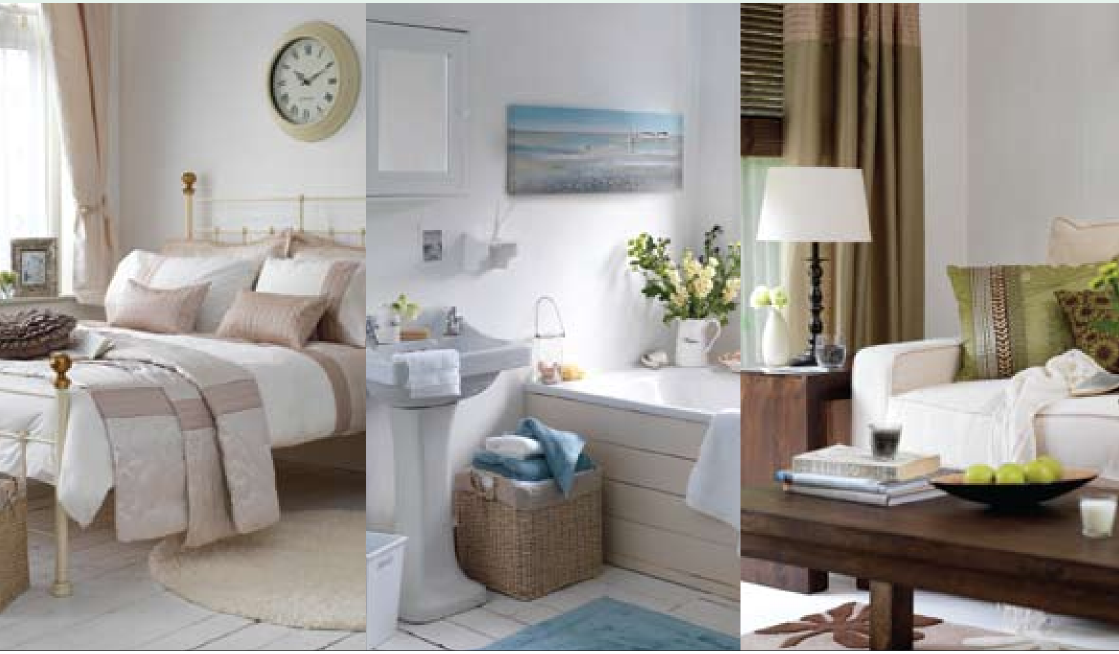
Dunelm mill



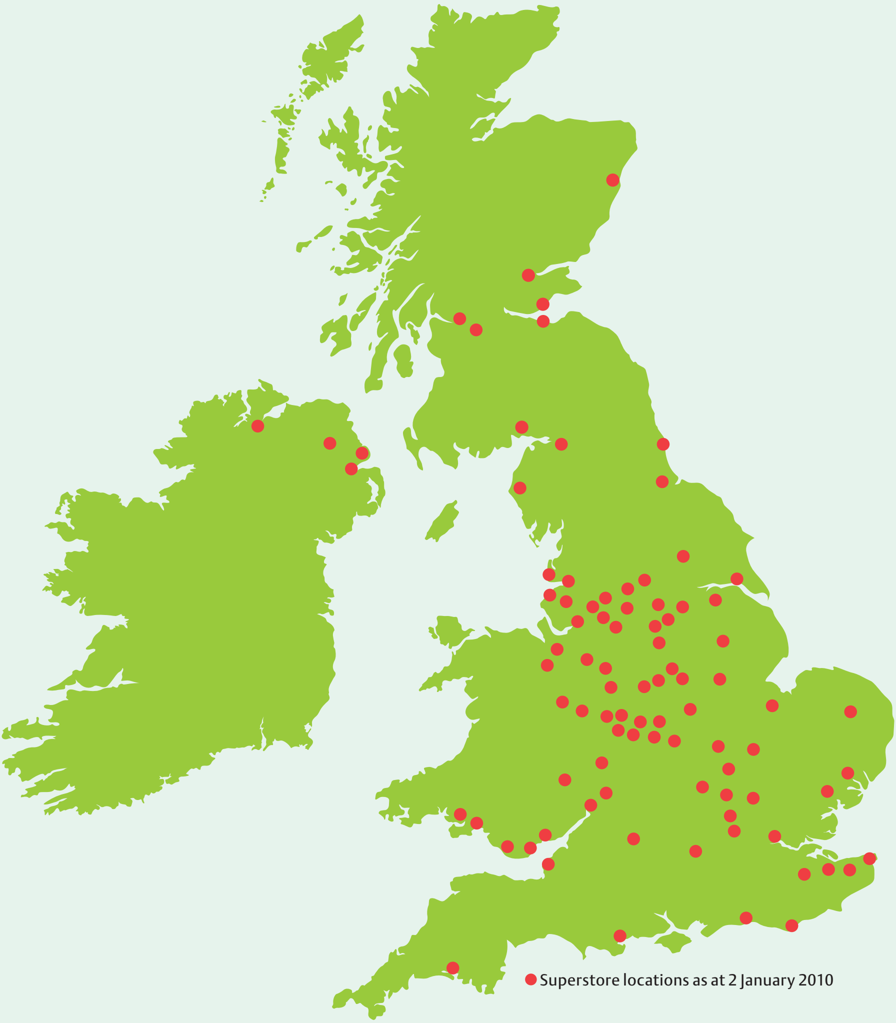
Simply value for money

Interim report 2009/2010

Dunelm Group plc

Contents

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



Chairman's statement

I am delighted to report excellent performance by Dunelm over the 26 weeks to 2 January 2010.

I am delighted to report an excellent performance by Dunelm over the 26 weeks to 2 January 2010. Whilst there was some help from weak comparatives and a timing benefit concerning the start of the winter sale, it is still a great achievement for the business to have delivered 15.4% sales growth on a like for like (LFL) basis. Equally importantly, the pace of new store openings increased, with six new stores in the half. With continuing close attention to gross margins and cost management, profit before tax moved ahead by almost 70% to £46.2m.

The business has continued to generate strong positive cash flow, even during a period of faster expansion. The Board has reviewed future cash requirements and has decided to return 21.5p per share, or approximately £43m, to shareholders, in addition to an interim dividend increase of 50% to 3.0p. Details of the proposed return of capital are provided in a separate circular to shareholders.

Whilst recognising that the retail environment could become much more challenging in the near term, your Board remains very confident in Dunelm's long-term growth potential.

G. I. Cooper

Geoff Cooper
Chairman
25 February 2010

Chief Executive's review

I am convinced that our 'Simply value for money' proposition remains highly attractive, with our industry-leading depth of range supported by highly competitive pricing.

Overview

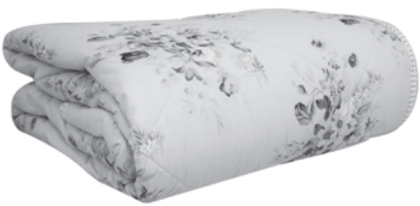
Over the first half of the financial year, we continued to attract new shoppers and to increase market share in LFL stores, as well as expanding our footprint with six new openings. I am convinced that our 'Simply value for money' proposition remains highly attractive, with our industry-leading depth of range supported by highly competitive pricing.

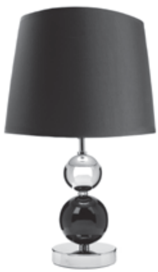
According to research from Verdict, our share of the homewares market stood at 4.6% at the end of 2009, up from 4.0% previously. This makes us the third largest homewares retailer in the UK, even though we have still to achieve nationwide coverage.

Financial performance

During the period, sales grew by 26.0% to £254.2m (FY09: £201.8m). LFL sales grew by 15.4% (against a soft comparative, with 5.6% decline in the equivalent period last year). This year's figures benefitted from the timing of the period end, which included eight days trading from the winter sale, traditionally our biggest trading days, compared with only two last year – we estimate this calendar benefit contributed approximately 2 percentage points to LFL growth over the half year. Nevertheless, our underlying sales performance was undoubtedly strong, driven mainly by increased footfall.

Product gross margin increased by 200 basis points. We saw some small increases in input prices as the effect of sterling weakness fed through the supply





chain. However, active management of gross margin enabled us to offset those cost increases whilst maintaining our very competitive pricing position.

Operating costs remained under tight control, increasing by just under 3% in LFL stores. Consequently, the benefit of sales and gross margin growth fed through to an operating profit increase of over 75% (£45.9m compared with £26.1m). The operating margin was 18.0% (FY09: 12.9%).

Financial income and expenditure contained no significant items this year, leaving profit before tax of £46.2m (FY09: £27.3m).

Profit after tax of £32.4m (FY09: £19.2m) reflects the projected full year effective tax rate of 29.8%.

Fully diluted earnings per share were 15.9p, an increase of 67% against last year.

Cash generated from operations was £60.7m (FY09: £52.5m). Stock levels were £9.5m lower than a year ago – this reflects both the timing benefit of the winter sale, and our continuing progress in stock management. Creditors were £7.5m lower as our December payments to suppliers were accounted for in the first half (whereas they fell after the half-year cut-off last time).

We made capital investments of £9.6m during the period (FY09: £11.4m, including acquisition of rights to the Dorma brand), primarily relating to new stores and store refits.

We ended the period with our balance sheet showing cash of £59.2m (FY09: £23.4m net of bank borrowings). Our average daily cleared funds over the half were £40.1m. We are therefore in a very strong financial position with no gearing and available facilities of up to £40m.

An interim dividend of 3.0p per ordinary share (FY09: 2.0p) will be paid on 1 April 2010 to shareholders on the register at 12 March 2010.

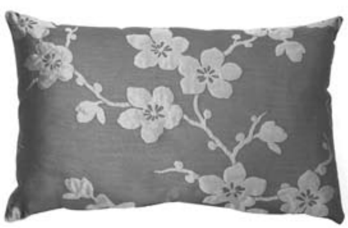
Return of Capital

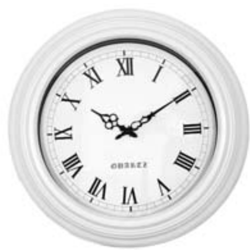
Our financial strength and the cash generative nature of our business are such that we are able to announce a proposal to return 21.5p per share (approximately £43m) to shareholders.

This is to be achieved via a bonus issue of B shares, pro rata to existing holdings, which can either be redeemed for 21.5p each or retained to enable the holder to receive a once-only dividend of 21.5p per share. Further details are set out in a separate circular to shareholders.

Risks and uncertainties

There are a number of potential risks and uncertainties which could have a material impact on the Group's performance over the remaining six months of the financial year and could cause actual results to differ materially from expected and historical results. The Directors do not consider that the principal risks and uncertainties have changed since the publication of the annual





Chief Executive's review continued

report for the year ended 4 July 2009. A detailed explanation of these key risks can be found on pages 8 and 9 of the annual report which is available at www.dunelm-mill.com.

New Store Openings

During the period we opened new superstores in Londonderry, Norwich, Broadstairs, Bridgend, St Helens and Cheltenham. We therefore ended the period with 100 stores, of which 90 are out of town superstores (this includes the transfer of two stores, Rugby and Wellington, previously treated as high street shops).

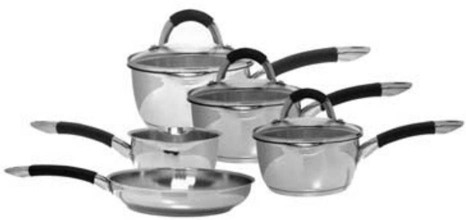
We remain committed to our target of achieving full national coverage. Based on the number of stores operated by other large-format out of town retailers as well as our own experience of store clusters in conurbations like Manchester and Birmingham, we are confident that we will be able to expand the chain to at least 150–200 superstores. We will however remain committed to our financial appraisal disciplines and will continue to target discounted cash flow payback of 36 months or better in all new locations.

We now anticipate five more new store openings in the current financial year. We have a further seven units legally committed for next financial year.

Specialist Offer

We continue to introduce exciting developments to our proposition. The arts and crafts offer which was first trialled about a year ago has now been rolled out to over 50 stores. We have overhauled our furniture range and improved presentation in stores; in larger stores we have also introduced a more extensive furniture department. Our new 'Dunelm at Home' proposition offers a delivery and fitting service from over 20 stores, and a free home consultancy service is available from these same stores to enable customers to choose window treatments in their own home. These developments, together with further initiatives under consideration for longer term implementation, give significant scope for further sales growth.

We have also continued our programme of store refits, with four stores receiving a major refit during the half year. The cost of a typical refit is now approximately £0.7m, reflecting the investment required not only to improve the overall store environment but also to introduce the new elements of our offer. Sales uplifts in recently refitted stores are encouraging, with an average uplift of approximately 10% measured against comparable non-refitted stores. We intend to accelerate our refit programme and five further refits are planned in the current financial year.



Dunelm Direct (www.dunelm-mill.com)
Our new on-line platform was launched in September and has enabled a continuing increase in business. Over the last few months, the on-line channel has developed to become as important in sales terms as one of our top 20 stores. Further investments are planned to capture increased business by continuing to improve the quality of our on-line offering.

Infrastructure
Our warehouse facility at Stoke has again performed well through our peak trading period. With the continuing growth in store numbers we have now decided to extend our capacity at Stoke and have committed to a new lease which doubles the available warehousing footprint on the site. The new facility will require capital expenditure of £2.0m to fit out and will be fully operational by August 2010.

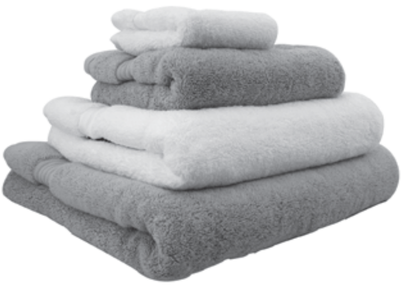
We have indicated previously that we will need to move to a new head office building to support future business growth. We have exchanged contracts, conditional on planning permission, for the purchase of land near to our existing offices. We aim to begin construction of new offices this spring and to be in a position to occupy them by summer 2011.

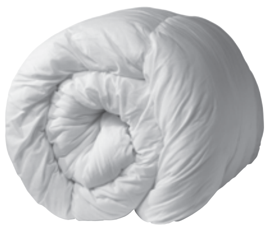
Current Trading and Outlook
During the first seven weeks of the second half, the business continued to grow with a sales increase of 9.1%. On a LFL basis, sales were marginally negative (–0.2%). However, this includes the reversal of the calendar effect relating to winter sale timing, which gave us a benefit in the first half as previously reported; adjusting for this calendar effect, underlying LFL growth was over 6%.

Gross margin gains have continued at a level of +200bps over the most recent seven weeks. However this is flattered by the non-comparable winter sale timing; adjusting for the calendar effect, underlying gross margin growth slowed to +110bps over the seven week period.

We expect consumer spending to weaken in 2010 compared with 2009 as a result of broader economic and political factors. However, our business is in excellent shape and our customer proposition remains compelling. I am confident that, even if LFL growth does prove challenging, overall Dunelm will continue to grow and to become an even stronger business.

Will Adderley
Chief Executive
25 February 2010





Consolidated income statement (unaudited)

For the 26 weeks ended 2 January 2010

	Note	**26 weeks ended 2 January 2010 £'000**	26 weeks ended 27 December 2008 £'000	53 weeks ended 4 July 2009 £'000
Revenue	2	**254,211**	201,814	423,783
Cost of sales		**(132,203)**	(109,039)	(229,701)
Gross profit		**122,008**	92,775	194,082
Operating Costs		**(76,150)**	(66,681)	(141,487)
Operating profit		**45,858**	26,094	52,595
Financial income		**352**	1,877	1,563
Financial expenses		**(28)**	(686)	(667)
Profit before taxation		**46,182**	27,285	53,491
Taxation	4	**(13,749)**	(8,131)	(15,870)
Profit for the period		**32,433**	19,154	37,621
Earnings per share – basic	5	**16.1p**	9.6p	18.8p
Earnings per share – diluted	5	**15.9p**	9.5p	18.6p
Dividend proposed per share	6	**3.0p**	2.0p	4.0p
Dividend paid per share	6	**4.0p**	3.5p	5.5p

All activities relate to continuing operations. All profit is attributable to equity shareholders.

Consolidated balance sheet (unaudited)

As at 2 January 2010

	2 January 2010 £'000	27 December 2008 £'000	4 July 2009 £'000
Non current assets			
Intangible assets	**5,714**	5,663	5,843
Property, plant and equipment	**93,093**	79,312	88,771
Deferred tax asset	**273**	–	–
Total non-current assets	**99,080**	84,975	94,614
Current assets			
Inventories	**61,377**	70,910	57,895
Trade and other receivables	**11,311**	12,781	10,739
Cash and cash equivalents	**59,231**	32,453	24,016
Total current assets	**131,919**	116,144	92,650
Total assets	**230,999**	201,119	187,264
Current liabilities			
Trade and other payables	**(78,369)**	(85,855)	(65,550)
Liability for current tax	**(14,528)**	(8,223)	(8,797)
Interest-bearing loans and borrowings	**–**	(20)	(18)
Total current liabilities	**(92,897)**	(94,098)	(74,365)
Non-current liabilities			
Deferred tax liability	**–**	(277)	(127)
Interest-bearing loans and borrowings	**–**	(9,000)	–
Total non-current liabilities	**–**	(9,277)	(127)
Total liabilities	**(92,897)**	(103,375)	(74,492)
Net assets	**138,102**	97,744	112,772
Equity			
Issued capital	**2,008**	2,008	2,008
Share premium	**345**	345	345
Retained earnings	**135,749**	95,391	110,419
Total equity attributable to equity holders of the Parent	**138,102**	97,744	112,772

Consolidated cash flow statement (unaudited)

For the 26 weeks ended 2 January 2010

	26 weeks ended 2 January 2010 £'000	26 weeks ended 27 December 2008 £'000	53 weeks ended 4 July 2009 £'000
Cash flows from operating activities			
Profit before taxation	**46,182**	27,285	53,491
Adjusted for:			
Net financing income	**(324)**	(1,191)	(896)
Depreciation and amortisation	**5,426**	5,644	10,555
Loss on disposal of property, plant and equipment	**–**	–	26
Operating cash flows before movement in working capital	**51,284**	31,738	63,176
(Increase)/decrease in inventories	**(3,482)**	(10,200)	2,815
(Increase)/decrease in trade and other receivables	**(572)**	(1,145)	897
Increase in trade and other payables	**12,826**	31,391	11,132
Net movement in working capital	**8,772**	20,046	14,844
Share based payment expense	**759**	313	599
Foreign exchange gains/(losses)	**(93)**	440	323
Cash flows from operating activities	**60,722**	52,537	78,942
Interest paid	**(34)**	(793)	(821)
Interest received	**231**	442	523
Tax paid	**(8,399)**	(4,100)	(11,200)
Net cash generated from operating activities	**52,520**	48,086	67,444
Cash flows from investing activities			
Proceeds on disposal of property, plant and equipment	**–**	–	1
Acquisition of property, plant and equipment	**(8,821)**	(6,098)	(19,647)
Acquisition of intangible assets	**(798)**	(5,268)	(6,295)
Net cash utilised in investing activities	**(9,619)**	(11,366)	(25,941)
Cash flows from financing activities			
Purchase of treasury shares	**–**	(186)	(186)
Proceeds from issue of treasury shares	**126**	64	124
Net repayment of bank loan	**–**	(1,000)	(10,000)
Dividends paid	**(8,008)**	(6,994)	(10,993)
Net cash utilised in financing activities	**(7,882)**	(8,116)	(21,055)
Net increase in cash and cash equivalents	**35,019**	28,604	20,448
Foreign exchange revaluations	**214**	996	717
Cash and cash equivalents at the beginning of the period	**23,998**	2,833	2,833
Cash and cash equivalents at the end of the period	**59,231**	32,433	23,998

Statement of changes in equity (unaudited)

For the 26 weeks ended 2 January 2010

	Share capital £'000	Share premium £'000	Retained earnings £'000	Total equity £'000
As at 28 June 2008	2,008	345	83,036	85,389
Profit for the period	–	–	19,154	19,154
Purchase of treasury shares	–	–	(186)	(186)
Treasury shares reissued in respect of share option schemes	–	–	64	64
Share based payments	–	–	313	313
Deferred tax on share based payments	–	–	4	4
Dividends	–	–	(6,994)	(6,994)
As at 27 December 2008	2,008	345	95,391	97,744
Profit for the period	–	–	18,467	18,467
Treasury shares reissued in respect of share option schemes	–	–	59	59
Share based payments	–	–	286	286
Deferred tax on share based payments	–	–	135	135
Current corporation tax on share options exercised	–	–	80	80
Dividends	–	–	(3,999)	(3,999)
As at 4 July 2009	2,008	345	110,419	112,772
Profit for the period	–	–	32,433	32,433
Treasury shares reissued in respect of share option schemes	–	–	126	126
Share based payments	–	–	759	759
Deferred tax on share based payments	–	–	20	20
Dividends	–	–	(8,008)	(8,008)
As at 2 January 2010	**2,008**	**345**	**135,749**	**138,102**

Notes to the interim results

1 Basis of preparation

The condensed financial statements have been prepared using accounting policies consistent with International Financial Reporting Standards and in accordance with International Accounting Standard (IAS) 34 Interim Financial Reporting.

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

2 Accounting policies

The condensed financial statements have been prepared under the historical cost convention, except for share based payments which are stated at their fair value.

The accounting policies adopted are consistent with those of the annual financial statements for the year ended 4 July 2009, as described in those financial statements.

3 Segmental reporting

The Group has only one class of business, retail, and operates entirely in the UK market.

4 Taxation

The taxation charge for the interim period has been calculated on the basis of the estimated effective tax rate for the full year of 29.8% (26 weeks ended 27 December 2008: 29.8%)

5 Earnings per share

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

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

Weighted average numbers of shares:

	26 weeks ended 2 January 2010 000	26 weeks ended 27 December 2008 000	52 weeks ended 4 July 2009 000
Weighted average number of shares in issue during the period	**201,039**	199,841	199,874
Impact of share options	**3,319**	1,894	2,559
Number of shares for diluted earnings per share	**204,358**	201,735	202,433

6 Dividends

	26 weeks ended 2 January 2010 £'000	26 weeks ended 27 December 2008 £'000	52 weeks ended 4 July 2009 £'000
Final for the period ended 28 June 2008 – paid 3.5p	**–**	(6,994)	(6,994)
Interim for the period ended 4 July 2009 – paid 2.0p	**–**	–	(3,999)
Final for the period ended 4 July 2009 – paid 4.0p	**(8,008)**	–	–
	(8,008)	(6,994)	(10,993)

The Directors are proposing an interim dividend of 3.0p per ordinary share for the period ended 2 January 2010 which equates to £6.0m. The dividend will be paid on 1 April 2010 to shareholders on the register at the close of business on 12 March 2010.

7 Announcement

The interim report was approved by the Board on 25 February 2010 and copies are available from the registered office at Fosse Way, Syston, Leicester, LE7 1NF or from the website at www.dunelm-mill.co.uk

Responsibility statement of the Directors in respect of the half-yearly financial report

We confirm that to the best of our knowledge:

- the condensed set of financial statements has been prepared in accordance with IAS 34 Interim Financial Reporting as adopted by the EU
- the interim management report includes a fair review of the information required by:

(a) DTR 4.2.7R of the Disclosure and Transparency Rules, being an indication of important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements; and a description of the principal risks and uncertainties for the remaining six months of the year; and

(b) DTR 4.2.8R of the Disclosure and Transparency Rules, being related party transactions that have taken place in the first six months of the current financial year and that have materially affected the financial position or performance of the entity during that period; and any changes in the related party transactions described in the last annual report that could do so.

By order of the Board

Will Adderley
Chief Executive
25 February 2010

David Stead
Finance Director
25 February 2010

Designed and produced by **Emperor Design Consultants Ltd**
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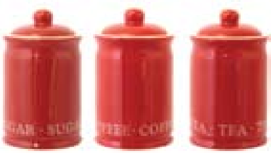

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