

For the year ended 31 July 2018 the Group financial performance targets were exceeded and as a result, short-term cash incentives were paid to the extent of 60% (100% of potential) of fixed annual remuneration for the Chief Executive Officer.

**5 Year CEO Remuneration (NZD)**

| | | Single Figure Remuneration[1] | % STI Achieved Against Maximum | Percentage Vested LTI's against Maximum | Span of LTI Performance Period |
|---|---|---|---|---|---|
| 2018 | Xavier Simonet | 1,408,315 | 100% | N/A | N/A |
| 2017 | Xavier Simonet | 1,290,026 | 86% | N/A | N/A |
| 2016 | Xavier Simonet | 1,391,983 | 100% | N/A | N/A |
| 2015 | Xavier Simonet | 136,267 | - | N/A | N/A |
| | Mark Todd[2] | 715,539 | - | 54% | 2010-2014 |
| 2014 | Peter Halkett | 1,009,108 | 33% | 74% | 2010-2013 |

1. Comprises of cash salary and fees, non-monetary benefits, superannuation.
2. Acting CEO during FY2015.

Details of the remuneration of the Directors and Key Management Personnel and total remuneration of other Executives of the Group, for the current and prior financial years are set out in section 6.3 of the financial statements.

## 6. Executive Service agreements

All Executives are on employment terms consistent with the remuneration framework outlined in this report. Each of the agreements has an open term, and the period of notice to be given by the employee is three months (six months for the CEO). The agreements provide for three months base salary inclusive of any applicable superannuation to be paid in the event of a redundancy (six months for the CEO).

## 7. Non-Executive Directors' fees

The current aggregate limit for non-Executive Directors' fees is $A800,000 per annum. In FY2018 the base fee payable (including superannuation if applicable) to the Chairman was $A229,000 and to a non-Executive Director $A120,000 per annum. No additional fees are paid for sub-committee attendances. No increase was made in 2017.

Any Executive Directors do not receive Directors' fees. The amounts approved for Directors' fees are expressed in AUD given the specific requirements for remuneration reporting applying to ASX listed companies, however all amounts reported in the tables within this report are specified in NZD, being the reporting currency of the Company.

The Board reviews Directors' fees annually seeking advice from external independent remuneration consultants as necessary.

Non-Executive Directors do not participate in the Company short or long term incentive schemes.

The following fees apply per annum:

| Total Fees | AUD $ |
|---|---|
| Chairman | 229,000 |
| Other non-Executive Directors | 120,000 |
| Actual fees paid in year ended 31 July 2018 (converted to reporting currency) | NZD $ |
| Chairman | 241,302 |
| Other non-Executive Directors | 126,236 |

## 8. Details of share-based compensation

The Company Long term incentive plan entitles the Board to grant performance rights for no cash consideration, at intervals determined by the Board.

The number of rights granted and the applicable performance period over which EPS and relative TSR is measured is set out below, along with the fair value of the rights at the grant date.

| | Grant Date | Rights Granted during the year | Date Exercisable | Expiry Date | Total fair value of Performance Rights at Grant Date $ |
|---|---|---|---|---|---|
| Executive Director – Xavier Simonet | | | | | |
| 2017 | 20 Dec 2017 | 292,809 | 1 Dec 2020 | 1 Dec 2020 | 488,420 |
| 2016 | 19 Dec 2016 | 293,078 | 1 Dec 2019 | 1 Dec 2019 | 378,071 |
| 2015 | 16 Dec 2015 | 407,463 | 1 Dec 2018 | 1 Dec 2018 | 433,948 |

**Shares issued to Directors and Other Executives on Vesting of Performance Rights:**

| | Date Granted | Date Shares Issued | Number of Shares Issued |
|---|---|---|---|
| 2018 | 18 Dec 2015 | 22 Aug 2017 | 669,669 |
| 2017 | 18 Dec 2015 | 29 Mar 2017 | 12,537 |

Performance rights granted to each Executive will, subject to satisfaction of performance conditions, vest on the basis of one ordinary share for each performance right which vests, at the end of each performance period.

## 9. Additional information, Performance Rights Vesting

Performance rights granted, the percentage that vested, the percentage that forfeited and future potential vesting periods are shown in the table below:

| | Grant Date | Vested % | Forfeited % | Financial periods in which rights may vest | Maximum total number of rights yet to vest | Maximum total value of grants yet to vest |
|---|---|---|---|---|---|---|
| Executive Director – Xavier Simonet | | | | | | |
| | FY2018 | 0.0% | 0.0% | FY2021 | 292,809 | 488,420 |
| | FY2017 | 0.0% | 0.0% | FY2020 | 293,078 | 378,071 |
| | FY2016 | 0.0% | 0.0% | FY2019 | 407,463 | 433,948 |
| Other Executives and Senior Management: | | | | | | |
| | FY2018 | 0.0% | 0.0% | FY2021 | 81,628 | 136,159 |
| | FY2018 | 0.0% | 0.0% | FY2020 | 568,941 | 1,217,534 |
| | FY2017 | 0.0% | 0.0% | FY2020 | 82,732 | 106,724 |
| | FY2017 | 0.0% | 0.0% | FY2019[1] | 466,249 | 797,286 |

1. Shares were issued on 10 August 2018

The maximum value of performance rights yet to vest has been determined as the total number of performance rights still to vest multiplied by the fair value of each performance right at grant date.

### Company performance

All Executives' short term incentive is dependent upon the Company's overall financial performance for each financial year. Long term incentive is dependent upon both earnings per share growth and relative total shareholder returns over a range of performance periods.

With reference to the measurement of long term incentive performance the table below outlines the Company's earnings and share performance since its listing on 13 November 2009:

| Year | NPAT | Growth | EPS cents per share | EPS Growth | Share price at start of year | Share price at end of year | Share price growth | Ordinary dividends paid or declared per share |
|---|---|---|---|---|---|---|---|---|
| FY2010 | $9.4m | NA | 0.3 | NA | $2.13 | $2.05 | (3.8%) | $0.07 |
| FY2011 | $39.1m | 316.0% | 19.5 | 65x | $2.05 | $2.20 | 7.3% | $0.10 |
| FY2012 | $34.9m | (10.7%) | 17.4 | 0.9x | $2.20 | $1.59 | (27.7%) | $0.10 |
| FY2013 | $44.2m | 26.6% | 22.1 | 1.3x | $1.59 | $2.37 | 49.1% | $0.12 |
| FY2014 | $42.2m | (4.5%) | 21.0 | 1.0x | $2.37 | $3.33 | 40.5% | $0.12 |
| FY2015 | $20.4m | (51.7%) | 10.1 | 0.5x | $3.33 | $1.70 | (48.9%) | $0.08 |
| FY2016 | $33.5m | 64.2% | 16.6 | 1.6x | $1.70 | $1.80 | 5.9% | $0.11 |
| FY2017 | $38.0m | 13.4% | 18.7 | 1.1x | $1.80 | $2.27 | 26.1% | $0.13 |
| FY2018 | $50.5m | 32.9% | 23.9 | 1.3x | $2.27 | $3.08 | 35.6% | $0.15 |

Share price quoted is the NZX listing price. The Company is listed on both the ASX and NZX and options will vest on both exchanges, dependent on where the employee is based.

### Shares under options or performance rights

There are no unissued ordinary shares of the Company under any vested options or performance rights at the date of this report.


## 10. Remuneration of Auditors

Details of remuneration of Auditors is set out in Note 6.8 of the Financial Statements.

**Non-Audit Services**

PricewaterhouseCoopers were appointed auditors of Kathmandu Holdings Limited in 2009 and whilst their main role is to provide audit services to the Company, the Company does employ their specialist advice where appropriate. In each instance, the Board has considered the nature of the advice sought in the context of the audit relationship and in accordance with the advice received from the Audit and Risk Committee, does not consider these services compromised the auditor independence for the following reasons:

- All non-audit services have been reviewed by Audit and Risk Committee to ensure they do not impact the impartiality and objectivity of the auditor
- None of the services undermined the general principles relating to auditor independence, including not reviewing or auditing the auditor's own work, not acting in a management or a decision making capacity for the Company, not acting as advocate for the Company or not jointly sharing economic risk or rewards.

This report is made in accordance with a resolution of the Directors.

**David Kirk**
Chairman

**Xavier Simonet**
Managing Director

# Corporate Governance

The Board and management of the Company are committed to the Company adhering to best practice governance principles and maintaining the highest ethical standards. The Board is responsible for the overall corporate governance of the Company, including adopting the appropriate policies and procedures and seeking to ensure Directors, management and employees fulfil their functions effectively and responsibly.

The Company is listed on both the New Zealand and Australian stock exchanges. Corporate governance principles and guidelines have been introduced in both countries. These include the Australian Securities Exchange (ASX) Corporate Governance Council Corporate Governance Principles and Recommendations (Third Edition) (ASX Code), the New Zealand Stock Exchange Listing Rules relating to corporate governance, and the NZX Corporate Governance Code 2017 (NZX Code) (collectively, the Principles).

The Company has followed each of the recommendations set out in the Principles where appropriate for the size of the Company and the Board, the resources available and the activities of the Company. After due consideration, the Board considers that the Company's corporate governance practices and procedures depart from the Principles during the reporting period only as set out below. The information in this statement is current as at 31 July 2018 (except where otherwise specified).

**Explanation for departure from NZX Corporate Governance Code 2017 and ASX Corporate Governance Principles and Recommendations (3rd Edition)**

| Reference | Recommendation | Departure | Explanation for Departure |
|---|---|---|---|
| NZX Code 3.4<br>ASX Code 2.1 | An issuer should establish a nomination committee to recommend director appointments to the Board | The Company has not maintained a separate nomination committee | Due to the size of the Board, the Board as a whole retains the responsibility for recommending new Director appointments. The Board considers that it is able to deal efficiently and effectively with the processes of appointment and reappointment of directors to the Board and considerations of Board composition and succession planning |
| NZX Code 7.3<br>ASX Code 7.3 | Internal audit functions should be disclosed | The Company does not have an internal audit function | The Company considers that the external advisors it currently engages provide a sufficient system for evaluating and continually improving the effectiveness of risk management for the Company and delivers appropriate objective assurance on risk management. |

The full content of the Company's Corporate governance policies, practices and procedures can be found on the Company's website (kathmanduholdings.com).

## Board of Directors, Charter and its Committees

The Board has adopted a written charter to provide a framework for the effective operation of the Board. The charter addresses the following matters and responsibilities of the Board:

- the long-term growth and profitability of the Company;
- oversight of the Company, including its control and accountability systems;
- appointing and removing the Managing Director (or equivalent);
- ratifying the appointment, and where appropriate, the removal of the senior Executives;
- input into and approval of corporate strategy and performance objectives;
- reviewing and ratifying systems of risk management and internal compliance and control, codes of conduct and legal compliance;
- monitoring senior management's performance and implementation strategy, and seeking to ensure appropriate resources are available;
- approving and monitoring the progress of major capital expenditure, capital management and acquisitions and divestitures;
- approving budgets developed by management; and
- approving and monitoring financial and other reporting.

A copy of the Kathmandu Board charter is available at www.kathmanduholdings.com/investor-relations/governance/

### Board Composition

At present, there are six Directors on the Board. Five out of the six Directors are non-Executive Directors. Xavier Simonet (Managing Director and Chief Executive Officer,) is the only Executive Director on the Board. The Chairman of the Board is David Kirk. The biography of each Board member, including each Director's skills, experience, expertise and the term of office held by each Director at the date of this Annual Report is set out in "The Board" section of this Annual Report. Director ownership interests are set out in the "Statutory Information" section of this Annual Report. New directors are selected through a nomination and appointment procedure administered by the Board, as outlined in the Board charter. The Company enters into written agreements with each newly appointed Director establishing the terms of their appointment.

### Board and executive performance

The Board Charter provides for an annual performance evaluation that compares the performance of the Board with the requirements of the Charter, reviews the performance of the Board's committees and each individual Director, considers the goals and objectives of the Board for the upcoming year and effects any amendments to the Charter considered necessary or desirable of the Board and its Committees. The Board ensures that there is appropriate training available to all Directors to enable them to remain current on how best to discharge their responsibilities and to keep up to date on changes in areas relevant to their roles. The Board is currently undertaking a review of its performance during the reporting period by the anonymous completion by directors and executives of evaluation questionnaires relating to Board and committee composition and performance, and individual interviews of directors with the Chairman.

The Group has a robust process for annual evaluation of its senior executives that compares the performance of each individual senior executive against the goals and objectives set for the year. A performance evaluation of each senior executive was undertaken in relation to the reporting period in accordance with this process.

### Independence of Directors

The factors that the Company will take into account when assessing the independence of its Directors are set out in its Charter, a copy of which is available on the Company's website (kathmanduholdings.com).

The Managing Director (Xavier Simonet) is employed by the Company or another Group member in an Executive capacity and is not considered to be an independent Director based on the criteria set out in the Board Charter. All remaining Directors satisfy the criteria and are considered independent Directors, namely David Kirk, John Harvey, Sandra McPhee, Philip Bowman and Brent Scrimshaw.

## Board committees

The Board may from time to time establish appropriate committees to assist in the discharge of its responsibilities. The Board has established the Audit and Risk Committee and the Remuneration Committee. The Board may establish other committees as and when required. Membership of Board committees will be based on the needs of the Company, relevant legislative and other requirements and the skills and experience of individual Directors. Copies of the Committee charters are available at www.kathmanduholdings.com/investor-relations/governance/. The membership of each Committee is noted below and a report on member attendance at each Committee meeting is set out in the "Director's Report" section of this Annual Report.

The Board has appropriate protocols in place that set out the procedure to be followed if there is a takeover offer for the Company. A committee of Independent Directors would be formed who would have responsibility for managing the takeover process in accordance with the Board protocols and the New Zealand Takeovers Code.

## Audit and Risk Committee

Under its charter, this committee must have at least three members, a majority of whom must be independent Directors and all of whom must be non-Executive Directors. Currently, all the non-Executive Directors are members of this committee. John Harvey is Chair of the committee. The primary role of this committee includes:

- overseeing the process of financial reporting, internal control, continuous disclosure, financial and non-financial risk management and compliance and external audit;
- monitoring Kathmandu's compliance with laws and regulations and Kathmandu's own codes of conduct and ethics;
- encouraging effective relationships with, and communication between, the Board, Management and Kathmandu's external auditor; and
- evaluating the adequacy of processes and controls established to identify and manage areas of potential risk and to seek to safeguard the Company's assets.


Under the charter, it is the policy of the Company that its external auditing firm must be independent of the Company. The committee will review and assess the independence of the external auditor on an annual basis.

As noted above, the Company does not currently have an internal audit function. The Committee will continue to monitor whether this current practice is sufficient for the Company's requirements.

## Remuneration Committee

Under its charter, this committee must have at least three members, a majority of whom must be independent Directors and all of whom must be non-Executive Directors. Currently, all the non-Executive Directors are members of this committee. Sandra McPhee is Chair of the committee. The purpose of this committee is to ensure the remuneration programme of the Kathmandu Group delivers the business plan, is fit for purpose and is one that considers the current business needs of the Group whilst supporting shareholder and customer value. The main functions of the committee are to assist the Board in fulfilling its responsibilities to stakeholders on management activities for the Kathmandu Group in relation to:

- Overseeing the development and application of the Group Human Resources strategy, the remuneration framework and associated policies;
- The remuneration of senior executives, non-executive Directors and Directors;
- Providing effective remuneration policies and programs to motivate high performance from all employees; and
- Policies for managing the performance and development of employees at all levels are appropriate and effective.

## Policies, practices and processes

The main policies and practices adopted by the Company are summarised below. A copy of each policy is available at www.kathmanduholdings.com/investor-relations/governance/

### Risk management policy

The identification and proper management of the Company's risk are an important priority of the Board. The Company has a Risk Management Policy appropriate for its business. This policy highlights the risks relevant to the Company's operations, and the Company's commitment to designing and implementing systems and methods appropriate to minimise and control its risk. The Audit and Risk Committee assists the Board in discharging its responsibility for monitoring risk management and that Committee is responsible for establishing procedures which seek to provide assurance that major business risks are identified, consistently assessed and appropriately addressed. A risk management framework is in place to identify, oversee, manage and control risk. The Committee undertook a formal review of the risk framework during the reporting period. A robust risk assessment process of reviewing existing risks and identifying any new and emerging risks facing the Company, and how these are to be managed, was carried out during the reporting period.

### Health and Safety

The Company is committed to cultivating a strong safety culture and awareness of health and safety risks, performance and management within the Group. The Group has adopted an integrated approach to safety and wellbeing, which recognises that workplace safety, health and mental health all contribute to an employee's overall wellbeing. The Company maintains a Safety and Wellbeing intranet site 'Destination Safe' which contains a range of resources, tools and information employees can access to assist in keeping workplaces safe covering incident and emergency response and hazard and risk management.

Lag indicators of health and safety risks during the reporting period are set out below:

Lost time injury* frequency rate (number of lost time injuries per 1,000,000 hours worked): 5.0 (2017: 5.3)

* A lost time injury is an injury resulting in time lost greater than 1 shift

More information on Health, Safety and Wellbeing in the Group can be found in the Company's Sustainability Report available at www.kathmanduholdings.com/investor-relations/governance/

### Continuous disclosure policy

The Company is committed to observing its disclosure obligations under the Listing Rules. The Company has a policy that establishes procedures that are aimed at ensuring that Directors and Executives are aware of and fulfil their obligations in relation to the timely disclosure of material price-sensitive information.

### Remuneration policy

Kathmandu maintains a remuneration policy in relation to its Directors, executives and employees which provides for remuneration at fair and reasonable levels throughout the Kathmandu Group. Further information on Director remuneration, including the arrangements in place for remuneration of the Group's CEO, is set out in the "Director's Report" section of this Annual Report.

### Securities trading policy

The Company has guidelines for dealing in securities, which are intended to explain the prohibited type of conduct in relation to dealings in securities under the Corporations Act 2001 (Australia) and the Financial Markets Conduct Act 2013 (NZ) and to establish a best practice procedure in relation to Directors', Executives' and employees' dealings in Shares in the Company. Subject to the overriding restriction that persons may not deal in Shares while they are in possession of material price sensitive information, Directors, Executives and Key management personnel will only be permitted to deal in Shares during certain 'window periods', following the release of the Company's full and half year financial results or the release of a disclosure document offering shares in the Company. Outside of these periods, Directors, Executives and key management personnel must receive clearance in accordance with the protocols detailed in the policy for any proposed dealing in Shares.

### Code of Conduct

The Board recognises the need to observe the highest standards of ethical corporate practice and business conduct. Accordingly, the Board has a formal code of conduct, to be followed by all employees and officers. All employees receive induction training on the Code of Conduct on joining the Kathmandu Group and training is provided regularly. The key aspects of this code are to:

- act with honesty, integrity and fairness and in the best interest of the Company;
- act in accordance with all applicable laws, regulations, policies and procedures; and
- use Company resources and property properly.

## Diversity Policy

Kathmandu recognises the value of a diverse and skilled workforce and is committed to creating and maintaining an inclusive and collaborative workplace culture that will provide sustainability for our business into the future. Different perspectives arising from diversity encourage an innovative, responsive, productive and competitive business and create value for our customers and shareholders.

We are committed to leveraging the diverse backgrounds, experiences and perspectives of our people to provide excellent customer service and innovative products to an equally diverse community.

Kathmandu's commitment to recognising the importance of diversity extends to all areas of the business including talent acquisition, learning and development, succession planning, internal transfer & promotion, retention of employees, and company policy and procedures.

Kathmandu has established a Diversity Policy in accordance with ASX CGC Corporate Governance Principles and Recommendation 1.5, NZX Corporate Governance Code Recommendation 2.5, the NZX Listing rules relating to diversity and the NZX Diversity Policies and Disclosure Guidance note. This policy encompasses Kathmandu's Diversity Principles, which affirm the Company's commitment to harnessing differences to encourage an innovative, responsive and productive workplace, creating value and rewards for customers, the team, shareholders and the community.

As part of its Diversity Policy, Kathmandu has established measurable objectives for achieving diversity, including across the Gender, Generation and Culture profiles of the Company. Kathmandu has carried out an annual assessment of its diversity objectives for FY18. The Company considers that it has continued to make good progress towards achieving these objectives. In relation to gender diversity, Kathmandu considers its current level of employee gender diversity to be efficacious; however, it remains vigilant in the review of this measureable diversity objective. The benefits of diversity will continue to be tested and re-affirmed with reference to Kathmandu team composition.

As at 31 July 2018, in relation to Kathmandu's:

- Board of Directors, one out of six Directors is a women (this is one less than FY17)
- Executive Management, one out of nine positions were held by women (for FY17 this was one out of eight positions).

Kathmandu will continue to support strategies and initiatives that address any significant adverse changes in diversity ratios through employee turnover. Kathmandu is also proud of its ethnic diversity, which reflects the diversity of its customers; business partners and community.

Kathmandu is committed to rewarding its employees with compensation and benefit programmes that are based on performance merit and experience. In 2018, an audit on employee pay parity was completed. Based upon the results of this audit, Kathmandu has evidence that supports pay equality between gender and other diversity indicators, with no evidence of pay disparity between persons holding the same or similar roles. A review of gender pay parity is conducted annually.

## Communications with Shareholders

The Company is committed to keeping Shareholders informed of all major developments affecting the Company's state of affairs relevant to Shareholders in accordance with all applicable laws. Information is communicated to Shareholders through the lodgement of all relevant financial and other information with ASX and NZX and publishing information on the Company's website (kathmanduholdings.com). In particular, the Company's website contains information about the Company, including media releases, key policies and the terms of reference of the Company's Board Committees.

All relevant announcements made to the market and any other relevant information will be posted on the Company's website as soon as they have been released to ASX and NZX. Shareholders can communicate with the Company through the investor website at www.kathmanduholdings.com/contact/, and have the option of receiving their communications from the Company electronically. Where voting by shareholders on a matter concerning the Company is required, the Board encourages investors to attend the shareholders meeting or to send in a proxy vote. The Company conducts voting at its annual shareholder meetings by way of poll on the basis of one share, one vote. The Company's notice of meeting will be available at least 28 days prior to the meeting at www.kathmanduholdings.com/investor-relations/nzx-announcements/

## Economic, Environmental and Social Sustainability

The Company prepares a separate sustainability report in accordance with the Global Reporting Initiative (GRI) Standards framework. It is available online at www.kathmanduholdings.com/investor-relations/reports/

# Financial Statements

**For the Year Ended 31 July 2018**

## In this Section

The financial statements have been presented in a style which attempts to make them less complex and more relevant to shareholders. We have grouped the note disclosures into six sections: 'Basis of Preparation', 'Results for the Year', 'Operating Assets and Liabilities', 'Capital Structure and Financing Costs', 'Group Structure' and 'Other Notes'. Each section sets out the accounting policies applied in producing the relevant notes. The purpose of this format is to provide readers with a clearer understanding of what drives financial performance of the Group. The aim of the text boxes is to provide commentary on each section, or note, in plain English.

## Keeping It Simple

Notes to the financial statements provide information required by accounting standards or Listing Rules to explain a particular feature of the financial statements. The notes which follow will also provide explanations and additional disclosure to assist readers' understanding and interpretation of the annual report and the financial statements.

## Table of Contents

# Directors' Approval of Consolidated Financial Statements

**For the Year Ended 31 July 2018**

**Authorisation for Issue**

The Board of Directors authorised the issue of these Consolidated Financial Statements on 18 September 2018.

**Approval by Directors**

The Directors are pleased to present the Consolidated Financial Statements of Kathmandu Holdings Limited for the year ended 31 July 2018 on pages 31 to 69.

| | |
|---|---|
| David Kirk | 18 September 2018<br>Date |
| Xavier Simonet | 18 September 2018<br>Date |

For and on behalf of the Board of Directors

# Consolidated Statement of Comprehensive Income

**For the Year Ended 31 July 2018**

| | Section | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|---|
| Sales | | 497,437 | 445,348 |
| Cost of sales | | (181,961) | (169,165) |
| Gross profit | | 315,476 | 276,183 |
| Selling expenses | | (155,677) | (143,740) |
| Administration and general expenses | | (70,038) | (61,613) |
| | | (225,715) | (205,353) |
| **Earnings before interest, tax, depreciation and amortisation** | | **89,761** | **70,830** |
| Depreciation and amortisation | 3.2/3.3 | (15,151) | (13,826) |
| **Earnings before interest and tax** | | **74,610** | **57,004** |
| Finance income | | 47 | 28 |
| Finance expenses | | (1,106) | (2,058) |
| Finance costs - net | 4.1.1 | (1,059) | (2,030) |
| **Profit before income tax** | | **73,551** | **54,974** |
| Income tax expense | 2.3 | (23,019) | (16,935) |
| **Profit after income tax** | | **50,532** | **38,039** |
| **Other comprehensive income that may be recycled through profit or loss:** | | | |
| Movement in cash flow hedge reserve | 4.3.2 | 8,820 | 209 |
| Movement in foreign currency translation reserve | 4.3.2 | 10,518 | 209 |
| **Other comprehensive income for the year, net of tax** | | **19,338** | **418** |
| **Total comprehensive income for the year attributable to shareholders** | | **69,870** | **38,457** |
| **Basic earnings per share** | 2.4 | 23.9cps | 18.7cps |
| **Diluted earnings per share** | 2.4 | 23.7cps | 18.5cps |
| **Weighted average basic ordinary shares outstanding ('000)** | 2.4 | 211,261 | 203,587 |
| **Weighted average diluted ordinary shares outstanding ('000)** | 2.4 | 213,187 | 205,409 |

# Consolidated Statement of Changes in Equity

**For the Year Ended 31 July 2018**

| | Share Capital NZ$'000 | Cash Flow Hedge Reserve NZ$'000 | Foreign Currency Translation Reserve NZ$'000 | Share Based Payments Reserve NZ$'000 | Retained Earnings NZ$'000 | Total Equity NZ$'000 |
|---|---|---|---|---|---|---|
| **Balance as at 31 July 2016** | **200,191** | **(5,531)** | **(19,702)** | **692** | **136,033** | **311,683** |
| Profit after tax | - | - | - | - | 38,039 | 38,039 |
| Other comprehensive income | - | 209 | 209 | - | - | 418 |
| Dividends paid | - | - | - | - | (24,179) | (24,179) |
| Issue of share capital | 18 | - | - | (18) | - | - |
| Share based payment expense | - | - | - | 1,139 | - | 1,139 |
| **Balance as at 31 July 2017** | **200,209** | **(5,322)** | **(19,493)** | **1,813** | **149,893** | **327,100** |
| Profit after tax | - | - | - | - | 50,532 | 50,532 |
| Other comprehensive income | - | 8,820 | 10,518 | - | - | 19,338 |
| Dividends paid | - | - | - | - | (27,208) | (27,208) |
| Issue of share capital | 49,673 | - | - | (971) | - | 48,702 |
| Share based payment expense | - | - | - | 1,489 | - | 1,489 |
| Deferred tax on share-based payments transactions | - | - | - | 429 | - | 429 |
| **Balance as at 31 July 2018** | **249,882** | **3,498** | **(8,975)** | **2,760** | **173,217** | **420,382** |

# Consolidated Balance Sheet

**As at 31 July 2018**

| | Section | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 3.1.2 | 8,146 | 3,537 |
| Trade and other receivables | 3.1.3 | 13,453 | 6,284 |
| Inventories | 3.1.1 | 111,929 | 89,206 |
| Derivative financial instruments | 4.2 | 5,076 | - |
| Other financial assets | 3.1.4 | 22,180 | - |
| **Total current assets** | | **160,784** | **99,027** |
| **Non-current assets** | | | |
| Property, plant and equipment | 3.2 | 63,514 | 61,026 |
| Intangible assets | 3.3 | 390,319 | 279,014 |
| **Total non-current assets** | | **453,833** | **340,040** |
| **Total assets** | | **614,617** | **439,067** |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 3.1.5 | 72,770 | 56,735 |
| Derivative financial instruments | 4.2 | 156 | 7,034 |
| Current tax liabilities | | 9,968 | 3,475 |
| Other financial liabilities | 3.1.6 | 21,994 | - |
| **Total current liabilities** | | **104,888** | **67,244** |
| **Non-current liabilities** | | | |
| Derivative financial instruments | 4.2 | 62 | 265 |
| Interest bearing liabilities | 4.1 | 39,500 | 10,431 |
| Deferred tax | 2.3 | 49,785 | 34,027 |
| **Total non-current liabilities** | | **89,347** | **44,723** |
| **Total liabilities** | | **194,235** | **111,967** |
| **Net assets** | | **420,382** | **327,100** |
| **EQUITY** | | | |
| Contributed equity - ordinary shares | 4.3.1 | 249,882 | 200,209 |
| Reserves | 4.3.2 | (2,717) | (23,002) |
| Retained earnings | | 173,217 | 149,893 |
| **Total equity** | | **420,382** | **327,100** |

# Consolidated Statement of Cash Flows

**For the Year Ended 31 July 2018**

| | Section | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| **Cash was provided from:** | | | |
| Receipts from customers | | 502,703 | 444,100 |
| Income tax received | | 156 | - |
| Interest received | | 47 | 28 |
| | | 502,906 | 444,128 |
| **Cash was applied to:** | | | |
| Payments to suppliers and employees | | 406,508 | 360,122 |
| Income tax paid | | 18,710 | 14,571 |
| Interest paid | | 2,087 | 2,162 |
| | | 427,305 | 376,855 |
| **Net cash inflow from operating activities** | | **75,601** | **67,273** |
| **Cash flows from investing activities** | | | |
| **Cash was provided from:** | | | |
| Proceeds from sale of property, plant and equipment | | - | 1 |
| | | - | 1 |
| **Cash was applied to:** | | | |
| Purchase of property, plant and equipment | 3.2 | 14,300 | 11,419 |
| Purchase of intangibles | 3.3 | 2,394 | 1,857 |
| Acquisition of subsidiaries | 5.1 | 82,746 | - |
| Investments in other financial assets | 3.1.4 | 22,180 | - |
| | | 121,620 | 13,276 |
| **Net cash outflow from investing activities** | | **(121,620)** | **(13,275)** |
| **Cash flows from financing activities** | | | |
| **Cash was provided from:** | | | |
| Proceeds of loan advances | | 148,815 | 90,330 |
| Proceeds from share issues | | 48,702 | - |
| | | 197,517 | 90,330 |
| **Cash was applied to:** | | | |
| Dividends paid | | 27,208 | 24,179 |
| Repayment of loan advances | | 119,907 | 123,533 |
| | | 147,115 | 147,712 |
| **Net cash inflow / (outflow) from financing activities** | | **50,402** | **(57,382)** |
| **Net increase / (decrease) in cash held** | | **4,383** | **(3,384)** |
| Opening cash and cash equivalents | | 3,537 | 6,891 |
| Effect of foreign exchange rates | | 226 | 30 |
| **Closing cash and cash equivalents** | **3.1.2** | **8,146** | **3,537** |

## Reconciliation of net profit after taxation with cash inflow from operating activities

| | Section | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|---|
| Profit after taxation | | 50,532 | 38,039 |
| *Movement in working capital:* | | | |
| (Increase) / decrease in trade and other receivables | | 5,272 | (1,249) |
| (Increase) / decrease in inventories | | (13,873) | 6,283 |
| Increase / (decrease) in trade and other payables | | 10,884 | 5,596 |
| Increase / (decrease) in tax liability | | 6,405 | 2,257 |
| | | 8,688 | 12,887 |
| *Add non cash items:* | | | |
| Depreciation | 3.2 | 11,576 | 10,630 |
| Amortisation of intangibles | 3.3 | 3,575 | 3,196 |
| Foreign currency translation of working capital balances | | (431) | (816) |
| Increase / (decrease) in deferred taxation | | (1,944) | 733 |
| Employee share based remuneration | 6.4 | 1,489 | 1,139 |
| Loss on sale of property, plant and equipment | 3.2 | 2,116 | 1,465 |
| | | 16,381 | 16,347 |
| **Cash inflow from operating activities** | | **75,601** | **67,273** |

## Reconciliation of movement in term loans

| | |
|---|---|
| **Balance 31 July 2017** | 10,431 |
| Net cash flow movement | 28,908 |
| Foreign exchange movement | 161 |
| **Balance 31 July 2018** | **39,500** |

Notes to the Financial Statements

# Section 1 Basis of preparation

## In this section

This section sets out the Group's accounting policies that relate to the financial statements as a whole. Where an accounting policy is specific to one note, the policy is described in the note to which it relates.

## 1.1 General information

Kathmandu Holdings Limited (the Company) and its subsidiaries (together the Group) is a designer, marketer, retailer and wholesaler of clothing, footwear and equipment for travel and adventure. It operates in New Zealand, Australia, United Kingdom and the USA.

The Company is a limited liability company incorporated and domiciled in New Zealand. Kathmandu Holdings Limited is a company registered under the Companies Act 1993 and is a FMC reporting entity under Part 7 of the Financial Markets Conduct Act 2013. The address of its registered office is 223 Tuam Street, Central Christchurch, Christchurch.

The Company is listed on the NZX and ASX.

The financial statements of the Group have been prepared in accordance with the requirements of Part 7 of the Financial Markets Conduct Act 2013 and the NZX Listing Rules.

These audited consolidated financial statements have been approved for issue by the Board of Directors on 18 September 2018.

## 1.2 Summary of significant accounting policies

These financial statements have been prepared in accordance with Generally Accepted Accounting Practice. They comply with the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards, as appropriate for profit-oriented entities. The financial statements also comply with International Financial Reporting Standards (IFRS).

The financial statements are presented in New Zealand dollars, which is the Company's functional currency and Group's presentation currency.

### *1.2.1 Basis of preparation*

The principal accounting policies adopted in the preparation of the financial statements are set out below. These policies have been consistently applied to all periods presented, unless otherwise stated.

**Basis of Consolidation**

The financial statements reported are for the consolidated "Group" which is the economic entity comprising Kathmandu Holdings Limited and its subsidiaries.

The Group is designated as a for profit entity for financial reporting purposes.

Subsidiaries are consolidated from the date on which control is obtained to the date on which control is lost.

In preparing the Group financial statements, all material intra-group transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. When necessary, amounts reported by subsidiaries have been adjusted to conform to the Group's accounting policies.

**Historical cost convention**

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of certain assets as identified in specific accounting policies below.

**Critical accounting estimates**

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Estimates and judgements are continually evaluated and are based on historical experience as adjusted for current market conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Further explanation as to estimates and assumptions made by the Group can be found in the following notes to the financial statements:

| Area of Estimation | Section |
|---|---|
| Business Combinations<br>– purchase price allocation | 5.1 |
| Goodwill<br>– assumptions underlying recoverable value | 3.3 |
| Inventory<br>– estimates of obsolescence | 3.1.1 |
| Fair value of derivatives<br>– assumptions underlying fair value | 4.2 |

**Foreign currency translation**

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

Assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

Income and expenses for each statement of comprehensive income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and

All resulting exchange differences are recognised in other comprehensive income.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity.

# Section 2 Results for the Year

## In this section

This section focuses on the results and performance of the Group. On the following pages you will find disclosures explaining the Group's results for the year, segmental information, taxation and earnings per share.

## 2.1 Segment information

An operating segment is a component of an entity that engages in business activities which earns revenue and incurs expenses and where the chief decision maker reviews the operating results on a regular basis and makes decisions on resource allocation. The Group is organised into four operating segments, depicting the four geographical regions the Group operates in. The New Zealand segment has been represented to exclude holding company balances. Other represents holding companies and consolidation eliminations.

The Group operates in four geographical areas: New Zealand, Australia, North America and Rest of World. The North American segment was established during the financial year upon acquisition of Obōz Footwear LLC.

| 31 July 2018 | Australia NZ$'000 | New Zealand NZ$'000 | North America NZ$'000 | Rest of World NZ$'000 | Other NZ$'000 | Total NZ$'000 |
|---|---|---|---|---|---|---|
| Total segment sales | 335,876 | 143,167 | 16,785 | 6,932 | - | 502,760 |
| Inter-segment sales | (2,193) | (190) | (666) | (2,274) | - | (5,323) |
| Sales from external customers | 333,683 | 142,977 | 16,119 | 4,658 | - | 497,437 |
| **EBITDA** | **57,744** | **35,154** | **2,768** | **(685)** | **(5,220)** | **89,761** |
| Depreciation and software amortisation | 8,687 | 6,125 | 309 | 30 | - | 15,151 |
| **EBIT** | **49,057** | **29,029** | **2,459** | **(715)** | **(5,220)** | **74,610** |
| Income tax expense | 14,566 | 8,129 | 707 | (225) | (158) | 23,019 |
| **Total segment assets** | **246,178** | **297,700** | **127,373** | **8,591** | **(65,225)** | **614,617** |
| Total assets includes: | | | | | | |
| Non-current assets | 177,540 | 23,943 | 103,325 | - | 149,025 | 453,833 |
| Additions to non-current assets | 11,298 | 5,352 | 103,314 | - | - | 119,964 |
| **Total segment liabilities** | **82,916** | **59,060** | **27,975** | **21,227** | **3,057** | **194,235** |

| 31 July 2017 | Australia NZ$'000 | New Zealand NZ$'000 | North America NZ$'000 | Rest of World NZ$'000 | Other NZ$'000 | Total NZ$'000 |
|---|---|---|---|---|---|---|
| Total segment sales | 298,013 | 146,779 | - | 3,338 | - | 448,130 |
| Inter-segment sales | (1,581) | (407) | - | (794) | - | (2,782) |
| Sales from external customers | 296,432 | 146,372 | - | 2,544 | - | 445,348 |
| **EBITDA** | **39,317** | **36,001** | **-** | **(713)** | **(3,775)** | **70,830** |
| Depreciation and software amortisation | 7,783 | 6,039 | - | 3 | 1 | 13,826 |
| **EBIT** | **31,534** | **29,962** | **-** | **(716)** | **(3,776)** | **57,004** |
| Income tax expense | 8,792 | 8,595 | - | (225) | (227) | 16,935 |
| **Total segment assets** | **233,082** | **235,834** | **-** | **849** | **(30,698)** | **439,067** |
| Total assets includes: | | | | | | |
| Non-current assets | 171,273 | 25,529 | - | 1 | 143,237 | 340,040 |
| Additions to non-current assets | 9,662 | 3,614 | - | - | - | 13,276 |
| **Total segment liabilities** | **150,209** | **22,097** | **-** | **12,356** | **(72,695)** | **111,967** |

EBITDA represents earnings before income taxes (a non-GAAP measure), excluding interest income, interest expense, depreciation and amortisation, as reported in the financial statements. EBIT represents EBITDA less depreciation and amortisation. EBITDA and EBIT are key measurement criteria on which operating segments are reviewed by the Chief Operating Decision Maker (the Executive Management Team).

The Group operates in one industry being outdoor clothing, footwear and equipment.

Revenue is allocated based on the country in which the customer is located. The Group has no reliance on any single major customer.

Costs recharged between Group companies are calculated on normal commercial terms. The default basis of allocation is % of revenue with other bases being used where appropriate.

Assets / liabilities are allocated based on where the assets / liabilities are located.

## 2.2 Profit before tax

### Accounting policies

#### *Revenue recognition*

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services, excluding Goods and Services Tax, rebates and discounts and after eliminating sales within the Group. Revenue is recognised as follows:

***(i) Sale of goods***

Sale of goods are recognised at point of sale for retail customers and when product is dispatched to the customer for online and wholesale sales. Retail sales are usually in cash or by credit card. The recorded revenue is the gross amount of the sale (excluding GST).

### Operating expenses

#### *Employee entitlements*

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Wages, salaries and other short term benefits | 90,024 | 82,935 |
| Employee share based remuneration | 1,489 | 1,139 |

The number of full-time equivalent employees (excluding short-term contractors), as at 31 July was:

| | 2018 | 2017 |
|---|---|---|
| Australia | 762 | 762 |
| New Zealand | 468 | 506 |
| United Kingdom | 5 | 5 |
| United States of America | 21 | - |

***(i) Wages and salaries, annual leave and sick leave***

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for non-accumulating sick leave are recognised when the leave is taken and measured at the rates paid or payable. The liability for employee entitlements is carried at the present value of the estimated future cash flows.

#### *Rental and operating leases*

The Group is a Lessee. Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the statement of comprehensive income on a straight-line basis over the period of the lease.

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Rental and operating lease expenses | 67,429 | 62,205 |

Rent expenses reported in these financial statements relate to non-cancellable operating leases. The future commitments on these leases are as follows:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Due within 1 year | 55,707 | 50,496 |
| Due within 1-2 years | 45,728 | 44,055 |
| Due within 2-5 years | 86,729 | 81,146 |
| Due after 5 years | 35,013 | 45,808 |
| | 223,177 | 221,505 |

Some of the existing lease agreements have right of renewal options for varying terms. The Group leases various properties under non-cancellable lease agreements. These leases are generally between 1 - 10 years.

## 2.3 Taxation

### Keeping it simple

This section lays out the tax accounting policies, the current and deferred tax charges or credits in the year (which together make up the total tax charge or credit in the statement of comprehensive income), a reconciliation of profit before tax to the tax charge and the movements in deferred tax assets and liabilities.

### Accounting policies

*Current and deferred income tax*

The tax expense for the period comprises current and deferred tax. Tax is recognised in the statement of comprehensive income, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company and Company's subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax liability is not recognised if it arises from the initial recognition of goodwill. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

*Goods and Services Tax (GST)*

The statement of comprehensive income and the cash flow statement have been prepared so that all components are stated exclusive of GST. All items in the balance sheet are stated net of GST, with the exception of receivables and payables, which include GST invoiced.

### Taxation – Statement of comprehensive income

The total taxation charge in the income statement is analysed as follows:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Current income tax charge | 24,964 | 16,829 |
| Deferred income tax charge / (credit) | (1,945) | 106 |
| Income tax charge reported in statement of comprehensive income | 23,019 | 16,935 |

In order to understand how, in the statement of comprehensive income, a tax charge of $23,019,193 (2017: $16,934,513) arises on profit before income tax of $73,550,592 (2017: $54,973,991), the taxation charge that would arise at the standard rate of New Zealand corporate tax is reconciled to the actual tax charge as follows:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Profit before income tax | 73,551 | 54,974 |
| Income tax calculated at 28% | 20,594 | 15,393 |
| | | |
| Adjustments to taxation: | | |
| Adjustments due to different rate in different jurisdictions | 1,011 | 578 |
| Non-taxable income | (246) | (16) |
| Expenses not deductible for tax purposes | 725 | 1,064 |
| Tax legislation enacted for employee share schemes | (87) | - |
| Utilisation of tax losses by group companies | (26) | - |
| Tax expense transferred to foreign currency translation reserve | 1,173 | (164) |
| Adjustments in respect of prior years | (125) | 80 |
| Income tax charge reported in statement of comprehensive income | 23,019 | 16,935 |

Adjustments for prior periods primarily arise where an outcome is obtained on certain tax matters which differs from expectations held when the related provision was made. Where the outcome is more favourable than the provision made, the difference is released, lowering the current year tax charge. Where the outcome is less favourable than the provision, an additional charge to the current year tax will occur.

The tax charge / (credit) relating to components of other comprehensive income is as follows:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Movement in cash flow hedge reserve before tax | 12,180 | 837 |
| Tax impact relating to cash flow hedge reserve | (3,360) | (628) |
| Movement in cash flow hedge reserve after tax | 8,820 | 209 |
| | | |
| Foreign currency translation reserve before tax | 10,518 | 209 |
| Tax credit / (charge) relating to foreign currency translation reserve | - | - |
| Movement in foreign currency translation reserve after tax | 10,518 | 209 |
| | | |
| Total other comprehensive income before tax | 22,698 | 1,046 |
| Total tax credit / (charge) on other comprehensive income | (3,360) | (628) |
| Total other comprehensive income after tax | 19,338 | 418 |
| | | |
| Current tax | - | - |
| Deferred tax | (3,360) | (628) |
| Total tax credit / (charge) on other comprehensive income | (3,360) | (628) |

## Unrecognised tax losses

The Group has estimated tax losses to carry forward from Kathmandu (U.K.) Limited of £10,172,139 (NZ$19,561,807) (2017: £11,177,874 (NZ$19,854,128)) which can be carried forward to be offset against future profits generated within the UK. These losses do not expire and no benefit has been recognised in respect to these losses.

### Imputation credits

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Imputation credits available for use in subsequent reporting periods based on a tax rate of 28% | 4,424 | 3,602 |

The above amounts represent the balance of the imputation account as at the end of July 2018, adjusted for:

- Imputation credits that will arise from the payment of the amount of the provision for income tax;
- Imputation debits that will arise from the payment of dividends recognised as a liability at the reporting date; and
- Imputation credits that will arise from the receipt of dividends recognised as receivables at the reporting date.

The balance of Australian franking credits able to be used by the Group in subsequent periods as at 31 July 2018 is A$3,891,706 (2017: A$4,501,155).

### Taxation – Balance sheet

The following are the major deferred taxation liabilities and assets recognised by the Group and movements thereon during the current and prior year:

| | Tax depreciation NZ$'000 | Employee obligations NZ$'000 | Brand NZ$'000 | Foreign exchange NZ$'000 | Other temporary differences NZ$'000 | Reserves NZ$'000 | Total NZ$'000 |
|---|---|---|---|---|---|---|---|
| **As at 31 July 2016** | (161) | 1,370 | (43,518) | 749 | 5,928 | 2,385 | (33,247) |
| Recognised in the statement of comprehensive income | 209 | 349 | - | (931) | 267 | - | (106) |
| Recognised in other comprehensive income | - | - | - | - | - | (628) | (628) |
| Exchange differences | - | 3 | (62) | (3) | 16 | - | (46) |
| **As at 31 July 2017** | 48 | 1,722 | (43,580) | (185) | 6,211 | 1,757 | (34,027) |
| Recognised in the statement of comprehensive income | 157 | 942 | 71 | (212) | 987 | - | 1,945 |
| Recognised in other comprehensive income | - | - | - | - | - | (3,360) | (3,360) |
| Recognised directly in equity | - | 429 | - | - | - | - | 429 |
| Exchange differences | - | 30 | (1,612) | (5) | 169 | - | (1,418) |
| Deferred tax on business combinations (5.1) | - | - | (13,354) | - | - | - | (13,354) |
| **As at 31 July 2018** | 205 | 3,123 | (58,475) | (402) | 7,367 | (1,603) | (49,785) |

The deferred tax balance relates to:

- Property, plant and equipment temporary differences arising on differences in accounting and tax depreciation rates
- Employee benefit accruals
- Kathmandu brand and Obōz brand and customer relationship
- Unrealised foreign exchange gain/loss on intercompany loan (Kathmandu Pty Ltd)
- Realised gain/loss on foreign exchange contracts not yet charged in the statement of comprehensive income
- Inventory provisioning
- Temporary differences arising from landlord contributions and rent free periods
- Temporary differences on the unrealised gain/loss in hedge reserve
- Employee share schemes
- Other temporary differences on miscellaneous items.

## 2.4 Earnings per share

### Keeping it simple

Earnings per share ('EPS') is the amount of post-tax profit attributable to each share.

Basic EPS is calculated by dividing the profit after tax attributable to equity holders of the Company of $50,531,599 (2017: $38,039,478) by the weighted average number of ordinary shares in issue during the year of 211,260,697 (2017: 203,587,322).

Diluted EPS reflects any commitments the Group has to issue shares in the future that would decrease EPS. In 2018, these are in the form of share options / performance rights. To calculate the impact it is assumed that all share options are exercised / performance rights taken, and therefore, adjusting the weighted average number of shares.

| | 2018 '000 | Restated 2017 '000 |
|---|---|---|
| Weighted average number of shares in issue | 211,261 | 203,587 |
| Adjustment for: | | |
| - Share options / performance rights | 1,926 | 1,822 |
| | 213,187 | 205,409 |

The Group has restated the prior year basic and diluted EPS to reflect the impact of the implied bonus element on shares issued from the institutional share placement on 26 March 2018 and share purchase plan on 20 April 2018 (Note 4.3.1). Shares were issued at an issue price of NZ$2.16, representing a 10% discount to the closing price on the NZX of NZ$2.40 on 19 March 2018.

# Section 3 Operating Assets and Liabilities

## In this section

This section shows the assets used to generate the Group's trading performance and the liabilities incurred as a result. Liabilities relating to the Group's financing activities are addressed in Section 4. Deferred tax assets and liabilities are shown in note 2.3.

## Keeping it simple

Working capital represents the assets and liabilities the Group generates through its trading activity. The Group therefore defines working capital as inventory, cash, trade and other receivables, other financial assets, trade and other payables and other financial liabilities.

## 3.1 Working capital

### *3.1.1 Inventory*

#### Accounting policies

Inventories are stated at the lower of cost and net realisable value. Cost is determined on a weighted average cost method and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses. Inventory is considered in transit when the risk and rewards of ownership have transferred to the Group.

The Group assesses the likely residual value of inventory. Stock provisions are recognised for inventory which is expected to sell for less than cost and also for the value of inventory likely to have been lost to the business through shrinkage between the date of the last applicable stocktake and balance sheet date. In recognising the provision for inventory, judgement has been applied by considering a range of factors including historical results, stock shrinkage trends and product lifecycle.

Inventory is broken down into trading stock and goods in transit below:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Trading stock | 89,802 | 76,678 |
| Goods in transit | 22,127 | 12,528 |
| | 111,929 | 89,206 |

Inventory has been reviewed for obsolescence and a provision of $627,362 (2017: $337,970) has been made.

### *3.1.2 Cash and cash equivalents*

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Cash on hand | 178 | 172 |
| Cash at bank | 7,951 | 3,352 |
| Short term deposits | 17 | 13 |
| | 8,146 | 3,537 |

The carrying amount of the Group's cash and cash equivalents are denominated in the following currencies:

| | | |
|---|---|---|
| NZD | 298 | 996 |
| AUD | 1,931 | 2,096 |
| GBP | 789 | 205 |
| USD | 4,905 | 163 |
| EUR | 223 | 77 |
| | 8,146 | 3,537 |

### *3.1.3 Trade and other receivables*

#### Accounting policies

Trade receivables are recognised initially at the value of the invoice sent to the customer and subsequently at the amounts considered recoverable (amortised cost). The collectability of trade receivables is reviewed on an on-going basis. Debts, which are known to be uncollectible, are written off. A provision for doubtful receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The provision currently held is $212,610 (2017: nil).

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Trade receivables | 8,251 | 240 |
| Other receivables and prepayments | 5,202 | 6,044 |
| | 13,453 | 6,284 |

Other receivables and prepayments includes balances in relation to landlord incentives.

The carrying amount of the Group's trade and other receivables are denominated in the following currencies:

| | | |
|---|---|---|
| NZD | 1,959 | 3,176 |
| AUD | 2,918 | 2,933 |
| USD | 8,488 | - |
| GBP | 88 | 175 |
| | 13,453 | 6,284 |

### 3.1.4 Other financial assets

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Other financial assets | 22,180 | - |

Other financial assets relates to the USD$15,000,000 term deposit and associated earned interest held in escrow in relation to the Obōz acquisition (Note 5.1).

### 3.1.5 Trade and other payables due within one year

#### Accounting policies

Trade payables are recognised at the value of the invoice received from a supplier. The carrying value of trade payables is considered to approximate fair value as amounts are unsecured and are usually paid by the 30th of the month following recognition.

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Trade payables | 24,001 | 14,402 |
| Employee entitlements | 13,957 | 10,315 |
| Sundry creditors and accruals | 33,659 | 31,401 |
| Provisions | 1,153 | 617 |
| | 72,770 | 56,735 |

The carrying amount of the Group's trade and other payables are denominated in the following currencies:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| NZD | 12,648 | 11,129 |
| AUD | 45,419 | 38,968 |
| GBP | 925 | 624 |
| EUR | 32 | 5 |
| USD | 13,746 | 6,009 |
| | 72,770 | 56,735 |

Provisions primarily relate to the restoration of leased properties. These provisions are expected to be fully utilised within the next 12 months.

### 3.1.6 Other financial liabilities

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Other financial liabilities | 21,994 | - |

Other financial liabilities relates to the fair value of the USD$15,000,000 contingent earn out in relation to the Obōz acquisition (Note 5.1).

### 3.1.7 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.

| Risk | Exposure arising from | Monitoring | Management |
|---|---|---|---|
| Credit risk | Cash and cash equivalents<br>Trade and other receivables<br>Other financial assets | Credit ratings, aging analysis and review of exposure within regular terms of trade | Credit is given to customers following obtaining credit rating information, confirming references and setting appropriate credit limits |

Concentration of credit risk is within the geographic segment of North America, where the 5 largest customers represent 54% of trade receivables.

### Exposure to credit risk

The below balances are recorded at their carrying amount after any provision for loss on these financial instruments. The maximum exposure to credit risk at reporting date was (carrying amount):

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Cash and cash equivalents | 8,146 | 3,537 |
| Trade receivables | 8,251 | 240 |
| Sundry debtors | 2,255 | 3,098 |
| Other financial assets | 22,180 | - |
| | 40,832 | 6,875 |

As at balance sheet date the carrying amount is also considered to approximate fair value for each of the financial instruments. There are no impaired balances.

The credit quality of cash and cash equivalents can be assessed by reference to external credit ratings (if available) or to historical information about counterparty default rates:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Cash and cash equivalents: | | |
| Standard & Poors - AA- | 2,580 | 3,272 |
| Standard & Poors - A+ | 4,571 | - |
| Standard & Poors - BBB+ | 995 | 265 |
| Total cash and cash equivalents | 8,146 | 3,537 |

### Past due but not impaired

As at balance sheet date, trade receivables of $1,411,000 were past due but not impaired. These relate to wholesale customers following the acquisition of Obōz, and where there is no history of default. The ageing analysis of these trade receivables are as follows:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| 0 to 30 days | 883 | - |
| 30 to 60 days | 297 | - |
| 60 to 90 days | 134 | - |
| 90 days and over | 127 | - |
| | 1,441 | - |

## 3.2 Property, plant and equipment

### Keeping it simple

The following section shows the physical assets used by the Group to operate the business, generating revenues and profits. These assets include store and office fit-out, as well as equipment used in sales and support activities.

Assets are recognised only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably.

## Accounting policies

### *Property, plant and equipment*

All property, plant and equipment are stated at historical cost less depreciation and impairment. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains/losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

The assets' residual value and useful lives are reviewed and adjusted if appropriate at each balance sheet date. Capital work in progress is not depreciated until available for use.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

### *Depreciation*

Depreciation of property, plant and equipment is calculated using straight line and diminishing value methods so as to expense the cost of the assets over their useful lives. The rates are as follows:

| | |
|---|---|
| Leasehold improvements | 5 – 50 % |
| Office, plant and equipment | 8 – 50 % |
| Furniture and fittings | 10 – 50 % |
| Computer equipment | 10 – 60 % |

### *Impairment of assets*

Property, plant and equipment is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use.

Property, plant and equipment can be analysed as follows:

| | Leasehold improvement $'000 | Office, plant & equipment $'000 | Furniture & fittings $'000 | Computer equipment $'000 | Total $'000 |
|---|---|---|---|---|---|
| **Year ended 31 July 2017** | | | | | |
| Opening net book value | 40,113 | 1,775 | 17,496 | 2,225 | 61,609 |
| Additions | 7,139 | 47 | 3,700 | 533 | 11,419 |
| Disposals | (962) | (12) | (486) | (6) | (1,466) |
| Depreciation charge | (6,350) | (278) | (3,347) | (655) | (10,630) |
| Exchange differences | 63 | 1 | 29 | 1 | 94 |
| Closing net book value | 40,003 | 1,533 | 17,392 | 2,098 | 61,026 |
| **As at 31 July 2017** | | | | | |
| Cost | 73,794 | 5,418 | 34,385 | 8,580 | 122,177 |
| Accumulated depreciation | (33,791) | (3,885) | (16,993) | (6,482) | (61,151) |
| Closing net book value | 40,003 | 1,533 | 17,392 | 2,098 | 61,026 |
| **Year ended 31 July 2018** | | | | | |
| Opening net book value | 40,003 | 1,533 | 17,392 | 2,098 | 61,026 |
| Additions | 7,897 | 149 | 5,772 | 482 | 14,300 |
| Acquisition of businesses (Note 5.1) | 132 | 441 | - | 90 | 663 |
| Disposals | (1,370) | (10) | (655) | (3) | (2,038) |
| Depreciation charge | (7,006) | (266) | (3,745) | (559) | (11,576) |
| Exchange differences | 736 | 42 | 337 | 24 | 1,139 |
| Closing net book value | 40,392 | 1,889 | 19,101 | 2,132 | 63,514 |
| **As at 31 July 2018** | | | | | |
| Cost | 78,824 | 6,263 | 39,640 | 9,243 | 133,970 |
| Accumulated depreciation | (38,432) | (4,374) | (20,539) | (7,111) | (70,456) |
| Closing net book value | 40,392 | 1,889 | 19,101 | 2,132 | 63,514 |

### *Depreciation*

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Leasehold improvement | 7,006 | 6,350 |
| Office, plant and equipment | 266 | 278 |
| Furniture and fittings | 3,745 | 3,347 |
| Computer equipment | 559 | 655 |
| Total depreciation | 11,576 | 10,630 |

Depreciation expenditure is excluded from administration and general expenses in the statement of comprehensive income.

### *Sale of property, plant and equipment*

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the statement of comprehensive income.

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Loss/(gain) on sale of property, plant and equipment | 2,116 | 1,465 |

### *Capital commitments*

Capital commitments contracted for at balance sheet date include property, plant and equipment of $2,461,029 (2017: $2,093,450).

## 3.3 Intangible assets

### Keeping it simple

The following section shows the non-physical assets used by the Group to operate the business, generating revenues and profits. These assets include brands, customer relationship, software development and goodwill.

This section explains the accounting policies applied and the specific judgements and estimates made by the Directors in arriving at the net book value of these assets.

### Accounting policies

#### *Goodwill*

Goodwill arises on the acquisition of subsidiaries. Goodwill represents the excess of the cost of the acquisition over the Group's interest in the net fair value of the assets and liabilities of the acquiree. Separately recognised goodwill is tested annually for impairment or more frequently if events or changes in circumstances indicate that it might be impaired. It is carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

#### *Brand*

Acquired brands are carried at original cost based on independent valuation obtained at the date of acquisition. The brand represents the price paid to acquire the rights to use the Kathmandu or Obōz brand. The brand is not amortised. Instead the brand is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired, and is carried at cost less accumulated impairment losses.

### *Customer Relationship*

Acquired customer relationships are carried at original cost based on independent valuation obtained at the date of acquisition less accumulated amortisation. They are amortised on a straight line basis over a useful life of 18 years. The estimated useful life and amortisation period is reviewed at the end of each annual reporting period.

### *Software costs*

Software costs have a finite useful life. Software costs are capitalised and written off over the useful economic life.

Costs associated with developing or maintaining computer software programs are recognised as an expense when incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include the costs of software development employees.

Software is amortised using straight line and diminishing value methods at rates of 20-67%.

### *Impairment*

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Intangible assets that have an indefinite useful life, including goodwill, are not subject to amortisation and are tested annually for impairment irrespective of whether any circumstances identifying a possible impairment have been identified. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use.

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows e.g. cash generating units.

## Intangible assets

| | Goodwill NZ$'000 | Brand NZ$'000 | Customer Relationship NZ$'000 | Software NZ$'000 | Total NZ$'000 |
|---|---|---|---|---|---|
| **Year ended 31 July 2017** | | | | | |
| Opening net book value | 121,474 | 148,457 | - | 10,152 | 280,083 |
| Additions | - | - | - | 1,857 | 1,857 |
| Amortisation | - | - | - | (3,196) | (3,196) |
| Exchange differences | 62 | 207 | - | 1 | 270 |
| Closing net book value | 121,536 | 148,664 | - | 8,814 | 279,014 |
| **As at 31 July 2017** | | | | | |
| Cost | 122,807 | 148,664 | - | 26,573 | 298,044 |
| Accumulated amortisation/impairment | (1,271) | - | - | (17,759) | (19,030) |
| Closing net book value | 121,536 | 148,664 | - | 8,814 | 279,014 |
| **Year ended 31 July 2018** | | | | | |
| Opening net book value | 121,536 | 148,664 | - | 8,814 | 279,014 |
| Additions | - | - | - | 2,394 | 2,394 |
| Acquisition of businesses (Note 5.1) | 54,849 | 34,541 | 13,125 | 92 | 102,607 |
| Disposals | - | - | - | (78) | (78) |
| Amortisation | - | - | (253) | (3,322) | (3,575) |
| Exchange differences | 4,352 | 4,723 | 859 | 23 | 9,957 |
| Closing net book value | 180,737 | 187,928 | 13,731 | 7,923 | 390,319 |
| **As at 31 July 2018** | | | | | |
| Cost | 182,008 | 187,928 | 13,984 | 29,109 | 413,029 |
| Accumulated amortisation/impairment | (1,271) | - | (253) | (21,186) | (22,710) |
| Closing net book value | 180,737 | 187,928 | 13,731 | 7,923 | 390,319 |

### Impairment tests for Kathmandu goodwill and brand

The aggregate carrying amounts of Kathmandu goodwill and brand allocated to each unit for impairment testing are as follows:

| GROUP | GOODWILL | | BRAND | |
|---|---|---|---|---|
| | 2018 NZ$'000 | 2017 NZ$'000 | 2018 NZ$'000 | 2017 NZ$'000 |
| New Zealand | 45,484 | 45,484 | 51,000 | 51,000 |
| Australia | 76,785 | 76,052 | 100,108 | 97,664 |
| | 122,269 | 121,536 | 151,108 | 148,664 |

For the purposes of Kathmandu goodwill and brand impairment testing, the Group operates as two groups of cash generating units, New Zealand and Australia. The recoverable amount of the cash generating units has been determined based on value in use.

The discounted cash flow valuations were calculated using projected five-year future cash flows based on Board approved business plans. Business plans are modelled assuming like for like sales growth based on historical performance taking into account changing market conditions and the continuation of the store rollout programme. The key assumptions used for the value in use calculation are as follows:

| | 2018 | 2017 |
|---|---|---|
| Terminal growth rate | 1.0% | 1.0% |
| New Zealand CGU pre-tax discount rate | 12.4% | 12.5% |
| Australia CGU pre-tax discount rate | 12.2% | 12.1% |

The terminal growth rate assumption is based on a conservative estimate considering the current inflationary environment. Pre-tax discount rates are calculated based on a market participants expected capital structure and cost of debt to derive a weighted average cost of capital.

The calculations confirmed that there was no impairment of Kathmandu goodwill and brand during the year (2017: nil). The Board believes that any reasonably possible change in the key assumptions used in the calculations would not cause the carrying amount to exceed its recoverable amount.

The expected continued promotion and marketing of the Kathmandu brand support the assumption that the brand has an indefinite life.

### Obōz goodwill and brand

The purchase price allocation of goodwill of $58,468,000 and brand of $36,820,000 relating to the acquisition of Obōz is provisional at balance sheet date. There have been no indicators of impairment identified following acquisition therefore no impairment test has been performed. Refer to 5.1 for disclosures in relation to the purchase price allocation.

The expected continued promotion and marketing of the Obōz brand support the assumption that the brand has an indefinite life.

### *Capital commitments*

Capital commitments contracted for at balance sheet date include intangible assets of $748,139 (2017: $850,000).

# Section 4 Capital Structure and Financing Costs

## In this section

This section outlines how the Group manages its capital structure and related financing costs, including its balance sheet liquidity and access to capital markets.

Capital structure is how a company finances its overall operations and growth by using different sources of funds. The Directors determine and monitor the appropriate capital structure of Kathmandu, specifically how much is raised from shareholders (equity) and how much is borrowed from financial institutions (debt) in order to finance the Group's activities both now and in the future.

The Directors consider the Group's capital structure and dividend policy at least twice a year ahead of announcing results and do so in the context of its ability to continue as a going concern, to execute strategy and to deliver its business plan.

## 4.1 Interest bearing liabilities

### Accounting policies

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

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

The table below separates borrowings into current and non-current liabilities:

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Current portion | - | - |
| Non-current portion | 39,500 | 10,431 |
| Total term loans | 39,500 | 10,431 |

The Group has a multi-option facility agreement with Commonwealth Bank of Australia and ASB Bank Limited, with A$60 million repayable in full on 1 August 2019, and a multi-option facility agreement with Bank of New Zealand with $40 million and $30 million repayable in full on 21 March 2020 and 21 March 2021, respectively.

Interest is payable based on the BKBM rate (NZD borrowings), the BBSY rate (AUD borrowings), or the applicable short term rate for interest periods less than 30 days, plus a margin of up to 1.30%. There are no assets pledged as security in relation to the unsecured debt in the 2018 financial year (2017: nil).

The covenants entered into by the Group require specified calculations of Group earnings before interest, tax, depreciation and amortisation (EBITDA) plus lease rental costs to exceed total fixed charges (net interest expense and lease rental costs) at the end of each half during the financial year. Similarly EBITDA must be no less than a specified proportion of total net debt at the end of each six month interim period. The calculations of these covenants are specified in the bank facility agreements of 19 December 2011 and have been complied with at 31 July 2018.

The current interest rates, prior to hedging, on the term loans ranged between 2.60% - 3.17% (2017: 2.24% - 2.52%).

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| The principal of interest bearing liabilities is: | | |
| Payable within 1 year | - | - |
| Payable 1 to 2 years | 39,500 | 10,431 |
| Payable 2 to 3 years | - | - |
| Payable 3 to 4 years | - | - |
| | 39,500 | 10,431 |

### 4.1.1 Finance costs

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Interest income | (47) | (28) |
| Interest expense | 1,389 | 1,887 |
| Other finance costs | 652 | 360 |
| Net exchange loss/(gain) on foreign currency borrowings | (935) | (189) |
| | 1,059 | 2,030 |

Other finance costs relates to facility fees on banking arrangements.

### 4.1.2 Cash flow and fair value interest rate risk

Interest rate risk is the risk that fluctuations in interest rates impact the Group's financial performance.

| Risk | Exposure arising from | Monitoring | Management |
|---|---|---|---|
| Interest rate risk | Interest bearing liabilities at floating rates | Cash flow forecasting<br>Sensitivity analysis | Interest rate swaps |

Refer to section 4.2 for notional principal amounts and valuations of interest rate swaps outstanding at balance sheet date. A sensitivity analysis of interest rate risk on the Group's financial assets and liabilities is provided in the table below.

At the reporting date the interest rate profile of the Group's banking facilities was (carrying amount):

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Total secured loans | 39,500 | 10,431 |
| less Principal covered by interest rate swaps | (37,587) | (37,724) |
| Net Principal subject to floating interest rates[1] | 1,913 | (27,293) |

[1.] Debt levels fluctuate throughout the year and as at 31 July, are at a cyclical low. Forecast debt levels are expected to remain in excess of the interest rate swaps for a significant majority of the year.

Interest rate swaps have the economic effect of converting borrowings from floating to fixed rates. The cash flow hedge (gain)/ loss on interest rate swaps at balance sheet date was $117,340 (2017: $330,041).

### Summarised sensitivity analysis

The following table summarises the sensitivity of the Group's financial assets and financial liabilities to interest rate risk.

A sensitivity of 1% (2017: 1%) has been selected for interest rate risk. The 1% is based on reasonably possible changes over a financial year, using the observed range of historical data for the preceding five year period.

Amounts are shown net of income tax. All variables other than applicable interest rates are held constant. The impact on equity is presented exclusive of the impact on retained earnings.

| | | -1% | | +1% | |
|---|---|---|---|---|---|
| **31 July 2018** | **Carrying amount $'000** | **Profit $'000** | **Equity $'000** | **Profit $'000** | **Equity $'000** |
| Derivative financial instruments (asset) / liability | (4,858) | (376) | 323 | 376 | (312) |
| **Financial assets** | | | | | |
| Cash | 8,146 | (59) | - | 59 | - |
| | | (59) | - | 59 | - |
| **Financial liabilities** | | | | | |
| Borrowings | 39,500 | 395 | - | (395) | - |
| | | 395 | - | (395) | - |
| Total increase / (decrease) | | **(40)** | **323** | **40** | **(312)** |

| | | -1% | | +1% | |
|---|---|---|---|---|---|
| **31 July 2017** | **Carrying amount $'000** | **Profit $'000** | **Equity $'000** | **Profit $'000** | **Equity $'000** |
| Derivative financial instruments (asset) / liability | 7,299 | (377) | 497 | 377 | (479) |
| **Financial assets** | | | | | |
| Cash | 3,537 | (25) | - | 25 | - |
| | | (25) | - | 25 | - |
| **Financial liabilities** | | | | | |
| Borrowings | 10,431 | 104 | - | (104) | - |
| | | 104 | - | (104) | - |
| Total increase / (decrease) | | **(298)** | **497** | **298** | **(479)** |

### *4.1.3 Liquidity Risk*

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due.

| Risk | Exposure arising from | Monitoring | Management |
|---|---|---|---|
| Liquidity risk | Interest bearing and other liabilities | Forecast and actual cash flows | Active working capital management and flexibility in funding arrangements |

The Group has borrowing facilities of NZD $140,729,053 / AUD $129,330,000 (2017: NZD $116,772,823 / AUD $110,000,000 AUD) and operates well within this facility. This includes short term bank overdraft requirements, and at balance sheet date no bank accounts were in overdraft.

## Keeping it simple

The table below analyses the Group's financial liabilities and net-settled derivative financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows, so will not always reconcile with the amounts disclosed on the balance sheet.

| | Less than 1 year NZ$'000 | Between 1 and 2 years NZ$'000 | Between 2 and 5 years NZ$'000 | Over 5 years NZ$'000 |
|---|---|---|---|---|
| *Group 2018* | | | | |
| Trade and other payables | 72,770 | - | - | - |
| Other financial liabilities | 21,994 | - | - | - |
| Borrowings | 1,116 | 40,619 | - | - |
| | 95,880 | 40,619 | - | - |
| *Group 2017* | | | | |
| Trade and other payables | 56,735 | - | - | - |
| Other financial liabilities | - | - | - | - |
| Borrowings | 242 | 10,653 | - | - |
| | 56,977 | 10,653 | - | - |

The Group enters into forward exchange contracts to manage the risks associated with the purchase of foreign currency denominated products.

The table below analyses the Group's derivative financial instruments that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. They are expected to occur and affect the profit or loss at various dates between balance sheet dates and the following five years.

| | Less than 1 year NZ$'000 | Between 1 and 2 years NZ$'000 | Between 2 and 5 years NZ$'000 |
|---|---|---|---|
| *At 31 July 2018* | | | |
| Forward foreign exchange contracts | | | |
| - Inflow | 147,505 | - | - |
| - Outflow | (142,530) | - | - |
| Net Inflow / (Outflow) | 4,975 | - | - |
| Net settled derivatives – interest rate swaps | | | |
| Net Inflow / (Outflow) | (81) | (24) | - |
| *At 31 July 2017* | | | |
| Forward foreign exchange contracts | | | |
| - Inflow | 123,172 | - | - |
| - Outflow | (130,141) | - | - |
| Net Inflow / (Outflow) | (6,969) | - | - |
| Net settled derivatives – interest rate swaps | | | |
| Net Inflow / (Outflow) | (248) | (99) | (24) |

## 4.2 Derivative financial instruments

### Keeping it simple

A derivative is a type of financial instrument typically used to manage risk. A derivative's value changes over time in response to underlying variables such as exchange rates or interest rates and is entered into for a fixed period. A hedge is where a derivative is used to manage an underlying exposure.

The Group is exposed to changes in interest rates on its borrowings and to changes in foreign exchange rates on its foreign currency (largely USD) purchases. The Group uses derivatives to hedge these underlying exposures.

Derivative financial instruments are initially included in the balance sheet at their fair value, either as assets or liabilities, and are subsequently re-measured at fair value at each reporting date.

An interest rate swap is an instrument to exchange a fixed rate of interest for a floating rate, or vice versa, or one type of floating rate for another.

**Accounting policies**

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured to their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as hedges of highly probable forecast transactions (cash flow hedges).

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

***Cash flow hedge***

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity in the hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in the statement of comprehensive income. Amounts accumulated in equity are recycled in the statement of comprehensive income in the periods when the hedged item will affect profit or loss. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory) or a non-financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the measurement of the initial cost or carrying amount of the asset or liability.

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

***Foreign currency translation***

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income, except when deferred in other comprehensive income. Translation differences on monetary financial assets and liabilities are reported as part of the fair value gain or loss.

## Derivative financial instruments

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| **Foreign exchange contracts** | | |
| Current asset | 5,076 | - |
| Current liability | (101) | (6,969) |
| Net foreign change contracts – cash flow hedge (asset / (liability)) | 4,975 | (6,969) |
| | | |
| **Interest rate swaps** | | |
| Non-current asset | - | - |
| Current liability | (55) | (65) |
| Non-current liability | (62) | (265) |
| Net interest rate swaps – cash flow hedge (asset / (liability)) | (117) | (330) |
| **Total derivative financial instruments** | **4,858** | **(7,299)** |

The above table shows the Group's financial derivative holdings at year end.

### *Interest rate swaps - cash flow hedge*

Interest rate swaps are to exchange a floating rate of interest for a fixed rate of interest. The objective of the transaction is to hedge the core floating rate borrowings of the business to minimise the impact of interest rate volatility within acceptable levels of risk thereby limiting the volatility on the Group's financial results. The notional amount of interest rate swaps at balance sheet date was $37,586,507 (2017: $37,723,992). The fixed interest rates range between 2.12% and 3.05% (2017: 2.13% and 3.52%). Refer section 4.1.3 for timing of contractual cash flows relating to interest rate swaps.

### *Foreign exchange contracts - cash flow hedge*

The objective of these contracts is to hedge highly probable anticipated foreign currency purchases against currency fluctuations. These contracts are timed to mature when import purchases are scheduled for payment. The notional amount of foreign exchange contracts amount to US$102,300,000, NZ$144,562,936 (2017: US$92,450,000, NZ$130,140,594).

No material hedge ineffectiveness for interest rate swaps or foreign exchange contracts exists as at balance sheet date (2017: nil).

Refer to section 4.2.1 for a sensitivity analysis of foreign exchange risk associated with derivative financial instruments.

### *4.2.1 Foreign exchange risk*

Foreign exchange risk is the risk that fluctuations in exchange rates will impact the Group's financial performance. The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the AUD, USD and the GBP.

| Risk | Exposure arising from | Monitoring | Management |
|---|---|---|---|
| Foreign exchange risk | Foreign currency purchases – over 90% of purchases are in USD | Forecast purchases<br>Reviewing exchange rate movements | USD foreign exchange derivatives |

The Group is exposed to currency risk on any cash remitted between Australia, the United Kingdom, USA and New Zealand. The Group does not hedge for such remittances. Interest on borrowings is denominated in either New Zealand dollars or Australian dollars, and is paid for out of surplus operating cashflows generated in New Zealand or Australia.

## Summarised sensitivity analysis

The following table summarises the sensitivity of the Group's financial assets and financial liabilities to foreign exchange risk.

A sensitivity of -10% / +10% (2017: -10% / +10%) for foreign exchange risk has been selected. While it is unlikely that an equal movement of the New Zealand dollar would be observed against all currencies, an overall sensitivity of -10% / +10% (2017: -10% / +10%) is reasonable given the exchange rate volatility observed on a historic basis for the preceding five year period and market expectation for potential future movements.

Amounts are shown net of income tax. All variables other than applicable exchange rates are held constant. The impact on equity is presented exclusive of the impact on retained earnings.

| | | -10% | | +10% | |
|---|---|---|---|---|---|
| **31 July 2018** | **Carrying amount $'000** | **Profit $'000** | **Equity $'000** | **Profit $'000** | **Equity $'000** |
| Derivative financial instruments (asset) / liability | (4,858) | - | (16,456) | - | 13,464 |
| **Financial assets** | | | | | |
| Cash | 8,146 | 628 | - | (514) | - |
| Trade receivables and sundry debtors | 10,506 | (802) | - | 656 | - |
| Other financial assets | 22,180 | (1,774) | - | 1,452 | - |
| | | (1,948) | - | 1,594 | - |
| **Financial liabilities** | | | | | |
| Trade payables | 72,770 | (4,810) | - | 3,935 | - |
| Other financial liabilities | 21,994 | (1,760) | - | 1,440 | - |
| Borrowings | 39,500 | - | - | - | - |
| | | (6,570) | - | 5,375 | - |
| **Total increase / (decrease)** | | **(8,518)** | **(16,456)** | **6,969** | **13,464** |

| | | -10% | | +10% | |
|---|---|---|---|---|---|
| | **Carrying amount $'000** | **Profit $'000** | **Equity $'000** | **Profit $'000** | **Equity $'000** |
| Derivative financial instruments (asset) / liability | 7,299 | - | (13,549) | - | 11,086 |
| **Financial assets** | | | | | |
| Cash | 3,537 | 203 | - | (166) | - |
| Trade receivables and sundry debtors | 3,338 | (129) | - | 105 | - |
| Other financial assets | - | - | - | - | - |
| | | 74 | - | (61) | - |
| **Financial liabilities** | | | | | |
| Trade payables | 56,735 | (3,648) | - | 2,985 | - |
| Other financial liabilities | - | - | - | - | - |
| Borrowings | 10,431 | - | (594) | - | 486 |
| | | (3,648) | (594) | 2,985 | 486 |
| **Total increase / (decrease)** | | **(3,574)** | **(14,143)** | **2,924** | **11,572** |

## 4.3 Equity

### Keeping it simple

This section explains material movements recorded in shareholders' equity that are not explained elsewhere in the financial statements. The movements in equity and the balance at 31 July 2018 are presented in the statement of changes in equity.

### Accounting policies

***Share capital***

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

***Dividends***

Dividends are recognised through equity following the approval by the Company's directors.

### *4.3.1 Contributed equity - ordinary shares*

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Ordinary shares fully paid ($) | 249,882 | 200,209 |
| | | |
| Balance at beginning of year | 200,209 | 200,191 |
| Issue of shares under Executive and Senior Management Long Term Incentive Plan | 971 | 18 |
| Shares issued under share placement and share purchase plan | 48,702 | - |
| Balance at end of year | 249,882 | 200,209 |

| Number of issued shares | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Ordinary shares issued at beginning of the year | 201,497 | 201,484 |
| Shares issued under Executive and Senior Management Long Term Incentive Plan | 670 | 13 |
| Shares issued under share placement and share purchase plan | 23,148 | - |
| Ordinary shares issued at end of the year | 225,315 | 201,497 |

As at 31 July 2018 there were 225,314,819 ordinary issued shares in Kathmandu Holdings Limited and these are classified as equity. 669,669 shares (2017: 12,537) were issued under the "Executive and Senior Management Long Term Incentive Plan 24 November 2010" during the year.

During the year 18,518,519 shares were issued in relation to the share placement and 4,629,511 were issued in relation to the share purchase plan. Total capital raised of $48,702,000 is net of directly attributable share issue costs of $1,298,000.

All ordinary shares carry equal rights in respect of voting and the receipt of dividends. Ordinary shares do not have a par value. Refer to section 6.4 for Employee share based remuneration plans.

### *4.3.2 Reserves and retained earnings*

***Cash flow hedging reserve***

The hedging reserve is used to record gains or losses on a hedging instrument in a cash flow hedge that are recognised directly in other comprehensive income, as described in the accounting policy in section 4.2. The amounts are recognised in profit or loss when the associated hedged transaction affects profit or loss.

### Foreign currency translation reserve

The FCTR is used to record foreign currency translation differences arising on the translation of the Group entities results and financial position. The amounts are accumulated in other comprehensive income and recognised in profit or loss when the foreign operation is partially disposed of or sold.

### Share based payments reserve

The share based payments reserve is used to recognise the fair value of share options and performance rights granted but not exercised or lapsed. Amounts are transferred to share capital when vested options are exercised by the employee or performance rights are vested.

| Reserves | | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|---|
| (i) Cash flow hedging reserve | | | |
| Opening balance | | (5,322) | (5,531) |
| Revaluation - gross | | 13,865 | 8,142 |
| Deferred taxation on revaluation | 2.3 | (3,360) | (628) |
| Transfer to hedged asset | | (1,757) | (7,171) |
| Transfer to net profit - gross | | 72 | (134) |
| Closing balance | | 3,498 | (5,322) |
| (ii) Foreign currency translation reserve | | | |
| Opening balance | | (19,493) | (19,702) |
| Currency translation differences – Gross | | 10,518 | 209 |
| Currency translation differences – Taxation | 2.3 | - | - |
| Closing balance | | (8,975) | (19,493) |
| (iii) Share based payments reserve | | | |
| Opening balance | | 1,813 | 692 |
| Current year amortisation | | 1,489 | 1,139 |
| Deferred taxation on share options | 2.3 | 429 | - |
| Transfer to Share Capital on vesting of shares to Employees | | (971) | (18) |
| Closing balance | | 2,760 | 1,813 |
| **Total Reserves** | | **(2,717)** | **(23,002)** |

### 4.3.3 Dividends

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Prior year final dividend paid | 18,195 | 16,119 |
| Current year interim dividend paid | 9,013 | 8,060 |
| Dividends paid ($0.13 per share (2017: $0.12)) | 27,208 | 24,179 |

### 4.3.4 Capital risk management

The Group's capital includes contributed equity, reserves and retained earnings.

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

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

# Section 5 Group Structure

## In this section

This section provides information about the entities that make up the Kathmandu Group and how they affect the financial performance and position of the Group.

## 5.1 Acquisition of Obōz Footwear LLC

On 4 April 2018 Kathmandu Holdings Limited through its wholly-owned subsidiary Kathmandu US Holdings LLC acquired 100% of the equity interests in Obōz Footwear LLC based out of Bozeman, Montana. The total purchase price was USD $60,000,000 plus a proportionate contingent earn out of up to USD $15,000,000.

Obōz designs and sells outdoor footwear through a wholesale model with distribution to leading outdoor retailers primarily in North America. It was acquired as part of Kathmandu's continued international growth strategy due to its wholesale business model, complementary product offering and shared common values.

At the time the financial statements were authorised for issue, the Group had not yet finalised the purchase price allocation for the acquisition of Obōz. Fair values of the assets and liabilities disclosed below, including goodwill, are determined provisionally as management is in process of reviewing the details of independent valuations. In segment information (Note 2.1), management temporarily allocates related assets and liabilities of the acquired business in the "North America" segment. The Group expects to finalise the purchase price allocation in the next few months and will record any allocation adjustments in next financial period.

| **Provisional Purchase Price Allocation** | **NZD$'000** |
|---|---|
| **Purchase price** | 103,164 |
| Less indebtedness settled on acquisition | (8,510) |
| Plus settlement adjustments | 2,176 |
| **Total net consideration** | 96,830 |
| *Recognised amounts of identifiable assets acquired and liabilities assumed;* | |
| **Current assets** | |
| Cash and cash equivalents | 600 |
| Trade and other receivables | 11,682 |
| Inventories | 6,786 |
| **Non-current assets** | |
| Property, plant and equipment | 663 |
| Intangible assets | 92 |
| Customer relationships | 13,125 |
| Brand | 34,541 |
| **Current liabilities** | |
| Trade and other payables | (5,239) |
| **Non-current liabilities** | |
| Interest bearing liabilities | (6,915) |
| Deferred tax | (13,354) |
| **Net assets acquired** | 41,981 |
| Goodwill on acquisition | 54,849 |
| **Total net consideration** | 96,830 |
| Less cash and cash equivalents acquired | (600) |
| Less contingent consideration | (21,994) |
| Plus indebtedness settled on acquisition | 8,510 |
| **Net cash outflow on acquisition** | 82,746 |

Under the sale and purchase agreement, the Group is required to pay a proportionate contingent earn out of up to USD $15,000,000 (NZD $21,994,000) based on an EBITDA target for the year ending 31 December 2018. $21,994,000 represents the estimated fair value of this obligation at the acquisition date and this remains unchanged at balance sheet date.

Acquisition related costs of $1,990,000 have been excluded from the consideration transferred and are included in administration and general expenses in the statement of comprehensive income and in operating cash flows in the statement of cash flows in the current year.

### Goodwill arising on acquisition

Goodwill arose on the acquisition of Obōz because of the established workforce and control premiums paid. This is not recognised separately from goodwill as the expected future economic benefits arising cannot be reliably measured and they do not meet the definition of identifiable intangible assets.

None of the goodwill arising on this acquisition is expected to be deductible for tax purposes.

### Impact of the acquisition on the results of the Group

Obōz contributed $1,922,000 to the group profit for the year. Group revenue for the year includes $16,548,000 in respect of Obōz. Had the Obōz acquisition been effective from 1 August 2017, the unaudited revenue of the Group would have been $529,179,000 and the unaudited profit for the year would have been $54,637,000.

## 5.2 Subsidiary Companies

Subsidiaries are all entities over which the Group has control. Control is achieved when the Group

- has power over the entity;
- is exposed to, or has rights to, variable returns from its involvement with the entity; and
- has the ability to use its power to affect returns.

Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary.

| | | | HOLDING | | |
|---|---|---|---|---|---|
| **Subsidiary Companies:** | **Principal Activity** | **Country of Incorporation** | **2018** | **2017** | **Balance Sheet Date** |
| Milford Group Holdings Limited | Holding company | New Zealand | 100% | 100% | 31 July |
| Kathmandu Limited | Outdoor retailer | New Zealand | 100% | 100% | 31 July |
| Kathmandu Pty Limited | Outdoor retailer | Australia | 100% | 100% | 31 July |
| Kathmandu (U.K.) Limited | Outdoor retailer | United Kingdom | 100% | 100% | 31 July |
| Kathmandu US Holdings LLC | Holding company | USA | 100% | N/A | 31 July |
| Obōz Footwear LLC | Footwear wholesaler | USA | 100% | N/A | 31 December |

Kathmandu US Holdings LLC was incorporated on 20 March 2018.

# Section 6 Other Notes

## 6.1 Related parties

During the year, operating lease costs of $89,263 (2017: $223,258) were paid to Chalmers Properties Limited, a subsidiary of Port Otago Limited. John Harvey retired as a Director of both of these companies on 8 December 2017.

All transactions with related parties were in the normal course of business and provided on commercial terms.

### Key Management Personnel

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Salaries | 3,031 | 2,778 |
| Other short-term employee benefits | 1,195 | 987 |
| Post-employment benefits | 111 | 104 |
| Employee performance rights | 929 | 675 |
| | 5,266 | 4,544 |

Key management personnel include the following employees:

**Executive Directors:**

- Chief Executive Officer

**Senior Managers:**

- Chief Operating and Financial Officer

**Other Key Management Personnel:**

- General Manager, Product
- General Manager, Marketing, Online and International
- General Manager, Supply Chain
- General Manager, Human Resources
- Chief Information Officer
- General Manager, Retail Stores and Operations
- General Manager Merchandising

Remuneration Detail – refer to section 6.3.

## 6.2 Fair values

The following methods and assumptions were used to estimate the fair values for each class of financial instrument:

**Trade debtors, trade creditors and bank balances**
The carrying value of these items is equivalent to their fair value.

**Term liabilities**
The fair value of the Group's term liabilities is estimated based on current market rates available to the Group for debt of similar maturity. The fair value of term liabilities equates to their current carrying value.

**Foreign exchange contracts and interest rate swaps**
The fair value of these instruments is determined by using valuation techniques (as they are not traded in an active market). These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates.

Specific valuation techniques used to value financial instruments include the fair value of interest rate swaps calculated as the present value of the estimated future cash flows based on observable yield curves and the fair value of forward foreign exchange contracts determined using forward exchange rates at the balance sheet date, with the resulting value discounted back to present value.

These derivatives have all been determined to be within level 2 (for the purposes of NZ IFRS 13) of the fair value hierarchy as all significant inputs required to ascertain the fair value of these derivatives are observable.

**Guarantees and overdraft facilities**
The fair value of these instruments is estimated on the basis that management do not expect settlement at face value to arise. The carrying value and fair value of these instruments are approximately nil. All guarantees are payable on demand.

## 6.3 Remuneration Detail

| 2018 | Short-Term Benefits | | | Post-Employment Benefits | Share Based Payments | | | |
|---|---|---|---|---|---|---|---|---|
| Name | Cash Salary and fees $ | Cash bonus $ | Non-Monetary benefits $ | Super-annuation $ | Performance Rights[1] $ | Equity related % | Total $ | Performance related % |
| **Non-Executive Directors** | | | | | | | | |
| David Kirk | 241,302 | - | - | - | - | 0.0% | 241,302 | 0.0% |
| John Harvey | 126,236 | - | - | - | - | 0.0% | 126,236 | 0.0% |
| Sandra McPhee | 126,236 | - | - | - | - | 0.0% | 126,236 | 0.0% |
| Philip Bowman | 105,197 | - | - | - | - | 0.0% | 105,197 | 0.0% |
| Brent Scrimshaw | 105,197 | - | - | - | - | 0.0% | 105,197 | 0.0% |
| John Holland | 21,039 | - | - | - | - | 0.0% | 21,039 | 0.0% |
| Christine Cross | 21,039 | - | - | - | - | 0.0% | 21,039 | 0.0% |
| | **746,246** | **-** | **-** | **-** | **-** | **0.0%** | **746,246** | **0.0%** |
| **Executive Directors** | | | | | | | | |
| Xavier Simonet | 858,480 | 528,091 | - | 21,744 | 398,637 | 22.1% | 1,806,952 | 51.3% |
| | **858,480** | **528,091** | **-** | **21,744** | **398,637** | **22.1%** | **1,806,952** | **51.3%** |
| **Senior Managers and Other Key Management Personnel** | | | | | | | | |
| Reuben Casey | 394,810 | 136,500 | 2,791 | 11,841 | 166,055 | 23.3% | 711,997 | 42.5% |
| Other Management | 1,777,855 | 519,977 | 8,072 | 77,685 | 364,065 | 13.3% | 2,747,654 | 32.2% |
| **Total** | **3,777,391** | **1,184,568** | **10,863** | **111,270** | **928,757** | **15.5%** | **6,012,849** | **35.2%** |

1. This represents the accounting expense of amortising the value of performance rights during the year (refer to note 6.4). 173,271 performance rights were vested and issued to key management personnel during FY2018 of which 59,167 related to Reuben Casey and nil related to Xavier Simonet.

| 2017 | Short-Term Benefits | | | Post-employment benefits | Share based payments | | | |
|---|---|---|---|---|---|---|---|---|
| Name | Cash Salary and fees $ | Cash bonus $ | Non-Monetary benefits $ | Super-annuation $ | Performance Rights[1] $ | Equity related % | Total $ | Performance related % |
| **Non-Executive Directors** | | | | | | | | |
| David Kirk | 236,428 | - | - | - | - | 0.0% | 236,428 | 0.0% |
| John Harvey | 123,687 | - | - | - | - | 0.0% | 123,687 | 0.0% |
| John Holland | 123,687 | - | - | - | - | 0.0% | 123,687 | 0.0% |
| Sandra McPhee | 123,687 | - | - | - | - | 0.0% | 123,687 | 0.0% |
| Christine Cross | 123,687 | - | - | - | - | 0.0% | 123,687 | 0.0% |
| | **731,176** | **-** | **-** | **-** | **-** | **0.0%** | **731,176** | **0.0%** |
| **Executive Directors** | | | | | | | | |
| Xavier Simonet | 821,965 | 446,891 | - | 21,170 | 203,866 | 13.6% | 1,493,892 | 43.6% |
| | 821,965 | 446,891 | - | 21,170 | 203,866 | 13.6% | 1,493,892 | 43.6% |
| **Senior Managers and Other Key Management Personnel** | | | | | | | | |
| Reuben Casey | 366,651 | 116,033 | 3,123 | 11,000 | 121,992 | 19.7% | 618,799 | 38.5% |
| Other Management | 1,589,914 | 411,520 | 9,031 | 71,879 | 349,281 | 14.4% | 2,431,625 | 31.3% |
| **Total** | **3,509,706** | **974,444** | **12,154** | **104,049** | **675,139** | **12.8%** | **5,275,492** | **31.3%** |

1. No performance rights were vested and issued to key management personnel during 2017, this represents the accounting expense of amortising the value of performance rights during the year (refer to note 6.4).

## 6.4 Employee Share Based Remuneration

### Accounting policy

***Equity settled long term incentive plan***
The Executive and Senior Management Long Term Incentive plan grants Group employees performance rights subject to performance hurdles being met. The fair value of rights granted is recognised as an employee expense in the Statement of comprehensive income with a corresponding increase in the employee share based payments reserve. The fair value is measured at grant date and amortised over the vesting periods. The fair value of the rights granted is measured using the Kathmandu Holdings Limited share price as at the grant date less the present value of the dividends forecast to be paid prior to each vesting date. When performance rights vest, the amount in the share based payments reserve relating to those rights are transferred to share capital. When any vested performance rights lapse upon employee termination, the amount in the share based payments reserve relating to those rights is transferred to retained earnings.

**Executive and Senior Management Long Term Incentive Plan**
On 20 November 2013, shareholders approved at the Annual General Meeting the continuation of an Employee Long Term Incentive Plan (LTI) (previously established 24 November 2010) to grant performance rights to Executive Directors, Senior Managers, Other Key Management Personnel and Wider Leadership Management.

***Executive Directors and Senior Managers***
Performance rights granted to Executive Directors and Senior Managers are summarised below:

| Grant Date | Balance at start of year number | Granted during the year number | Vested during the year number | Lapsed during the year number | Balance at the end of year number |
|---|---|---|---|---|---|
| 20 Dec 2017 | - | 374,437 | - | - | 374,437 |
| 19 Dec 2016 | 375,810 | - | - | - | 375,810 |
| 16 Dec 2015 | 407,463 | - | - | - | 407,463 |
| | 783,273 | 374,437 | - | - | 1,157,710 |

The performance rights granted on 20 December 2017 are Long Term Incentive components only.

Long Term Incentive performance rights vest in equal tranches. In each tranche the rights are subject to a combination of a relative Total Shareholder Return (TSR) hurdle and/or an EPS growth hurdle. The relative weighting and number of tranches for each grant date are shown in the table below:

| Grant Date | Tranches | EPS Weighting | TSR Weighting |
|---|---|---|---|
| 20 Dec 2017 | 1 | 50% | 50% |
| 19 Dec 2016 | 1 | 50% | 50% |
| 16 Dec 2015 | 1 | 50% | 50% |

The proportion of rights subject to the relative TSR hurdle is dependent on Kathmandu Holdings Limited's TSR performance relative to a defined comparable group of companies in New Zealand and Australia listed on either the ASX or NZX. The percentage of TSR related rights vest according to the following performance criteria:

| Kathmandu Holdings Limited relative TSR ranking | % Vesting |
|---|---|
| Below the 50th percentile | 0% |
| 50th percentile | 50% |
| 51st – 74th percentile | 50% + 2% for each percentile above the 50th |
| 75th percentile or above | 100% |

The TSR performance is calculated for the following performance periods:

| Tranche | 2018 | 2017 |
|---|---|---|
| Tranche 1 | 36 months to 1 December 2020 | 36 months to 1 December 2019 |

The fair value of the TSR rights have been valued under a Monte Carlo simulation approach predicting Kathmandu Holdings Limited's TSR relative to the comparable group of companies at the respective vesting dates for each tranche. The fair value of TSR rights, along with the assumptions used to simulate the future share prices using a random-walk process are shown below:

| | 2018 | 2017 |
|---|---|---|
| Fair value of TSR rights | $208,920 | $167,054 |
| Current price at grant date | $2.42 | $1.96 |
| Risk free interest rate | 2.06% | 2.40% |
| Expected life (years) | 3 | 3 |
| Expected share volatility | 43.0% | 44.3% |

The estimated fair value for each tranche of rights issued is amortised over the vesting period from the grant date.

The proportion of rights subject to the EPS growth hurdle is dependent on the compound average annual growth in Kathmandu Holdings Limited's EPS relative to the year ending 31 July 2017. The applicable performance periods are:

| Tranche | 2018 Performance Period | 2017 Performance Period |
|---|---|---|
| Tranche 1 | FY20 EPS relative to FY17 EPS | FY19 EPS relative to FY16 EPS |

The percentage of the 2018 EPS growth related rights scales according to the compound average annual EPS growth achieved as follows:

| EPS Growth | 2018 % Rights Vesting | EPS Growth | 2017 % Rights Vesting |
|---|---|---|---|
| < 7% | 0% | < 10% | 0% |
| >=7%, < 8% | 50% | >=10%, < 11% | 50% |
| >=8%, < 9% | 60% | >=11%, < 12% | 60% |
| >=9%, < 10% | 70% | >=12%, < 13% | 70% |
| >=10%, < 11% | 80% | >=13%, < 14% | 80% |
| >=11%, < 12% | 90% | >=14%, < 15% | 90% |
| >=12% | 100% | >=15% | 100% |

The fair value of the EPS rights have been assessed as the Kathmandu Holdings Limited share price as at the grant date less the present value of the dividends forecast to be paid prior to each vesting date. The estimated fair value for each tranche of options issued is amortised over the vesting period from the grant date.

Vesting of Long Term Incentive performance rights also require remaining in employment with the Company during the performance period.

### Other Key Management Personnel and Wider Leadership Management

Performance rights granted to Other Key Management Personnel and Wider Leadership Management, all Short Term Incentives under the shareholder approved Employee Long Term Incentive Plan are summarised below:

| Grant Date | Balance at start of year number | Granted during the year number | Vested during the year number | Lapsed during the year number | Balance at the end of year number |
|---|---|---|---|---|---|
| 11 Dec 2017 | - | 591,932 | - | (22,991) | 568,941 |
| 07 Dec 2016 | 510,322 | - | - | (44,073) | 466,249[1] |
| 18 Dec 2015 | 669,669 | - | (669,669) | - | - |

[1] Remaining performance rights on vesting date 31 July 2018, which were subsequently issued on 10 August 2018.

Short Term Incentive performance rights vest:
- upon the Company achieving non-market performance hurdles; and
- the employee remaining in employment with the Company until the vesting date.

The performance period and vesting dates are summarised below:

| | 2018 | 2017 |
|---|---|---|
| Grant Date | 11 Dec 2017 | 7 Dec 2016 |
| Performance period (year ending) | 31 Jul 2018 | 31 Jul 2017 |
| Vesting Date – Other Key Management Personnel and Wider Leadership Management | 31 Jul 2019 | 31 Jul 2018 |

The fair value of the rights were assessed as the Kathmandu Holdings Limited share price as at the grant date less the present value of the dividends forecast to be paid prior to the vesting date. The fair value of each right has been calculated to be NZ$2.14 per right (2017: NZ$1.71).

The non-market performance hurdles set for the year ending 31 July 2018 were met and accordingly an expense has been recognised in the Statement of Comprehensive Income.

**Expenses arising from equity settled share based payments transactions**

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Executive Director | 399 | 204 |
| Key Management Personnel and Wider Leadership Management | 1,090 | 935 |
| | 1,489 | 1,139 |

## 6.5 Contingent liabilities

There are no contingent liabilities in 2018 (2017: nil).

## 6.6 Contingent assets

There are no contingent assets in 2018 (2017: nil).

## 6.7 Events occurring after the balance sheet date

There are no events after balance sheet date which materially affect the information within the financial statements.

## 6.8 Supplementary Information

### *Directors fees*

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Directors' fees | 746 | 731 |

Directors fees for the Parent company were paid to the following:

- David Kirk (Chairman)
- Sandra McPhee
- John Harvey
- Philip Bowman
- Brent Scrimshaw
- John Holland
- Christine Cross

### *Audit fees*

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

| | 2018 NZ$'000 | 2017 NZ$'000 |
|---|---|---|
| Audit services - PricewaterhouseCoopers | | |
| Statutory audit | 175 | 133 |
| Half year review | 33 | 32 |
| Other assurance services* | 18 | 19 |
| Total remuneration for audit services | 226 | 184 |

* Other assurance services relate the preparation of revenue certificates, and banking compliance certificates and a treasury review in the previous year.

## 6.9 New Accounting Standards

**New standards first applied in the year**

There are no standards or amendments adopted by the Group since 1 August 2017 that have a significant impact on the Group.

**Standards, interpretations and amendments to published standards that are not yet effective**

| New Accounting Standard | Effective Date Applicable to the Group | Summary of Changes | Group Impact |
|---|---|---|---|
| NZ IFRS 9 Financial Instruments | 1 August 2018 | Addresses the classification, measurement and de-recognition of financial assets and financial liabilities and new rules for hedge accounting. | The Group has reviewed its financial assets and liabilities and noted no material impact from the adoption of NZ IFRS 9.<br>The Group currently has financial assets classified as fair value through profit or loss, and loans and receivables. NZ IFRS 9 does not impact the measurement of the Group's financial assets classified as fair value through profit or loss. The financial assets currently classified as loans and receivables will fall into the amortised cost category under NZ IFRS 9.<br>The financial assets classified in the amortised cost category will be subject to the new impairment model which requires the recognition of impairment provisions based on expected credit losses (ECL). Under NZ IAS 39 an incurred credit loss model was applied. Based on the Group's assessment of historical provision rates and forward-looking analysis, there is no material financial impact on the impairment provisions in the year of adoption.<br>The Group currently has financial liabilities classified as fair value through profit or loss and amortised cost. NZ IFRS 9 does not impact the classification or measurement of the Group's financial liabilities.<br>The new hedge accounting rules will align the accounting for hedging instruments more closely with the group's risk management practices. The Group has confirmed that its current hedge relationships would qualify as continuing hedges upon the adoption of NZ IFRS 9. Accordingly, there is no significant impact on the accounting treatment for the Group's hedging relationships. The nature and extent of the Group's disclosure note in relation to its hedging relationships will change in the consolidated financial statements for the period ending 31 July 2019. |

| | | | |
|---|---|---|---|
| NZ IFRS 15 Revenue from Contracts with Customers | 1 August 2018 | Establishes the reporting principles relating to the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. | During the financial year, the Group assessed the potential impact of IFRS 15. Work focused on segregating the different revenue streams that exist within the business. The majority of revenue is made up of in store transactions with less than 14% earned through online and wholesale sales.<br>The following matters are relevant to the Group under NZ IFRS 15:<br>- A customers' right of return in determining revenue to be recognised and how it should be accounted for<br>- For online sales and wholesale sales, whether arranging the delivery of goods is a separate performance obligation as it may impact the timing, measurement and classification of revenue recognised.<br>There is no material impact from the adoption of NZ IFRS 15 in relation to the above matters. |
| NZ IFRS 16 Leases | 1 August 2019 | Introduces a single lessee accounting model requiring a lessee to recognise assets and liabilities for all leases with a term of more than 12 months where they are not considered low value. A right-of-use asset will be recognised representing the right to use the underlying leased asset and a lease liability representing the obligations to make lease payments. As a consequence, a lessee recognises depreciation of the right-of-use asset and interest on the lease liability. | This standard will materially impact the Group's consolidated financial statements at transition and in future years, as the Group's operating leases (primarily in relation to store, distribution centre and office leases) are recognised on balance sheet.<br>During the financial year, the implementation plan for the new leases standard has commenced in a number of areas including;<br>- Identification of leases and contracts that could be determined to include a lease;<br>- Collation of lease data required for the calculation of the impact assessment;<br>- Identification of areas of complexity and judgement to the Group; and<br>- Identification of necessary changes to systems and processes required to enable reporting and accounting in accordance with the new standard.<br>Note 2.2 reflects that as at 31 July 2018 the Group had lease commitments for operating leases of $223 million. A preliminary assessment indicates that lease arrangements will meet the definition of a lease under NZ IFRS 16, and hence the group will recognise a right-of-use asset and a corresponding liability in respect of all these leases unless they qualify for low value short-term leases upon the application of NZ IFRS 16.<br>A reliable estimate of the financial impact on the group is dependent on the finalisation of a number of areas, including;<br>- Choice of transition method;<br>- Selection of discount rates;<br>- Estimates of lease-term for leases with options; and<br>- Assessment of completeness of data.<br>The financial impact is dependent on the composition of the lease portfolio at the time of transition. Therefore it is not yet practical to determine a reliable estimate of the financial impact on the group. |

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# *Independent auditor's report*

To the shareholders of Kathmandu Holdings Limited

The consolidated financial statements comprise:

- the consolidated balance sheet as at 31 July 2018;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

## *Our opinion*

In our opinion, the consolidated financial statements of Kathmandu Holdings Limited (the Company), including its subsidiaries (the Group), present fairly, in all material respects, the financial position of the Group as at 31 July 2018, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

## *Basis for opinion*

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs NZ) and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

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

We are independent of the Group in accordance with Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* (PES 1) issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our firm carries out other services for the Group in the areas of covenant compliance and agreed upon procedures for store turnover certificates. The provision of these other services has not impaired our independence as auditor of the Group.

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## *Our audit approach*

### Overview


An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement.

Overall Group materiality: $3.65 million, which represents approximately 5% of profit before tax.

We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Group is most commonly measured by users, and is a generally accepted benchmark.

We agreed with the Audit and Risk Committee that we would report to them misstatements identified during the audit above $365,000.

We have determined that there are two key audit matters:

- Identification and valuation of intangible assets arising from the acquisition of Oboz Footwear LLC (Oboz)
- Inventory valuation and existence

### Materiality

The scope of our audit was influenced by our application of materiality.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Group materiality for the consolidated financial statements as a whole as set out above. These, together with qualitative considerations, helped us to determine the scope of our audit, the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the consolidated financial statements as a whole.

### Audit scope

We designed our audit by assessing the risks of material misstatement in the consolidated financial statements and our application of materiality. As in all of our audits, we also addressed the risk of management override of internal controls including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industries in which the Group operates.

The accounting function for the Company is maintained in New Zealand, the Oboz accounting function is located in the USA. The Group audit was conducted by a New Zealand based team.

### *Key audit matters*

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current year. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

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| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| *Identification and valuation of intangible assets arising from the acquisition of Oboz Footwear LLC.*<br><br>As disclosed in note 5.1 of the financial statements, the Group acquired 100% of the shares of Oboz Footwear LLC (Oboz), on 4 April 2018, for consideration of \$103.1 million of which \$22.0 million is contingent on an EBITDA target being met for the year ending 31 December 2018.<br><br>The purchase price included identifiable tangible and intangible assets acquired and liabilities assumed.<br><br>Management engaged a third party (management expert) to assist in a process to identify and determine the fair value of these assets and liabilities.<br><br>In addition to Goodwill of \$54.8 million management have provisionally identified intangible assets relating to Brand and Customer Relationships held by Oboz valued at \$34.5 million and \$13.1 million respectively.<br><br>Our audit focused on this area because significant judgement and estimates are involved in identifying and determining the fair value of the intangible assets acquired. | In responding to the significant judgements involved in identifying and valuing the intangible assets acquired we:<br><br>• Reviewed the sale and purchase agreement and other documents related to the acquisition to obtain an understanding of the transaction and to confirm the consideration;<br>• Reviewed the year to date trading of Oboz against the EBITDA earn out target to confirm the recognition and valuation of the deferred consideration is appropriate;<br>• Met with Group and Oboz management to obtain an understanding of the business process undertaken to identify and value the assets acquired and liabilities assumed;<br>• Considered whether identification and recognition of intangible assets was consistent with the requirements of the accounting standards;<br>• We engaged our internal valuation specialist to assess the appropriateness of assets identified and the valuation methodology applied by managements expert; and<br>• Considered whether the relevant disclosures were appropriate in the consolidated financial statements.<br><br>From the procedures performed we have no matters to report. |
| *Inventory valuation and existence*<br><br>At 31 July 2018, the Group held inventories of \$111.9 million. Inventory valuation and existence was an audit focus area because of the number of stores/locations that inventory was held at, and the judgement applied in the valuation of inventory to incorporate inventory shrinkage.<br><br>As described in note 3.1.1 of the financial statements, inventories are carried at the lower of cost and net realisable value on a weighted average basis. | We performed a number of audit procedures over inventory existence and valuation. We<br>• Observed the stocktake process at selected store locations near period end and undertook our own test counts;<br>• Attended the year end Oboz distribution centre count and performed independent test counts;<br>• Validated all stores had been counted twice in the year by selecting a sample of locations not visited by us and inspected results of stock counts held and confirmed variances were correctly accounted for and approved by head office management; |

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| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| The Group has systems and processes including a barcode inventory management system to accurately record inventory movements.<br><br>Management engage an independent third party to complete full stock takes at each store twice a year. This process is managed centrally by head office for consistency. Daily cycle counts are performed at the New Zealand and Australian distribution centres. A full inventory count was performed at the US Oboz distribution centre at year end.<br><br>There are judgements applied in assessing the level of provision for inventory shrinkage. Management provide for shrinkage each month on a location by location basis. The level of provision is based on historical inventory counts and stocktake shrinkage trends. | • Observed the daily stocktake process at the Christchurch and Melbourne distribution centres near period end and undertook our own test counts. We also validated that daily counts occurred by selecting a sample of days for each location and inspected the count records for those days;<br>• Assessed the inventory shrinkage provision by reviewing the level of inventory write downs during the period. We tested the shrinkage rate used to calculate the provision for each store since the last stocktake by comparing it to the actual shrinkage rate in prior periods;<br>• Assessed store inventory counts performed post year end to ensure the actual level of shrinkage was consistent with the year-end provisioning;<br>• Held discussions with management, including merchandising personnel, to understand and corroborate the assumptions applied in estimating inventory provisions;<br>• Evaluated key assumption made by management that current shrinkage levels were consistent with historical levels through an analysis of inventory items by category and age and the level of inventory write-downs in these categories during the period compared to prior periods; and<br>• Tested that inventory on hand at the end of the period was recorded at the lower of cost and net realisable value by testing a sample of inventory items to the most recent retail price.<br><br>From the procedures performed we have no matters to report. |

## *Information other than the financial statements and auditor's report*

The Directors are responsible for the annual report. Our opinion on the consolidated financial statements does not cover the other information included in the annual report and we do not, and will not express any form of assurance conclusion on the other information.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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## *Responsibilities of the Directors for the consolidated financial statements*

The Directors are responsible, on behalf of the Company, for the preparation and fair presentation of the consolidated financial statements in accordance with NZ IFRS and IFRS, and for such internal control as the Directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

## *Auditor's responsibilities for the audit of the consolidated financial statements*

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

A further description of our responsibilities for the audit of the financial statements is located at the External Reporting Board's website at:

https://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-1/

This description forms part of our auditor's report.

## *Who we report to*

This report is made solely to the Company's shareholders, as a body. Our audit work has been undertaken so that we might state those matters which we are required to state to them in an auditor's 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 shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

The engagement partner on the audit resulting in this independent auditor's report is Leopino Foliaki.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants
18 September 2018

Christchurch

# Statutory Information

## Employee Remuneration

The Group operates in New Zealand, Australia, USA and the UK where remuneration market levels differ. The offshore remuneration amounts are converted into New Zealand dollars. Of the employees noted in the table below, 51% are employed by the Group outside New Zealand. During the year a number of employees or former employees, not being Non-Executive Directors of the Group, received remuneration and other benefits that exceeded NZ$100,000 in value as follows:

| Remuneration $ | | $ | Number of Employees |
|---|---|---|---|
| 100,000 | - | 110,000 | 10 |
| 110,000 | - | 120,000 | 12 |
| 120,000 | - | 130,000 | 8 |
| 130,000 | - | 140,000 | 8 |
| 140,000 | - | 150,000 | 10 |
| 150,000 | - | 160,000 | 3 |
| 160,000 | - | 170,000 | 2 |
| 170,000 | - | 180,000 | 6 |
| 190,000 | - | 200,000 | 3 |
| 200,000 | - | 210,000 | 1 |
| 230,000 | - | 240,000 | 3 |
| 240,000 | - | 250,000 | 1 |
| 260,000 | - | 270,000 | 1 |
| 280,000 | - | 290,000 | 1 |
| 290,000 | - | 300,000 | 1 |
| 300,000 | - | 310,000 | 1 |
| 320,000 | - | 330,000 | 1 |
| 350,000 | - | 360,000 | 1 |
| 400,000 | - | 410,000 | 1 |
| 410,000 | - | 420,000 | 1 |
| 450,000 | - | 460,000 | 1 |
| 630,000 | - | 640,000 | 1 |
| 680,000 | - | 690,000 | 1 |
| 1,400,000 | - | 1,410,000 | 1 |

## Distribution of shareholders and holdings

| | Number of Holders | % | Number of Ordinary Shares | % |
|---|---|---|---|---|
| 1 to 999 | 955 | 27% | 471,085 | 0% |
| 1,000 to 4,999 | 1,376 | 39% | 3,682,268 | 2% |
| 5,000 to 9,999 | 530 | 15% | 3,907,692 | 2% |
| 10,000 to 99,999 | 589 | 17% | 14,071,414 | 6% |
| 100,000 and over | 56 | 2% | 203,648,609 | 90% |
| **Total** | **3,506** | **100%** | **225,781,068** | **100%** |

The details set out above were as at 7 September 2018.

The Company has only one class of shares on issue, ordinary shares, and these shares are listed on the NZX and ASX. There are no other classes or equity security currently on issue. The Company's ordinary shares each carry a right to vote on any resolution on a poll at a meeting of shareholders. Holders of ordinary shares may vote at a meeting in person, or by proxy, representative or attorney. Voting may be conducted by voice, by show of hands, or poll. There are no voting rights attached to options.

There were 124 shareholders holding less than a marketable parcel, as defined by ASX Listing Rules, of the Company's ordinary shares, based on the market price as at 7 September 2018.

There are no restricted securities or securities subject to voluntary escrow on issue.

## Limitations on the Acquisition of Securities

The Company is not subject to Chapters 6, 6A, 6B and 6C of the Corporations Act 2001 (Australia) dealing with the acquisition of shares (i.e. substantial holdings and takeovers).

Limitations on the acquisition of the securities imposed by the jurisdiction in which the Company is incorporated (New Zealand) are:

(a) In general, securities in the Company are freely transferable and the only significant restrictions or limitations in relation to the acquisition of securities are those imposed by New Zealand laws relating to takeovers, overseas investment and competition.

(b) The New Zealand Takeovers Code creates a general rule under which the acquisition of 20% or more of the voting rights in the Company or the increase of an existing holding of 20% or more of the voting rights of the Company can only occur in certain permitted ways. These include a full takeover offer in accordance with the Takeovers Code, a partial takeover offer in accordance with the Takeovers Code, an acquisition approved by an ordinary resolution, an allotment approved by an ordinary resolution, a creeping acquisition (in certain circumstances) or compulsory acquisition of a shareholder holds 90% or more of the shares of the Company.

(c) The New Zealand Overseas Investment Act 2005 and Overseas Investment Regulations 2005 (New Zealand) regulate certain investments in New Zealand by overseas persons. In general terms, the consent of the New Zealand Overseas Investment Office is likely to be required where an "overseas person" acquires shares in the Company that amount to 25% or more of the shares issued by the Company, or if the overseas person already holds 25% or more, the acquisition increases that holding.

(d) The New Zealand Commerce Act 1986 is likely to prevent a person from acquiring shares in the Company if the acquisition would have, or would be likely to have, the effect of substantially lessening competition in the market.

## Substantial Security Holders

According to notices given under the Securities Markets Act 1988 (New Zealand), the substantial security holders in ordinary shares (being the only class of listed voting securities) of the Company and their relevant interests according to the substantial security holder file as at 7 September 2018, were as follows:

| | Ordinary Shares | % |
|---|---|---|
| Briscoe Group Limited (21 August 2018) | 42,673,302 | 18.9% |
| TA Universal Investment Holdings and others (15 August 2017) | 24,212,664 | 10.7% |
| First NZ Capital Group Limited | 23,504,333 | 10.4% |
| Novaport Capital (23 July 2018) | 13,518,094 | 6.0% |
| Challenger Limited (23 July 2018) | 13,571,798 | 6.0% |

As at 7 September 2018, the Company had 225,781,068 ordinary shares on issue.

## Principal shareholders

The names and holdings of the twenty largest shareholders as at 7 September 2018 were:

| | Name | Ordinary Shares | % |
|---|---|---|---|
| 1 | NEW ZEALAND CENTRAL SECURITIES DEPOSITORY LIMITED | 75,765,413 | 33.56% |
| 2 | BRISCOE GROUP LIMITED | 42,673,302 | 18.90% |
| 3 | J P MORGAN NOMINEES AUSTRALIA LIMITED | 18,103,743 | 8.02% |
| 4 | HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED | 15,947,586 | 7.06% |
| 5 | BNP PARIBAS NOMINEES PTY LTD | 13,677,224 | 6.06% |
| 6 | CITICORP NOMINEES PTY LIMITED | 12,221,627 | 5.41% |
| 7 | GRAHGER RETAIL SECURITIES PTY LTD | 4,202,860 | 1.86% |
| 8 | NATIONAL NOMINEES LIMITED | 3,269,417 | 1.45% |
| 9 | GRAHGER CAPITAL SECURITIES PTY LTD | 2,000,000 | 0.89% |
| 10 | FORSYTH BARR CUSTODIANS LIMITED | 1,731,876 | 0.77% |
| 11 | NEW ZEALAND DEPOSITORY NOMINEE LIMITED | 1,620,845 | 0.72% |
| 12 | UBS NOMINEES PTY LTD | 1,492,825 | 0.66% |
| 13 | BNP PARIBAS NOMS PTY LTD | 975,559 | 0.43% |
| 14 | GRAHGER RETAIL SECURITIES PTY LTD | 800,000 | 0.35% |
| 15 | GRAHGER CAPITAL SECURITIES MANAGEMENT PTY LTD | 700,000 | 0.31% |
| 16 | BNP PARIBAS NOMINEES PTY LTD | 645,391 | 0.29% |
| 17 | LITTLE BLUE PORSCHE PTY LTD | 500,000 | 0.22% |
| 18 | CITICORP NOMINEES PTY LIMITED | 424,239 | 0.19% |
| 19 | HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED-GSCO ECA | 385,403 | 0.17% |
| 20 | GUANQUAN LU | 380,300 | 0.17% |

## Directors' Shareholdings

Directors held interests in the following shares of the Company at 31 July 2018:

| | | |
|---|---|---|
| David Kirk | beneficially owned | 68,955 |
| Sandra McPhee | beneficially owned | 65,767 |
| John Harvey | beneficially owned | 58,508 |
| Xavier Simonet | beneficially owned | 16,262 |

## Share Dealings by Directors

In accordance with Section 148(2) of the Companies Act 1993, the Board has not received any disclosures from the Directors in relation to acquisitions or disposals of relevant interests in the Company between 1 August 2017 and 31 July 2018.

## Subsidiary Company Directors

Section 211(2) of the Companies Act 1993 requires the Company to disclose, in relation to its subsidiaries, the total remuneration and value of other benefits received by Directors and former Directors, and particulars of entries in the interests registers made during the year ended 31 July 2018.

No subsidiary has Directors who are not full-time employees of the Group.

The remuneration and other benefits of such employees (received as employees) totalling $100,000 or more during the year ended 31 July 2018, are included in the relevant bandings for remuneration disclosed at the beginning of the "Statutory Information" section of this annual report.

No employee of the Group appointed as a Director of Kathmandu Holdings Limited or its subsidiaries receives or retains any remuneration or other benefits in their capacity as a Director.

The persons who held office as Directors of subsidiary companies at 31 July 2018, and those who ceased to hold office during the year ended 31 July 2018, are as follows:

**Milford Group Holdings Limited**
Paul Stern, Reuben Casey, Xavier Simonet

**Kathmandu Limited**
Reuben Casey, Xavier Simonet

**Kathmandu Pty Limited**
Paul Stern, Reuben Casey, Xavier Simonet

**Kathmandu (U.K.) Limited**
Paul Stern, Reuben Casey, Xavier Simonet

**Kathmandu US Holdings LLC**
Xavier Simonet

## Disclosure of Interests by Directors

In accordance with Section 140(2) of the Companies Act 1993, the Directors named below have made a general disclosure of interest, by a general notice disclosed to the Board and entered in the Company's interests register. General notices given by Directors which remain current as at 31 July 2018 are as follows:

**David Kirk**

| | |
|---|---|
| TradeMe Group Limited | Chairman |
| New Zealand Foodshare Trust | Chairman |
| Sydney Grammar School Board of Trustees | Chairman |
| NZ Rugby Players Association | Chairman |
| Forsyth Barr Group Limited | Chairman |
| Bailador Investment Management Pty Limited | Managing Partner |
| Bailador Technology Investments Limited (including investee companies) | Chairman |

**John Harvey**

| | |
|---|---|
| New Zealand Opera Limited | Chairman |
| Stride Property Limited | Director |
| Investore Property Limited | Director |
| Heartland Bank Limited | Director |
| Resource Coordination Partnership Limited | Advisor to the Board |

**Sandra McPhee**

| | |
|---|---|
| JP Morgan Advisory Council | Member |
| St Vincents and Mater Health Sydney Community Advisory Council | Chairman |
| NSW Public Service Commission Advisory Board | Member |
| Australian Public Service Commission | Advisor |

**Philip Bowman**

| | |
|---|---|
| Majid al Futtaim Properties LLC | Chairman |
| Potrero Distilling Holdings LLC | Chairman |
| Ferrovial SA | Director |
| Atropos SCI | Director |
| Better Capital PCC Limited | Director |
| Potrero Distilling Holdings LLC | Director |
| Vinula Pty Ltd | Director |
| Vinula Superfund Pty Ltd | Director |
| Tom Tom Holdings Inc | Director |

**Brent Scrimshaw**

| | |
|---|---|
| Unscriptd Limited | CEO and Co-Founder |
| Rhinomed Limited | Director |
| Catapault Group International Limited | Director |

## Directors' and Officers' Insurance And Indemnity

The Group has arranged, as provided for under the Company's Constitution, policies of Directors' and Officers' Liability Insurance which, with a Deed of Indemnity entered into with all Directors, ensures that generally Directors will incur no monetary loss as a result of actions undertaken by them as Directors. Certain actions are specifically excluded, for example, the incurring of penalties and fines which may be imposed in respect of breaches of the law.

## Use of Company Information

There were no notices from Directors of the Company requesting to use Company information received in their capacity as Directors which would not otherwise have been available to them.

## Group Structure

Kathmandu Holdings Limited owns 100% of the following companies:

Milford Group Holdings Limited
Kathmandu Limited
Kathmandu Pty Limited
Kathmandu (UK) Limited
Kathmandu US Holdings LLC
Oboz Footwear LLC

## Directors' Details

| | |
|---|---|
| David Kirk | Chairman, Non-Executive Director |
| Xavier Simonet | Managing Director and Chief Executive Officer |
| John Harvey | Non-Executive Director |
| Sandra McPhee | Non-Executive Director |
| Philip Bowman | Non-Executive Director (appointed 2 October 2017) |
| Brent Scrimshaw | Non-Executive Director (appointed 2 October 2017) |
| John Holland | Non-Executive Director (ceased on 2 October 2017) |
| Christine Cross | Non-Executive Director (ceased on 2 October 2017) |

## Executives' Details

| | |
|---|---|
| Xavier Simonet | Chief Executive Officer |

## Directory

The details of the Company's principal administrative and registered office in New Zealand is:

223 Tuam Street
Christchurch Central
PO Box 1234
Christchurch 8011

# Directory

## Share registry

| | |
|---|---|
| **In New Zealand:** | Link Market Services (LINK) |
| Physical Address: | Level 11, Deloitte Centre,<br>80 Queen Street, Auckland 1010<br>New Zealand |
| Postal Address: | PO Box 91976,<br>Auckland, 1142<br>New Zealand |
| Telephone: | +64 9 375 5999 |
| Investor enquiries: | +64 9 375 5998 |
| Facsimile: | +64 9 375 5990 |
| Internet address: | www.linkmarketservices.com |

| | |
|---|---|
| **In Australia:** | Link Market Services (LINK) |
| Physical Address: | Level 1, 333 Collins Street<br>Melbourne, VIC 3000<br>Australia |
| Postal Address: | Locked Bag A14<br>Sydney, South NSW 1235<br>Australia |
| Telephone: | +61 2 8280 7111 |
| Investor enquiries: | +61 2 8280 7111 |
| Facsimile: | +61 2 9287 0303 |
| Internet address: | www.linkmarketservices.com.au |

## Stock exchanges

The Company's shares are listed on the NZX and the ASX.

## Incorporation

The Company is incorporated in New Zealand.

**Design direction by Kathmandu.**

**Design and print production by MOSHA.**

This document is digitally printed on an environmentally responsible paper, produced using Elemental Chlorine Free (ECF), FSC® certified, Mixed Source pulp from Responsible Sources, and manufactured under strict ISO14001 Environmental Management System.

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kathmanduholdings.com