James Johnston & Co. of Elgin Limited

Annual report and consolidated financial statements

Registered number SC022553

31 December 2018

Contents

Company information

Directors
IGM Urquhart
DA Harrison
NE Urquhart
NAC Bannerman
CJM Gaffney
SJ Cotton
JM Urquhart
MS Wikstrom

Secretary
CJM Gaffney

Auditor
KPMG LLP
37 Albyn Place
Aberdeen
AB10 1JB

Bankers
Royal Bank of Scotland
6th Floor
2 Marischal Square
Broad Street
Aberdeen
AB10 1BL

Solicitors
MacRoberts LLP
Capella
60 York Street
Glasgow
G2 8JX

Registered Office
Newmill
Elgin
Morayshire
IV30 4AF

Strategic report

Principal activities

The group is principally engaged in the manufacture and sale of cashmere and woollen goods.

Business model

The business adds value through its vertically integrated business model. The entire process from designing products and sourcing raw fibre through the production steps of dying, yarn manufacture, weaving, knitting, finishing, embroidery and labelling can all be conducted at our Scottish based sites. This allows control of quality throughout the process and retains the value added in each step in the business.

Manufacturing facilities are in Elgin in the Scottish Highlands (Wovens) and in Hawick in the Borders (Knitted), producing across broad categories of accessories (scarves, gloves, hats, socks), garments and cloth for clothing and home interiors.

The company sells to internationally recognisable luxury brands with their label and to department stores, boutiques and consumers with our own "Johnstons of Elgin" brand. There are four retail sites in the UK, one at each of our manufacturing sites, a shop in St Andrews and a flagship store on New Bond Street in London. The retail business also operates through e-commerce and mail order. A sales company in Germany (Johnstons Gmbh) and a small retail outlet on Nantucket island (Johnstons of Elgin USA Inc.) are wholly owned subsidiaries.

Business review and results

Profit before tax fell to £6.5m in 2018, down 35% on the prior year.

Total turnover grew by 7%, with export sales growing slightly faster than the UK.

Gross margin fell back, after a very strong performance in 2017, from 34.7% to 29.5%. This was due to a significant movement in the market price for cashmere, particularly in the second half of the year. Prices increased to over 40% higher than 2017 values. Higher sales to key customers than was expected also resulted in the consumption of material more quickly than anticipated, with more expensive fibre being utilised before prices could be corrected to reflect the change.

Higher cashmere prices also resulted in increased working capital in stock (increase of £3.8m), contributing to a lower cash balance at year end of £12.7m (2017: £16.9m).

Monitoring of performance

Budgets are set at the beginning of the financial year and reviewed by the board quarterly against figures achieved.

Key Performance Indicators

	2018	2017	**Measure**
Stock days	**221.9**	227.4	Stock/Cost of sales *365
Debtor days	**37.7**	35.1	Average trade debtors/Sales *365
Creditor days	**25.4**	21.8	Average trade creditors/Cost of sales *365
Gross margin	**29.5%**	34.7%	Gross profit/Turnover
Operating margin	**8.5%**	14.0%	Operating profit/Turnover
Return on capital employed	**13.1%**	22.8%	Profit before tax/Net assets less deferred tax

Strategic report *(continued)*

Principal risks and uncertainties

The main risks and uncertainties centre on raw material prices and supply, currency variations on both sales and purchases and demand profiles from customers. The risk attached to raw material prices is managed by maintaining close contact with the market and suppliers at source and holding significant forward inventory of both fibre and yarn. We also seek to work closely with our major customers to collaboratively plan demand and reduce fluctuations where possible.

Close attention is paid to the stock position in the market and those held within the group's possession. Our currency position is hedged by conservative forward contracts in the major currencies with which we conduct our business.

Brexit

Johnstons are an international business and will be impacted adversely should the UK leave the EU without a comprehensive trade deal. Tariffs could be levied at an average of up to 10% on sales of £16m to European customers, and to customers in Japan, Canada and South Korea with whom trade arrangement are in place through the EU. In the short term there would also be interference in the smooth running of supply chains which involve moving product into the EU and from our partner vendors, many of whom operate in Italy. In the longer term there are also concerns regarding the availability of labour and a decreasing working age population in the semi-rural locations in which we operate. Johnstons has more than 220 years history of managing through change and will rise to the challenges presented by any political uncertainty in our established markets, whilst taking opportunities to grow new markets, particularly in China.

Funding and going concern

After making enquiries, the directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future.

Future developments

We continue to pursue a strategy of growth with our major luxury branded customers and through our own brand in wholesale, retail and online. High fibre prices will constrain margin growth in 2019, but the market does recognise that prices will go up to reflect the increased cost base.

Signed on behalf of the board

CJM Gaffney
Secretary

Newmill
Elgin
Morayshire
IV30 4AF

15th March 2019

Directors' report

Dividends
Dividends paid during the year total £1,287,000 *(2017: £197,000)*.

No further dividend payment has been approved by the board at the date of approving the financial statements.

Directors
The directors who held office during the year and up to the date of this report are as follows:

IGM Urquhart
DA Harrison
NE Urquhart
NAC Bannerman
CJM Gaffney
SJ Cotton
JM Urquhart
MS Wikstrom

The Company provided qualifying third party indemnity provisions to the directors of the Company during the financial year and at the date of this report.

Employee involvement
Regular management meetings enable both executives and employees to be aware of and discuss matters which can affect the future of the business. A consultative forum made up of employee representatives from each area of the business is in existence and meets quarterly.

Financial instruments
The Group's financial instruments comprise cash, working capital balances and derivative forward currency contracts. Further details are presented in note 16 of the financial statements.

Disclosure of information to auditor
The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each director has taken all the steps that he/she ought to have taken as a director to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Auditor
Pursuant to Section 487 of the Companies Act 2006, the auditor will be deemed to be reappointed and KPMG LLP will therefore continue in office.

By order of the board

CJM Gaffney
Secretary

Newmill
Elgin
Morayshire
IV30 4AF

15th March 2019

Statement of directors' responsibilities in respect of the annual report and the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the group and parent company financial statements in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland.

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

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- assess the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

KPMG

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF JAMES JOHNSTON & CO. OF ELGIN LIMITED

Opinion

We have audited the financial statements of James Johnston & Co. of Elgin Limited ("the company") for the year ended 31 December 2018 which comprise the consolidated profit and loss account, consolidated balance sheet, company balance sheet, consolidated statement of changes in equity, company statement of changes in equity, consolidated cash flow statement and related notes, including the accounting policies in note 1.

In our opinion the financial statements:

- give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2018 and of the group's profit for the year then ended;
- have been properly prepared in accordance with UK accounting standards, including FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the group in accordance with, UK ethical requirements including the FRC Ethical Standard. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

The impact of uncertainties due to the UK exiting the European Union on our audit

Uncertainties related to the effects of Brexit are relevant to understanding our audit of the financial statements. All audits assess and challenge the reasonableness of estimates made by the directors, such as the carrying value of inventory and valuation of the defined benefit pension obligation, and related disclosures, and the appropriateness of the going concern basis of preparation of the financial statements. All of these depend on assessments of the future economic environment and the group's future prospects and performance.

Brexit is one of the most significant economic events for the UK, and at the date of this report its effects are subject to unprecedented levels of uncertainty of outcomes, with the full range of possible effects unknown. We applied a standardised firm-wide approach in response to that uncertainty when assessing the group's future prospects and performance. However, no audit should be expected to predict the unknowable factors or all possible future implications for a company and this is particularly the case in relation to Brexit.

Going concern

The directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the group or the company or to cease their operations, and as they have concluded that the group and the company's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over their ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least a year from the date of approval of the financial statements. In our evaluation of the directors' conclusions, we considered the inherent risks to the group's business model, including the impact of Brexit, and analysed how those risks might affect the group and company's financial resources or ability to continue operations over the going concern period. We have nothing to report in these respects.

However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the group or the company will continue in operation.

Strategic report and directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Matters on which we are required to report by exception

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

Directors' responsibilities

As explained more fully in their statement set out on page 5, the directors are responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the group and parent company'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 they either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

The purpose of our audit work and to whom we owe our responsibilities

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an 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 members, as a body, for our audit work, for this report, or for the opinions we have formed.

David Derbyshire

David Derbyshire (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
37 Albyn Place
Aberdeen
AB10 1JB

19 March 2019

Consolidated profit and loss account

for the year ended 31 December 2018

	Note	2018 £000	2017 £000
Turnover	3	**79,030**	73,891
Cost of sales		**(55,689)**	(48,247)
Gross profit		**23,341**	25,644
Distribution costs		**(7,669)**	(6,511)
Administrative expenses		**(8,982)**	(8,794)
Operating profit		**6,690**	10,339
Interest receivable and similar income	7	**30**	11
Interest payable and similar expenses	8	**(225)**	(427)
Profit before taxation	4	**6,495**	9,923
Tax on profit	9	**(1,349)**	(2,075)
Profit for the financial year		**5,146**	7,848

All of the turnover and operating profit above relates to continuing operations.

Consolidated statement of comprehensive income

for the year ended 31 December 2018

	2018 £000	2017 £000
Profit for the financial year	**5,146**	7,848
Actuarial gains recognised in the pension scheme (note 17)	**1,324**	5,457
Deferred and current tax arising on gains in the pension scheme (note 9)	**(225)**	(906)
Exchange differences on retranslation	**(11)**	17
Net change in fair value of cash flow hedges (note 16)	**638**	(474)
Deferred tax arising on cash flow hedges (note 9)	**(107)**	81
Other comprehensive income	**1,619**	4,175
Total comprehensive income for the financial year	**6,765**	12,023

Consolidated balance sheet
at 31 December 2018

	Note	2018 £000	2017 £000
Fixed assets			
Tangible assets	*11*	**9,506**	7,689
		9,506	7,689
Current assets			
Stocks	*13*	**33,855**	30,061
Debtors	*14*	**9,560**	12,158
Cash at bank and in hand		**12,706**	16,855
		56,121	59,074
Creditors: amounts falling due within one year	*15*	**(9,841)**	(12,082)
Net current assets		**46,280**	46,992
Total assets less current liabilities		**55,786**	54,681
Provision for liabilities			
Defined benefit scheme with liabilities	*17*	**(5,263)**	(9,556)
Net assets		**50,523**	45,125
Capital and reserves			
Called up share capital	*18*	**780**	790
Share premium account	*19*	**113**	113
Profit and loss account		**48,988**	44,121
Cash flow hedging reserve	*19*	**322**	(209)
Capital redemption reserve	*19*	**320**	310
Shareholders' funds		**50,523**	45,125

These financial statements were approved by the board of directors on 15th March 2019 and were signed on its behalf by:

Simon Cotton

SJ Cotton
Director

Company balance sheet
at 31 December 2018

	Note	2018 £000	2017 £000
Fixed assets			
Tangible assets	*11*	**9,494**	7,665
Investments	*12*	**-**	-
		9,494	7,665
Current assets			
Stocks	*13*	**33,718**	29,922
Debtors	*14*	**10,066**	12,624
Cash at bank and in hand		**12,621**	16,736
		56,405	59,282
Creditors: amounts falling due within one year	*15*	**(9,807)**	(12,031)
Net current assets		**46,598**	47,251
Total assets less current liabilities		**56,092**	54,916
Provision for liabilities			
Defined benefit scheme with liabilities	*17*	**(5,263)**	(9,556)
Net assets		**50,829**	45,360
Capital and reserves			
Called up share capital	*18*	**780**	790
Share premium account	*19*	**113**	113
Profit and loss account		**49,294**	44,356
Cash flow hedging reserve	*19*	**322**	(209)
Capital redemption reserve	*19*	**320**	310
Shareholders' funds		**50,829**	45,360

These financial statements were approved by the board of directors on 15th March 2019 and were signed on its behalf by:

SJ Cotton
Director

Consolidated statement of changes in equity

for the year ended 31 December 2018

	Called up share capital £000	Share premium £000	Profit and loss account £000	Cash flow hedging reserve £000	Capital redemption reserve £000	Total equity £000
At 1 January 2017	**790**	**113**	**31,902**	**184**	**310**	**33,299**
Profit for the financial year	-	-	7,848	-	-	7,848
Actuarial gains recognised in the pension scheme	-	-	5,457	-	-	5,457
Deferred and current tax arising on gains in the pension scheme	-	-	(906)	-	-	(906)
Exchange differences on retranslation	-	-	17	-	-	17
Net change in fair value of cash flow hedges	-	-	-	(474)	-	(474)
Deferred tax arising on cash flow hedges	-	-	-	81	-	81
Transactions with owners recorded directly in equity						
Dividends paid	-	-	(197)	-	-	(197)
At 31 December 2017	**790**	**113**	**44,121**	**(209)**	**310**	**45,125**
Profit for the financial year	-	-	5,146	-	-	5,146
Actuarial gains recognised in the pension scheme	-	-	1,324	-	-	1,324
Deferred and current tax arising on gains in the pension scheme	-	-	(225)	-	-	(225)
Exchange differences on retranslation	-	-	(11)	-	-	(11)
Net change in fair value of cash flow hedges	-	-	-	638	-	638
Deferred tax arising on cash flow hedges	-	-	-	(107)	-	(107)
Transactions with owners recorded directly in equity						
Dividends paid	-	-	(1,287)	-	-	(1,287)
Company purchase of own shares	(10)	-	(80)	-	10	(80)
At 31 December 2018	**780**	**113**	**48,988**	**322**	**320**	**50,523**

Company statement of changes in equity
for the year ended 31 December 2018

	Called up share capital £000	Share premium £000	Profit and loss account £000	Cash flow hedging reserve £000	Capital redemption reserve £000	Total equity £000
At 1 January 2017	**790**	**113**	**32,066**	**184**	**310**	**33,463**
Profit for the financial year	-	-	7,936	-	-	7,936
Actuarial gains recognised in the pension scheme	-	-	5,457	-	-	5,457
Deferred and current tax arising on gains in the pension scheme	-	-	(906)	-	-	(906)
Net change in fair value of cash flow hedges	-	-	-	(474)	-	(474)
Deferred tax arising on cash flow hedges	-	-	-	81	-	81
Transactions with owners recorded directly in equity						
Dividends paid	-	-	(197)	-	-	(197)
At 31 December 2017	**790**	**113**	**44,356**	**(209)**	**310**	**45,360**
Profit for the financial year	-	-	5,207	-	-	5,207
Actuarial gains recognised in the pension scheme	-	-	1,323	-	-	1,323
Deferred and current tax arising on gains in the pension scheme	-	-	(225)	-	-	(225)
Net change in fair value of cash flow hedges	-	-	-	638	-	638
Deferred tax arising on cash flow hedges	-	-	-	(107)	-	(107)
Transactions with owners recorded directly in equity						
Dividends paid	-	-	(1,287)	-	-	(1,287)
Company purchase of own shares	(10)	-	(80)	-	10	(80)
At 31 December 2018	**780**	**113**	**49,294**	**322**	**320**	**50,829**

Consolidated cash flow statement

for the year ended 31 December 2018

	2018	2017
	£000	£000
Cash flows from operating activities		
Profit for the year	**5,146**	7,848
Adjustments for:		
Depreciation charge	**1,309**	1,179
Interest receivable and similar income	**(30)**	(11)
Interest payable and similar expenses	**225**	427
Profit on sale of tangible fixed assets	**(7)**	(23)
Taxation	**1,349**	2,075
Pension scheme contributions	**(3,177)**	(1,400)
Increase in stock	**(3,794)**	(112)
Decrease/(increase) in debtors	**2,315**	(4,054)
(Decrease)/increase in creditors	**(1,924)**	3,434
Cash from operations	**1,412**	9,363
Taxation paid	**(1,849)**	(1,317)
Net cash (used in)/generated from operating activities	**(437)**	8,046
Cash flows from investing activities		
Interest received	**30**	11
Proceeds on disposal of fixed assets	**8**	23
Purchase of fixed assets	**(2,356)**	(1,662)
Net cash used in investing activities	**(2,318)**	(1,628)
Cash flows from financing activities		
Dividends paid	**(1,287)**	(197)
Interest paid	**(17)**	(4)
Purchase of own shares	**(80)**	-
Net cash used in financing activities	**(1,384)**	(201)
Net (decrease)/increase in cash and cash equivalents	**(4,139)**	6,217
Effect of exchange rate fluctuations on cash held	**(10)**	17
Cash and cash equivalents at the beginning of the year	**16,855**	10,621
Cash and cash equivalents at the end of the year	**12,706**	16,855

Notes to the financial statements
(forming part of the financial statements)

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements.

Basis of preparation

These Group and parent company financial statements were prepared in accordance with Financial Reporting Standard 102, The Financial Reporting Standard applicable in the UK and Republic of Ireland ("FRS 102"). All amounts in the financial statements have been rounded to the nearest £1,000.

The parent company is included in the consolidated financial statements, and is considered to be a qualifying entity under FRS 102 paragraphs 1.8 to 1.12. The following exemptions available under FRS 102 in respect of certain disclosures for the parent company financial statements have been applied:

- The reconciliation of the number of shares outstanding from the beginning to the end of the period has not been included a second time;
- No separate parent company Cash Flow Statement with related notes is included; and
- Key Management Personnel compensation has not been included a second time.
- Certain disclosures required by FRS 102.11 Basic Financial Instruments and FRS 102.12 Other Financial Instrument Issues in respect of financial instruments not falling within the fair value accounting rules of Paragraph 36(4) of Schedule 1.

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

Judgements made by the directors, in the application of these accounting policies that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 2.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiary undertakings made up to 31 December 2018. A subsidiary is an entity that is controlled by the parent. The results of subsidiary undertakings are included in the consolidated profit and loss account from the date that control commences until the date that control ceases. Control is established when the Company has the power to govern the operating and financial policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that are currently exercisable.

Under Section 408 of the Companies Act 2006 the Company is exempt from the requirement to present its own profit and loss account.

In the parent financial statements, investments in subsidiaries are carried at cost less provision for impairment.

Going concern

The group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 2 and 3.

After making enquiries, the directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and consolidated financial statements.

Notes to the financial statements *(continued)*

1 Accounting policies *(continued)*

Tangible fixed assets and depreciation

The cost of tangible fixed assets is their purchase cost, together with any other costs directly attributable to bringing the asset into working condition for its intended use.

Depreciation is provided to write off the cost less the estimated residual value of tangible fixed assets by equal instalments over their estimated useful economic lives as follows:

Freehold buildings	25 years
Motor vehicles	4 years
Plant and machinery	4 to 8 years
Computer hardware	3 to 4 years

No depreciation is provided on freehold land.

The Group performs impairment reviews in respect of fixed assets whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. If the recoverable amount of the asset, being the higher of the asset's net realisable value and its value in use, is found to be less than the carrying value, then an impairment loss is recognised in the profit and loss account.

Investments

In the company's financial statements, investments in subsidiary undertakings are stated at cost less provision for impairment.

Stocks

Stocks are stated at the lower of cost and net realisable value. In the case of raw materials, cost is purchase price. In the case of work in progress and finished goods, cost consists of direct materials, direct labour plus attributable overheads based on the normal level of activity. Net realisable value is based on estimated selling price less estimated further costs of completion and disposal.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by the accounting standard.

Contributions to pension funds

The group operates three pension schemes. The first, a defined benefit scheme provides benefits based on final pensionable pay. This scheme is now closed to new entrants and future accrual. The assets of the defined benefit scheme are held separately from those of the group, being invested by professional investment managers. Pension scheme assets are measured using current bid price. Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on a high quality corporate bond of equivalent term to the liability. The movement in pension scheme deficit is split between interest payable and similar expenses in the profit and loss account and actuarial gains and losses in the statement of other comprehensive income.

The two remaining schemes are Stakeholder schemes providing individual arrangements for either permanent or temporary employees. The assets of the schemes are held separately from those of the group in independently administered individual funds. The amount charged to the profit and loss account represents the contributions payable by the employer to the schemes in respect of the accounting year.

Notes to the financial statements *(continued)*

1 Accounting policies *(continued)*

Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account.

The assets and liabilities of overseas subsidiary undertakings are translated at the closing exchange rates. Profit and loss accounts of such undertakings are consolidated at the average rates of exchange during the year. Gains and losses arising on these translations are taken to reserves, net of exchange differences arising on related foreign currency borrowings.

Turnover

Turnover represents the amounts (excluding value added tax) derived from the provision of goods to third party customers.

Turnover from the sale of goods is recognised when the significant risks and rewards of ownership of the goods has transferred to the buyer, usually on despatch of the goods.

Leases

Operating lease rentals are charged to the profit and loss account on a straight line basis over the period of the lease.

Dividends

Dividends unpaid at the balance sheet date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the company. Unpaid dividends that do not meet these criteria are disclosed in the notes to the financial statements.

Basic financial instruments

Basic financial instruments such as debtors and creditors are recognised at cost, less any impairment for bad debts in the case of trade debtors.

Derivatives

The Group uses derivative financial instruments to manage its exposure to fluctuations in foreign exchange rates. Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are re-measured at their fair value at each subsequent reporting date

Currently the group only has cash flow hedge relationships. Cash flow hedges are hedges of particular risks that might change the amount or timing of future cash flows. For qualifying cash flow hedges, the hedging instrument is recorded at fair value. The portion of any change in fair value that is an effective hedge is included in equity, and any remaining ineffective portion is reported in the income statement. Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, no longer qualifies for hedge accounting or the Group revokes the designation.

The fair value of the forward currency contract is calculated by reference to current forward exchange contracts with similar maturity profiles.

Cash

Cash, for the purposes of the cashflow statement, comprises cash on hand and cash in short term deposits.

Notes to the financial statements *(continued)*

2 Accounting estimates and judgements

Preparation of the financial statements requires management to make significant judgements and estimates. The items in the financial statements where these judgements and estimates have been made include:

Defined benefit pension plan

The Group operates a defined benefit plan. The estimation of the defined benefit obligation liabilities depends on such factors as life expectancy of the members, future inflation assumptions and the discount rate used to calculate the present value of the liabilities. The Group uses previous experience and impartial actuarial advice to select the values of these critical estimates. The estimates adopted, and the sensitivity of key estimates, are disclosed in note 17.

Stock provisioning

The Group has recognised provisions for the impairment of stock. The judgements, estimates and other associated assumptions necessary to calculate these provisions are based on historical experience and other reasonable factors. This provision is based on an assessment of stock value taking into account the ageing of the stock, the quantities on hand, date of last usage, and the quality of stock. The value of stock in note 13 is net of the provision for impairment of stock.

3 Analysis of turnover

A geographical analysis of turnover is set out below:

	2018	2017
	£000	£000
United Kingdom	**51,753**	48,418
Rest of the World	**27,277**	25,473
	79,030	73,891

Turnover represents the amounts (excluding value added tax) derived from the provision of goods to third party customers.

Turnover is derived entirely from the sale of cashmere and woollen goods.

Notes to the financial statements *(continued)*

4 Expenses and auditor's remuneration

	2018 £000	2017 £000
Profit before taxation is stated after charging/(crediting):		
Depreciation (see note 11)	**1,309**	1,179
Operating lease rentals – land and buildings	**545**	496
Operating lease rentals – cars	**76**	65
Auditor's remuneration	**108**	107
Profit on disposal of tangible fixed assets	**(7)**	(23)

The remuneration of the auditor's is further analysed as follows:	2018 £000	2017 £000
Audit of the financial statements	**44**	43
Audit of the pension scheme	**6**	6
Total audit services	**50**	49
Taxation compliance services	**21**	20
Taxation advisory services	**37**	38
Total non-audit services	**58**	58
	108	107

5 Directors' remuneration and key management compensation

	2018 £000	2017 £000
Directors' emoluments	**945**	1,092
Company contributions paid to defined contribution pension schemes	**42**	31
	987	1,123

Retirement benefits are accruing to the following number of directors under:

	2018	2017
Defined contribution scheme	**4**	4

The aggregate remuneration of the highest paid director was £313,000 *(2017: £379,000)*. Pension contributions of £18,000 were made on behalf of this director *(2017: £17,000)*.

Certain directors participate in a long term incentive plan for the period from 2015 to 2019. No amounts were received or receivable in the current or prior year under long term incentive plans.

The directors' are the Key Management Personnel of the Group.

Notes to the financial statements *(continued)*

6 Staff numbers and costs

The average number of persons employed by the group (including directors) during the year analysed by category, was as follows:

	Number of employees Group	
	2018	2017
Factory employees	**721**	661
Sales and administration employees	**303**	295
	1,024	956

The aggregate payroll costs of those persons were as follows:

	Group	
	2018	2017
	£000	£000
Wages and salaries	**22,392**	20,313
Social security costs	**1,893**	1,711
Other pension costs (note 17)	**1,057**	934
	25,342	22,958

7 Interest receivable and similar income

	2018	2017
	£000	£000
Bank interest receivable	**30**	11

8 Interest payable and similar expenses

	2018	2017
	£000	£000
Bank interest payable	**16**	2
Other interest payable	**1**	2
Net interest on net defined benefit liability	**208**	423
	225	427

Notes to the financial statements *(continued)*

9 Taxation

	2018 £000 Current tax	2018 £000 Deferred tax	2018 £000 Total tax	2017 £000 Current tax	2017 £000 Deferred tax	2017 £000 Total tax
Recognised in profit and loss account	1,364	(15)	1,349	1,914	161	2,075
Recognised in equity	(355)	687	332	-	825	825
Total tax	1,009	672	1,681	1,914	986	2,900

Analysis of charge in year in profit and loss

	2018 £000	£000	2017 £000	£000
Current tax				
UK corporation tax	1,313		1,907	
Foreign tax	30		4	
Adjustments in respect of prior years	21		3	
Total current tax charge		1,364		1,914
Deferred tax				
Origination and reversal of timing differences	(15)		156	
Adjustment in respect of prior years	-		5	
Total deferred tax credit		(15)		161
Tax on profit		1,349		2,075

The tax charge for the year is higher *(2017: higher)* than the standard rate of corporation tax in the UK of 19%, *(2017: 19.25%)*. The differences are explained below:

	2018 £000	2017 £000
Total tax reconciliation		
Profit before tax	6,495	9,923
Tax at 19% (2017: 19.25%)	1,234	1,910
Effects of:		
Adjust deferred tax to closing average rate	(79)	(129)
Non-deductible fixed asset depreciation	91	120
Overseas tax loss not recognised	16	19
Movement on deferred tax on pension scheme	39	144
Adjustments in respect of prior years	21	8
Foreign tax adjustment	30	-
Other adjustments	(3)	3
Total tax expense included in profit and loss account	1,349	2,075

Notes to the financial statements *(continued)*

9 Taxation *(continued)*

Deferred tax

The elements of deferred taxation are as follows:	**2018 £000**	2017 £000
Accelerated capital allowances	**(193)**	(127)
Timing differences on defined benefit pension scheme	**1,080**	1,626
Other timing difference	**92**	152
Capital gains	**(12)**	(12)
Deferred tax asset	**967**	1,639

The movement in deferred taxation is as follows:	£000
At 1 January 2018	1,639
Deferred taxation credited in the profit and loss account for the period	15
Deferred taxation charged in other comprehensive income for the period	(687)
At 31 December 2018	967

Factors affecting the tax charge for the current year

A reduction in the rate of corporation tax to 17% (effective from 1 April 2020) was substantively enacted on 6 September 2016. This will reduce the Group's future tax charge accordingly. The deferred tax asset at 31 December has been calculated based on the rate of corporation tax that is expected to be in place at the date on which the deferred tax asset reverses.

10 Dividends

The aggregate amount of dividends comprises:	**2018 £000**	2017 £000
Dividends paid in year	**1,287**	197

Notes to the financial statements *(continued)*

11 Tangible fixed assets

Group	Freehold land and buildings £000	Plant and machinery, motor vehicles and computer hardware £000	Total £000
Cost			
At beginning of year	11,251	21,648	32,899
Additions	648	2,479	3,127
Disposals	-	(14)	(14)
At end of year	11,899	24,113	36,012
Depreciation			
At beginning of year	7,540	17,670	25,210
Charge for year	442	867	1,309
Disposals	-	(13)	(13)
At end of year	7,982	18,524	26,506
Net book value			
At 31 December 2018	**3,917**	**5,589**	**9,506**
At 31 December 2017	3,711	3,978	7,689

Company	Freehold land and buildings £000	Plant and machinery, motor vehicles and computer hardware £000	Total £000
Cost			
At beginning of year	11,159	21,566	32,725
Additions	648	2,479	3,127
Disposals	-	(14)	(14)
At end of year	11,807	24,031	35,838
Depreciation			
At beginning of year	7,448	17,612	25,060
Charge for year	442	855	1,297
Disposals	-	(13)	(13)
At end of year	7,890	18,454	26,344
Net book value			
At 31 December 2018	**3,917**	**5,577**	**9,494**
At 31 December 2017	3,711	3,954	7,665

Included within Group and Company freehold land and buildings is land of £272,000 *(2017: £272,000)* which is not depreciated.

Notes to the financial statements *(continued)*

12 Investments

	Shares in subsidiary undertakings £000
Company	
Cost and net book value	
At beginning of the year and at the end of the year	-

At 31 December 2018 the company had the following wholly owned subsidiary undertakings:

Company name	Class of shares held	Nature of business	Country of incorporation
Johnstons of Elgin Limited (i)	Ordinary	Dormant	Scotland
Johnstons GmbH (ii)	Ordinary	Sale of cashmere and woollens	Germany
Johnstons of Elgin USA Inc (iii)	Ordinary	Sale of cashmere and woollens	USA

The registered offices of the subsidiary companies is as per below for the references noted:
(i) Newmill, Elgin, IV30 4AF, UK,
(ii) Kaiserswertherstrasse 140, 40474 Düsseldorf, Germany
(iii) 4 Federal Street, Nantucket, MA 02554, USA.

13 Stocks

	Group		Company	
	2018	2017	**2018**	2017
	£000	£000	**£000**	£000
Raw materials	**19,768**	16,778	**19,768**	16,778
Work in progress	**3,027**	2,450	**3,027**	2,450
Finished goods	**11,060**	10,833	**10,923**	10,694
	33,855	30,061	**33,718**	29,922

Raw materials, work in progress and finished goods recognised as cost of sales in the year amounted to £55,689,000 (2017: £48,247,000) for the Group, and £55,559,000 (2017: £48,263,000) for the Company.

The movement in the provision to allow for the write down of stocks to net realisable value was a decrease of £197,000 in the year (2017: increase of £1,542,000). The write down is included in cost of sales.

14 Debtors

	Group		Company	
	2018	2017	**2018**	2017
	£000	£000	**£000**	£000
Trade debtors	**7,061**	9,277	**7,061**	9,277
Amounts due from subsidiary undertakings	**-**	-	**515**	482
Other financial assets (note 16)	**388**	-	**388**	-
Other debtors	**429**	323	**429**	323
Deferred tax asset (note 9)	**967**	1,639	**967**	1,639
Prepayments	**715**	919	**706**	903
	9,560	12,158	**10,066**	12,624

Included in prepayments is an amount of £160,298 (2017: £160,298) which is due after more than one year.

Notes to the financial statements *(continued)*

15 Creditors: amounts falling due within one year

	Group		Company	
	2018	2017	**2018**	2017
	£000	£000	**£000**	£000
Trade creditors	**4,381**	3,365	**4,369**	3,352
Other financial liabilities (note 16)	**-**	250	**-**	250
Corporation tax payable	**473**	1,313	**473**	1,313
Other taxes and social security	**934**	1,275	**928**	1,269
Accruals and deferred income	**4,053**	5,879	**4,037**	5,847
	9,841	12,082	**9,807**	12,031

16 Financial instruments

Carrying amount of financial instruments

The Group's principal financial instruments are cash and cash equivalents, trade debtors, trade creditors and accruals all of which are carried at cost (notes 14 and 15).

Derivative financial instruments are carried at fair value and are included within debtors or creditors. Valuations are based on equivalent market prices or information derived indirectly from market prices.

Financial risk management

The Group operates a centralised treasury management which is responsible for managing the credit, liquidity, interest and foreign currency risk.

Credit risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in a financial loss to the Group.

The Group's credit risk arises from bank balances and trade debtors from customers. At 31 December 2018, the maximum exposure is represented by the carrying value of each financial asset in the balance sheet. The bulk of the Group's business is conducted with large companies which have strong credit ratings. The Group also holds credit insurance to cover certain trade debtors. Management is of the opinion that adequate provision currently exists in respect of trade debtors.

Foreign currency risk

Foreign currency risk refers to the risk that unfavourable movement in exchange rates may cause financial loss to the Group. Foreign currency risk is monitored on a regular basis. Forward contracts may be used to mitigate the risk of adverse exchange rate movements.

Interest rate risk

Interest rate risk refers to the likelihood that changes in interest rates will result in fluctuations of the value of balance sheet items or changes in interest income or expenses. Where required and appropriate, the Group will manage the risk relating to interest rate fluctuations.

Notes to the financial statements *(continued)*

16 Financial instruments *(continued)*

Hedge accounting and derivative financial instruments

Hedge accounting was adopted in respect of forward currency derivative financial instruments during the current and prior year. Derivative financial instruments are presented within debtors or creditors.

At 31 December 2018, the group had entered into forward currency contracts to sell GBP and buy USD, in order to hedge the future purchase of raw materials in USD. This included the purchase of $15,000,000 through fifteen forward currency contracts, with execution dates falling between January and July 2019. The average exchange rate of these contracts is $1.3279. The fair value of these financial instruments at 31 December 2018 was an asset of £388,000.

At 31 December 2017 the group had entered into forward contracts which had a liability fair value at that date of £250,000. These forward contracts were all fully settled during the current financial year.

The net change in fair value of hedging instruments recognised in other comprehensive income during the year was a gain of £638,000 (being the difference between the fair value liability at the end of the prior year of £250,000 and the fair value asset at the end of the current year of £388,00).

17 Pension commitments

Defined benefit scheme

The group operates a pension scheme providing benefits based on final pensionable pay. The scheme is closed to new entrants and is closed to future accrual for current employees. The assets of the scheme are held separately from those of the group, being invested by professional investment managers.

The information disclosed below is in respect of the whole of the scheme for which the group is the sponsoring employer throughout the periods shown.

	Group and company	
	2018	2017
	£000	£000
Present value of funded defined benefit obligations	**(75,195)**	(84,612)
Fair value of plan assets	**69,932**	75,056
Recognised liability for defined benefit obligations	**(5,263)**	(9,556)

Movements in present value of defined benefit obligation	**Group and company**	
	2018	2017
	£000	£000
At 1 January	**84,612**	85,826
Interest cost	**2,110**	2,291
Gain on curtailments	**(260)**	-
Loss on settlements	**260**	-
Settlement payments from plan assets	**(2,169)**	
Actuarial gains	**(5,644)**	(1,521)
Benefits paid	**(3,714)**	(1,984)
At 31 December	**75,195**	84,612

Notes to the financial statements *(continued)*

17 Pension commitments *(continued)*

Movements in fair value of plan assets

	Group and company	
	2018	2017
	£000	£000
At 1 January	**75,056**	69,836
Interest income	**1,902**	1,868
Return on plan assets	**(4,320)**	3,936
Contributions by employer	**3,177**	1,400
Settlement payments from plan assets	**(2,169)**	-
Benefits paid	**(3,714)**	(1,984)
At 31 December	**69,932**	75,056

(Credit)/expense recognised in the profit and loss account

	Group and company	
	2018	2017
	£000	£000
Net interest on net defined benefit pension liability	**208**	423

The (credit)/expense is recognised in the following line items in the profit and loss account:

	Group and company	
	2018	2017
	£000	£000
Interest payable and similar expenses	**208**	423

The total amount recognised in the consolidated statement of comprehensive income in respect of actuarial gains and losses are gains of £1,324,000 *(2017: £5,457,000)*. Cumulative actuarial gains/losses reported in the consolidated statement of comprehensive income for accounting periods ending on or after 22 June 2002 are losses of £12,001,000 *(2017: £13,325,000)*.

The fair value of the scheme's assets and the return on those assets were as follows:

	Fair value 2018 £000	Fair value 2017 £000
Equities	**23,087**	25,930
Bonds	**26,116**	25,385
Diversified growth funds	**21,018**	21,736
Insured assets	**1,551**	1,640
Cash and cash equivalents	**329**	365
Pending transfer value payments	**(2,169)**	-
Total	**69,932**	75,056

Notes to the financial statements *(continued)*

17 Pension commitments *(continued)*

The major assumptions used by the actuary at the year end were as follows:

	2018	2017
Inflation assumption	**2.20%**	2.15%
Discount rate	**2.90%**	2.55%
Rate of Limited Price Indexation (with 5% cap)	**3.00%**	2.95%

	2018 **£000**	2017 £000
Expected return on plan assets	**1,902**	1,868
(Losses)/gains on plan assets	**(4,320)**	3,936
Total	**(2,418)**	5,804

The last full actuarial valuation was performed as at 5 April 2016 and was completed in July 2017. To measure the defined benefit obligation as at 31 December 2018, the Company projected the results of the 5 April 2016 valuation allowing for interest on the liabilities, the actual benefit payments paid and an estimate of the effect of changes in the actuarial assumptions. All other experience was assumed to be in line with assumptions.

In valuing the liabilities of the pension scheme at 31 December 2018, mortality assumptions have been made as indicated below. If life expectancy had been changed to assume that all members of the scheme lived for one year longer, the value of the reported liabilities at 31 December 2018 would have increased by approximately £3,007,000 before deferred tax.

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date are based on standard actuarial mortality tables and include an allowance for future improvements in longevity. The assumptions are equivalent to expecting a 65-year old to live for a number of years as follows:

- Current pensioner aged 65: 22.1 years (male), 24.1 years (female) *(2017: 22.3 years (male), 24.1 years (female)).*
- Future retiree, currently aged 45, upon reaching 65: 23.8 years (male), 25.9 years (female) *(2017: 24.0 years (male), 26.0 years (female)).*

Following a High Court ruling on 28 October 2018, all defined benefit schemes are required to equalize for the effect of unequal Guaranteed Minimum Pensions ('GMP') accrued between 1990 and 1997 by adjusting other non-GMP benefits. Under FRS 102, this change is accounted for as a past service cost which vests immediately and is taken through the profit and loss account in full in 2018. The Group's actuary have calculated the impact of the GMP equalization through applying a standard methodology calculation. The impact on the 2018 financial statements was an increase in the defined benefit pension liabilities of £440,000 (0.6% of the scheme's liabilities).

The group expects to contribute a minimum of £1,400,000 to its defined benefit plan in the next financial year.

Stakeholder pension schemes

The group contributes towards stakeholders' individual pension arrangements. The pension charge for the year was £1,057,000 *(2017: £934,000).*

18 Called up share capital

	2018 **£000**	2017 £000
Allotted, called up and fully paid		
779,700 *(2017: 789,700)* Ordinary shares of £1 each	**780**	790

Notes to the financial statements *(continued)*

19 Reserves

Share premium account

This reserve records the amount above the nominal value received for shares sold, less transaction costs.

Cash flow hedging reserve

The hedging reserve comprises the effective position of the cumulative net change in the fair value of cash flow hedging instruments related to hedge transactions that have not yet occurred.

Capital redemption reserve

This reserve records the nominal value of shares repurchased by the company.

20 Capital commitments

Amounts contracted for but not provided for in the financial statements amounted to £392,000 for the Group and the Company *(2017: £61,000).*

21 Leasing commitments

Non-cancellable operating lease rentals are payable as follows:

	Group and company Land and buildings	
	2018	2017
	£000	£000
Amounts payable:		
Less than one year	**631**	494
Between one and five years	**2,400**	1,644
More than five years	**1,751**	888
	4,782	3,026

	Motor vehicles	
	2018	2017
	£000	£000
Amounts payable:		
Less than one year	**65**	68
Between one and five years	**77**	109
	142	177

22 Ultimate parent company

The Company is controlled by its shareholders. No other group financial statements include the results of the Company.