

J Sainsbury plc

# Live Well For Less



# Performance highlights

## £29,112m

Group sales (inc. VAT)  
up 12.7%

## £581m

Underlying profit before tax  
down 1%

## -0.6%

Sainsbury's like-for-like sales  
(inc. VAT, ex fuel)

## 10.2p

Full-year dividend

## 21.8p

Underlying basic earnings  
per share

## 17.5p

Basic earnings per share

## £503m

Statutory profit before tax

## 8.8%

Return on capital employed  
down 4 bps

 Read more about our financial KPIs on **page 40**

## 3,000



Food will always be at the heart of our business and we have completed our programme to improve the quality of 3,000 Sainsbury's branded products. We have a strong and differentiated offer that gives our customers market leading **choice, quality and value**.

 Read more about our food business on **page 15**

## £6bn



We are one of the largest general merchandise and clothing retailers in the UK, offering customers a wide range of products across **Sainsbury's, Argos** and **Habitat**.

 Read more about our General Merchandise and Clothing business on **page 18**

## 1.8m



Financial Services are an important part of our business. Sainsbury's Bank played a key part in our acquisition of Argos and Habitat, enabling us to finance the deal in an efficient way. Sainsbury's Bank and Argos Financial Services each have 1.8m active customers.

 Read more about Sainsbury's Bank and Argos Financial Services on **page 21**

## £500m



We are on track to reach our **£500 million cost savings** target by 2017/18 and benefit from a **strong balance sheet**. We plan to reduce costs by a further £500m over three years from 2018/19.

 Read more about our approach to managing costs and maintaining balance sheet strength on **page 22**

# Helping customers live well for less has been at the heart of what we do since 1869.

We offer our customers great quality, choice and value and continue to make their lives better and easier every day. We sell over 90,000 products and employ around 195,000 colleagues across the UK and Ireland.



Find out more at  
[www.j-sainsbury.co.uk/ar17](http://www.j-sainsbury.co.uk/ar17)

## Strategic Report

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# Sainsbury's Group at a glance

## Our vision is to be the most trusted retailer where people love to work and shop

Our goal is to make our customers' lives easier by offering great quality products and service at fair prices.

We offer customers choice across our wide range of food, general merchandise, clothing and financial services. On 2 September 2016 we acquired Home Retail Group plc, the owner of Argos and Habitat, creating one of the UK's leading food, general merchandise and clothing retailers – a multi-product, multi-channel business with fast delivery networks.

Sainsbury's Bank offers accessible financial services products such as credit cards, insurance, travel money and personal loans that reward customer loyalty.

Our 195,000 colleagues, strong culture and values are integral to achieving our vision and driving our success – now and in the future.

## The new Sainsbury's Group

### Food

Sainsbury's has sold great quality food at fair prices **since 1869**. We have a strong heritage of innovation and were the **first retailer of organic produce in the UK**. We continue to build our strength in food innovation, targeting growing food markets where we can increase our market share, such as **Food to Go** and **FreeFrom**, where we can be a market leader.

## 125

reviews underway covering around 60% of our food ranges

## 26m+

weekly customer transactions

 See more on **page 15**



### General Merchandise & Clothing

Our General Merchandise and Clothing business is one of the biggest in the UK and offers customers a wide range of products across **home, clothing, technology** and **leisure**. We have a market-leading position in key product categories such as **toys** and **electricals** and our **Tu** clothing brand offers customers high street style at supermarket prices.

## £6bn

of sales generated by Sainsbury's General Merchandise and Clothing business, including Argos.

 See more on **page 18**



### Financial Services

Sainsbury's Bank has 1.8m active customers. We offer accessible financial services products such as **credit cards, insurance, travel money** and **personal loans** that reward loyalty. This year **Argos Financial Services** became part of our financial services offer and also has approximately **1.8m active customers**.

## 1.9m

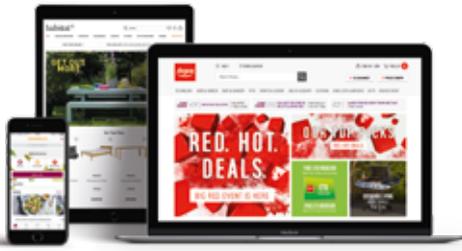
visits to Sainsbury's Bank website every month

## 1,728

ATMs in our estate

 See more on **page 21**





## The world is changing faster than at any time

Convenience, speed and flexibility are key in today's retail environment. Our strategy is to sell products whenever and wherever customers want.

Our supermarkets offer customers a comprehensive mix of food, general merchandise and clothing. Our smaller convenience stores are located where our customers live and work, with a product mix designed for regular top-up shopping and to meet their day-to-day needs.

We have a well-established and growing online offer that allows customers to shop from the comfort of their home, or on the go via a mobile phone or tablet, opting for either convenient delivery to their home or to Click & Collect from our stores.

Our acquisition of Home Retail Group plc has accelerated our strategy. Customers now have access to Argos products, market-leading Argos digital channels and delivery systems. Argos's unique Hub and Spoke supply chain network and *Fast Track* delivery and collection service are points of competitive advantage.

 Read more about our market context on **page 6**

## Whenever and wherever

**809**

Convenience stores

**605**

Sainsbury's supermarkets

**151**

Groceries Online **Click & Collect** points

**59**

Argos Digital stores in Sainsbury's supermarkets

**207**

Digital Collection points for *Tu* clothing, eBay, DPD and, in 90 stores, Argos

**11**

Habitat stores, including four standalone and seven Mini Habitats in Sainsbury's

**276,000**

Average number of customer orders made through Groceries Online channel per week

**26m+**

weekly customer transactions

**10%**

of Groceries Online orders made through new app



\*All numbers are correct at the time of signing the Annual Report and Accounts.

# Our business model

Our business model is designed to create value for our shareholders, customers and colleagues, both now and in the future.

## How we create value and build customer loyalty

We achieve this by listening to our customers and anticipating their needs. We deliver quality products and great value through multiple channels and are there for our customers whenever and wherever they want to shop.

Our values make us different and underpin everything we do, from sourcing with integrity to helping our customers lead healthier lives and providing a great place to work. Our colleagues make the difference, anchoring us in our communities and connecting us to the lives of our customers, day in, day out.

## Power of the Sainsbury's Group

We are one of the largest retailers of quality food, general merchandise, clothing and financial services in the UK and we believe people trust the Sainsbury's brand. Customers can shop with us whenever and wherever they want and we have a logistics network that gives us market-leading product availability in-store and online.

## Our values key



A great place to work



Respect for our environment



Sourcing with integrity



Living healthier lives



Making a positive difference to our community

## What makes us different

We are a multi-product, multi-channel business with a strong, differentiated food proposition and respected brands in Sainsbury's, Sainsbury's Bank, Argos and Habitat.

We benefit from a structurally advantaged store estate, world-class property assets, an efficient supply chain and a market-leading digital presence with fast delivery networks.

All this is underpinned by customer insights that enable us to adapt our business to customers' changing lives.

## Supply chain

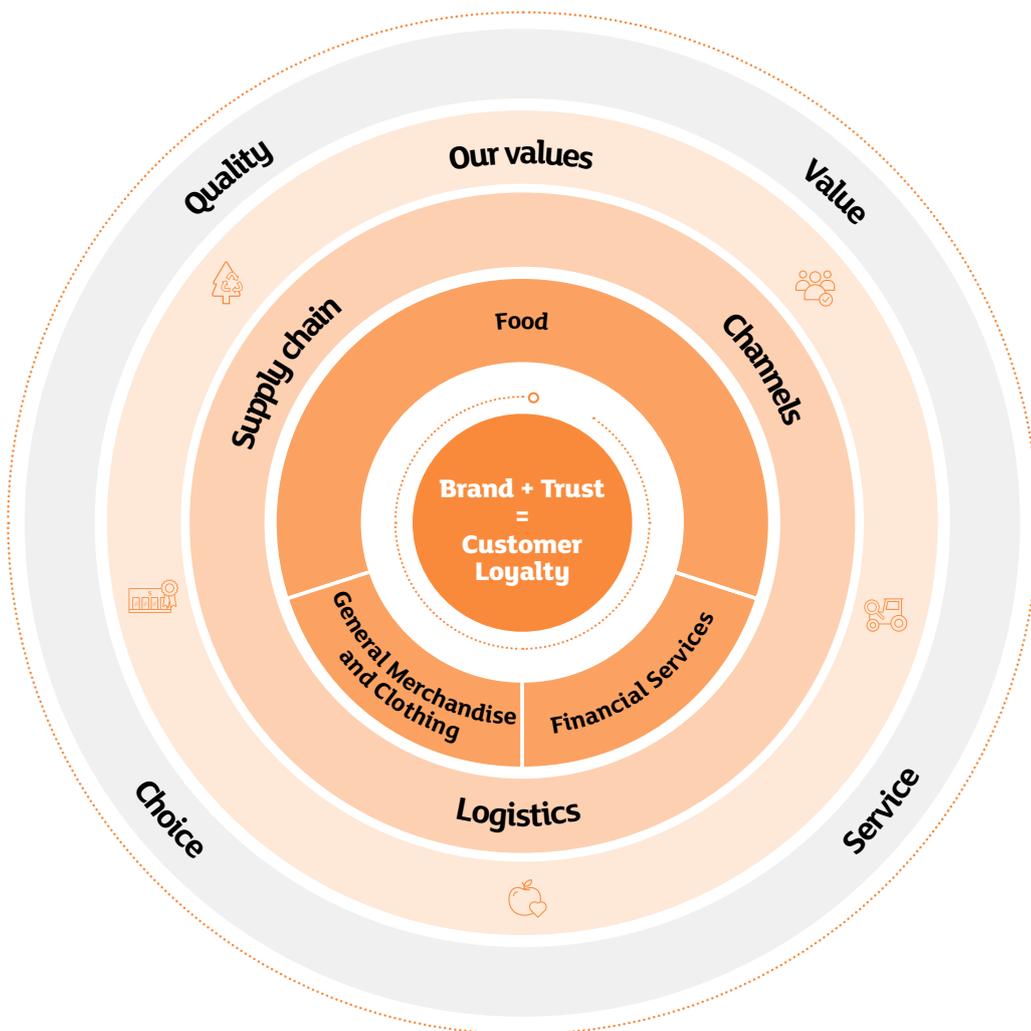
Our business is built on excellent, often long-standing relationships with our suppliers. We source Sainsbury's branded products from the UK and over 70 other countries, according to the ability of suppliers to meet our regularly audited quality, safety and ethical standards. The investment we make in our farmer and grower Development Groups, R&D programme and Apprenticeship Scheme supports the British agricultural sector and encourages young talent into British farming. We are also the world's largest retailer of fairly traded products.

## Logistics

We have invested in our logistics capability and capacity to ensure we can meet our customers' requirements for flexible, convenient shopping now and in the future. Across Sainsbury's and Argos we operate 34 distribution centres. They cover our store and online businesses, across food, general merchandise and clothing, making home and store deliveries seven days per week. Argos's unique Hub and Spoke logistics network enables us to fulfil *Fast Track* same day deliveries – to a customer's home or to a store for collection.

## Channels

Customer shopping habits are changing and our multi-channel proposition gives people the flexibility to shop with us whenever and wherever they want. We have over 2,200 supermarkets, convenience stores and Argos stores across the UK and Ireland and we have made it easy and convenient to shop on the go using our mobile apps. In fact, almost 20 per cent of Sainsbury's Group sales now originate online. We have General Merchandise & Clothing businesses of scale and Sainsbury's Bank is a growing, strategic part of our business.



**Quality**

Selling great quality food has been at the heart of our business since 1869. Customers value the wide range of products and services on offer when they shop with Sainsbury's and this differentiates us. Most of our customers buy Sainsbury's branded products, which account for around half of our food sales. We recently invested in the quality of 3,000 Sainsbury's branded food lines and have moved on to the next stage of our quality improvement programme. Our passion for quality extends to everything we sell – food, general merchandise, clothing and financial services.

**Value**

Offering great quality products and services at fair prices is part of our commitment to help our customers live well for less. Quality and price are both important in the value proposition and our regular lower prices reassure customers that they can always get good value at Sainsbury's. We will always be competitive on price and will continue to invest in lowering prices and improving quality to ensure that we are well-positioned to meet the challenges of an increasingly competitive marketplace.

**Service**

In shops, depots and store support centres, our colleagues provide award-winning service day in, day out, offering customers choice, flexibility and convenience whenever and wherever they want to shop with us. We employ around 195,000 colleagues who are the foundation of our business and make a real difference in the communities they serve. We take pride in the service we offer and our well-run shops and committed, well-trained colleagues have helped us win the Grocer Gold Awards for both Customer Service and Availability for the past four years.

**Choice**

We are one of the UK's largest retailers, with over 90,000 products to choose from across food, general merchandise, clothing and financial services. Shopping for an evening meal, party dress, cookware or car insurance has never been easier at Sainsbury's. Customers can choose between well-known food brands and our extensive own-brand differentiated food offer. In homeware, cookware and electrical products, customers now have an even wider choice of products, across Sainsbury's, Argos and Habitat.

**Sainsbury's business model is supported through a structured approach to managing the business:**

**Governance**  
 ⓘ Read more on **page 58**

**Cost management**  
 ⓘ Read more on **page 22**

**Risk management**  
 ⓘ Read more on **page 42**

# Market context

Customer shopping habits and the UK retail landscape continue to change rapidly. Our strategy reflects this and our business is well set to continue adapting to changing customer needs.

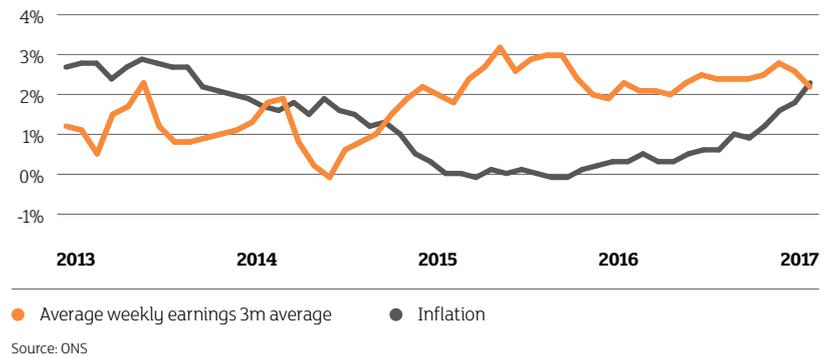
## The market

The UK economy has been stronger than anticipated since the European Union Referendum in June 2016. Conditions have remained supportive for UK consumers, with wage growth remaining higher than inflation. Consistent with recent years, the main beneficiaries of these conditions have been higher ticket discretionary categories such as eating out, car sales and holidays.

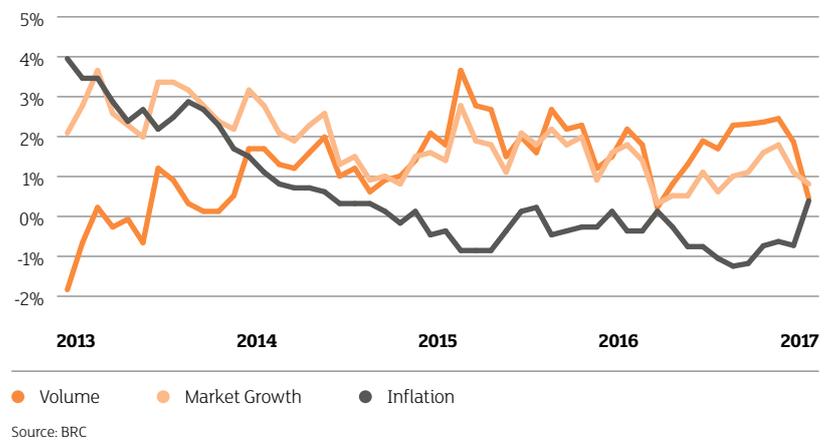
However, the picture is changing now, as the impact of the devaluation of sterling and a higher oil price filter through to food, general merchandise, clothing and fuel prices and the gap between inflation and wage growth narrows.

After more than two years of deflation, food and fuel prices started to rise towards the end of our financial year, driven by the devaluation of sterling and commodity price increases. While this has benefited food retail market growth, general merchandise and clothing sales growth have been impacted by reduced consumer confidence and a marked slowdown in real pay growth. Economic commentators are divided on the implications for the UK economy, but there are fears that this slowdown in real income might drive a reduction in GDP growth, an increase in unemployment and a reduction in the rate of unsecured credit growth.

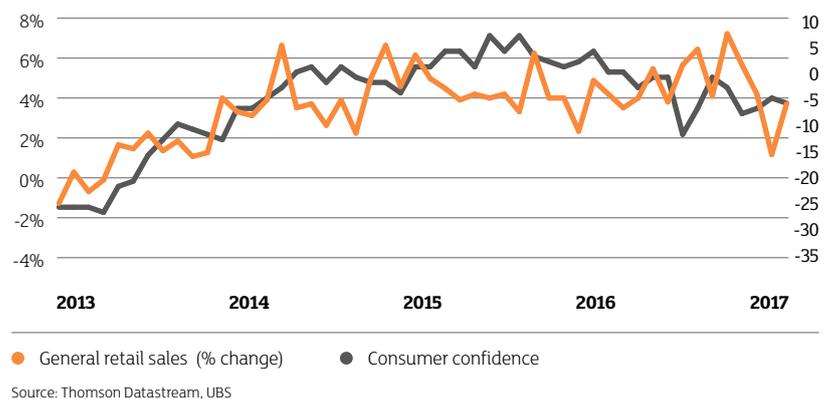
UK average weekly earning growth vs inflation



BRC market growth and inflation



Consumer confidence



## Shopping habits

Shopping habits continue to evolve rapidly, with consumers expecting far greater choice and flexibility in how, when and where they shop for food, general merchandise and clothing.

The UK grocery market remains very competitive. Convenience stores and online retail continue to show strong growth, as consumers shop more frequently across different channels and store formats. Discount food retailers continue to open significant numbers of new stores and gain market share, but at lower rates than in recent years. In line with our expectations, these trends place pressure on volumes through the supermarket format. However, we continue to expect supermarkets to remain the key channel for groceries.

Within general merchandise and clothing, traditional store formats, particularly on the high street, continue to see footfall and sales declines as online participation grows. The combination of a strong online proposition and a wide variety of delivery and collection options is popular with consumers, with Click & Collect accounting for a significant and growing proportion of UK online general merchandise and clothing sales.

## Future retail trends

Consumers will increasingly expect a seamless, flexible retail offer across all products and channels, to fulfil their orders rapidly in a location and at a time that is most convenient to them.

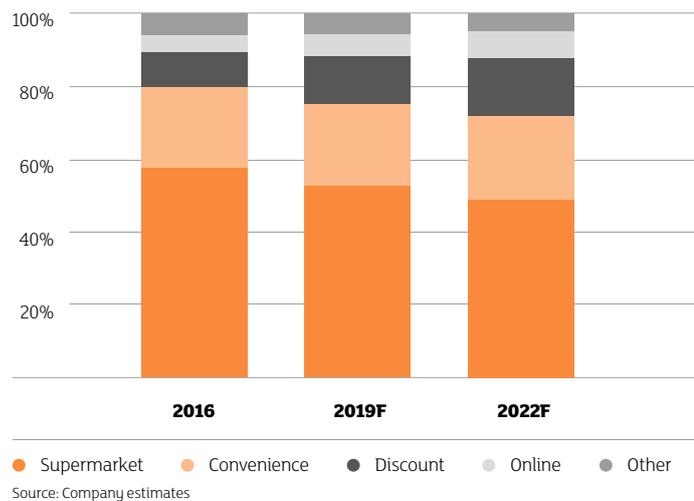
## Addressing a changing marketplace

As our customers' lives change, so will our business. To address the changing marketplace and changing shopping patterns we have prioritised four key areas of our business where we can differentiate ourselves, grow and create value. These priorities are: to further enhance our differentiated food proposition; to grow General Merchandise and Clothing and deliver synergies by integrating Argos; to diversify and grow Sainsbury's Bank; and to continue to cut costs and maintain our balance sheet strength.

**i** To **read more** about the progress we are making against these priorities please see **pages 15 to 23**

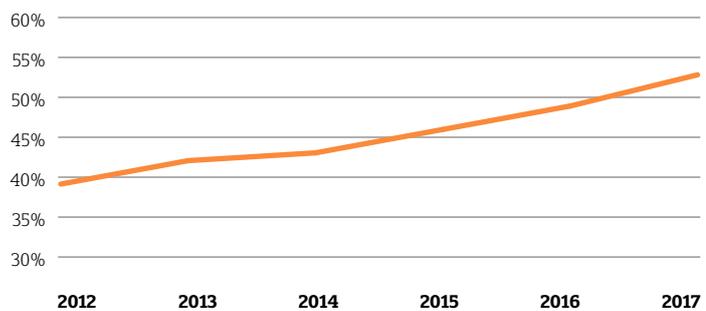
### Grocery market channel share

2016 – 22 % of market



### Argos

Internet sales as proportion of total sales over the last 5 years



“

**Consumers will increasingly expect a seamless, flexible retail offer across all products and channels, which is able to rapidly fulfil their orders in a location and at a time that is most convenient to them.”**

# Chairman's Letter

This year has been an important year in the history of Sainsbury's. Our primary responsibility as a Board is to create value for shareholders in a sustainable way over the medium and long term and we have taken significant steps this year in delivering this objective.



Food is at the heart of our business. We continue to improve the quality and ranging of our grocery offer and with great products at fair prices, we have a clearly differentiated proposition in an increasingly competitive market. With the acquisition of Home Retail Group plc, owner of Argos (including Argos Financial Services) and Habitat, we have created one of the UK's leading retailers in food, general merchandise, clothing and financial services providing customers with a choice, breadth and quality of product whenever and wherever they shop with us. We have also successfully implemented a new banking platform and introduced new products and services at Sainsbury's Bank which are generating increased customer demand.

These changes are all in line with the five pillars of the strategy we outlined in November 2014 (see page 11). By knowing our customers well and anticipating what they want, we will help to make their lives easier every day and achieve our vision of being the most trusted retailer where people love to work and shop.

In the competitive market conditions of the last 12 months, underlying profit before tax, which includes the Argos contribution from 2 September 2016, was £581 million, down one per cent. Underlying basic earnings per share were down 9.9 per cent to 21.8 pence per share. The last three years have been challenging for grocery retailers and the full impact of the vote to leave the European Union remains uncertain. However, we are pleased with the resilience of our business and the progress we are making with our strategy against this backdrop.

### Acquisition of Home Retail Group plc

In September, we completed the acquisition of Home Retail Group plc – owner of Argos and Habitat. Putting aside cash and store card receivables (which can be converted to cash), we purchased the business for an effective cash consideration of £156 million. We believe this will prove to be a very economic acquisition of a valuable asset. The acquisition has accelerated our strategy, allowing us to offer our customers choice and convenience across food, general merchandise, clothing and financial services.

Argos is making great progress, delivering strong like-for-like growth of 4.1 per cent in the six months since the acquisition. We also see a sales increase of between one to two per cent in Sainsbury's supermarkets with an Argos Digital store. We are confident that we will achieve the £160 million of annual synergies we outlined at the time of the transaction six months ahead of schedule.

### Dividend

We are committed to paying an affordable dividend to our shareholders and have fixed dividend cover at two times cover. We are therefore recommending a final dividend of 6.6 pence per share, making the proposed full-year dividend 10.2 pence per share. This brings our dividend payments over the last five years to 69.5 pence per share, equivalent to £1.4 billion of cash paid to our shareholders.

### Management and colleagues

Mike Coupe leads a highly talented and experienced management team. In September 2016, following the acquisition of Argos, we appointed John Rogers, previously Chief Financial Officer, as the Chief Executive of Sainsbury's Argos, where he has put together a strong leadership team from both Argos and Sainsbury's. In January, we were delighted to welcome our new Chief Financial Officer, Kevin O'Byrne, to the Company. Kevin has a wealth of retail and financial experience in executive leadership roles at Dixons, Kingfisher and Poundland and a track record of growing businesses. Finally, we were very pleased to welcome Simon Roberts as Retail and Operations Director. Previously President of Boots, I am sure Simon will make a significant contribution to our business, with his strong customer focus and extensive retail experience.

Our Sainsbury's store colleagues provide industry-leading service to customers every day and we have been awarded the Grocer Gold Awards for both Customer Service and Availability for the past four years. On behalf of the Board, I would like to thank all our colleagues for their commitment and enthusiasm over the last year. We were pleased to increase the standard rate of pay of Sainsbury's store colleagues by four per cent this year, the same rate as last year and well above the National Living Wage. In addition, colleagues across the Group will share a bonus of £78 million this year.

As we announced in March, Mary Harris will step down as a Non-Executive Director at our AGM in July 2017. I would like to thank Mary for her extremely valuable contribution to Sainsbury's over the past nine years and particularly for her skilful leadership of the Remuneration Committee. We expect to announce the appointment of a new Non-Executive Director in due course. Susan Rice, our Senior Independent Director, is appointed Chair of the Remuneration Committee.

### Outlook

The retail market remains very competitive. However, I am convinced that we have the right strategy in place to meet future opportunities and challenges. With our talented leadership team and highly engaged and committed colleagues, we are well placed to navigate the external environment and to create value for shareholders.



**David Tyler**  
Chairman

# Chief Executive's Letter

The world is changing faster than ever before, shaping the way our customers live their lives. Growth of shopping via digital channels and customer expectations of speed and convenience are changing the retail industry. To meet these challenges, we will continue to adapt and evolve our business to meet new shopping habits and provide customers with great products and services at fair prices whenever and wherever they want to shop with us.



# £29,112m

Group sales (inc. VAT)

# £581m

Underlying profit before tax

“

**This has been a pivotal year for Sainsbury's. The strategy we set out in November 2014 was designed to address a changing marketplace and the investments we have made in our core Food business mean we are clearly differentiated by our combination of quality, choice and value.”**

**Mike Coupe** Chief Executive Officer,  
J Sainsbury plc

This has been a pivotal year for Sainsbury's. The strategy we set out in November 2014 was designed to address a changing marketplace and the investments we have made in our core Food business differentiated us through our combination of quality, choice and value. We will continue to enhance our food proposition further and to grow our General Merchandise, Clothing and Financial Services businesses. We welcomed 30,000 colleagues to our business in September when we acquired Home Retail Group plc – owner of Argos and Habitat. The acquisition will accelerate our strategy and gives us a strong platform to deliver synergies and future growth.

The retail market remains very competitive. Underlying profit before tax for the Group is £581 million, down one per cent, and Group sales are £29,112 million, up 12.7 per cent on last year. These numbers reflect the positive contribution made by Argos to the Group. Sainsbury's market share dropped by 23 basis points to 16.3 per cent and, while like-for-like sales are down 0.6 per cent, this is an improvement on last year, demonstrating the resilience of our Food business in a competitive market. Profits at Sainsbury's continue to be impacted by ongoing price investment and cost price pressures.

Our balance sheet is robust and we are managing costs carefully. We are on track to achieve our current cost saving target of £500 million by 2017/18 and we have committed to a further three-year cost saving target of £500 million from 2018/19. Net debt has reduced by £349 million this year. Consistent with our affordable dividend policy, this year's final dividend is 6.6 pence per share, bringing the full-year dividend to 10.2 pence per share.

## A pivotal year

Our goal is to make our customers' lives easier every day by offering great quality products and services at fair prices. Food is at the heart of what we do and we have completed our programme to improve the quality of 3,000 food lines that matter most to our customers. We are now reviewing 125 food categories, touching around 60 per cent of our food range, to further develop our food quality and value.

When we acquired Argos and Habitat in September, we became one of the UK's leading food, general merchandise, clothing and financial services retailers – a multi-product, multi-channel business that offers our customers more choice and gives us the capability to serve them with even greater speed and convenience.

Sainsbury's Bank is a great asset to the Group and played a key part in the acquisition by enabling us to finance the deal in a very cost efficient way. Sainsbury's Bank reached a major milestone this year when we successfully transferred savings customers and our ATM estate on to our newly built, wholly-owned banking platform. We continue to make good progress and will introduce our new loans platform by the end of 2017. This gives Sainsbury's Bank a solid base from which to grow. We also offer an enhanced range of products and services, such as a choice of home and car insurance options with our new panel of insurers and our new mortgage proposition which launched in April 2017.

## Our Business Strategy



## The new Sainsbury's Group

We are building a business for now and the future. We go forward as a combined Sainsbury's Group, strengthened by the addition of Argos, Habitat and Sainsbury's Bank. We benefit from the trust customers have in our brands and from the ability to offer our customers great value and choice across multiple product categories and channels. We are well placed to increase customer loyalty across food, general merchandise, clothing and financial services, driving sales, profit and maximising the opportunities for growth to create value for all our stakeholders.

To focus on our four key priorities we have closed Netto, Sainsbury's Entertainment and our Phone Shops.

## Four key priorities for growth

Our strategy remains based on five pillars (see page 11). Within this we have prioritised four key areas of our business where we can differentiate ourselves, grow and create value:

### 1 Further enhance our differentiated food offer

We continue to invest in our core Food business and to focus on the quality of Sainsbury's branded food products. We have removed multi-buy promotions across our food ranges in favour of lower regular prices and we invest in our prices to ensure we offer customers value for money. We will always be competitive on price.

Sainsbury's has a strong heritage of innovation in key products and categories. For example, we were the first retailer of organic produce in the UK. We continue to innovate, targeting growing food categories where we can increase our market share, such as *Food to Go* and *Free From*, where we can build on the trust customers have in the Sainsbury's brand to develop and strengthen our offer and become a market leader.

We regularly review the layouts of our stores so that customers can do their shopping with us quickly and more conveniently. We are investing in our Groceries Online service, improving the customer experience on our website and expanding our Click & Collect service. Demonstrating the speed of change within retail, the Groceries Online shopping app we launched in May 2016 now accounts for over ten per cent of online food orders.

### 2 Grow General Merchandise & Clothing and deliver synergies

Sainsbury's General Merchandise business is well-established and growing. We are focused on developing complementary, clearly defined general merchandise ranges across Sainsbury's, Argos and Habitat, offering our customers the best choice and quality at fair prices.

Our *Tu* clothing business provides high street style at supermarket prices and eight million customers buy our clothing. Our market share by volume increased by 20 basis points and we are the sixth largest clothing retailer by volume in the UK, with a strong position in womenswear and childrenswear and opportunities for future growth in menswear. We are integrating Argos in to our business at pace. The 59 Argos Digital stores located in Sainsbury's supermarkets are performing well and sales in stores open for more than a year are delivering like-for-like sales increases of between 20 and 30 per cent. Reflecting the strong performance of the Argos Digital stores, we are accelerating our plans to open the planned 250 Argos Digital stores six months ahead of schedule.

Our 207 digital collection points offer customers a fast, convenient delivery service across eBay, DPD, *Tu* clothing and, in 90 stores customers can also collect Argos deliveries. This gives customers the flexibility to pick-up their parcels when it is convenient to them and drives footfall in to our supermarkets.

18 per cent of Group sales at peak times now originate online and our strength in digital, combined with Argos's leading delivery services, including *Fast Track*, will enable us to grow both now and in the future and give us a crucial competitive advantage.

### 3 Diversify and grow Sainsbury's Bank

Sainsbury's Bank continues to grow and generates strong customer loyalty. We know that people who buy our financial services products shop with us more frequently and spend more money than those who do not, giving us a strong platform for growth. We have integrated Argos Financial Services in to Sainsbury's Bank. There is opportunity for this to give us a significant boost in customer base and operations and we are injecting additional capital in areas of Sainsbury's Bank which will generate good returns. Sainsbury's Bank is well set to deliver strong profit growth.



**The market remains very competitive and the impact of cost price pressures remains uncertain. However, we are well placed to navigate the external environment and remain focused on delivering our strategy.”**

**Mike Coupe** Chief Executive Officer, J Sainsbury plc

#### 4 Continue cost savings and maintain balance sheet strength

In line with other UK retailers, we anticipate that cost pressures will continue over the next few years. The price of raw materials and energy is increasing, along with wages and business rates. Across our business we are focused on finding ways to mitigate the impact of these rising costs so that we can continue to deliver for customers, colleagues and shareholders.

We remain focused on cost reduction and efficiency. By the end of 2017/18 we will have delivered £500 million of cost savings in three years across our business and we are committed to a further £500 million reduction over the next three years, starting in 2018/19.

This focus will allow us to continue to invest in our business and our colleagues, as well as provide our shareholders with a return on the investment they have made in Sainsbury's.

#### Our values

As a major retailer, in a highly competitive industry, our values differentiate us from our competitors, make strong commercial sense and enable us to play a leading role in tackling some of the challenges facing our customers every day. Our values enable us to be more efficient in our own operations, for example, by using less electricity in our stores and also by protecting security of supply in our supply chain. Through our *living healthier lives* commitments we are also making it easier for our customers to make healthier choices through product reformulation and innovation. We are also helping customers to save money and reduce household food waste through our five-year *Waste less, Save more* initiative. This is now being rolled out to more than 140 communities across the UK. As well as building trust among our customers, we know our values help to make Sainsbury's a great place to work.

#### We are optimistic about the future

Our success relies on knowing our customers better than anyone else. We must offer them what they want now and anticipate what they will want in the future, across food, general merchandise, clothing and financial services. As we grow we will become a bigger part of our customers' lives and find more ways to save them time and money, offering them the same great quality at fair prices that has been the core of what we do since 1869.

I would like to thank the 195,000 colleagues from across the Group for the market-leading service they deliver and the difference they make to our customers every day. Together with the values that underpin our business, they differentiate us from our competitors and I am pleased that colleagues across the Group will share in this year's bonus of £78 million.

The market remains very competitive and the impact of cost price pressures remains uncertain. However, we are well placed to navigate the external environment and remain focused on delivering our strategy.



**Mike Coupe**  
Chief Executive Officer,  
J Sainsbury plc

Read about our key priorities on the following pages:

**Priority #1**  
**Further enhance our differentiated food proposition**

Read more on **page 15**

**Priority #2**  
**Grow General Merchandise & Clothing and deliver synergies**

Read more on **page 18**

**Priority #3**  
**Diversify and grow Sainsbury's Bank**

Read more on **page 20**

**Priority #4**  
**Continue cost savings and maintain balance sheet strength**

Read more on **page 22**



**18%**

of Group sales at peak times now originate online and our strength in digital, combined with Argos's leading delivery services, including *Fast Track*, will enable us to grow both now and in the future and give us a crucial competitive advantage.



In September we launched our **On the Go** range of breakfast, lunch and snacking lines



We launched our **Deliciously FreeFrom** range reflecting the increasing importance of allergen-free food to customers



Our new **same day delivery** service launched from eight London stores



We improved 3,000 Sainsbury's branded products and are now reviewing **125 food categories**, covering around 60 per cent of our range



Our innovative **prepared vegetable range** has been a great success with customers



## Priority #1

# Further enhance our differentiated food proposition

Food will always be at the heart of our business.

We have a strong and differentiated food proposition that offers customers market-leading quality, choice and value. We have now completed our 3,000 Sainsbury's own-brand product quality investment programme and will continue to make quality improvements where they matter most to our customers. Over the course of the next year, we will review 125 food ranges, touching around 60 per cent of our food sales. Customers continue to rank us ahead of our supermarket peers for food quality<sup>1</sup>.

### Great quality at fair prices

Our Food business is resilient. While the grocery retailing market remains competitive, investment in the quality and price of our core *by Sainsbury's* range delivered volume growth of two per cent. Our strategic focus is on growing categories where we can increase market share such as *Deliciously FreeFrom*, our new *On the Go* range and prepared vegetables. In September, we launched our *On the Go* range of breakfast, lunch and snacking lines. It is a market worth around £16 billion and we invested £8 million in our range, introducing new sandwich and bread options, salads and sushi. We also increased the number of breakfast and snacking options on offer, as well as improving existing lines. Snacking, in particular, has performed well.

The successful launch of our *Deliciously FreeFrom* range reflected the increasing importance of allergen-free food to our customers. Around 25 per cent of the UK population includes free from products in their weekly shop<sup>2</sup>. We have doubled the new range, incorporating fresh, frozen, chilled and ambient lines, offering customers more variety, improved products and market-leading allergen information on the packaging. We also became the only supermarket to offer gluten-free bread freshly baked in our store bakeries. The range has proved very popular and we sell nearly 12,000 loaves a week.

Our innovative prepared vegetable range has been a great success with customers who are increasingly looking for filling, healthy alternatives to carbohydrates and want to introduce more vegetables in to their diet. We responded to last year's demand for courgetti (courgette spaghetti) and boodles (butternut squash noodles) by introducing eight more prepared vegetable lines this year, including first-to-market vegetable lasagne sheets and butternut squash waffles. These innovative new lines have helped drive double-digit year-on-year growth for the prepared vegetables category.

We continue to develop our overall food offer to ensure customers can buy great quality food at Sainsbury's for different shopping missions. Our in-store sushi concessions are all performing well and offer customers something new to try when they visit our stores.

As a major retailer, in a highly competitive industry, our values make us different and make strong commercial sense. Our values help us strengthen relationships with all our stakeholders, build trust, reduce operating costs, mitigate risks and attract and retain talent in a crowded marketplace. Our values also enable us to play a leading role in tackling some of the challenges facing our customers every day such as household food waste.

To help our customers live healthier lives we have reduced the sugar in our cereal range by an average of 13 per cent, exceeding the Government's 2017 targets of a five per cent reduction. We also removed more than three tonnes of salt from our canned corned beef products without impacting taste or flavour.

All our products are *sourced with integrity* and this year we were proud to be named the World's Best Sustainable Seafood Supermarket by the Marine Stewardship Council. We sold over £490 million of RSPCA-assured products this year and worked with our Dairy Development Group to reduce the need for certain classes of antibiotics, leading to a voluntary withdrawal.

<sup>1</sup> HPI Brand & Communications Tracker.  
<sup>2</sup> Kantar Worldpanel, 2016.

### Product quality

We know customers value quality when deciding where to shop and it is therefore important for us to be ranked above our peers in relation to the quality perception of our brand.

**Definition:** Our rank is based on a sample of approximately 1,000 consumers who rated the product quality of Sainsbury's, Tesco, Morrisons and Asda.



Source: HPI Quality Survey

### Price perception

Our new pricing strategy of regular lower prices reassures customers that they can always get a good price, on and off promotion.

**Definition:** See above.



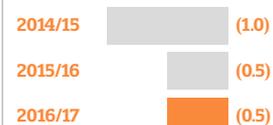
Source: HPI Price Perception Survey

### Sales growth – Food

Food is our core business but growing our Clothing, General Merchandising and Financial Services businesses is an important part of our strategy. We know that our customers value greater choice and that there is a firm correlation between increased loyalty and spend across our whole offer when customers buy into these categories.

**Definition:** Year-on-year growth of total sales, including VAT.

### Food (%)



Demonstrating our *respect for our environment* we now use nearly 12 per cent less electricity than we did in 2005, despite growing store space by over 54 per cent. Also since 2005, we have reduced packaging across Sainsbury's branded ranges by almost 33 per cent and we continue to work towards our target of a 50 per cent reduction by 2020. This year marked a significant milestone on food waste, as we moved to transparent reporting – one of only two major retailers to do so and we have set a clear benchmark against which we can measure progress. We completed a trial of *Waste less, Save more*, our five-year initiative to help our customers tackle household food waste in Swadlincote, Derbyshire, with 20 intervention trials. These trials ranged from apps to weigh and report on food waste to pioneering school programmes to engage young people on the issue.

In addition to providing excellent customer service, our colleagues are committed to *making a positive difference to our community*. In 2016/17, we generated over £53 million for charities through the efforts of our colleagues and customers. This includes nearly £12 million raised through our support of Comic Relief's Red Nose Day.

We aim to be a company where people love to work and our colleagues are integral to the success of our business. We offer a competitive rewards package, including paid breaks, colleague discount and pension. This year, colleagues across the Group will share a bonus of £78 million.

### Serving customers whenever and wherever they want

A key part of our strategy is to be available to our customers whenever and wherever they want to shop with us. As at the end of this financial year we have 605 supermarkets and 806 convenience stores<sup>3</sup>. Supermarket sales declined nearly two per cent and sales at our convenience stores grew by over six per cent.

Supermarkets continue to be the main grocery shopping channel, responsible for over half of the grocery spend in the UK, and we expect this to remain the case. We are adapting our space and layouts to reflect customer requirements for convenience, flexibility, speed and choice. Supermarket shoppers can take advantage of extensive food ranges, Grocery Click & Collect services and in-store cafes and restaurants.

Our Convenience business grew by over six per cent and we opened 41 new shops including trials of seven franchises in Euro Garages' petrol station forecourts.

Sales in our Groceries Online channel grew by over eight per cent and orders increased by nearly 12 per cent during the year. We deliver around 276,000 orders per week. We expect that demand for our online grocery service in London will double over the next eight years and to help meet that growing demand we opened our first purpose-built online fulfilment centre in Bromley-by-Bow, East London. With its cutting-edge technology, it has the capacity to fulfil 25,000 customer orders each week. We now have 151 Groceries Online Click & Collect sites and a growing number of our customers place their order online and collect their shopping at their local supermarket. To add to customer choice, we offer same-day delivery from 29 stores across the UK and are trialling one hour delivery to over 40,000 London postcodes through our Chop Chop bicycle delivery service. We introduced our Groceries Online app in 2016 to give customers more ways to shop with us. Penetration is steadily increasing, with over ten per cent of orders received through the app, demonstrating the rapidly changing nature of customer shopping behaviour.

### Leading customer service

Our colleagues continue to deliver market-leading customer service and we won 17 weekly Grocer 33 Awards this year<sup>4</sup>. In addition, for the past four years we have won the Grocer Gold Awards for Service and Availability and we continue to exceed our Mystery Shopper internal targets.

<sup>3</sup> The number of convenience stores stated includes our partnership with Euro Garages.  
<sup>4</sup> Grocer 33 for 52 weeks to 11 March.

### Availability

Offering our customers the products they want ensures they have a good shopping experience. This makes availability very important. We measure availability daily and have a minimum standard we expect to achieve.

**Definition:** Minimum standards have been exceeded.

| 2015/16           | 2016/17           |
|-------------------|-------------------|
| Supermarkets<br>✓ | Supermarkets<br>✓ |
| Convenience<br>✓  | Convenience<br>✓  |
| Online<br>✓       | Online<br>✓       |

### Sales growth

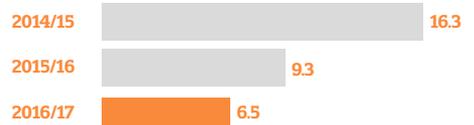
Customers are choosing to shop across channels and are using convenience and online more frequently, leading to a decline in supermarket sales. It is therefore important that we invest strategically so that we can serve our customers whenever, however and wherever they want.

**Definition:** Year-on-year growth of total sales, including VAT, excluding fuel.

#### Supermarkets (%)



#### Convenience (%)



#### Online (%)



### Customer service

Our colleagues make the difference by delivering great customer service. We monitor this every fortnight with a Mystery Shopper programme which measures the service level of the three main components of the customer shopping experience.

**Definition:** Minimum standards have been exceeded in all three of the main components of the customer shopping experience.

| 2015/16                     | 2016/17                     |
|-----------------------------|-----------------------------|
| Supermarkets<br><b>Gold</b> | Supermarkets<br><b>Gold</b> |
| Convenience<br><b>Gold</b>  | Convenience<br><b>Gold</b>  |

Source: ABA



Our new **Groceries Online app** now accounts for ten per cent of orders via our Groceries Online channel



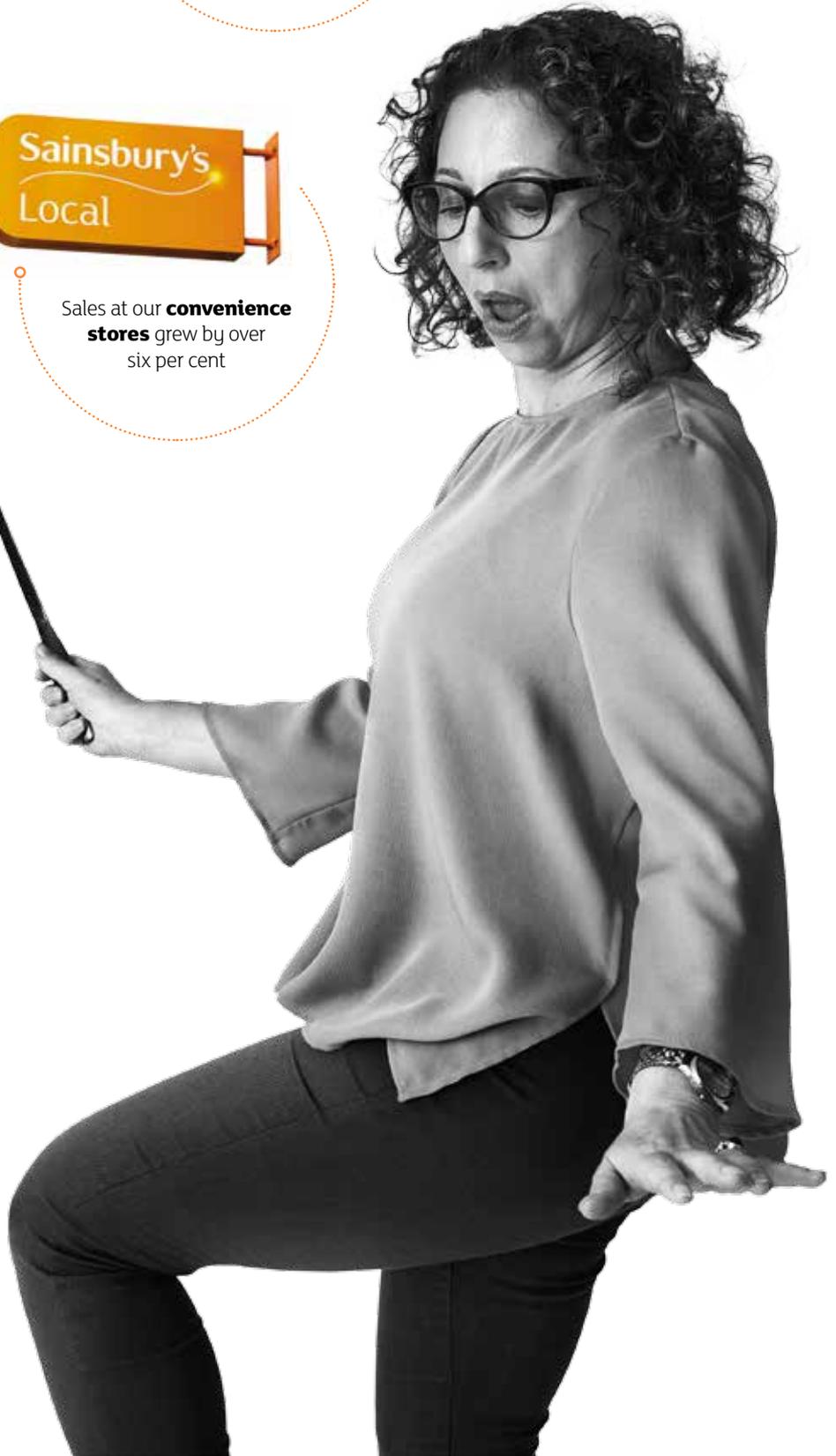
Our colleagues continue to deliver market-leading **customer service**



Sales at our **convenience stores** grew by over six per cent



**Supermarkets** continue to be the main grocery shopping channel



## Priority #2

# Grow General Merchandise & Clothing and deliver synergies

### General Merchandise

Sainsbury's General Merchandise sales grew by over two per cent. We increased our market share by both volume and value driven by seasonal events such as Christmas and Halloween by offering design-led, ethically-sourced homeware products that are accessible to everyone. The ranges are updated every eight to ten weeks, at prices that are significantly better value than high street stores and homeware specialists. On-trend, in-house designed ranges and classic designs such as Harvest, Shore and Blue Daisy, displayed in an attractive department store-style setting, have proved to be very popular with our customers.

### Clothing

Shopping for clothing in supermarkets has become firmly established and our strategy of offering customers high street style at supermarket prices has helped to increase our sales by over four per cent in the year and to outperform a challenging market. Eight million customers buy our *Tu* clothing. Our market share by volume increased by 20 basis points and we are the sixth largest clothing retailer by volume in the UK<sup>5</sup>, with a strong position in the womenswear and childrenswear markets and opportunities for future growth in menswear.

We launched our *Tu Premium* womenswear collection in September, offering our customers quality styling and fabrics that rival high street fashion brands, at significantly lower prices. The range has been well received by our customers with standout performers such as our women's leather biker jacket at £95 and a silk blouse at £30.

<sup>5</sup> Kantar Worldpanel.

### Acquisition of Home Retail Group plc

Our acquisition of Home Retail Group plc in September 2016 created a £6 billion General Merchandise and Clothing business. This made us one of the UK's largest food, general merchandise, clothing and financial services retailers, with over 90,000 products across 2,200 stores. The deal was financially compelling and makes clear strategic sense.

Argos is the UK's number one retailer for toys and a market leader in homeware and electrical products. With around one billion hits a year, Argos is the third most visited retail website in the UK and over half of all Argos's sales originate online. The first UK retailer to achieve £1 billion annual sales online, Argos was also the first to achieve £1 billion sales through mobile devices. The unique Hub and Spoke supply chain network offers customers a wide choice of quick, efficient delivery options – Fast Tracked to their home the same day, or for collection at Argos and participating Sainsbury's stores.

Argos is performing well both commercially and operationally, with strong results during the Black Friday and Christmas periods. With 10 million webpage visits on the day, 65 per cent of Black Friday sales were initiated online. Nearly 100,000 *Fast Track* deliveries were made over that weekend alone. There were over 120 million visits to the Argos website in the run up to Christmas, an increase of over nine per cent.

There are now 59 Argos Digital stores in our supermarkets and they are performing well. Sales at stores that have been open for over a year are delivering like-for-like sales growth of between 20 to 30 per cent. There is also a clear sales uplift of between one to two per cent in Sainsbury's stores where there is an Argos Digital store.

Customer satisfaction scores at our Argos stores are at their highest levels ever and digital remains a key differentiator. In 2017/18 we plan to transform 60 existing Argos high street stores to a new digital format, meaning that over a third of the Argos store estate will be digital in a year's time.

We also have 207 digital collection points where customers can collect their *Tu* clothing, eBay and DPD orders conveniently. Over 700,000 parcels have been collected to date. Argos orders can be collected at 90 of these collection points.

We now have seven Mini Habitat stores to date in Sainsbury's supermarkets, to support Habitat's multi-channel business strategy.

### Synergies

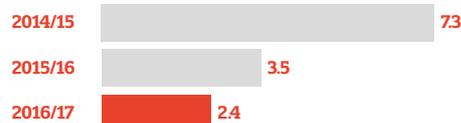
The opportunity to deliver £160 million of EBITDA synergies over three years was a key factor in our decision to acquire Home Retail Group plc. The synergies identified at the time of the deal included the integration of central and store support functions across the two businesses, as well as cost savings from opening Argos Digital stores in Sainsbury's supermarkets. This year we have achieved £7 million of synergies. The integration of Argos and Sainsbury's is happening at pace. Our retail expertise and experience of delivering change programmes in our stores has enabled us to accelerate the roll-out of 250 Argos Digital stores in Sainsbury's supermarkets. We now expect this roll-out, together with our £160 million synergy target, to be achieved by March 2019, six months ahead of schedule.

### Sales growth

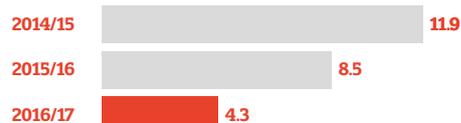
Food is our core business but growing our General Merchandising, Clothing and Financial Services businesses is an important part of our strategy. We know that our customers value greater choice and that there is a firm correlation between increased loyalty and spend across our whole offer when customers buy into these categories.

**Definition:** Year-on-year growth of total sales, including VAT.

#### General merchandise (excluding Argos) (%)



#### Clothing (excluding Argos) (%)



#### EBITDA Synergies (£m)





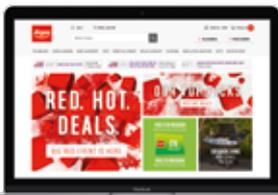
#1 for toys and a market leader in homeware and electrical products



We are now a multi-product retailer, offering customers over **90,000** products across a diverse range of categories



Clothing business continues to grow and we **launched Tu Premium**



Digital is a key differentiator and **18 per cent of Group sales** are now online during peak periods



**Admiral menswear** performed well reflecting the strong trend for wearing casual sports clothing





Strong growth in **cards, loans** and **travel money**



Launch of **mortgages** and new **insurance broker model**



Sainsbury's Bank has seen a **four per cent** increase in customer numbers taking the total to **1.8 million** active customer accounts



70 per cent growth year-on-year in **new card accounts** and a six per cent year-on-year increase in cards being used in Sainsbury's



## Priority #3

# Diversify and grow Sainsbury's Bank

Sainsbury's Bank is a growing and profitable part of our business and a key strategic asset.

Our vision is to be the destination bank for Sainsbury's customers, listening to what they want and designing products, offers and services that meet their needs. We recently launched an innovative mortgage product, which introduced a money off reward on shopping, and is a strong channel to grow our assets and customer base in both mortgages and savings.

Offering our customers complementary financial services products encourages loyalty across all our businesses – when customers take out a Bank product we see that they go on to spend more with us. Since taking full ownership of Sainsbury's Bank, we have embarked on a programme to transition our banking services on to our own infrastructure. We successfully migrated savings customers and ATMs to our new banking platforms during the year. We continue to make good progress and will introduce our new loans platform by the end of 2017.

Sainsbury's Bank, including Argos Financial Services, achieved £62 million underlying profit. Sainsbury's Bank profits declined nearly five per cent due to the impact of reduced interchange fees and investment required to enter the mortgage market.

Sainsbury's Bank has 1.8 million active customers, up nearly four per cent. Additionally, Argos Financial Services has 1.8 million customers. We take our responsibilities as a lender of consumer credit very seriously and saw strong growth in personal lending, with ten per cent year-on-year growth in the number of advances to new personal loan customers.

We offered Sainsbury's customers a strong range of credit cards throughout the year with the incentive of additional Nectar points. This resulted in a 70 per cent growth year-on-year in new card accounts and a six per cent year-on-year increase in our credit cards being used in Sainsbury's stores. We are regularly featured as a best buy credit card throughout the year.

In line with our strong lending performance, savings accounts grew by almost 60 per cent year-on-year with a strong performance across fixed term, easy access and ISA products.

Our growth in customer lending and continued investment in the transition programme saw our Tier 1 capital ratio decrease to 13.3 per cent which remains comfortably above regulatory requirements. Capital and liquidity plans are robust and support future growth in secured and unsecured lending.

In the last quarter, we launched new home and car insurance products. Our new products provide quotes from a bespoke panel of specially selected insurers, giving a greater number of Sainsbury's customers more competitive pricing. In addition, we are rewarding Nectar card customers with a guaranteed discount on their insurance premium.

We saw strong growth in travel money with transactions up 25 per cent year-on-year, despite market volatility and the impact of the vote to leave the European Union. We opened a further 26 Travel Money bureaux across the UK, taking our estate to 232 bureaux. We have also successfully launched our new pre-paid travel money card which offers contactless functionality and no ATM fees.

Our 'free-to-use' ATM estate grew by five per cent to 1,728 in the year and ATM transactions grew by almost one per cent year-on-year to nearly 240 million. This represents a significant UK market share with £1 for every £11 dispensed from a LINK ATM transaction coming from Sainsbury's Bank.

In September 2016 the Bank played a key role in the acquisition of Home Retail Group plc, successfully detailing full UK Regulatory permission and expanding the Bank's savings portfolio which provided around £500 million of funding for the transaction. The integration of Sainsbury's Bank with Argos Financial Services will be phased, initially integrating certain reporting and governance capabilities. The planned nature, depth and pace of integration is expected to evolve within the Bank's strategy during the 2017/18 financial year.

The acquisition of Argos Financial Services presents significant operational synergies. Argos Financial Services manages an existing store card estate which we will leverage by moving our credit cards onto the same platform. This will take place during the summer of 2018.

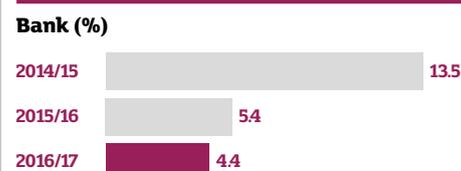
Sainsbury's Bank is committed to delivering customer service that is convenient, reliable and helpful. Our website receives over 1.9 million visits every month, up 50 per cent year-on-year. We continue to report industry-low levels of customer complaints, consistently recording fewer than 1.3 complaints per 1,000 customer accounts over the last two years. We have won industry awards for customer service and quality of our products including Best Balance Transfer Credit Card (The Personal Finance Awards), Best Online Personal Loan Provider (Your Money) and Trusted Personal Loan and Pet Insurance provider (Moneywise Customer Services).

We continue to invest in Sainsbury's Bank and will inject further capital for lending growth, increased regulatory requirements and to complete the Bank's ongoing transformation.

### Sales growth

Food is our core business but growing our General Merchandising, Clothing and Financial Services businesses is an important part of our strategy. We know that our customers value greater choice and that there is a firm correlation between increased loyalty and spend across our whole offer when customers buy into these categories.

**Definition:** Year-on-year growth of total sales, including VAT.



## Priority #4

# Continue cost savings and maintain balance sheet strength

In line with other UK retailers, we anticipate that cost pressures will continue over the next few years – the price of raw materials and energy is increasing, along with wages and business rates.

Across our business we are focused on finding ways to mitigate the impact of rising costs so that we can continue to deliver for customers, colleagues and shareholders.

We continue to find ways to simplify our business and reduce costs. We have achieved £130 million of cost savings this year, £355 million in the last two years, and by the end of 2017/18 we will have delivered our target of £500m of cost savings over three years across our business. We are committed to a further £500 million cost savings over the next three years, starting in 2018/19.

Our focus on efficiency and cost reduction will allow us to continue to invest in the value of our proposition and the development of our colleagues as well as provide our shareholders with a return on the investment they have made in Sainsbury's.

### Sainsbury's food and grocery operations

Over the last three years we have made significant progress in developing our food and grocery proposition. We have simplified our prices and replaced multi-buys with lower regular prices – helping customers avoid waste at home and enabling us to forecast demand more accurately. We have invested in the quality of over 3,000 Sainsbury's branded products and shortened the time it takes to get innovative new food ranges on to our shelves. We source directly from farmers and growers and use cutting-edge technology to forecast demand to give our food extra shelf life. We have also invested in our ranging strategy and tools

to bring greater incremental choice and quality into each of our stores, while reducing duplication and products previously on multi-buy or high-low promotion. Changes we have made to our in-store operating model have helped to reduce costs throughout our store estate.

As retailers we must continually respond to the changes in the way people shop and continue to identify how we can meet our customers' needs while also achieving our cost savings target. We have identified a number of areas where we believe we can deliver significant savings at pace. These include:

- Improving product availability throughout the supply chain
- Making our checkouts more efficient, easier and faster to use
- Using improved technology to eliminate unnecessary complexity in some aspects of the in-store experience, making it faster and more efficient for both customers and colleagues
- Simplifying our offer so that we can deliver the food and groceries our customers want, whenever and wherever they want them

These are all areas we can address with agile solutions that we can test and deliver at pace, using technology whenever possible. In whatever we do, our colleagues and customers will remain firmly at the forefront of our thinking.

### Balance sheet strength

Our balance sheet remains strong with a significant reduction in net debt and high levels of liquidity. We have reduced net debt by £349 million in the year to £1,477 million. The reduction is as a result of continued strong cash generation from our retail operations, the financing of the acquisition of Home Retail Group plc and further working capital improvements, offset by exceptional pension payments, capital expenditure and dividends. Group core retail capital expenditure of £547 million was in line with last year (2015/16: £542 million), even with the addition of Argos core retail capital

expenditure of £38 million. However, in line with our strategy, this is significantly lower than the average capital expenditure in the previous five years of £931 million.

The Group has financing facilities of £3.9 billion, of which only £2.7 billion was drawn at the year-end. These are from diverse funding sources in order to minimise refinancing risk and to maintain appropriate contingent liquidity. We have also concluded the Sainsbury's pension scheme triennial valuation and recovery payments will increase by £6 million to £84 million per year. As part of the acquisition of Home Retail Group plc, we will also be paying recovery payments of £40 million per year to the Home Retail Group plc defined benefit pension scheme until October 2021.

The Board has recommended a final dividend of 6.6 pence per share (2015/16: 8.1 pence), making a full-year dividend of 10.2 pence per share (2015/16: 12.1 pence), covered two times by underlying earnings, in line with Sainsbury's policy to pay an affordable dividend. Over the last five years Sainsbury's has paid a total dividend of 69.5 pence per share, returning over £1.4 billion of cash to shareholders.

### Like-for-like transactions

The structural change in the market means that customers have more choice than ever when it comes to doing their grocery shopping. This means that like-for-like transactions are at risk and we need to ensure that we execute our strategy effectively. Customers will then continue to see that we offer great products at great prices.

**Definition:** Year-on-year growth in transactions from stores that have been open for at least a year.

### Like-for-like transactions (%)

|         |     |
|---------|-----|
| 2014/15 | 0.0 |
| 2015/16 | 0.3 |
| 2016/17 | 1.3 |

**£349m**

We reduced net debt by £349 million to £1,477 million



Reduction in spend on property in favour of **digital** and **IT infrastructure**



The Group has **financing facilities of £3.9 billion**, of which only £2.7 billion was drawn at the year-end

**£500m**

On track for **£500 million** cost savings by 2017/18. Committed to a further **three-year reduction** of £500 million from 2018/19



# Our values make us different

In a highly competitive industry, where price can often dominate the conversation, our values differentiate us from our competitors, strengthen our relationships with suppliers, colleagues and other stakeholders, and provide guiding principles that enable our teams to do their best work.

To achieve our vision to be the most trusted retailer, where people love to work and shop, at a time when trust in business and institutions is generally low, our values are more important than ever. We must live up to them through the choices we make across our business, so that we can play a leading role in tackling some of the challenges facing households and society.

For example, we are transparent about our economic contribution to the UK, such as how much tax we pay, as well as how much we pay our colleagues. In 2016/17, we paid £1.9 billion<sup>1</sup> in tax and were ranked 7th for taxes borne in the PwC 2016 Total Taxes Contribution survey of the 100 Group. We also want to help our customers to live well for less – whether that is through providing solutions for how to live a healthier life, and waste less food, or by playing our part in helping the UK become a better place to work and live.

As well as building trust among our customers, our Sustainability Plan drives efficiencies and helps us reduce our operating costs, for example, by using less electricity and natural resources. It is also one of the ways that we manage risk across our business. For example, elements of our Sourcing with integrity commitments help us to protect security of supply of key raw materials at risk due to climate change

affecting our global supply chain. We know that our commitment to sustainable business and our values helps us to attract and retain top talent too – according to our 2016/17 Talkback survey, 80 per cent of colleagues trust us to do the right thing for the world we live in.

Our Sustainability Plan publicly sets out our ambitions across our values, and provides the measurement framework to track our progress. Also, by supporting the UN Sustainable Development Goals, we aim to contribute to the creation of a fairer, more sustainable and prosperous society – in the UK and internationally in places where our business can make a positive difference.

Following the acquisition of Home Retail Group plc – owner of Argos and Habitat – in September 2016, we have begun work to develop an integrated Sustainability Plan for the new Sainsbury's Group. As this work is still underway, the information on the following pages focuses on the progress Sainsbury's has made against our existing Sustainability Plan. We are working to review targets and programmes across our business and will share further details in the coming year.

<sup>1</sup> During the year ended March 2017 the Sainsbury's Group (including HRG companies post acquisition) paid £1.9 billion (2015/16: £1.7 billion) to the UK Government, of which £927 million (2015/16: £890 million) was borne by Sainsbury's and the remaining £1 billion (2015/16: £822 million) was collected on behalf of our colleagues, customers and suppliers.

“

**Our values are the thread running through every part of our business. Whether it's making it easier to choose healthier products, or saving money and reducing food waste at home – we're always looking for ways to make life better for our customers while also doing the right thing for our colleagues, shareholders, the planet and society.”**

**Mike Coupe** Chief Executive Officer, J Sainsbury plc

## 50

Our key suppliers, producers and more than 50 independent organisations have been involved in the peer review of sustainability standards for our key raw materials.

**i** Read more on **page 30**

## 80%

80% of our colleagues trust us to do the right thing for the world we live in



# Find out more about our values



**Making a positive difference to our community**

page 28



**Sourcing with integrity**

page 30



**Respect for our environment**

page 34



**Living healthier lives**

page 26



**A great place to work**

page 38





We want to help our customers to live well and living well starts with eating well.

More than half of adults in the UK are overweight or obese, increasing their risk of a range of health problems, including heart disease, diabetes and stroke.

As one of the UK's leading food retailers, we have an important role to play in providing customers with healthy, accessible food options that fit in with their lifestyles and their budgets.

We offer a wide range of healthy and nutritious food products, created by a team of dedicated product developers, product technologists and registered nutritionists. We continually reformulate our own-brand products to make them healthier and we aim to make it easy for our customers to make the right choices for them by offering a varied range of products, including many appealing options for those with allergies and intolerances. We also make it easier for customers to add more fruit and vegetables in their diets through product innovation and inspire kids to get active and lead healthier lives through our Active Kids scheme.

We engage our suppliers in our approach on health, for example through training and articles in our *Working Together* magazine.

We have always led the way in helping our customers make informed healthier choices. We were the first UK food retailer to introduce front of pack traffic light labelling in 2005 and one of the first retailers to set stretching targets for salt reduction in our own-brand products. Our allergen-free range is clearly colour coded to highlight the allergens that they are free from. In 2014, we became the first UK retailer to include calorie labelling on our own-brand alcohol products, along with clear and consistent front of pack alcohol by volume (ABV) on our own-brand wine.



£173m

invested in activities for kids of all abilities since 2005

## Our commitments

**Our customers can trust that they can always choose nutritious and healthy food when they shop with us.**

| What we'll do  | How we measure our progress  | 2015/16 | 2016/17 | 2020 target |
|--|--|---------|---------|-------------|
| We'll improve the healthy balance of our customers' food baskets | Healthy products sold as a proportion of total sales volume <sup>1</sup> | 41%     | 42%     | 45%         |

<sup>1</sup> We measure this through the proportion of products in our customers' baskets that are defined as healthy based on the product's multiple traffic light (MTL) ratings around salt, sugar, fat and saturates.

We reformulate our products to reduce salt, sugar, fat and saturated fats. This year, we removed more than three tonnes (over 700,000 teaspoons) of salt from our canned corned beef products to meet the Government's 2017 salt targets without impacting taste or flavour. Our own-brand breakfast cereal range was reformulated to meet the 2017 Public Health England guidelines on sugar and salt reduction: they now meet the average 2017 salt targets, with 100 per cent below the maximum target. We have reduced sugar across the range by an average of 13 per cent, exceeding the Government's 2017 targets of a five per cent reduction. We have also removed all illustrated characters from our breakfast cereal range as part of our commitment to responsibly market products to children.

In addition to the 37 tonnes of sugar we removed from our own-brand fruit yogurts range in 2015, we removed 36 tonnes of sugar from our *Taste the Difference* yogurts and other own-brand yogurt products, representing a reduction of up to nearly 20 per cent across these products.

We changed the recipe for our in-store doughnuts and cookies, removing 75 tonnes of sugar and 204 tonnes of fat, including 70 tonnes of saturated fat, and a potential 1.5 billion calories from customer baskets. Our cafés now use semi-skimmed milk in our hot and cold beverages, unless the customer specifically requests whole milk, potentially saving a further 58.5 tonnes of fat and 0.5 billion calories annually from customer diets.

Many of our customers suffer from food allergies, but do not want to miss out on healthy and tasty food choices. In 2016/17, based on customer feedback, we improved and doubled our allergen-free range, re-branding it as *Deliciously FreeFrom*. The new product range uses market-leading product innovation to offer 97 allergen-free options, from everyday staples like bread to treats such as cakes and cookies. We also launched white and seeded gluten free bread batons, farmhouse loaves and rolls baked fresh in our stores – a result of a long and intense product development process.

We offer prepared vegetable products that not only make it easier for customers to eat more vegetables, but also help them save on cooking time. We have introduced courgetti, butternut squash boodles, cauliflower rice as well as butternut squash and courgette lasagne sheets. We added new product lines in 2017, including butternut squash waffles and sweet potato tagliatelle. Our broccoli rice and boodles not only taste great but help us reduce food waste by using up more of every vegetable and making use of wonky veg too (see page 33).

## We will encourage kids to live a healthy, balanced lifestyle.

| What we'll do   | How we measure our progress                | 2015/16 | 2016/17 | 2020 target |
|---|--|---------|---------|-------------|
| We'll continue to develop our Active Kids scheme, investing £200 million <sup>1</sup> in activities for kids of all abilities | Total investment in our Active Kids scheme | £161m   | £173m   | £200m       |

<sup>1</sup> Target to invest £200m between 2015 and 2020.

At the heart of the UK's obesity crisis lies the concerning statistic that in the UK, by the time children leave primary school, one in three is overweight and one in five is obese.

Our commitment to helping children to lead healthy, active lives is well known – we have been encouraging children, regardless of ability or impairment, to get active and lead healthier lives for the last 11 years with our Active Kids scheme. The initiative emphasises both calories in and calories out, helping children to understand the importance of diet and exercise. We use cooking competitions, teacher training, ambassador endorsements and education campaigns to inspire kids to eat and live well. Through Active Kids, schools and community clubs can redeem Sainsbury's Active Kids vouchers in return for sports and cooking equipment and experiences.

In 2016/17, we introduced the Active Kids Paralympic Challenge, which offered specialist sports equipment to more than 8,000 schools to get kids to try four Paralympic sports. We also published research into the barriers faced by 11-14 year olds that prevent them from leading healthier lifestyles.



# 36

We removed **36 tonnes** of sugar from our *Taste the Difference* yogurts and other own-brand yogurt products



We have doubled our allergen-free *Deliciously FreeFrom* range.

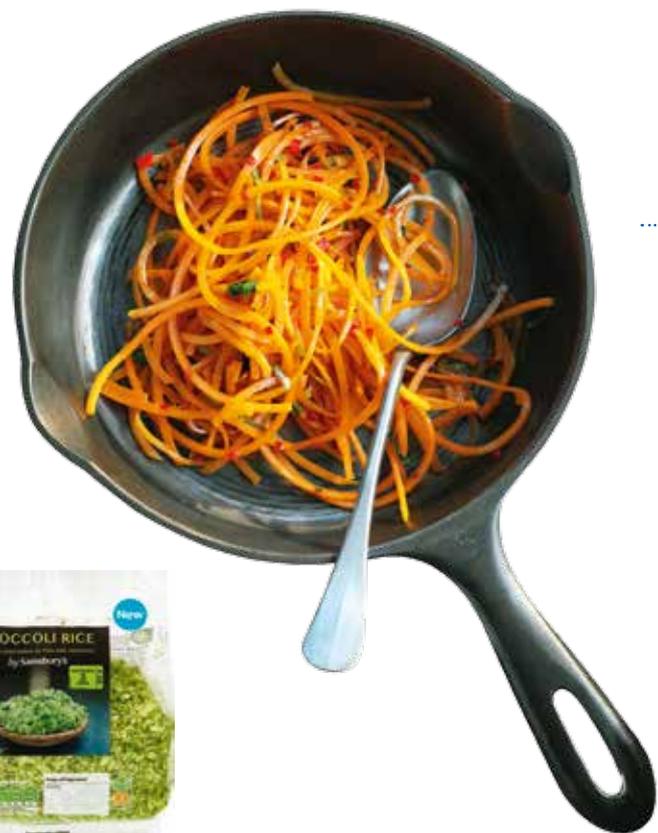
Our prepared vegetable range, including butternut squash waffles, sweet potato tagliatelle and broccoli rice, helps customers to eat more vegetables and save on cooking time, while also enabling us to make the most of products that might otherwise have gone to waste.

## boodles

made from butternut squashes that we would otherwise not be able to sell.

## broccoli rice

uses 20 per cent stalk and 80 per cent floret – saving 42 tonnes of product that would have gone to waste.





## Making a positive difference to our community

Our stores are at the centre of local communities, helping customers live well for less. But our support goes beyond what we sell. Our colleagues help us build meaningful relationships with our customers and communities, positively impacting those in need through fundraising, volunteering, donations and by building awareness.

In 2016/17, we generated over £53 million for charities, communities and good causes<sup>1</sup>. Our longstanding national partnerships with Comic Relief and The Royal British Legion helped us engage our customers to give to good causes. We improved the way customers vote as part of our Local Charity of the Year programme, and saw a dramatic increase in participation. Our award-winning Payroll Giving systems made it easy for our colleagues to donate to causes they support. We also became an official partner of Oxfam's Emergency Response Network which provides an effective channel through which we can respond to disasters and humanitarian crises around the world.

### Fundraising and volunteering at Argos

During 2016/17, Argos colleagues and customers raised more than £900,000 for Macmillan Cancer Support and the Irish Cancer Society. The funds are being used to help the charities ensure that no one faces cancer alone. As part of our colleagues' contribution, they ran collections in stores and participated in Macmillan's flagship event, the World's Biggest Coffee Morning.



## Our commitments

**We will support our local communities in relevant and impactful ways and donate over £400m<sup>2</sup> to charitable causes by 2020.**

| What we'll do  | How we measure our progress   | 2015/16                            | 2016/17               | 2020 target |
|--|---|------------------------------------|-----------------------|-------------|
| We will continue to develop our Local Charity of the Year programme. | Number of stores supporting their Local Charity of the Year partner through awareness-raising, fundraising and volunteering | 1,240 (90% of stores) <sup>3</sup> | 1,286 (92% of stores) | All stores  |

<sup>1</sup> Includes corporate donations to national charities such as Comic Relief/Sport Relief and The Royal British Legion, funds raised by customers and colleagues in our stores for local charity partners, and investment in community programmes such as Active Kids.

<sup>2</sup> We aim to donate £400m between 2011 and 2020.

<sup>3</sup> As we continue to grow our estate we have moved to include the percentage of stores participating in these schemes, for ease of comparison year-on-year. These numbers reflect local charity partners across our supermarket and convenience stores.

In 2016/17, we generated over £53 million for charities, communities and good causes, through the efforts of our customers and colleagues, taking our total to £265 million since 2011.

The efforts of our customers and colleagues allowed us to support over 3,400 charity partnerships, across Comic Relief, The Royal British Legion and Oxfam, Local Charity of the Year programme and our front and back of store food donation partnerships, delivering much-needed services on a local, national and international level.

Our partnership with Comic Relief raised nearly £12 million for the charity's Red Nose Day campaign this year, supporting their work to help those in need in the UK, Africa and India. We also celebrated 22 years of our partnership with The Royal British Legion (RBL) to support current members and veterans of the forces, raising over £3.1 million. We are the exclusive retailer of RBL poppy seeds to increase the number of wild poppy fields to commemorate the centenary of the end of the First World War in 2018.

Our annual Christmas advertising campaign raised more than £500,000 for the Great Ormond Street Hospital through merchandise sales and customer donations. We engaged 8,000 schools as part of our support for Paralympics GB, donating kits to encourage children to understand and participate in inclusive sports. We also supported Oxfam's disaster relief and humanitarian efforts and were named as an official partner to their Emergency Response Network.

In addition to our national partnerships, we continued to deliver great impact at a local level. Since 2009, we have donated more than £11 million for good causes through our Local Charity of the Year programme. Not only is this hugely beneficial for local communities – this year we expect to raise £2 million for more than 1,200 local charity partnerships – but it is a great engagement tool for customers and colleagues alike. Charities are initially shortlisted by our in-store teams, before the vote opens to customers, colleagues and the wider community. Thanks to refreshed and focused communications, we received an unprecedented 1.9 million votes, an increase of 440 per cent from last year.

To better understand our impact through this programme, we sent a survey to our 2015/16<sup>4</sup> local charity partners. Every Sainsbury's local charity partnership offers a different mix of money, volunteering time, food donations and support as needed. We have carried out research into the social return on our charitable activities and early results suggest that the programme delivered an equivalent of £11 worth of social impact for every £1 of investment. From these initial findings we also know we impacted over 360,000 people, across a variety of causes, including community and neighbourhood and health.

We saw an increase in our colleague volunteering through our Local Heroes programme, which sees us donate £5 for every hour that colleagues volunteer in their own time. This resulted in nearly £76,500 being donated across a broad spectrum of charities and community groups throughout 2016/17. Our colleagues also donated over half a million pounds through the Payroll Giving scheme to support causes they care about. We are delighted that our scheme was externally recognised, with two wins from Payroll Giving Awards, including one for the Most Successful Sustained Scheme, which recognised our 27 years of support. Our colleagues were also recognised for their continued support of Community Alcohol Partnerships to encourage responsible drinking.

<sup>4</sup> We surveyed 2015/16 Local Charity of the Year partners – rather than those taking part in the 2016/17 programme – to gather data from those who had completed a full year's partnership.

“

**Each year, a large number of our poppy collectors are welcomed into Sainsbury's stores across the country, raising money and awareness for our Poppy Appeal and the Legion's work to help the British Armed Forces, younger and older veterans and their families to live on to a more hopeful future. We're thrilled with the high level of support from Sainsbury's and are extremely grateful for our growing relationship.”**

**Claire Rowcliffe**, Director of Fundraising,  
The Royal British Legion

# 3,400

Supporting more than 3,400 charity partnerships



# £12m

nearly £12 million raised for Comic Relief's Red Nose Day campaign

# £53m

over £53 million generated for charities and good causes





## Sourcing with integrity

Our vision is to be the most trusted retailer where people love to work and shop. That means staying true to our values and aligning our strategy with the UN Sustainable Development Goals to ensure we build a business that plays its part for the long term.

Customers care about where products they buy come from and they put their trust in us to make the right decisions on their behalf. This is why sourcing with integrity is key to our work with farmers, growers and suppliers in the UK and around the world. From our Research & Development and Ethical Trade conferences with almost 300 and over 120 attendees respectively, our Farmer Development Groups with almost 2,000 members, our technical director's forum of our 36 top suppliers through to our quarterly digital *Working Together* magazine going out to over 3,500 recipients, we collaborate specifically and engage broadly with a wide network of stakeholders.

In 2016/17, we continued to build on the number of key raw materials that are sourced according to an independent sustainability standard. We were named the Best Sustainable Seafood Supermarket in the world by the Marine Stewardship Council (MSC). We sold more Fairtrade products than any other retailer around the world and we continued to strengthen our measures to prevent the exploitation of vulnerable workers in our extended value chains.

We know much work lies ahead. But we are on track to help our customers, suppliers, farmers and growers live better today, tomorrow and in the future.



**ISEAL's assessment of the Sainsbury's Sustainability Standards programme of work shows positive progress to date, with recommendations for improvement. The Sainsbury's Sustainability Standards programme is now taking steps to achieve full ISEAL membership, with the associated compliance requirements."**

ISEAL Alliance 2017



## Our commitments

**We will source our key raw materials sustainably to an independent standard.**

| What we'll do   | How we measure our progress   | 2015/16   | 2016/17   | 2020 target   |
|---|---|---|---|---|
| Each of our key raw materials is sourced sustainably to an independent standard | Number of key raw materials with sustainability standards   | 20 standards in development   | 35 standards developed  | Independent sustainability standards for all key raw materials                            |
|   | Quantity of raw materials sourced from supply chains working within our independent sustainability standards <sup>1</sup> | To date 13 have been peer reviewed by external organisations and one is currently being piloted | This is in pilot stage. Standards for 31 raw materials have been peer reviewed and one is currently being piloted in Thailand and Belize. Palm oil and timber are independently certified | Sustainability standards in operation in all of the value chains of our key raw materials |

<sup>1</sup> Our focus has been on authoring, securing independent peer reviews and developing self-assessment tools for our standards. We will share our progress as we pilot and roll out across our value chains.

We are committed to sourcing our key raw materials according to independently peer reviewed sustainability standards by 2020. These raw materials are key to our business, have significant social and environmental impacts and matter to our customers and wider stakeholders.

Our approach is to develop our own standards that build upon and give credit to existing independent third-party standards. Standards for 15 raw materials are ready to pilot, in addition to one already being piloted in Thailand and Belize. The remainder are in final stages of development and peer review with our chosen subject matter experts. Our key suppliers, producers and more than 50 independent organisations such as UNICEF, Care International, Ethical Tea Partnership and Solidaridad Network have been involved in the peer review. We are also working with ISEAL, the global Sustainability Standards membership body, to evaluate our standards.

We are working to ensure that our own-brand products do not contribute to deforestation; 98 per cent of the palm oil in our own-brand products is independently certified sustainable, and we are continuing work to certify the final two per cent. In addition, 93 per cent of the wood we use comes from recycled, Forest Stewardship Council (FSC) or Programme for the Endorsement of Forest Certification (PEFC) certified sources with full chain of custody. For palm oil and timber, our goal is to maintain our current performance, address pockets of opportunity and contribute to improving standards. We are also working with our suppliers and external partners to measure and map our soy usage – part of our process to source deforestation-free soy.

### Our own-brand fish will be independently certified as sustainable.

| What we'll do   | How we measure our progress   | 2015/16 | 2016/17 | 2020 target |
|---|---|---------|---------|-------------|
| All the wild caught fish we sell will be independently certified as sustainable | Proportion of wild caught seafood sales which is independently certified as sustainable | 70%     | 79%     | 100%        |
| All farmed fish will be independently certified as sustainable                  | Proportion of farmed seafood sales which is independently certified as sustainable      | 100%    | 100%    | 100%        |

According to the UN Food and Agriculture Organisation, 31 per cent of the world's fish stocks have been fished beyond sustainable limits (SOFIA report, 2016). We want to ensure that customers can enjoy the products we carry with the confidence that they were sourced from sustainable fisheries.

Our goal is to have 100 per cent of our wild caught seafood sales from certified sustainable sources by 2020. We carry over 200 Marine Stewardship Council (MSC) certified seafood products, comprising 79 per cent of our sales currently. In 2017 we were recognised by MSC for being the Best Sustainable Seafood Supermarket in the world, having held the number one spot in the UK since records began in 2010.

We are investing in fisheries improvement projects for wild caught species that are currently outside the MSC programme such as tuna, squid and crayfish. Our farmed salmon and trout are 100 per cent British and 100 per cent assured to RSPCA's welfare standards.

**No.1**



We were recognised by MSC for being the Best Sustainable Seafood Supermarket in the world in 2017, having held the number one spot in the UK since 2010.

### We are committed to selling products that are fairly traded, investing in the sustainability of our suppliers, farmers, growers and workers within our supply chains internationally.

| What we'll do  | How we measure our progress     | 2015/16 (14/15 figures) <sup>1</sup> | 2016/17 (15/16 figures) <sup>1</sup> | 2020 target |
|--|---------------------------------|--------------------------------------|--------------------------------------|-------------|
| We'll continue to grow the sales of fairly traded products in line with the business | Sales of fairly traded products | >£290m                               | >£280m                               | No target   |

<sup>1</sup> 2016/17 Fairtrade sales will be available after Fairtrade's external verification later this year.

Fairtrade products ensure farmers and workers are paid a fair price and receive an additional sum of money paid on top of the Fairtrade minimum price to invest in social, environmental and economic development projects to improve their businesses and their communities.

In 2015/16, we sold over £280 million worth of Fairtrade products, in line with business sales, making us the world's largest retailer of Fairtrade products. Our 100 per cent Fairtrade bananas generate a premium of £4 million per year for farming communities in the Dominican Republic, Colombia, St. Lucia and Ghana.

In addition to Fairtrade, just one of the projects that we are working on with our partners is to improve the livelihoods of small-scale cashew nut farmers in Madagascar. Through our work, farmers have more than doubled the price they receive for their cashew crop. In the factory, the breakage rate has reduced by 36 per cent, resulting in improved quality and better worker bonuses. The first 30 small scale farmers have begun the process to secure land tenure, and we aim to support all associated farmer groups through the life of the project.

In December 2016, as part of our work to tackle modern slavery, we launched new training for our British farmers and growers to identify vulnerable or exploited workers. It follows a successful pilot with our egg farmers to identify and address criminal or exploitative activities. We also hosted our third annual Ethical Trade conference for over 120 of our key suppliers and stakeholders, which included a focus on the Modern Slavery Act and its reporting requirements. For more information, read our 2016/17 Modern Slavery Statement.



**98%**

of the palm oil in our own-brand products is certified sustainable.

## We will invest in the future of British farming and be the leading retailer for British produce.

| What we'll do   | How we measure our progress  | 2015/16 | 2016/17         | 2020 target   |
|---|--|---------|-----------------|---|
| We'll continue to work with our farmer and grower development groups to help them increase productivity, whilst reducing their environmental impact | Number of R&D projects (participation either as a project lead or partner)             | 48      | 28 <sup>2</sup> | A fully developed portfolio of British farming R&D which delivers against strategic priorities, informed by the Food & Farming Strategy, and fully integrated into the total supply chain |
|   | Value of investment for projects involving Sainsbury's in British farming <sup>3</sup> | >£10m   | >£9m            |   |

<sup>2</sup> The value of investment over the lifetime of multi-year projects.

<sup>3</sup> Due to the multi-year nature of R&D projects and funding cycles we would expect the number of projects to fluctuate year-on-year.

Our own research has shown that supporting local, British producers is important to UK consumers. We work to offer consumers a wide selection of British products and partner with British farmers and growers to improve their productivity, while reducing their environmental impacts.

For example, we have worked closely with our farmers to make the most of the lambing season, and source 100 per cent British lamb in the British season. We are also the UK's largest retailer of English apples and pears.

Our farmers and growers are our partners; investing in their business benefits us too. We have invested in 28 Research & Development projects with a value of more than £9 million, focused on improving agricultural productivity and reducing the environmental impacts of British farmers. Through the year, we facilitated several farmer workshops, including 27 regional workshops for our Beef and Dairy Development Groups focused on soil health. Our annual farming conference focused on how farmers could use data to improve productivity and support animal welfare.

We also continued working with our Sainsbury's Dairy Development Group (SDDG), which was set up in 2007 with the more than 270 farmers who supply 97% of our *by Sainsbury's* own-brand milk, to improve herd health and efficiency, and reduce costs in our milk supply chain. The SDDG operates under a cost of production model, which was voted for by the majority of our farmers. It sets the price Sainsbury's pays for milk independently. The model was introduced in 2012 and ensures that our SDDG farmers receive a fair price for their milk. The overall goal of the group is to work in partnership with our dairy farmers to deliver a sustainable sourcing model that drives production efficiencies through improved animal welfare and reduced environmental impact.

We want to support the next generation of farmers. Our Farm Tech scholarship, delivered in partnership with Imperial College, is one of the first of its kind for a retailer. It helps our farmers and growers learn from experts and share best practice with each other. Twelve new apprentices joined Sainsbury's Agriculture and Horticulture apprenticeship scheme this year. The apprentices will gain practical experience at Reaseheath College before they seek opportunities within our grower and farmer base. We also sponsored Open Farm Sunday, which is managed by Linking Environment and Farming (LEAF), an organisation that promotes sustainable agriculture, food and farming. We worked with nine key farms to invite members of the public to learn about our good agricultural practices and sourcing criteria.

## Our meat, poultry, eggs and dairy products will be sourced from suppliers who adhere to independently verified higher animal health and welfare outcomes.

| What we'll do  | How we measure our progress  | 2015/16                                    | 2016/17                                    | 2020 target                                 |
|--|--|--|--|---|
| Our meat, poultry, eggs and dairy products will be sourced from suppliers who adhere to independently verified higher animal health and welfare outcomes | Proportion of sales from independently verified higher animal health and welfare outcome sources | Poultry – 13%<br>Egg – 100%<br>Veal – 100% | Poultry – 12%<br>Egg – 100%<br>Veal – 100% | Poultry – 100%<br>Egg – 100%<br>Veal – 100% |

Animal welfare is important to our customers and it is important to our business. High standards of animal welfare are good for animals and farm productivity and what is expected in our products.

We work hard to raise health and welfare standards in partnership with leading experts across our supply chains and offer the widest range of higher welfare food and cosmetics products of any retailer. In 2016/17, we sold over £490 million worth of RSPCA assured products, and in 2016 we had more RSPCA assured products on shelf than any other UK retailer. We were the first major supermarket to only sell cage-free fresh eggs in 2009. This winter, some of our free-range poultry, which includes chicken and turkey, were temporarily housed in barns to protect them from avian flu following guidance from Government and industry bodies.

We monitor health and welfare measures at abattoirs across all meat species and we are working to further measure on-farm health and welfare outcomes through our sustainability standards. Our Dairy and Cheese Development Groups are independently audited for compliance with our Higher Herd Health standard. Our chickens and turkeys have health and welfare outcomes recorded during their life on-farm and up to and including the point of slaughter. We are working closely with our farmers' processing partners and steering group members to deliver our Sustainability Plan commitment of sourcing birds from 100% independently verified higher health and welfare outcome flocks by 2020. We are already starting to see the benefits of expecting a high level of health and welfare at all stages of production and collaborating to create a continuous improvement culture related to outcome measures.

We hosted 54 members of our Cheese Development Group for two practical, on-farm workshops to help them address and measure lameness in their herds, a key welfare outcome and challenge for dairy cattle. We worked with our Dairy Development Group to reduce the need for certain priority classes of antibiotics, leading to a voluntary withdrawal of these antibiotics – part of our commitment to ensure responsible medicine use within our supply chains.

We are continuing to progress our two industry leading Research and Development projects to improve pig health and welfare outcomes in indoor production systems.

Following this year's Business Benchmark on Farm Animal Welfare results, we are assessing how we communicate our work to improve animal health and welfare so we can bring our communications in line with the extensive industry-leading work that we carry out in this area.

## We will reduce and optimise our own-brand packaging.

| What we'll do                                      | How we measure our progress                 | 2015/16 (14/15 figures) | 2016/17 (15/16 figures)* | 2020 target |
|--|---|-------------------------|--------------------------|-------------|
| Reduce own-brand packaging by 50% compared to 2005 | Reduction in own-brand packaging since 2005 | 31.5%                   | 33%                      | 50%         |

\*2016/17 figures will be available in Q2 in line with subsequent external reporting commitments.

Since 2005, we have reduced our own-brand packaging across all of our ranges by almost 33 per cent, and we continue to work towards our target of a 50 per cent reduction by 2020. For example, recently, we reduced the weight of our own-brand sherry bottles by 10 per cent, saving us 79 tonnes of glass packaging.

We are also working hard to make recycling easier for our customers. We have changed the spray bottles we use within our cleaning products so that the whole bottle – including the trigger – can now be recycled. Last year we sold over five million of these bottles and the changes mean over 130 tonnes of additional plastic can now be easily recycled at the kerbside.

Packaging plays an important role in protecting food and ensuring it stays fresh and tasty. We continue to introduce packaging that helps customers waste less food in their homes. For example, our resealable large family packs of ham and our snap-pack *Taste the Difference* sausages allow customers to keep one half of the pack fresh in the fridge or even to store in the freezer and use at a later date. We will continue to innovate in this way to reduce waste from packaging and food in the home.

## We will work with our key own-brand suppliers, farmers and growers to address the impact of our products.

| What we'll do   | How we measure our progress     | 2015/16             | 2016/17  | 2020 target |
|---|---------------------------------|---------------------|--|-------------|
| We'll work with and support our key suppliers, farmers and growers to help them reduce waste and put it to positive use | Participation in Courtauld 2025 | Signatory at launch | Involved in 5 major workstreams, and supporting the WRAP supply chain project road map development | No target   |

By 2050, the food supply chain could contribute two degrees to global warming. We know that the majority of our environmental impacts occur in our supply chains. As well as reducing our own environmental impacts, we want to work with our suppliers, farmers and growers to reduce the impacts associated with our products.

We were a founder signatory to the Courtauld Commitment in 2004 and have remained involved ever since. Courtauld 2025, among other commitments, seeks to reduce the greenhouse gas emissions associated with food and drink consumed in the UK by 20 per cent and improve water stewardship in food and drink supply chains.

We work to protect critical water sources, and ensure that we maintain water quality and availability in our supply chains. We work with partners such as Cranfield University to understand water vulnerability in our global supply chains, including the risk of water scarcity for fresh produce. We are also part of multi-stakeholder activities in the Doñana National Park in Spain and the East Anglian Water Stewardship Business Board and we fund and play an active role in the UK Water Partnership.

As part of our broader commitment on reducing food waste, we work with suppliers to reduce food surplus and food waste in our supply chains. We source directly from farmers and growers which speeds up the journey from farm to shelf, giving food extra shelf life. We use cutting-edge technology to forecast demand and have invested in Research & Development to help our farmers plan their crop cycles more accurately. This avoids having more product than we can sell.

We aim to use as much of every product as possible – for example, we have developed boodles, noodles made from butternut squashes that we would otherwise not be able to sell, and our broccoli rice uses 20 per cent stalk and 80 per cent floret – saving 42 tonnes of product that would have gone to waste.

In our General Merchandise and Clothing business, cotton is our most important natural resource and forms the basis of many of our products. Our cotton strategy will ensure that all of the cotton fibre used in our products originates from independently verifiable sustainably managed sources by 2020. Our membership of the Better Cotton Initiative underpins our cotton strategy and affirms our strong commitment to promoting and supporting positive environmental, social and economic change across the cotton value chain.

The leather tanning process is water and chemically intensive, which is why we are fully committed to strict environmental stewardship across our leather supply chain. We are working to ensure that all the leather used in our own-brand products is certified to a recognised international environmental standard by 2020, verified through independent audit.

For more information on how we are managing our environmental impact, see page 34.

# 12

new apprentices joined Sainsbury's Agriculture and Horticulture apprenticeship scheme this year





## Respect for our environment

We are committed to operating a sustainable business, working closely with colleagues and suppliers to reduce our impact on the environment. At the same time, we are also helping our customers live more sustainably, most notably with our efforts to help them cut food waste at home.

Through our investment in sustainable operations and technologies, we have reduced emissions by 8.2 per cent this year, compared to 2015/16. We are now using 11.6 per cent less electricity than we did in 2005 – despite growing our store space by 54.2 per cent. We are one of just three retailers worldwide to achieve an A rating in the 2016/17 FTSE 350 Climate Disclosure Leadership Index.

We have continued our work to keep food waste at a minimum by ensuring supply chain efficiency, while growing our network of charity partners to redistribute unsold food. We also released our inaugural food waste report, setting a public benchmark against which we can measure future performance.

Because we want to help make our customers' lives better and easier, we look for ways to support them too. We are investing in a five year, £10 million *Waste less, Save more* initiative which is helping customers to cut food waste and save money.

As the UK's second largest grocery retailer, even small actions by our 162,000 Sainsbury's store colleagues can have a big collective impact. We continue our work to be the Greenest Grocer by educating colleagues on how to grow our business while reducing our operational carbon emissions. We have also achieved our 2020 targets to reduce water use, driven largely by the introduction of waterless urinals across the business.

These actions help us progress towards our vision of being the most trusted retailer, while improving the efficiency of our operations and minimising risks and disruption to our business.

# 1,114

We now have 1,114 back of store food donation partnerships across 970 stores



## Our commitments

**We will work with our colleagues to reduce waste and put it to positive use.**

| What we'll do   | How we measure our progress                                   | 2015/16                          | 2016/17             | 2020 target |
|---|---|----------------------------------|---------------------|-------------|
| We will work with our colleagues to reduce waste and put it to positive use | Number of stores with Food Donation Partners for surplus food | 638 (45% of stores) <sup>1</sup> | 970 (68% of stores) | All stores  |

<sup>1</sup> This figure is based on our total estate of convenience stores, supermarkets, depots and online fulfilment centres. We are now reporting the percentage and total number of partnered stores.

This year marked a significant milestone as we moved to transparent reporting of our operational food waste. As one of only two major retailers to do this, we are leading the way and have set a clear benchmark against which we can measure progress. Our reporting also acts as a shared goal for colleagues across the business to ensure that we are all working together to make a difference, while helping build trust and engage customers through projects such as *Waste less, Save more*.

Our latest figures (2015/16) highlighted a 9.4 per cent reduction in operational food waste – driven in part by improved efficiencies in our supply chain. We are currently working to verify figures for 2016/17, which will be released later this year. We are also working to refine our measurement process to further improve accuracy.

We were the first UK retailer to remove multi-buys on food products from our shelves – helping customers avoid waste at home and enabling us to forecast demand more accurately. Our new strategy of everyday low prices ensures we are well placed to give our customers what they want, when they want it, so they can enjoy increased choice and flexibility while cutting down on waste.

We are also using data to make smarter predictions on the weekly requirements of seasonal products so we can stock up with the right amount. This reduces surplus from seasonal items like burgers, sausages, salads and soft fruit, and helps suppliers better manage their production. See page 33 for more information.

To minimise food waste, we are donating more unsold food to good causes than ever before by rapidly growing our charity network. We now have 1,114 back of store food donation partnerships across 970 stores, which enable us to redistribute surplus food to those in need. Eight out of ten of our supermarkets – which tend to generate more surplus food than other store formats – now have at least one charitable partner.

We partner with recycling companies to manage customer-recycling and donation facilities at our stores, and now have 271 stores with Sainsbury's recycling containers. Customers can also donate their mobile phones, clothing and books at Oxfam collection points in our car parks and our stores. In 2016/17, we collected 5,461 tonnes of clothing (over 16 million items) and 527 tonnes of books, making us the biggest single supplier of items to Oxfam shops.

**We will invest £10 million to help our customers reduce their waste through our *Waste less, Save more* initiative.**

| What we'll do   | How we measure our progress                | 2015/16 | 2016/17 | 2020 target |
|---|--|---------|---------|-------------|
| We will invest £10 million to help our customers reduce their waste through our <i>Waste less, Save more</i> initiative | Investment in <i>Waste less, Save more</i> | Launch  | £1.7m   | £10m        |

UK households throw away 7.3 million tonnes of food each year, accounting for 70 per cent of the UK's post-farm-gate total food waste. So it is no surprise that in 2015, our customers told us that they wanted help cutting their own food waste.

*Waste less, Save more* – our £10 million, five-year initiative to bring about behaviour change and help our customers tackle food waste – has gone from strength to strength. This year, we completed our 12 month trial in Swadlincote, Derbyshire, where we initiated over 20 trials, ranging from apps that weigh and report on food waste to pioneering school programmes designed to engage young people on the issue. Our aim was to identify which tactics had the biggest impact on reducing food waste, and learn how they could be rolled out in more households. We know that behaviour change programmes take time, but by trialling tools early on in the initiative, we can focus our efforts on the solutions that really work. Our work in Swadlincote is being carried out in partnership with WRAP, which we are working with to evaluate the trial.

As part of our ongoing efforts to expand the impact of the programme, we have recruited eight Waste Warriors from our in-store colleague network to champion the project across the UK. They have participated in some of the trials and are sharing what they have learned in their communities.

As promised, we are now delivering the next phase of the programme, rolling out successful solutions to some 130 Discovery Communities – towns and cities across the UK that have signed up to tackle food waste. To get them started, we have provided a handbook featuring lessons from Swadlincote and will also be making £1 million in grants available to support the roll-out of individual projects.

We will test and learn through our work in the Discovery Communities and ensure that the campaign reaches people outside these areas. We will also publish our findings so that customers, communities and competitors can join the fight against food waste.

“

**Many people still think that their unwanted clothes won't make a difference to charities, but at Oxfam we can reuse or recycle almost anything. The items donated through Sainsbury's raise millions, helping us continue our vital work to end extreme poverty around the world.”**

**Fee Gilfeather**, Head of Retail Brand for Oxfam

“

**We were the first UK retailer to remove multi-buys on food products from our shelves – helping customers avoid waste at home and enabling us to forecast demand better.”**

**Paul Mills-Hicks**, Food Commercial Director

**8.2%**

We have reduced total operational carbon emissions by 8.2 per cent this year, compared to 2015/16



**1m**

fridge thermometers given away to help customers cut food waste



## We will reduce our operational carbon emissions by 30 per cent absolute and 65 per cent relative (to 2005).

| What we'll do   | How we measure our progress | 2015/16  | 2016/17  | 2020 target  |
|---|-----------------------------|--|--|--|
| We'll continue to introduce proven and next generation renewable technologies in our new and existing stores to reduce our operational carbon emissions | Change in carbon emissions  | Absolute reduction: 3.4% since 2005/06 and 3.1% since 2014/15<br>Relative reduction: 6.9% since 2005/06 and 4.7% since 2014/15 | Absolute reduction: 11.4% since 2005/06 and 8.2% since 2015/16<br>Relative reduction: 42.5% since 2005/06 and 8.9% since 2015/16 | 30% absolute reduction versus 2005/06<br>65% relative reduction versus 2005/06 |

We have continued to make progress this year, with relative CO<sub>2</sub> emissions down by 8.9 per cent and absolute emissions falling by 8.2 per cent. We are now using 11.6 per cent less electricity than we did in 2005 – despite growing our operations by 54.2 per cent.

We have achieved these reductions through several initiatives. In 2016/17, we launched our Greenest Grocer – Energy Matters programme, which has helped our colleagues in-store to reduce our energy use and it has already saved us around three per cent on our electricity costs compared to 2015/16. As well as encouraging colleagues to close fridge doors, turn down ovens and avoid overfilling freezers, we have asked them for their own suggestions to help reduce energy use. The best ideas will be adopted into the programme for wider roll-out. Engaging colleagues in this collaborative way, and making the most of their expertise, will help to achieve even better results. Since the campaign launched we have saved £1.8 million from store budgets.

We installed LED lighting in 676 stores, depots and store support centres, which means around 49 per cent of our estate is using less energy on lighting. We will continue to roll out more LED lighting across our estate in 2017/18.

We work with anaerobic digestion suppliers to create carbon-neutral green gas from organic waste (including from our stores), which is fed into the grid. Around 20 per cent of our total gas use is this green gas. Our use of combined heat and power engines also reduces our impact on the National Grid, protects us from any potential outages and creates renewable heat to supply all our heating and hot water needs.

# 676

We now have LED lights in 676 stores, depots and store support centres. This means 49 per cent of our estate is using less energy on lighting.



In 2016/17, we increased the number of stores that use CO<sub>2</sub>e in their refrigeration to 246. This transition helps reduce our use of ozone-depleting refrigerant gases, such as hydrochlorofluorocarbons (HCFC) or hydrofluorocarbons (HFC), which can have a global warming potential that is 3,000 times higher than CO<sub>2</sub>e. The new fridges are also more energy efficient.

We also became the first company in the world to trial a refrigerated delivery truck cooled by a liquid nitrogen powered engine, which will eliminate all emissions associated with refrigeration. During the initial trial, the vehicle saved up to 1.6 tonnes of CO<sub>2</sub>; the equivalent of driving over 14,500 km in a modern family car – that is, ten trips from Land's End to John O'Groats. We are now continuing to work with our technology partner to get this innovative truck ready to market.

## Through robust water stewardship we will ensure that our business addresses and manages all areas of water vulnerability.

| What we'll do  | How we measure our progress  | 2015/16 | 2016/17 | 2020 target |
|--|--|---------|---------|-------------|
| We'll improve the efficiency of water use in our operations <sup>1</sup> | % change in water use in our operations (absolute) vs 2005/06 baseline | 29%     | 31%     | 30%         |
|  | % change in water use in our operations (relative) vs 2005/06 baseline | 54%     | 55%     | 55%         |

<sup>1</sup> Water use based on data for convenience stores, supermarkets and petrol filling stations.

Our ongoing work to improve water stewardship reached a significant milestone with the introduction of waterless urinals across our business. We achieved our 2020 target, reducing our absolute water usage by 30 per cent, and our relative usage by 55 per cent, relative to 2005/06. Since 2014/15, absolute water use has decreased by two per cent and relative water use has decreased by one per cent. We are also working with our farmers, suppliers and growers to improve their water efficiency (see page 33).

“

**We're proud of the progress in cutting our water use this year. Going forward we'll continue to set stretching targets and will test some significant innovations to further reduce consumption.”**

**Paul Crewe**, Head of Sustainability – Energy, Engineering & Environment

“

**I've learned that little things, like shopping with specific meals in mind and thinking about what you've already got in the fridge and cupboards, can all add up to make a big difference. I'm saving around £60 a week! We still enjoy an impromptu takeaway, but we're just better at remembering to use ingredients up the next day.”**

**Paula Chapman**, *Waste less, Save more* pilot participant, Swadlincote

## 7.3m

Designed to curb the 7.3 million tonnes of food thrown away by UK households each year

## 20

Over 20 waste-saving programmes trialled in Swadlincote

## £10m

investment over five years

## 130

More than 130 Discovery Communities





## A great place to work

We want to be a place where people love to work and shop. That means harnessing the talent, creativity and diversity of our colleagues to ensure that customers receive great service every time they shop at Sainsbury's.

Our colleagues are our foundation. We engage them in the long-term success of our business and invest in their training and development. We want to be the most inclusive retailer, where we celebrate the diversity of our colleagues and value the different perspectives they bring to help us meet the diverse needs of our customers. We listen to our colleagues' views so we can continue making Sainsbury's a place where everyone feels motivated, energised and enabled to offer the best value and service for our customers.

We offer a competitive rewards package, above the National Living Wage, we pay colleagues for breaks and we provide them with a range of benefits including a colleague discount and pension. It is important we remain a strong and competitive business for both current and past colleagues; we pay pension contributions for over 120,000 current colleagues, and look after defined benefit pensions for 80,000 former colleagues. Investors in People, the international standard for people management, awarded us a Gold accreditation for the third time – making us the largest UK employer to receive this distinction. We have grown our investment in apprenticeships that give people the chance to receive on the job training while earning a professional qualification.

### Our commitments

**We will be an employer where colleagues love to work.**

| What we'll do                                       | How we measure our progress | 2015/16  | 2016/17  | 2020 target  |
|---|-----------------------------|--|--|--|
| We are committed to exceed the National Living Wage | Colleague reward            | £7.36/hour (2.2% above the National Living Wage) | £7.66/hour (2.1% above the National Living Wage) | Standard colleague rate above the National Living Wage |

Our colleagues work hard to make a difference to our customers every day and we are committed to rewarding them fairly. We also support the Government's commitment to address the gender pay gap.

In August 2016, we announced a four per cent increase to our standard base rates for our retail colleagues, bringing our rate of pay to £7.66 per hour, ahead of the current National Living Wage of £7.50 per hour. We pay our colleagues for breaks.

To make Sainsbury's a great place to work, it is important that we listen to our colleagues. We use several tools to help us understand how our colleagues feel about working here. In 2016/17, more than 116,000 of our colleagues participated in our Talkback surveys. While we continue to look for ways to improve colleague engagement, we are pleased that 77 per cent of our colleagues feel Sainsbury's is a great place to work and over 78 per cent trust us to do the right thing for them.

In 2016/17, we piloted a new online engagement survey – We're Listening – across selected retail regions and store support centre divisions. Our new survey builds on traditional engagement;

it measures employee affection and loyalty to our brand over the long term and whether colleagues feel they have the support to be the best they can be in their role. We will be rolling out the new survey to the rest of the business in 2017/18.

To support making Sainsbury's a great place to work, the insights we gather through our colleague voice channels are shared with the Operating Board, as well as senior leaders across the business. From May 2017 our Non-Executive Directors will meet with a subset of our National Great Place To Work Group representatives from supermarkets, convenience and store support centres, so that they can hear the issues raised by our colleagues first hand.

We always welcome having our approach externally validated. We were delighted to receive a Gold accreditation by Investors in People – we are the largest employer to have reached the Gold standard and the only retailer to achieve three consecutive Gold awards. As part of the review, Investors in People considers how we listen and act on colleague feedback, how we develop and support our colleagues to learn and how we attract and retain talent.

### We will continue to invest in the training and development of our colleagues.

| What we'll do  | How we measure our progress   | 2015/16  | 2016/17  | 2020 target       |
|--|-------------------------------|--|--|-------------------|
| We'll offer colleagues externally accredited training to support our business strategy | Number of apprentices trained | 413 colleagues enrolled in or completed apprenticeship schemes covering: fish preparation & service, bakery skills, business administration, management skills and leading teams | 493 colleagues enrolled in or completed apprenticeship schemes covering: fish preparation & service, bakery skills, café hospitality, business administration, management skills, leading teams and software development | 2,500 apprentices |

Apprenticeships give colleagues on-the-job skills and training and they enable us to secure a talent pipeline to help Sainsbury's thrive in the future.

We have been exploring a range of new apprenticeships this year. In 2016/17, we introduced a café hospitality apprenticeship programme that builds hospitality and customer service skills; 59 colleagues are currently enrolled or have completed the pilot. We also piloted team leader and management apprenticeships: 112 retail and logistics colleagues will complete the programme in 2017. And in our store support centres, we recruited ten apprentices, including three women, for a new two-year structured software development apprenticeship programme.

We continued to run our industry-leading Diploma Level 2 craft apprenticeships in bakery and fish. In 2016/17, 304 colleagues were enrolled in or completed these apprenticeships, which last for a year and are awarded by City and Guilds. As part of the programmes, colleagues develop their Maths and English functional skills, and are awarded a full apprenticeship framework certificate. We continue to research new apprenticeships in preparation for the Apprenticeship Levy that will be introduced in 2017, to support colleague development.

## We will have an inclusive workforce that offers employment opportunities to all members of the community.

| What we'll do  | How we measure our progress   | 2015/16 | 2016/17 | 2020 target |
|--|---|---------|---------|-------------|
| We'll provide work opportunities and access to jobs for those who face barriers to the workplace | Number of colleagues employed through our You Can scheme since 2008 | 25,000  | 25,700  | 30,000      |

We value diversity not just because it is the right thing to do; research has shown that diverse teams perform better. In addition, we want our workforce to reflect and meet the needs of our diverse customer base.

Supported by our Chief Executive Officer Mike Coupe, Board sponsors including our Director of Human Resources, Angie Risley, Company Secretary and Corporate Services Director, Tim Fallowfield, and Chief Executive of Sainsbury's Bank, Peter Griffiths, together with Deborah Dorman, Director of Corporate HR, Iain Macmillan, Sainsbury's Argos Chief Finance Officer and Helen Paxton, Head of HR Sainsbury's Argos, form our Diversity Steering Group. The Group meets regularly to govern progress and updates the Board and Operating Board. We also have around 100 Diversity Champions who support diversity in every part of our business.

During 2016/17 we have continued to put strong emphasis on inclusion, and have identified it as a priority for our people and our business. During our first annual Inclusion Week in 2016, we launched the Embrace the Difference campaign. Companies leading on inclusion have found that using visible symbols that represent inclusion, such as badges, helps colleagues to be themselves at work. As part of the campaign, managers held inclusion-themed huddles, gave colleagues the opportunity to wear badges to show their visible commitment to inclusion, and used scenario-based exercises to help colleagues make positive and inclusive decisions. We also profiled a range of stories on topics related to diversity and inclusion, such as International Women's Day, Chinese New Year and Passover through our internal communications channels. Since 2008, we have employed 25,700 people through You Can, our scheme to provide jobs for people who might otherwise struggle to find employment.



We are working to increase the diversity of our retail managers. The assessment for You Can Be, the programme retail colleagues complete to progress to the next grade, now aims for gender balance and to better reflect regional ethnicity. Our female mentoring programme, which was launched by Mike Coupe in November 2015, reached 2,000 colleagues, and our subscription to the Everywoman Network has risen to over 750. We are also beginning to see a positive impact, having added 41 female store managers in 2016/17. Our Operating Board hosted a series of women's dinners and insights from these events helped us simplify our maternity policy and create our new Our Family Matters team. For a full breakdown of the gender diversity of our colleagues, see page 65.

Our Race, Religion and Belief reference group is helping us to tackle some of the challenges faced by our Black, Asian, and Ethnic Minority (BAME) colleagues. We used findings from one of the largest ever race at work surveys in the UK through Business in the Community to shape our first BAME colleague development event, which resulted in additional events being held at a local level. Diverse role models were leveraged to great effect at these events and the feedback was overwhelmingly positive.

We aspire to be a leader in creating disability-friendly workplaces. We were delighted to win a Business Disability Forum Disability-smart Award for the second year in a row. In June 2016, we celebrated our fifth year of partnership with Carers UK. Together we developed a policy specifically for carers, and we were one of the first FTSE 100 companies to do so. As part of our non-visible disabilities awareness week, we created a video to teach all our colleagues basic sign language to enable them to better communicate with deaf customers, which won gold at the EVCOM Clarion Awards. In December, Tim Fallowfield was announced as Chair of the Disability Confident Business Leaders Group. The Group will engage with the business community, enabling employers to provide opportunities for disabled people and supporting the government in its aspiration to halve the disability employment gap.

We are members of Stonewall's Diversity Champions programme and were featured in this year's Stonewall Workplace Equality Index. Our LGBTQIA (lesbian, gay, bisexual, transgender and allies) network, Proud@Sainsbury's, hosted networking events throughout the year. In 2016/17, we also attended Pride events across the UK and Jemma Kameen, one of our Co-Chairs of Proud@Sainsbury's, won Leeds Pride Partner of the Year for garnering the support of circa 400 colleagues.

“

**I've been at Sainsbury's for 35 years and I came out when I was 50. For me, it was about being open and visible – I chose to do this so that people could see that it's okay to be gay, to be a Store Manager, and bring all of yourself to work.”**

**Richard Easton**, Store Manager, New Cross Gate

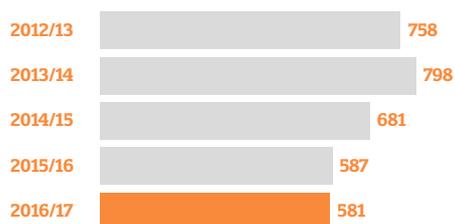
# Financial KPIs

Financial key performance indicators are critical to understanding and measuring our financial health.

## Group measures

### Underlying profit before tax (£m)

**Definition:** Profit before tax before items recognised which, by virtue of their size and or nature, do not reflect the Group's underlying performance



2012/13 restated for IAS 19

### Underlying basic earnings per share (pence)

**Definition:** Earnings per share using underlying profit



### Retail operating cashflow (£m)

**Definition:** Retail cash generated from operations after changes in working capital before exceptional pension contributions



### Retail underlying EBITDAR margin (%)

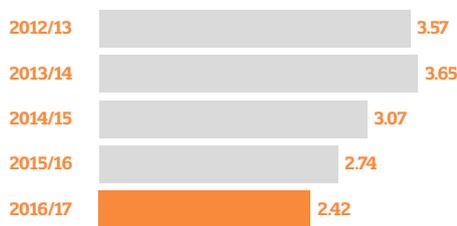
**Definition:** Underlying profit before tax before underlying net finance costs, underlying share of post-tax results from joint ventures, depreciation, amortisation and rent, divided by sales excluding VAT, including fuel, excluding Sainsbury's Bank



2012/13 restated for IAS 19

### Retail underlying operating margin (%)

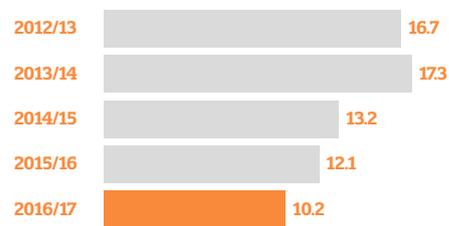
**Definition:** Underlying profit before tax before underlying net finance costs and underlying share of post-tax results from joint ventures, divided by retail sales excluding VAT, including fuel, excluding Sainsbury's Bank



2012/13 restated for IAS 19

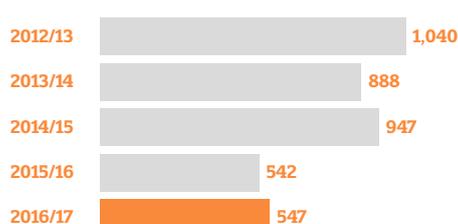
### Dividend per share (pence)

**Definition:** Total proposed dividend per share in relation to the financial year



### Core retail capital expenditure (£m)

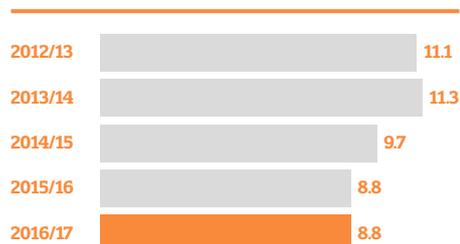
**Definition:** Capital expenditure excluding Sainsbury's Bank and before proceeds from sale and leasebacks and capital relating to the acquisition of freehold and trading properties



## Maintaining balance sheet strength

### Pre-tax return on capital employed (%)

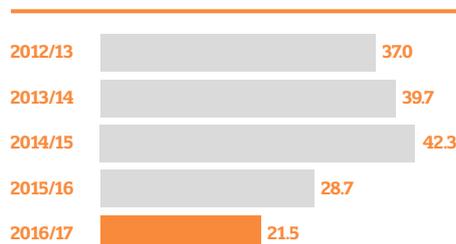
**Definition:** Underlying profit before interest and tax, divided by the average of opening and closing capital employed (net assets before net debt)



2013/14 closing capital employed has been adjusted to remove 50 per cent of Sainsbury's Bank net assets

### Gearing (%)

**Definition:** Net debt divided by net assets



2015/16 onwards has been displayed with the perpetual securities accounted for as equity. If treated as debt, gearing is 30.9 per cent

### Lease adjusted net debt/underlying EBITDAR (%)

**Definition:** Net debt plus capitalised lease obligations (5.5 per cent discount rate) divided by Group underlying EBITDAR

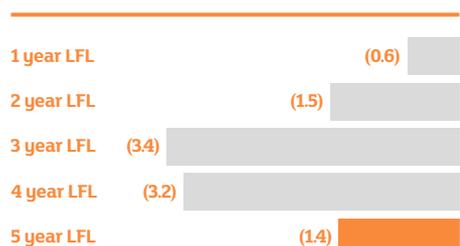


2015/16 onwards has been displayed with the perpetual securities accounted for as equity. If treated as debt, lease adjusted net debt/underlying EBITDAR is 4.0 times

## Sainsbury's (excluding Argos)

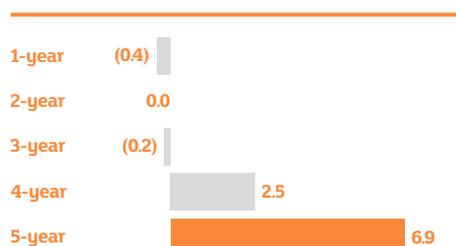
### Like-for-like sales 2016/17 (%)

**Definition:** Year-on-year growth in sales including VAT, excluding fuel, excluding Sainsbury's Bank, for stores that have been open for more than one year



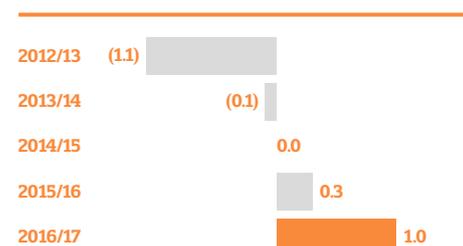
### Sales growth 2016/17 (%)

**Definition:** Year-on-year growth in sales including VAT, excluding fuel, excluding Sainsbury's Bank



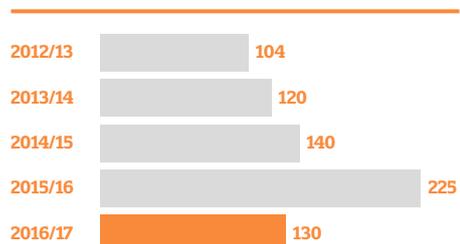
### Like-for-like transactions growth 2016/17 (%)

**Definition:** Year-on-year growth in transactions, excluding fuel, excluding Sainsbury's Bank, for stores that have been open for more than one year



### Cost savings (%)

**Definition:** Excludes Sainsbury's Bank and represents cost reductions as a result of identified initiatives



# Our principal risks and uncertainties

The risk management process is aligned to our strategy. Risk is an inherent part of doing business. The management of these risks is based on a balance of risk and reward determined through careful assessment of both the potential likelihood and impact as well as risk appetite. Consideration is given to both reputational as well as financial impact, recognising the significant commercial value attributable to the Sainsbury's Brand. Each principal risk and uncertainty is considered in the context of how it relates to the achievement of the Group's strategic objectives. As outlined on page 11, the current business strategy and objectives are categorised into the following areas:



The Sainsbury's Operating Board formally reviews the corporate risk map twice a year, which captures the principal risks to achieving Sainsbury's business objectives. The risk discussion includes assessment of both gross and net risk, where gross risk reflects the risk exposure and risk landscape before considering the mitigations in place, and net risk the residual risk after mitigations. The risk appetite for each key risk is also discussed and assessed with a target risk position agreed to reflect the level of risk that the business is willing to accept. The Sainsbury's Operating Board reviews risk dashboards during the year, comprised of key risk indicators, to ensure they identify any potential risk movement towards or away from their risk appetite. This enables the Operating Board to agree and monitor appropriate actions as required.

The gross risk movement from prior year for each principal risk and uncertainty has been assessed and is presented as follows:

- No change
- Increased gross risk exposure
- Reduced gross risk exposure

Mitigations in place supporting the management of the risk to a net risk position are also described for each principal risk and uncertainty.

Where principal risks have been included in the risk modelling undertaken as part of the preparation of the viability statement (see page 45), this has been indicated with the following symbol

## Key risk movements

The principal and emerging risks are discussed and monitored throughout the year to identify changes to the risk landscape. Risks are reviewed in line with the Company's strategic objectives. A new principal risk was disclosed in 2016 regarding the political and regulatory environment. Following the UK's decision to leave the European Union (EU) in June 2016, Sainsbury's believe that this risk has increased due to the ongoing uncertainty which may adversely impact trading performance across the sector.

All principal risks were reviewed following the acquisition of Home Retail Group to ensure that they reflect the risk across the Sainsbury's Group, including the acquired Argos business. It is considered that all of the risks are incorporated within the principal risks and uncertainties disclosed below, with no material change required. It was considered however that Sainsbury's Group's risk exposure to political and regulatory risks and business continuity incidents may be greater due to the increased size and complexity of the business.

The most significant principal risks identified by the Board and the corresponding mitigating controls are set out below in no order of priority.

### Business continuity and major incidents response

#### Risk

- A major incident or catastrophic event could impact on the Group's ability to trade. Following the acquisition of Home Retail Group, Sainsbury's exposure to business continuity and major incident risks may be greater due to the increased size and complexity of the business.

#### Mitigation

The Group has detailed plans in place, supported by senior representatives who are trained in dealing with major incidents and have the authority levels to make decisions in the event of a potentially disruptive incident.

The business continuity strategy, including incident management, resilience exercises and testing, has been aligned across the Group. The Business Continuity Steering Group, which includes representatives from Sainsbury's Bank, Argos and Habitat, meets quarterly to ensure that the business continuity (BC) policy and strategy is fit for purpose. In addition, it oversees the mitigation of all risks associated with BC and IT disaster recovery. In the event of any unplanned or unforeseen events, the Business Continuity Management Team is convened at short notice to manage the response and any associated risk to the business.

Group wide business continuity resilience exercises are undertaken to imitate real life business continuity scenarios and test the Group's ability to respond effectively.

Key strategic locations have secondary backup sites which would be made available within pre-defined timescales and are regularly tested.

## → Business strategy and change

### Risk

-  If the Board adopts the wrong business strategy or does not communicate or implement its strategies effectively, the business may be negatively impacted. Risks to delivering the strategy, change initiatives forming part of the strategy and other significant supporting change such as the integration with Argos need to be properly understood and managed to deliver long-term growth for the benefit of all stakeholders alongside management of business as usual.

### Mitigation

The business strategy is focused on the following:

- We know our customers better than anyone else;
- We will be there wherever and whenever they need us;
- We will offer great products and services at fair prices;
- Our colleagues make the difference; and
- Our values make us different.

The progress against strategic programmes and any risks to delivery, such as the ability to implement and deliver change and new business initiatives, are regularly reviewed by the Board and the overall strategy is reviewed at the annual two-day Strategy Conference. The Operating Board also holds regular sessions to discuss strategy. This activity is supported by a dedicated strategy team. To ensure the strategy is communicated and understood, the Group engages with a wide range of stakeholders including shareholders, colleagues, customers and suppliers on a continual basis. In addition, management performs ongoing monitoring of business as usual performance to determine indicators of potential negative performance as a result of change initiatives.

## → Colleague engagement, retention and capability

### Risk

-  The Group employs 195,000 colleagues who are critical to the success of our business. Attracting and maintaining good relations with talented colleagues and investing in their training and development are essential to the efficiency and sustainability of the Group's operations. Delivery of the strategic objectives, including integration with Argos and progress on multi-channel and digital, increases the risk impact of an inability to attract, motivate and retain talent, specific skill sets and capability. In addition, the challenging trading environment requires a focus on efficient operations which may include change initiatives impacting colleagues, therefore presenting a risk of loss of colleague trust or engagement.

### Mitigation

The Group's employment policies and remuneration and benefits packages are regularly reviewed and are designed to be competitive with other companies, as well as providing colleagues with fulfilling career opportunities. In addition to strong leadership and nurturing of talent by line managers, processes are also in place to identify talent and actively manage succession planning throughout the business. Ongoing reviews are performed to understand the nature of capability and specific skill sets required to deliver objectives. This is supported by embracing new ways of attracting talent and our corporate value 'Great Place to Work' reinforces our commitment to giving people the opportunity to be the best they can be.

Colleague surveys, performance reviews, listening groups, communications with trade unions, regular communication of business activities and colleague networking forums such as Yammer, the updated colleague portal (Our Sainsbury's) and colleague learning portal are some of the methods the Group uses to understand and respond to colleagues' needs. As change initiatives are implemented, the methods described above will continue to be employed to understand and maintain colleague trust and engagement.

## → Data security

### Risk

-  It is essential that the security of customer, colleague and company confidential data is maintained. A major breach of information security could have a major negative financial and reputational impact on the business. The risk landscape is increasingly challenging with deliberate acts of cybercrime on the rise, targeting all markets and heightening the risk exposure.

### Mitigation

A Data Governance Committee is established and is supported by focused working groups looking at the management of colleague data, customer data, information security, commercial data and awareness and training. Senior appointments have been made into roles specifically focused on data governance and information security. The Chief Information Security Officer continues to develop the Information Security Strategy and build the necessary capability to deliver against that strategy. The Head of Data Governance focuses on improving how we handle data across the organisation. Various information security policies and standards are in place which focus on encryption, network security, access controls, system security, data protection and information handling. A review of key third parties who hold sensitive customer or colleague data continues to take place, and progress is monitored by the Data Governance Committee. A risk based security testing approach across Group IT infrastructure and applications is in place to identify ongoing vulnerabilities.

## → Environment and sustainability

### Risk

-  Environment and sustainability are core to Sainsbury's values. The key risk facing the Group in this area relates to reducing the environmental impact of the business with a focus on reducing packaging and new ways of reducing waste and energy usage across stores, depots and offices.

### Mitigation

A number of initiatives are in place, which are being led by the Environmental Action Team and the Corporate Responsibility Steering Group, to reduce our environmental impact and to meet our customers' expectations in this area.

Further details are included in the Our values make us different section on pages 24 to 39.

## → Financial and treasury risk

### Risk

-  The main financial risks are the availability of short and long-term funding to meet business needs and fluctuations in interest, commodity and foreign currency rates. The business has acquired full ownership of Sainsbury's Bank which presents a risk that the Group's financial performance and position may be negatively impacted if the Bank transition and performance are not delivered as planned. In addition, there remains a risk around pensions as the Group operates two defined benefit pension arrangements that are subject to risks in relation to liabilities as a result of changes in interest rates, life expectancy and inflation and their alignment to the value of investments and the returns derived from such investments.
-  **V**

### Mitigation

The Group Treasury function is responsible for managing the Group's liquid resources, funding requirements, interest rate and currency exposures and the associated risks as set out in note 23 on page 139. The Group Treasury function has clear policies and operating procedures which are regularly reviewed and audited.

Sainsbury's Bank operates an enterprise wide risk management framework. The principal financial risks relating to the Bank and associated mitigations are set out in note 23 to the financial statements on page 139.

With regard to pensions, investment strategies are in place which have been developed by the pension trustees, in consultation with the Company, to manage the volatility risk of liabilities, to diversify investment risk and to manage cash. Both Group defined benefit schemes are closed to future accrual.

## → Health and safety – people and product

### Risk

-  Prevention of injury or loss of life for both colleagues and customers is of utmost importance. In addition, it is paramount to maintaining the confidence our customers have in our business.
-  **V**

### Mitigation

Clear policies and procedures are in place detailing the controls required to manage health and safety and product safety risks across the business and comply with all applicable regulations. These cover the end-to-end operation, from the auditing and vetting of construction contractors, to the health and safety processes in place in our depots, stores and offices to the controls in place to ensure people and product safety and integrity.

In addition, established product testing programmes are also in place to support rigorous monitoring of product traceability and provide assurance over product safety and integrity. Supplier terms and conditions and product specifications set clear standards for product/ raw material safety and quality which suppliers are expected to comply with.

Process compliance is supported by external accreditation and internal training programmes, which are aligned to both health and safety laws and Sainsbury's internal policies. In addition, resource is dedicated to manage the risk effectively, in the form of the Group Safety Committee and specialist safety teams.

## ↑ Political and regulatory environment

### Risk

-  There remain heightened levels of political and regulatory uncertainty in the UK following the referendum vote to leave the EU in June 2016, the triggering of Article 50 in March 2017, and the general election in June 2017. This uncertainty is expected to continue for the foreseeable future until EU exit negotiations have been completed and alternative trade deals have been put in place. This situation may adversely impact trading performance across the sector. An increasing focus on localism to drive and deliver policy and current legislative requirements including Business Rates, Workplace Pensions, the National Living Wage and Apprenticeship Levy place a cumulative burden on Sainsbury's.
-  **V**

### Mitigation

We continue to engage actively with governments, administrations and regulatory bodies. We publically communicate matters where we believe industry change is required with a view to enabling fair competition that is beneficial to our customers. We communicate our views, and those of our customers and colleagues, regarding geopolitical issues with the aim of informing the debate and ensuring our opinions are represented in the policy and decision making processes.

## → Trading environment and competitive landscape

### Risk

-  Effective management of the trading account is key to the achievement of performance targets. The sector outlook has been and is set to remain challenging. The challenging trading environment, driven by ongoing competitive retail pricing combined with growing inflationary cost pressures, may adversely impact performance. There is also an ongoing risk of supplier failure, with possible operational or financial consequences for the Group.
-  **V**

### Mitigation

We adopt a differentiated strategy with a continued focus on delivering quality products and services with 'universal appeal', at fair prices, helping our customers *Live Well for Less*. This is achieved through the continuous review of our product quality, key customer metrics, monitoring of current market trends and price points across competitors, active management of price positions, development of sales propositions and increased promotion and marketing activity. We continue with our commitment to provide customers even better value with lower regular prices. In delivering our strategic plan, including our price investment, we will maintain the strength of our balance sheet and have therefore identified a series of measures to conserve cash in the business. Through these measures we will deliver sustainable operating cost savings. With regards to supplier continuity, Sainsbury's maintains regular, open dialogue with key suppliers concerning their ability to trade.

## Statement of viability

### 1 How Sainsbury's assesses its prospects

The Group's business activities and strategy are central to assessing its future prospects. These, together with factors likely to affect its future development, performance and position, are set out in the Strategic Report on pages 01 to 53. The financial position of the Group, its cash flows and liquidity are highlighted in the Financial Review on pages 46 to 53. The Group manages its financing by diversifying funding sources, structuring core borrowings with long-term maturities and maintaining sufficient levels of standby liquidity.

The Group's prospects are assessed primarily through its corporate planning process. This includes an annual review which considers profitability, the Group's cash flows, committed funding and liquidity positions and forecast future funding requirements over three years, with a further two years of indicative movements. The most recent was signed off in November 2016, and refreshed in March 2017 as part of the normal budgeting process. This is reviewed by the Operating Board and ultimately by the PLC Board with involvement throughout from both the CFO and CEO. Part of the Board's role is to consider the appropriateness of any key assumptions, taking into account the external environment and business strategy.

### 2 The assessment period

The Directors have determined that the three years to March 2020 is an appropriate period over which to provide its viability statement. This period is consistent to that used for the Group's corporate planning process as detailed above, and reflects the Directors' best estimate of the future prospects of the business.

### 3 Assessment of viability

To make the assessment of viability, additional scenarios have been tested over and above those in the corporate plan, based upon a number of the Group's principal risks and uncertainties (as documented on pages 42 to 44). The scenarios were overlaid into the corporate plan to quantify the potential impact of one or more of these crystallising over the assessment period.

Whilst each of the risks on pages 42 to 44 has a potential impact and has been considered as part of the assessment, only those that represent severe but plausible scenarios were selected for modelling through the corporate plan. These were:

| Scenario modelled   | Link to principal risks and uncertainties   |
|---|---|
| <b>Scenario 1</b><br><b>Forecast savings targets are not achieved</b><br>The Group Corporate Plan currently assumes £160 million of synergies as a result of the HRG acquisition in the third full-year post acquisition, along with £500 million of cost savings to offset inflationary pressures by the end of 2017/18. A scenario has therefore been modelled in which all planned savings/synergies are not realised in the years planned and are delayed by one year during the assessment period. | <ul style="list-style-type: none"> <li>— Business strategy and change</li> </ul>  |
| <b>Scenario 2</b><br><b>Data breaches</b><br>The impact of any regulatory fines has been considered. The biggest of these is the General Data Protection Regulation (GDPR) fine for data breaches, which will be enacted in May 2018. This was considered both in isolation and in conjunction with a fall in sales volumes as a result of any reputational brand damage.   | <ul style="list-style-type: none"> <li>— Data security</li> </ul>   |
| <b>Scenario 3</b><br><b>Legal breaches</b><br>Similar to the above, we considered the reputational impact of any legal or health and safety incidents, modelling a fall in sales volumes in the year of occurrence. We also considered regulatory fines such as those levied by the Groceries Supply Code of Practice (GSCOP).  | <ul style="list-style-type: none"> <li>— Health and safety, people and product</li> <li>— Political and regulatory environment</li> </ul>         |
| <b>Scenario 4</b><br><b>Brexit</b><br>The impact of the UK's decision to leave the EU was considered. Scenarios were modelled assessing potential impacts of weakening sterling foreign exchange rates in all years, as well as World Trade Organisation (WTO) tariffs being applied to inventory purchases in year three of the assessment period.   | <ul style="list-style-type: none"> <li>— Political and regulatory environment</li> <li>— Trading environment and competitive landscape</li> </ul> |
| <b>Scenario 5</b><br><b>Bank transition</b><br>It was considered what level of sustained loss would be required in Sainsbury's Bank before its capital ratios were breached, leading to additional material funding requirements from the Group.  | <ul style="list-style-type: none"> <li>— Financial and treasury risk</li> </ul>   |

In performing the above analysis, the Directors have made certain assumptions around the availability of future funding options, including the ability to raise future finance.

The scenarios above are hypothetical and severe for the purpose of creating outcomes that have the ability to threaten the viability of the Group; however, multiple control measures are in place to prevent and mitigate any such occurrences from taking place. In the case of these scenarios arising, various options are available to the Group in order to maintain liquidity so as to continue in operation. These include reducing any non-essential capital expenditure and operating expenditure on projects, as well as not paying dividends.

The results of the above stress testing showed that the Group would be able to withstand the impact of these scenarios occurring over the assessment period.

### 4 Viability statement

Taking into account the Group's current position and principal risks and uncertainties, the Directors confirm that they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three years to March 2020.

### 5 Going concern

The Directors also considered it appropriate to adopt the going concern basis in preparing the financial statements, which are shown on pages 99 to 185.

# Financial Review



## Dear Shareholder,

2016/17 has been a pivotal year in Sainsbury's history, with the acquisition of Home Retail Group plc (HRG) on 2 September 2016. From an underlying trading perspective this has had a significant impact on the financial results, with £3,175 million (including VAT) of Argos (including Argos Financial Services) sales and £77 million of underlying profit before tax consolidated into the Group income statement for the 27 weeks Sainsbury's owned the business.

Sainsbury's Group sales (including VAT) were up 12.7 per cent to £29,112 million and improved 0.4 per cent when excluding the impact of the HRG acquisition. On a 52-week rolling basis Sainsbury's market share (as measured by Kantar for the 52 weeks to 26 February 2017) declined 23 basis points, due to continued price investment and the continuing pace of new store expansion from the discounters. Discounters' combined market share increased by 99 basis points, with the 'big four' declining on average by 35 basis points. However, there was like-for-like transaction growth across all channels – supermarkets, convenience and groceries online.

Sainsbury's continues to operate in a competitive and uncertain trading environment, impacting margins. In 2016/17, retail underlying operating profit decreased by 1.4 per cent to £626 million (2015/16: £635 million) reflecting lower like-for-like sales, investment in the customer offer and cost inflation. This was partly offset by cost savings of £130 million and a contribution from Argos of £77 million. Retail underlying operating margin declined 32 basis points to 2.42 per cent. Underlying profit before tax (UPBT) declined by 1.0 per cent to £581 million (2015/16: £587 million), and profit before tax of £503 million (2015/16: £548 million) was down 8.2 per cent as a result of a £78 million charge recognised outside of underlying results.

Sainsbury's Bank continues to perform in line with expectations. We have now migrated all of our savings customers and ATMs onto the new, more flexible banking platform. This has given us the opportunity to launch into the mortgage market in April 2017. Argos Financial Services (AFS) also transferred to the Bank in September, with its net £615 million customer loan book. This has enabled the Group to refinance the intercompany funding for AFS through increased customer deposits and wholesale funding – a significantly cheaper way to fund the Group than external debt. As a result the Group repaid the draw-down on the Revolving Credit Facility used for the cash consideration of the HRG acquisition.

The HRG acquisition completed on 2 September 2016. The economics of the deal were uniquely well set for Sainsbury's, both in terms of the £160 million of EBITDA synergies we are now confident of achieving six months earlier than expected in 2018/19, and our ability to finance the deal through our refinancing of the AFS loan book. Final consideration was just under £1.1 billion – paid for in cash and shares. The fair value of net assets acquired was just over £1.0 billion, resulting in goodwill of £58 million. The fair value of net assets acquired included a net £615 million customer loan book and £322 million of net cash (after the capital return to HRG shareholders).

The balance sheet remains strong with a significant reduction in net debt. Net debt at £1,477 million (£1,971 million treating the perpetual securities as debt) has reduced £349 million since the 2015/16 year-end, mainly as a result of continued strong cash generation from our retail operations, the financing of the acquisition of HRG and further working capital improvements, offset by exceptional pension payments, capital expenditure and dividends paid. The Group has facilities of £3.9 billion with only £2.7 billion drawn at the end of the year. Like many other companies, we have seen a significant fall in discount rates since the year-end. This has increased the Sainsbury's pension scheme IAS 19 accounting deficit (net of deferred tax) to £679 million (2015/16: £389 million deficit), and the acquired HRG pension scheme deficit (net of deferred tax) is £171 million as at 11 March 2017.

Underlying basic earnings per share decreased 9.9 per cent to 21.8 pence (2015/16: 24.2 pence), reflecting the fall in underlying profits and the effect of additional shares issued during the year, as a result of the HRG acquisition. Basic earnings per share decreased 26.8 per cent to 17.5 pence (2015/16: 23.9 pence), lower than the underlying earnings per share due to the £78 million charge recognised outside of underlying results and a change in tax rate due to the comparatively smaller benefit of a one per cent revaluation of non-underlying deferred tax balances (2015/16: two per cent).

The Board has recommended a final dividend of 6.6 pence (2015/16: 8.1 pence), making a full-year dividend of 10.2 pence per share (2015/16: 12.1 pence per share).

**Kevin O'Byrne**  
Chief Financial Officer

|   | 52 weeks to<br>11 March<br>2017<br>£m | 52 weeks to<br>12 March<br>2016<br>£m | Change<br>% |
|---|---------------------------------------|---------------------------------------|-------------|
| <b>Summary income statement<sup>1</sup></b>               |                                       |                                       |             |
| <b>Group sales (including VAT)</b>                        | <b>29,112</b>                         | 25,829                                | 12.7        |
| <b>Retail sales (including VAT)</b>                       | <b>28,705</b>                         | 25,502                                | 12.6        |
| <b>Group sales (excluding VAT)</b>                        | <b>26,224</b>                         | 23,506                                | 11.6        |
| <b>Retail sales (excluding VAT)</b>                       | <b>25,824</b>                         | 23,168                                | 11.5        |
| <b>Underlying operating profit</b>                        |                                       |                                       |             |
| Retail  | <b>626</b>                            | 635                                   | (1.4)       |
| Financial Services  | <b>62</b>                             | 65                                    | (4.6)       |
| <b>Total underlying operating profit</b>                  | <b>688</b>                            | 700                                   | (1.7)       |
| Underlying net finance costs <sup>2</sup>                 | <b>(119)</b>                          | (121)                                 | 1.7         |
| Underlying share of post-tax profit from JVs <sup>3</sup> | <b>12</b>                             | 8                                     | 50.0        |
| <b>Underlying profit before tax</b>                       | <b>581</b>                            | 587                                   | (1.0)       |
| Items excluded from underlying results                    | <b>(78)</b>                           | (39)                                  | 100.0       |
| <b>Profit before tax</b>                                  | <b>503</b>                            | 548                                   | (8.2)       |
| Income tax expense  | <b>(126)</b>                          | (77)                                  | (63.6)      |
| <b>Profit for the financial period</b>                    | <b>377</b>                            | 471                                   | (20.0)      |
| <b>Underlying basic earnings per share</b>                | <b>21.8p</b>                          | 24.2p                                 | (9.9)       |
| <b>Basic earnings per share</b>                           | <b>17.5p</b>                          | 23.9p                                 | (26.8)      |
| <b>Dividend per share</b>                                 | <b>10.2p</b>                          | 12.1p                                 | (15.7)      |

1 Group sales including Argos (including Financial Services) of £3,175 million including VAT and £2,661 million excluding VAT, and an underlying profit contribution of £77 million.

2 Net finance costs including perpetual securities coupons before non-underlying finance movements.

3 The underlying share of post-tax profit from JVs is stated before investment property fair value movements, financing fair value movements and profit on disposal of properties.

### Group sales

Group sales (including VAT) increased by 12.7 per cent. Retail sales (including VAT, excluding fuel) increased by 14.1 per cent, driven by a 14.5 per cent contribution from Argos, a 0.2 per cent contribution from new Sainsbury's

space (excluding extensions and replacements and net of Pharmacy), and a Sainsbury's like-for-like (LFL) sales decline of 0.6 per cent.

|   | 52 weeks to<br>11 March<br>2017<br>% | 52 weeks to<br>12 March<br>2016<br>% |
|---|--------------------------------------|--------------------------------------|
| <b>Group sales growth contribution (including VAT)</b>            |                                      |                                      |
| Sainsbury's like-for-like sales                                   | <b>(0.6)</b>                         | (0.9)                                |
| Sainsbury's net new space (excluding extensions and replacements) | <b>0.8</b>                           | 1.3                                  |
| Pharmacy  | <b>(0.6)</b>                         | –                                    |
| Contribution from Argos   | <b>14.5</b>                          | –                                    |
| <b>Retail (including VAT, excluding fuel)</b>                     | <b>14.1</b>                          | 0.4                                  |
| Fuel impact   | <b>(1.5)</b>                         | (1.6)                                |
| <b>Retail sales (including VAT, including fuel)</b>               | <b>12.6</b>                          | (1.2)                                |
| Bank impact   | <b>0.1</b>                           | 0.1                                  |
| <b>Group sales (including VAT)</b>                                | <b>12.7</b>                          | (1.1)                                |

Sainsbury's LFL sales, excluding fuel, declined by 1.0 per cent in the first half, and by 0.1 per cent in the second half, driven by continued food price deflation which slowed in the second half.

On a 52-week rolling basis Sainsbury's market share (as measured by Kantar) declined 23 basis points, due to continued price investment and the continuing pace of new store expansion from the discounters. Discounters' combined market share increased by 99 basis points, with the 'big four' declining on average by 35 basis points. However, there was like-for-like transaction number growth across all channels – supermarkets, convenience and groceries online.

Fuel sales grew 4.2 per cent, however as Argos sales contribution of 14.5 per cent is now included within sales growth (excluding fuel), this rate of growth was, in effect, dilutive to sales growth (including fuel).

Our multi-channel strategy enables customers to shop whenever, wherever and however they want. The convenience business grew sales by over six per cent. Groceries online grew by eight per cent year-on-year, with order growth of nearly 12 per cent being partially offset by a reduction in basket size due to deflation and a lower number of items per basket. Sainsbury's clothing and general merchandise offer continued to grow sales ahead of the market, supported by continued range development and the roll-out of new space.

Argos sales have contributed 14.5 per cent growth since acquisition and Argos like-for-like sales were up 4.1 per cent in the second half.

Contribution from Sainsbury's net new space (excluding extensions, replacements and the disposal of the Pharmacy business which completed on 31 August 2016) is expected to be around 0.6 per cent for the full-year with a first half contribution of 0.6 per cent and a second half contribution of 0.6 per cent.

After the impact of the disposal of the Pharmacy business, net new space contribution is expected to reduce to 0.1 per cent for the full-year with a negative contribution of 0.3 per cent in the first half and a positive contribution of 0.6 per cent in the second half.

### Space

The contribution from Sainsbury's net new space (excluding extensions, replacements and the disposal of the Pharmacy business) was 0.8 per cent in 2016/17 (2015/16: 1.3 per cent). The impact of the disposal of the Pharmacy business reduces this to 0.2 per cent in 2016/17.

In 2016/17, Sainsbury's opened six new supermarkets (2015/16: six new supermarkets), and closed two supermarkets. Convenience continues to grow, with 41 new stores opened in 2016/17 (2015/16: 69 stores). Eight convenience stores were closed in the year.

Net of replacements, closures and disposals, closing Sainsbury's space of 23,397,000 sq ft was 0.8 per cent higher than last year (12 March 2016: 23,202,000 sq ft).

In 2017/18, Sainsbury's expects to open three new supermarkets and around 25 new convenience stores.

| Sainsbury's store numbers and retailing space<br>52 weeks to 11 March 2017 | Supermarkets |                   | Convenience |                   | Total        |                   |
|--|--------------|-------------------|-------------|-------------------|--------------|-------------------|
|  | Number       | Area<br>000 sq ft | Number      | Area<br>000 sq ft | Number       | Area<br>000 sq ft |
| At 12 March 2016   | 601          | 21,402            | 773         | 1,800             | <b>1,374</b> | <b>23,202</b>     |
| New stores   | 6            | 163               | 41          | 98                | <b>47</b>    | <b>261</b>        |
| Disposals/closures   | (2)          | (56)              | (8)         | (14)              | <b>(10)</b>  | <b>(70)</b>       |
| Extensions/refurbishments/downsizes  | –            | 3                 | –           | 1                 | –            | <b>4</b>          |
| <b>At 11 March 2017</b>  | <b>605</b>   | <b>21,512</b>     | <b>806</b>  | <b>1,885</b>      | <b>1,411</b> | <b>23,397</b>     |

In addition, as at 11 March 2017, Argos had 858 stores (including Habitat).

| Argos and Habitat store numbers | Argos stores <sup>1</sup> | Argos in Sainsbury's | Argos in Homebase | Habitat  | Other <sup>2</sup> | Total       |
|---------------------------------|---------------------------|----------------------|-------------------|----------|--------------------|-------------|
| At 24 September 2016            | 725                       | 15                   | 95                | 4        | 4                  | <b>843</b>  |
| New stores                      | 2                         | 24                   | –                 | 4        | 37                 | <b>67</b>   |
| Disposals                       | (12)                      | –                    | (38)              | –        | (2)                | <b>(52)</b> |
| <b>At 11 March 2017</b>         | <b>715</b>                | <b>39</b>            | <b>57</b>         | <b>8</b> | <b>39</b>          | <b>858</b>  |

<sup>1</sup> Includes two stores located at Netto sites that were previously disclosed as Argos in Sainsbury's.

<sup>2</sup> Includes pop-up stores, convenience stores and collection points.

In 2017/18, Sainsbury's expects to open around 135 Argos Digital stores in supermarkets, resulting in around 175 Argos Digital stores in supermarkets by the end of the year. In addition, we expect to open a further ten Habitat stores within supermarkets in 2017/18.

In the first half of 2017/18, Sainsbury's expects to close 39 Argos stores within Homebase, with 18 to remain open longer.

### Retail underlying operating profit

Retail underlying operating profit decreased by 1.4 per cent to £626 million (2015/16: £635 million), reflecting lower LFL sales, investment in

the customer offer and cost inflation. This was partly offset by cost savings of £130 million and a contribution from Argos of £77 million. Underlying operating profit includes £7 million of EBITDA synergies (Argos: £5 million; Sainsbury's: £2 million).

Retail underlying operating margin declined by 32 basis points year-on-year to 2.42 per cent (2015/16: 2.74 per cent), equivalent to a 31 basis points decline at constant fuel prices. Retail underlying EBITDAR margin decreased by 18 basis points to 7.40 per cent, or a 15 basis points decline at constant fuel prices.

| Retail underlying operating profit                   | 52 weeks to 11 March 2017 | 52 weeks to 12 March 2016 | Change  | Change at constant fuel prices |
|--|---------------------------|---------------------------|---------|--------------------------------|
| Retail underlying operating profit (£m) <sup>1</sup> | <b>626</b>                | 635                       | (1.4)%  |                                |
| Retail underlying operating margin (%) <sup>2</sup>  | <b>2.42</b>               | 2.74                      | (32)bps | (31)bps                        |
| Retail underlying EBITDAR (£m) <sup>3</sup>          | <b>1,912</b>              | 1,755                     | 8.9%    |                                |
| Retail underlying EBITDAR margin (%) <sup>4</sup>    | <b>7.40</b>               | 7.58                      | (18)bps | (15)bps                        |

<sup>1</sup> Retail underlying earnings before interest, tax and Sainsbury's underlying share of post-tax profit from JVs.

<sup>2</sup> Retail underlying operating profit divided by retail sales excluding VAT.

<sup>3</sup> Retail underlying operating profit before rent, depreciation and amortisation.

<sup>4</sup> Retail underlying EBITDAR divided by retail sales excluding VAT.

In 2017/18, Sainsbury's expects cost inflation in the two to three per cent range. We expect efficiency savings of around £145 million in 2017/18. We remain on track to deliver the strategic target of £500 million of savings over three years by the end of 2017/18 and are developing plans to deliver a further three year £500 million cost saving target from 2018/19 onwards as we simplify the business.

We expect the first half 2017/18 Group underlying profit to be lower than the second half 2017/18 as a result of: the consolidation of first half Argos operating loss; and the annualisation of 2016/17 price investment and the second half 2016/17 step-up in cost inflation due to the effect of the four per cent wage increase for store colleagues effective from 28 August 2016.

We expect depreciation and amortisation of around £700 million, an increase of around £70 million as a result of the consolidation of a full-year of Argos.

### Argos acquisition impact on retail underlying profit

On 2 September 2016, Sainsbury's completed the acquisition of HRG. Argos contributed £3,110 million of sales (including VAT) and £77 million of underlying profit before tax to retail performance since the point of acquisition (which includes £5 million of EBITDA synergies).

Previously HRG analysed their business as Argos, Homebase, financial services, central activities and interest income. Homebase has now been sold. The financial services element of HRG is now included within the Group's Financial Services segment, and guidance on the effect of this is now included within the Sainsbury's Bank guidance. The remaining Argos and central activities segments of HRG will be combined into the Group's Retailing segment.

The consolidation of Argos has added an underlying profit contribution of £72 million in 2016/17 before synergies and Homebase transaction, separation and restructuring impact. The pre-acquisition loss of £27 million is not consolidated. Indicatively, a full-year profit contribution from Argos would have been £45 million.

Sainsbury's announced as part of the transaction to acquire HRG, that the Group expected to achieve £160 million of EBITDA synergies by the end of the first half of 2019/20. Due to the acceleration of some of the activity, we now expect to deliver these in 2018/19. The synergies are derived from three areas:

**Synergies from Argos stores in Sainsbury's – £75 million.** We will relocate some existing Argos stores into nearby Sainsbury's supermarkets, as well as opening Argos stores in supermarkets where there is no Argos presence nearby. This also gives cross-selling opportunities within Sainsbury's stores to the current food offer and a wider range of general merchandise products in Argos to Sainsbury's customers. At the same time we will benefit from lower operating costs, particularly rent and rates.

**Cost synergies from central and support – £70 million.** We will remove duplication and overlap from both central and support functions at

Sainsbury's and HRG. We will be able to realise product purchasing benefits from best practice and the combined Group's scale.

**Other revenue synergies – £15 million.** We will sell Sainsbury's clothing, homewares, seasonal and leisure ranges through the existing Argos network.

In order to achieve these synergies, £130 million of exceptional integration cost and £140 million of exceptional integration capital expenditure will be required. Exceptional costs will include the relocation of property, dilapidations, lease break costs and redundancy costs. Exceptional capital expenditure is required to reformat supermarket space and for fitting out the new Argos stores. The updated expected phasing of the synergies, exceptional costs and exceptional capital expenditure is shown below.

In 2017/18, we expect incremental EBITDA synergies of £58 million, resulting in total EBITDA synergies of £65 million since acquisition. EBITDA synergies of £160 million will be realised in 2018/19 (six months early).

Argos integration costs are expected to be around £60 million, integration capital expenditure is expected to be around £90 million.

| £m                                   | FY<br>2016/17 | FY<br>2017/18e | FY<br>2018/19e | Total        |
|--------------------------------------|---------------|----------------|----------------|--------------|
| Synergies (incremental year-on-year) | 7             | 58             | 95             | <b>160</b>   |
| Exceptional costs                    | (27)          | (60)           | (43)           | <b>(130)</b> |
| Exceptional capex                    | (18)          | (90)           | (32)           | <b>(140)</b> |

### Homebase separation

HRG announced on 18 January 2016 that the sale of Homebase would give rise to £75 million of additional exceptional costs in relation to transaction, separation and restructuring. Up to the date of the acquisition, HRG had incurred £30 million of these costs and incurred a further £4 million in

the period to 11 March 2017. It is currently anticipated that the total exceptional costs will now only be £60 million, a reduction of £15 million from the original estimate, with £15 million of the cost to be incurred in 2017/18.

### Financial Services

| Financial Services results <sup>1</sup>              | 12 months to<br>28 February<br>2017 | 12 months to<br>29 February<br>2016 | Change<br>% |
|--|-------------------------------------|-------------------------------------|-------------|
| Revenue (£m) <sup>2</sup>                            | <b>407</b>                          | 327                                 | 24.5        |
| Interest payable (£m)                                | <b>(60)</b>                         | (53)                                | (13.2)      |
| Total income (£m) <sup>3</sup>                       | <b>347</b>                          | 274                                 | 26.6        |
| Underlying operating profit (£m)                     | <b>62</b>                           | 65                                  | (4.6)       |
| Cost/Income ratio (%) <sup>4</sup>                   | <b>72</b>                           | 71                                  | (100)bps    |
| Active customers – Bank (m)                          | <b>1.77</b>                         | 1.71                                | 3.5         |
| Active customers – AFS (m)                           | <b>1.84</b>                         | n/a                                 | n/a         |
| Net interest margin (%) <sup>5</sup>                 | <b>4.4</b>                          | 4.1                                 | 30bps       |
| Bad debt as a percentage of lending (%) <sup>6</sup> | <b>0.8</b>                          | 0.4                                 | (40)bps     |
| Tier 1 capital ratio (%) <sup>7</sup>                | <b>13.3</b>                         | 15.8                                | (250)bps    |
| Loan balances (£m) <sup>8</sup>                      | <b>4,713</b>                        | 3,389                               | 39          |

1 Including AFS except where stated.

2 Revenue growth excluding AFS was 5.8 per cent.

3 Total income excluding AFS was £286 million, an increase of 4.4 per cent.

4 Excluding AFS.

5 Net interest receivable divided by average interest-bearing assets. Excluding AFS, 2016/17 was 3.9 per cent, a decrease of 20 basis points year-on-year.

6 Bad debt expense divided by gross lending. Excluding AFS, 2016/17 was 0.6 per cent, an increase of 20 basis points year-on-year.

7 Tier 1 capital divided by risk-weighted assets.

8 Loan balances excluding AFS was £4,003 million, an increase of 18 per cent year-on-year.

Financial Services total income increased to £347 million following a consolidation of AFS on 2 September 2016.

Financial Services delivered an underlying operating profit of £62 million, a 4.6 per cent decrease year-on-year. This decrease was mainly a result of the investment required to enter the mortgage market and the impact of reduced interchange fees.

Sainsbury's Bank cost/income ratio has increased by 100 basis points as a result of the strategic costs incurred on products and infrastructure which are expected to drive improved performance in future years.

Sainsbury's Bank active customers increased 3.5 per cent year-on-year to 1.77 million (2015/16: 1.71 million). The acquisition of AFS added a further 1.84 million customers in 2016/17.

Net interest margin increased by 30 basis points year-on-year to 4.4 per cent (2015/16: 4.1 per cent) driven by the acquisition of AFS that operates a higher risk and return operating model (excluding AFS, net interest margin was 3.9 per cent, a 20 basis point decrease year-on-year). Bad debt levels as a percentage of lending increased to 0.8 per cent (2015/16: 0.4 per cent), also as a result of the AFS operating model. The Tier 1 capital ratio decreased by 250 basis points year-on-year to 13.3 per cent (2015/16: 15.8 per cent), the primary drivers were increases to intangible assets and growth in customer lending. This growth in lending has led to an increase in the savings balance

of 28 per cent to £4,105 million (2015/16: £3,209 million). Loan balances including AFS increased by 39 per cent to £4,713 million, due to an increase in Sainsbury's Bank loan and credit card balances (13.4 per cent and 32.7 per cent respectively), as well as the addition of AFS store card balances of £710 million.

We have made good progress with our Bank transition programme. We have now delivered our flexible core platform, a new website, a new contact centre and migration of our savings customers took place successfully in September 2016, along with the migration of all our ATMs. We launched our new insurance offer in early 2017 and our new mortgage offer in April 2017, and our loans platform build is complete and now in test – we expect it to be operational by the end of 2017/18. Following the acquisition of HRG, we will now take the opportunity to create a common cards operating platform which we expect to launch by summer 2018. Spend to date totals £352 million, and we expect to spend a further £125 million to complete the transition – but with a significantly increased scope including the integration of AFS, insurance and mortgages. As a result of the growth opportunities Sainsbury's Bank now offers, we are well set to deliver strong profit growth.

At the end of the first half, AFS was transferred to Sainsbury's Bank and refinanced with the following key steps:

- £100 million capital injection from J Sainsbury plc to Sainsbury's Bank
- New customer deposits and a wholesale loan were raised by Sainsbury's Bank
- Sainsbury's Bank lent AFS circa £600 million by way of an intercompany loan
- AFS repaid its current circa £600 million intercompany loan with HRG subsidiaries which have previously funded the business
- HRG subsidiaries paid a dividend to J Sainsbury plc of circa £600 million
- The £448 million draw down on the Revolving Credit Facility used as consideration for the HRG acquisition was repaid in full

AFS holds a loan book with gross receivables of £699 million, offset by a provision of £63 million resulting in a 9.1 per cent provision as a percentage of receivables.

In 2017/18, underlying operating profit growth is expected to be ten per cent. Capital injections into the Bank are expected to be £160 million to £190 million in 2017/18. This is to cover card and loan platforms, regulatory capital and growth in loans, cards and mortgages.

Sainsbury's Bank transition cost is expected to be around £55 million (2016/17: £60 million) and transition capital costs are expected to be around £30 million (2016/17: £16 million).

### Underlying net finance costs

Underlying net finance costs decreased by £2 million year-on-year to £119 million (2015/16: £121 million), due to lower interest costs as a result of lower net debt, offset by the full-year effect of the perpetual securities coupons.

|                                     | 52 weeks to<br>11 March<br>2017<br>£m | 52 weeks to<br>12 March<br>2016<br>£m |
|-------------------------------------|---------------------------------------|---------------------------------------|
| <b>Underlying net finance costs</b> |                                       |                                       |
| <b>Underlying finance income</b>    | <b>18</b>                             | 19                                    |
| Interest costs                      | (121)                                 | (132)                                 |
| Perpetual securities coupons        | (23)                                  | (15)                                  |
| Capitalised interest                | 7                                     | 7                                     |
| <b>Underlying finance costs</b>     | <b>(137)</b>                          | (140)                                 |
| <b>Underlying net finance costs</b> | <b>(119)</b>                          | (121)                                 |

Sainsbury's expects net finance costs in 2017/18 to be similar year-on-year.

### Items excluded from underlying results

In order to provide shareholders with additional insight into the underlying performance of the business, items recognised in reported profit or loss before tax which, by virtue of their size and or nature, do not reflect the Group's underlying performance are excluded from the Group's underlying results and shown as items excluded from underlying results.

|  | 52 weeks to<br>11 March<br>2017<br>£m | 52 weeks to<br>12 March<br>2016<br>£m |
|--|---------------------------------------|---------------------------------------|
| <b>Items excluded from underlying results</b>                      |                                       |                                       |
| <b>Property related</b>  |                                       |                                       |
| Profit on disposal of properties                                   | 98                                    | 101                                   |
| Investment property fair value movements                           | (25)                                  | (18)                                  |
| Net impairment and onerous contract charge                         | (37)                                  | (1)                                   |
| <b>Argos</b>   |                                       |                                       |
| Transaction costs relating to the acquisition of Home Retail Group | (22)                                  | (12)                                  |
| Argos integration costs  | (27)                                  | –                                     |
| Homebase separation  | (4)                                   | –                                     |
| <b>Sainsbury's Bank transition</b>                                 | <b>(60)</b>                           | (59)                                  |
| <b>Focus</b>   |                                       |                                       |
| Business rationalisation   | 72                                    | (3)                                   |
| IT write-offs  | (57)                                  | –                                     |
| <b>Restructuring costs</b>   | <b>(33)</b>                           | (15)                                  |
| <b>Other</b>   |                                       |                                       |
| Perpetual securities coupons                                       | 23                                    | 15                                    |
| Non-underlying finance movements                                   | 10                                    | (22)                                  |
| Acquisition adjustments  | 8                                     | 3                                     |
| IAS 19 pension financing charge and scheme expenses                | (24)                                  | (28)                                  |
| <b>Items excluded from underlying results</b>                      | <b>(78)</b>                           | (39)                                  |

— Profit on disposal of properties includes the profit on the completion of the Nine Elms store which is a mixed use development opened in August 2016. Investment property fair value movements reflect the difference between the current and previous market values. The net impairment and onerous contract charge relates to lease exit and break costs and movements in the market value of land.

— The Group incurred £22 million of costs relating to the one-off legal and advisory fees in relation to the acquisition of HRG. Argos integration costs for the year of £27 million were part of the previously announced £130 million required over the three years in order to achieve the EBITDA synergies of £160 million. The Homebase separation and restructuring costs for the year of £4 million were part of the previously announced £75 million upon the sale of Homebase.

— Sainsbury's Bank transition costs of £60 million (2015/16: £59 million) relate to the costs incurred in transitioning to a new, more flexible banking platform.

— Business rationalisation includes £98 million profit on disposal of the Pharmacy business, offset by £26 million costs incurred closing non key businesses to enable the Group to focus on its core strategy. This included the closure of Netto, Sainsbury's Entertainment and Phoneshops. £57 million was incurred on cessation of non core IT projects.

— Internal restructuring costs of £33 million relate to changes to our store colleague structures and working practices.

— The coupons on the perpetual securities are added back as accounting standards determine that for statutory reporting purposes they are treated as dividends. The increase year-on-year reflects a full-year charge compared to a part-year charge in the previous year. Non-underlying finance movements mainly relate to a gain recognised in fixed power purchase agreements due to an increase in the forecast forward energy prices. Acquisition adjustments of £8 million (2015/16: £3 million) reflect the unwind of fair value adjustments arising from the Sainsbury's Bank and Home Retail Group acquisitions. Pension financing charge was £16 million (2015/16: £22 million) and defined benefit scheme expenses were £8 million (2015/16: £6 million).

## Taxation

The income tax charge was £126 million (2015/16: £77 million), with an underlying tax rate of 23.2 per cent (2015/16: 20.8 per cent) and an effective tax rate of 25.0 per cent (2015/16: 14.1 per cent). The underlying rate was higher than last year, mainly driven by the comparatively smaller benefit of a one per cent revaluation of underlying deferred tax balances in 2016/17 (2015/16: two per cent). The effective tax rate was higher than last year due to the comparatively smaller benefit of a one per cent revaluation of non-underlying deferred tax balances (2015/16: two per cent), and was also increased by non-tax deductible exceptional costs and the tax impact of transactions in 2016/17, including the recognition of a deferred tax liability on the Nine Elms replacement store.

| <b>Underlying tax rate</b><br>52 weeks to 11 March 2017                         | Profit<br>£m | Tax<br>£m    | Rate<br>%   |
|---|--------------|--------------|-------------|
| Underlying profit before tax, and tax thereon                                   | 581          | (135)        | 23.2        |
| Adjustments (and tax thereon) for:  |              |              |             |
| Items excluded from underlying results and revaluation of deferred tax balances | (78)         | 9            |             |
| <b>Profit before tax, and tax thereon</b>                                       | <b>503</b>   | <b>(126)</b> | <b>25.0</b> |

In 2017/18, Sainsbury's expects the full-year underlying tax rate to be between 23 and 24 per cent.

## Earnings per share

Underlying basic earnings per share decreased by 9.9 per cent to 21.8 pence (2015/16: 24.2 pence) reflecting the fall in underlying profits and the effect of additional shares issued during the year, as a result of the HRG acquisition and a higher year-on-year effective tax rate.

The weighted average number of shares in issue was 2,049.0 million (2015/16: 1,920.8 million), an increase of 128.2 million shares or 6.7 per cent primarily driven by the additional shares issued on acquisition of HRG.

In total, 261.1 million shares were issued as part of the HRG acquisition. These shares increased the full-year weighted average number of shares by 130.3 million. In 2017/18, the full effect of the shares issued on the weighted average number of shares will be 261.1 million.

Basic earnings per share was 17.5 pence (2015/16: 23.9 pence). The basic earnings per share was lower than the underlying basic earnings per share due to the items excluded from underlying results.

| <b>Underlying earnings per share</b><br>52 weeks to 11 March 2017                | <b>2017</b><br>pence<br>per share | 2016<br>pence<br>per share |
|--|-----------------------------------|----------------------------|
| <b>Basic earnings per share attributable to ordinary shareholders</b>            | <b>17.5</b>                       | 23.9                       |
| Adjustments (net of tax) for:  |                                   |                            |
| Items excluded from underlying results and revaluation of deferred tax balances  | <b>4.3</b>                        | 0.3                        |
| <b>Underlying basic earnings per share attributable to ordinary shareholders</b> | <b>21.8</b>                       | 24.2                       |

## Dividends

The Board has recommended a final dividend of 6.6 pence per share (2015/16: 8.1 pence). This will be paid on 7 July 2017 to shareholders on the Register of Members at the close of business on 12 May 2017, subject to approval by shareholders at the AGM. In line with the Group's policy to keep the dividend covered two times by underlying earnings, this will result in a decrease to the full-year dividend of 15.7 per cent to 10.2 pence per share (2015/16: 12.1 pence).

The proposed dividend will be, subject to approval, recommended by the Board on 2 May 2017 and, as such, has not been included as a liability as at 11 March 2017.

Sainsbury's plans to maintain a full-year dividend covered two times by our full-year underlying earnings.

## Acquisition of Home Retail Group plc

On 2 September 2016, Sainsbury's completed the acquisition of HRG for a total consideration of £1,093 million, primarily through a cash and shares offer, comprising 55 pence per share (£447 million) and 0.321 shares in J Sainsbury plc for each share held of HRG (£261 million new shares at a share price of £2.461).

The fair value of assets acquired at that date was £1,035 million. This included net £615 million customer loan book, £322 million of cash (after the capital return to HRG shareholders of £226 million, mainly in relation to the sale of Homebase by HRG) and £98 million of other net assets. The fair value of assets acquired was less than the fair value of the consideration by £58 million, which has been treated as goodwill. Putting aside the cash acquired and the customer loan back (which can be converted to cash), Sainsbury's effectively purchased the business for £156 million (£1,093 million consideration, less £615 million customer loan book and £322 million of net cash).

## Financing

The Group's key financing objectives are to diversify funding sources, to minimise refinancing risk and maintain appropriate contingent liquidity. As at 11 March 2017, Sainsbury's has drawn debt facilities of £2,700 million (including the perpetual securities) and undrawn committed credit facilities of £1,150 million. The Group also holds £85 million of uncommitted facilities which were undrawn as at 11 March 2017.

The principal element of Sainsbury's core funding comprises two long-term loans of £670 million due 2018 and £743 million due 2031 both secured on two ring-fenced portfolios of the Group's property assets. The Group has other secured facilities, namely a £200 million 'Green' Loan due 2019 and a five year £450 million Convertible Bond was entered into in November 2014. Further the Group has borrowed £138 million via six hire purchase facilities in respect of in-store moveable assets and finance leases. The Group maintains a syndicated committed Revolving Credit Facility of £1,150 million. The facility is split into two tranches, a £500 million Facility (A) maturing in May 2019 and a £650 million Facility (B) maturing in May 2020. As at 11 March 2017, £nil had been drawn from Facility (A) (March 2015/16: £nil) and £nil from Facility (B) (March 2015/16: £nil).

### Net debt and retail cash flows

Group net debt includes the capital injections in to Sainsbury's Bank, but excludes Sainsbury's Bank's own net debt balances. Sainsbury's Bank balances are excluded because they are required for business as usual activities. As at 11 March 2017, net debt was £1,477 million (12 March 2016: £1,826 million), a decrease of £349 million since the 2015/16 year-end. If the perpetual securities were treated as debt, net debt would increase from £1,477 million to £1,971 million (12 March 2016: £2,320 million).

|   | Retail<br>52 weeks to<br>11 March<br>2017<br>£m | Retail<br>52 weeks to<br>12 March<br>2016<br>£m |
|---|---|---|
| <b>Summary cash flow statement<sup>1</sup></b>                                  |   |   |
| <b>Retail operating cash flow before changes in working capital<sup>2</sup></b> | <b>1,172</b>                                    | 1,202   |
| Decrease in working capital   | <b>68</b>                                       | 23  |
| <b>Cash generated from retail operations<sup>3</sup></b>                        | <b>1,240</b>                                    | 1,225   |
| Pension contribution  | <b>(112)</b>                                    | (76)  |
| Net interest paid <sup>4</sup>  | <b>(108)</b>                                    | (102)   |
| Corporation tax paid  | <b>(87)</b>                                     | (124)   |
| <b>Net cash generated from retail operating activities<sup>5</sup></b>          | <b>933</b>                                      | 923   |
| Cash capital expenditure before strategic capital expenditure <sup>6</sup>      | <b>(588)</b>                                    | (627)   |
| <b>Retail free cash flow</b>  | <b>345</b>                                      | 296   |
| Dividends paid on Ordinary Shares   | <b>(230)</b>                                    | (234)   |
| Exceptional pension contributions   | <b>(199)</b>                                    | (125)   |
| Property related including strategic capital expenditure <sup>4</sup>           | <b>28</b>                                       | 155   |
| Proceeds from sale of Pharmacy  | –   | 125   |
| Bank capital injections   | <b>(130)</b>                                    | (137)   |
| HRG acquisition and AFS loan book refinancing <sup>4</sup>                      | <b>457</b>                                      | –   |
| Proceeds from issue of perpetual securities & convertible bonds                 | –   | 494   |
| Repayment of borrowings including finance leases <sup>4</sup>                   | <b>(211)</b>                                    | (363)   |
| Other <sup>4</sup>  | <b>(10)</b>                                     | (31)  |
| <b>Net increase in cash and cash equivalents</b>                                | <b>50</b>                                       | 180   |
| Decrease in debt  | <b>211</b>                                      | 363   |
| Acquisition movements   | <b>39</b>                                       | –   |
| Fair value and other non-cash movements   | <b>49</b>                                       | (26)  |
| <b>Movement in net debt</b>   | <b>349</b>                                      | 517   |
| <b>Opening net debt</b>   | <b>(1,826)</b>                                  | (2,343)   |
| <b>Closing net debt</b>   | <b>(1,477)</b>                                  | (1,826)   |
| <b>Closing net debt (including hybrid securities as debt)</b>                   | <b>(1,971)</b>                                  | (2,230)   |

1 See note 4 for a reconciliation between the Retail and Group cash flows.

2 Excludes working capital, pension contributions and exceptional pension contributions.

3 Excludes pension contributions and exceptional pension contributions.

4 Refer to the Alternative Performance Measures for definition.

5 Excludes exceptional pension contributions.

6 Excludes purchase of Chiswick freehold and Argos integration capital expenditure.

Operating cash flow before changes in working capital declined in the year to £1,172 million due to the fall in Group operating profit. However, due to continued focus on working capital and a reduction in capital expenditure, free cash flow increased in the year to £345 million (2016/17: £296 million).

Cash generated by operations were used to fund dividends and exceptional pension contributions. Dividends of £230 million were paid in year, which are covered 1.5 times by free cash flow. Exceptional pension contributions of £199 million were made in the year which included the £125 million announced in August 2016, to the Sainsbury's defined benefit pension scheme, and £74 million to the HRG defined benefit pension scheme which included £24 million in relation to the sale of Homebase and £50 million which was agreed as part of the acquisition of HRG.

Property related items generated £28 million in the year which is net of £92 million spent on the acquisition of the Chiswick freehold and Argos integration capital expenditure. In the prior year £155 million was generated from property related items and £125 million was received in advance of completion of the sale of Pharmacy which completed in the current year.

The HRG acquisition and AFS loan book reduced net debt by £457 million.

— Cash paid on acquisition of HRG (including £3 million on share issuance) totalled £450 million.

— HRG held £548 million in cash at the point of acquisition of which £226 million was immediately paid as a capital return to the HRG shareholders.

— Following the acquisition the Group was reorganised with the AFS business being transferred to the Financial Services division. This refinancing of the Argos Financial Services loan book generated £585 million.

Sainsbury's expects 2017/18 year-end net debt to remain around £1.5 billion. We expect net debt to reduce over the medium term.

### Group capital expenditure

Group capital expenditure was £703 million; made up of £639 million net retail capital expenditure and £64 million Financial Services capital expenditure.

Core retail expenditure of £547 million was up 0.9 per cent (2015/16: £542 million), driven by the addition of Argos core retail capital expenditure of £38 million.

Net retail capital expenditure was £639 million (2015/16: £543 million), which includes the purchase of a freehold at Chiswick, where there may be future potential for a mixed use development, and £18 million Argos integration capital expenditure.

|   | 52 weeks to<br>11 March<br>2017<br>£m | 52 weeks to<br>12 March<br>2016<br>£m <sup>1</sup> |
|---|---------------------------------------|--|
| <b>Group capital expenditure</b>                                    |                                       |  |
| Sainsbury's new store development                                   | <b>120</b>                            | 222  |
| Sainsbury's extensions and refurbishments                           | <b>133</b>                            | 168  |
| Sainsbury's other – including supply chain and digital & technology | <b>256</b>                            | 152  |
| <b>Sainsbury's core retail capital expenditure</b>                  | <b>509</b>                            | 542  |
| Argos core retail capital expenditure                               | <b>38</b>                             | –  |
| <b>Total core retail capital expenditure</b>                        | <b>547</b>                            | 542  |
| Acquisition of freehold and trading properties <sup>2</sup>         | <b>74</b>                             | –  |
| Debtor/creditor movements   | –                                     | 1  |
| Argos integration capital expenditure                               | <b>18</b>                             | –  |
| <b>Net retail capital expenditure</b>                               | <b>639</b>                            | 543  |
| Financial Services capital expenditure                              | <b>64</b>                             | 29   |
| Group net capital expenditure                                       | <b>703</b>                            | 572  |
| <b>Capex/sales ratio (%)<sup>3</sup></b>                            | <b>1.9</b>                            | 2.1  |

1 Comparative figures within core retail capital expenditure have been restated to reflect reclassification of certain types of capital expenditure.

2 2015/16 balance includes income from Harvest, our JV with Land Securities, relating to the repayment of a loan.

3 Core retail capital expenditure divided by retail sales (including fuel, including VAT).

In 2017/18, Sainsbury's expects core retail capital expenditure including business as usual Argos capital expenditure (excluding Sainsbury's Bank and Argos integration capital expenditure) to be around £600 million. Core retail capital expenditure is expected to be around £600 million per annum over the medium term.

Argos integration capital expenditure is expected to be around £90 million.

### Return on capital employed (ROCE)

The ROCE on the 14 point average basis over the 52 weeks to 11 March 2017 was 8.8 per cent (2015/16: 8.8 per cent), a year-on-year decrease of four basis points. Excluding the retirement benefit obligation (net of deferred tax) from capital employed, ROCE over the 52 weeks to 11 March 2017 was 8.0 per cent (2015/16: 8.3 per cent), 29 basis points lower than for the 52 weeks to 12 March 2016. ROCE decline was mainly due to the fall in underlying operating profit and the additional capital employed following the HRG acquisition.

|  | 52 weeks to<br>11 March 2017 | 52 weeks to<br>12 March 2016 |
|--|------------------------------|------------------------------|
| <b>Return on capital employed<sup>1</sup></b>              |                              |                              |
| Total underlying operating profit (£m)                     | <b>688</b>                   | 700                          |
| Underlying share of post-tax profit from JVs (£m)          | <b>12</b>                    | 8                            |
| Underlying profit before interest and tax (£m)             | <b>700</b>                   | 708                          |
| Average capital employed (£m)                              | <b>7,964</b>                 | 8,021                        |
| Return on capital employed (%)                             | <b>8.8</b>                   | 8.8                          |
| Return on capital employed (exc. pension fund deficit) (%) | <b>8.0</b>                   | 8.3                          |
| 52 week ROCE movement                                      | <b>(4)bps</b>                |                              |
| 52 week ROCE movement (exc. pension fund deficit)          | <b>(29)bps</b>               |                              |

1 The 14 point period average includes the opening capital employed as at 12 March 2016 and the closing capital employed for each of the 13 individual four week periods to 11 March 2017.

### Financial ratios

| Key Financial ratios<br>(with perpetual securities accounted for as equity) | As at<br>11 March<br>2017 | As at<br>12 March<br>2016 |
|---|---------------------------|---------------------------|
| Adjusted net debt to EBITDAR <sup>1</sup>                                   | <b>3.7 times</b>          | 4.0 times                 |
| Interest cover <sup>2</sup>   | <b>7.3 times</b>          | 6.7 times                 |
| Fixed charge cover <sup>3</sup>   | <b>2.7 times</b>          | 2.8 times                 |
| Gearing <sup>4</sup>  | <b>21.5%</b>              | 28.7%                     |
| Gearing (excluding pension deficit) <sup>5</sup>                            | <b>19.1%</b>              | 27.0%                     |

### Key Financial ratios (with perpetual securities treated as debt)<sup>6</sup>

|                                     |                  |           |
|-------------------------------------|------------------|-----------|
| Adjusted net debt to EBITDAR        | <b>4.0 times</b> | 4.3 times |
| Interest cover                      | <b>5.9 times</b> | 5.9 times |
| Fixed charge cover                  | <b>2.6 times</b> | 2.7 times |
| Gearing                             | <b>30.9%</b>     | 39.5%     |
| Gearing (excluding pension deficit) | <b>27.3%</b>     | 37.1%     |

1 Net debt of £1,477 million plus capitalised lease obligations of £5,938 million, divided by Group underlying EBITDAR of £2,000 million, calculated for a 52 week period to 11 March 2017.

2 Underlying profit before interest and tax divided by underlying net finance costs.

3 Group underlying EBITDAR divided by net rent and underlying net finance costs.

4 Net debt divided by net assets.

5 Net debt divided by net assets, excluding pension deficit.

6 Treating the perpetual securities, net of transaction fees, as debt increases net debt to £1,971 million, and reduces net assets to £6,426 million.

### Property value

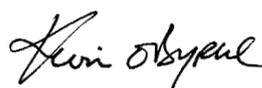
As at 11 March 2017, Sainsbury's estimated market value of properties, including our 50 per cent share of properties held within property JVs, was £10.3 billion (12 March 2016: £10.6 billion). The £0.3 billion decrease was mainly due to a reduction in market rental values and a small yield movement.

### Defined benefit pensions

At 11 March 2017, the net defined benefit obligation for the Group was £974 million (including HRG and the unfunded obligation). The increase in the deficit from the prior year-end is primarily driven by the consolidation of the HRG scheme, as well as a significant actuarial loss due to a fall in the discount rate from 3.65 per cent to 2.70 per cent.

Following agreement of the valuation of both schemes the Group is committed to make annual contributions of £124 million to the scheme (Sainsbury's scheme: £84 million; Argos scheme: £40 million). The next triennial valuations are for the March 2018 year-ends for both schemes.

|   | Argos<br>As at<br>11 March<br>2017<br>£m | Sainsbury's<br>As at<br>11 March<br>2017<br>£m | Group<br>As at<br>11 March<br>2017<br>£m | Group<br>As at<br>12 March<br>2016<br>£m |
|---|--|--|--|--|
| <b>Retirement benefit obligations</b>     |  |  |  |  |
| Present value of funded obligations       | <b>(1,413)</b>                           | <b>(9,441)</b>                                 | <b>(10,854)</b>                          | (7,625)                                  |
| Fair value of plan assets                 | <b>1,212</b>                             | <b>8,708</b>                                   | <b>9,920</b>                             | 7,235                                    |
| Pension deficit                           | <b>(201)</b>                             | <b>(733)</b>                                   | <b>(934)</b>                             | (390)                                    |
| Present value of unfunded obligations     | <b>(17)</b>                              | <b>(23)</b>                                    | <b>(40)</b>                              | (18)                                     |
| Retirement benefit obligations            | <b>(218)</b>                             | <b>(756)</b>                                   | <b>(974)</b>                             | (408)                                    |
| Deferred income tax asset                 | <b>47</b>                                | <b>77</b>                                      | <b>124</b>                               | 19                                       |
| <b>Net retirement benefit obligations</b> | <b>(171)</b>                             | <b>(679)</b>                                   | <b>(850)</b>                             | (389)                                    |



**Kevin O'Byrne**  
Chief Financial Officer

# J Sainsbury plc: Board of Directors



## 1 David Tyler (64)\* Chairman

**Date of appointment:** 1 October 2009  
David has served as a Non-Executive Director since 1 October 2009 and as Chairman since 1 November 2009.

**Skills and experience:** David has broad and extensive experience in both executive and non-executive roles across the consumer, retail, business services and the financial services sectors. He is also an experienced chairman having served in that role previously at Logica plc and 3i Quoted Private Equity plc and currently at Hammerson plc and Domestic and General Group Limited. His last executive position was as Finance Director of GUS plc, and previously he held senior financial and general management roles with Christie's International Plc, County NatWest Limited and Unilever PLC. He has also been a Non-Executive Director of Experian plc, Reckitt Benckiser Group plc and Burberry Group Plc.

**Other roles:** Chairman of Hammerson plc  
Chairman of Domestic and General Group Limited

## 2 Mike Coupe (56)♥ Chief Executive Officer

**Date of appointment:** 1 August 2007  
Mike has served as an Executive Director since 1 August 2007 and as Chief Executive Officer since 9 July 2014

**Skills and experience:** Appointed Chief Executive Officer on 9 July 2014, Mike has been a member of the Operating Board since October 2004. Mike has vast retail industry experience in trading, strategy, marketing, digital and online as well as multi-site store experience. He joined Sainsbury's from Big Food Group where he was a board director of Big Food Group plc and Managing Director of Iceland Food Stores. He previously worked for both ASDA and Tesco, where he served in a variety of senior management roles.

**Other roles:** Non-Executive Director of Greene King plc

**3 Kevin O'Byrne (52)****Chief Financial Officer****Date of appointment:** 9 January 2017**Skills and experience:** Kevin joined the Board on 9 January 2017 and brings a wealth of retail and finance experience. Kevin was previously Chief Executive Officer of Poundland Group until December 2016 and held executive roles at Kingfisher plc from 2008 to 2015, including Chief Executive Officer of B&Q UK & Ireland and Group Finance Director. Prior to this, Kevin was Group Finance Director of Dixons Retail plc.**Other roles:** Non-Executive Director and Chairman of the Audit Committee of Land Securities Group PLC**4 John Rogers (48)****Chief Executive Officer of Sainsbury's Argos****Date of appointment:** 19 July 2010

John served as Chief Financial Officer of J Sainsbury plc from 19 July 2010 until 5 September 2016 when he was appointed as Chief Executive Officer of Sainsbury's Argos.

**Skills and experience:** John has extensive experience in finance, strategy, digital, online, property and financial services. John became Chief Executive Officer of Sainsbury's Argos on 5 September 2016 following the acquisition of Home Retail Group. Prior to this appointment, John was Chief Financial Officer of J Sainsbury plc for six years and had responsibility for finance, group strategy, Sainsbury's online, business development, property, procurement and operational efficiency. He was also Director of Corporate Finance from 2005 to 2007, Director of Group Finance from 2007 to 2008 and in July 2008, he was appointed to the Operating Board as Property Director. John is also a member of the Sainsbury's Bank plc Board. Prior to Sainsbury's, John was Group Finance Director for Hanover Acceptances, a diversified corporation with wholly-owned subsidiaries in the food manufacturing, real estate and agri-business sectors.**Other roles:** Non-Executive Director of Travis Perkins plc**5 Matt Brittin (48) ♦ \*****Non-Executive Director****Date of appointment:** 27 January 2011**Skills and experience:** As Google's President – Europe, Middle East and Africa, Matt has extensive experience of running a high profile, fast moving, innovative, digital business. Before joining Google to run its UK operations at the start of 2007, Matt spent much of his career in media and marketing, with particular interests in strategy, commercial development and sales performance. This included commercial and digital leadership roles in UK media. He is also a Director of charitable organisation, The Media Trust.**Other roles:** Google's President – Europe, Middle East and Africa**6 Brian Cassin (49) ♦ \*****Non-Executive Director****Date of appointment:** 1 April 2016**Skills and experience:** Brian brings present day experience of running a FTSE40 company and of big data and analytics – topics of key importance to Sainsbury's. Brian joined Experian as Chief Financial Officer in April 2012, a post he held until his appointment as Chief Executive Officer in July 2014. Prior to this, Brian spent his career in investment banking at Baring Brothers International, Greenhill & Co where he was Managing Director and Partner and the London Stock Exchange where he held senior roles.**Other roles:** Chief Executive Officer of Experian plc**7 Mary Harris (51) ♦ ♥ \*****Non-Executive Director****Date of appointment:** 1 August 2007

Mary is due to step down from the Board on 5 July 2017.

**Skills and experience:** Mary has extensive strategic experience in consumer goods and brings a strong understanding of a customer led retail environment to the Board. Mary is a Non-Executive Director of ITV plc and Reckitt Benckiser Group plc and a Member of the supervisory board of Unibail-Rodamco S.E. She is former member of the Supervisory Board of TNT Express NV and spent much of her career with McKinsey & Company, most recently as a partner, where she worked primarily with retail/consumer clients in China, South East Asia and Europe. Her previous work experience includes working for PepsiCo in Greece and the UK, as a sales and marketing executive.**Other roles:** Non-Executive Director of ITV plc and Reckitt Benckiser Group plc and a member of the supervisory board of Unibail-Rodamco S.E.**8 David Keens (63) ♦ \*****Non-Executive Director****Date of appointment:** 29 April 2015**Skills and experience:** David has extensive retail experience and knowledge of consumer facing businesses, together with his core skills in finance. David is also a Non-Executive Director and the Senior Independent Director of Auto Trader Group plc, and chairs its Audit Committee. David was formerly Group Finance Director of NEXT plc from 1991 to 2015 and their Group Treasurer from 1986 to 1991. Previous management experience includes nine years in the UK and overseas operations of multinational food manufacturer Nabisco and, prior to that, seven years in the accountancy profession.**Other roles:** Non-Executive Director, the Senior Independent Director and Chair of the Audit Committee of Auto Trader Group plc**9 Susan Rice (71) ♦ \*****Senior Independent Director****Date of appointment:** 1 June 2013

Susan has served as a Non-Executive Director since 1 June 2013 and has been the Senior Independent Director since 6 July 2016.

**Skills and experience:** Susan has extensive experience as a Non-Executive Director, as well as in retail banking, financial services, leadership and sustainability. Her career in retail banking is particularly relevant to our ownership of Sainsbury's Bank. Susan is Chairman of Scottish Water and Business Stream. Previously, Susan was a member of the First Minister's Council of Economic Advisors, Managing Director of Lloyds Banking Group Scotland and was previously Chief Executive and then Chairman of Lloyds TSB Scotland plc. She has also held a range of other non-executive directorships including at the Bank of England and SSE plc.**Other roles:** Chairman of Scottish Water, Chairman of Business Stream, Chairman of the Scottish Fiscal Commission and a Non-Executive Director of the North American Income Trust.**10 Jean Tomlin (62) ♦ ♥ \*****Non-Executive Director****Date of appointment:** 1 January 2013**Skills and experience:** Jean has extensive experience and breadth of skills in human resources and corporate responsibility. Jean was formerly Director of HR, Workforce and Accreditation for The London Organising Committee of the Olympic and Paralympic Games, where she oversaw the creation and execution of the hugely successful Games Maker volunteering programme. She was previously Group HR Director at Marks and Spencer Group PLC, HR Director and founder member of Egg plc and Sales & Operations Director of Prudential Direct.**Other roles:** Independent Board member of Michael Kors Holdings Limited, a Trustee of Step Up To Serve, and a Council Member at Loughborough University.**Retirements in 2016/17:** In line with best practice, John McAdam retired from the Board on 6 July 2016.**Life President****Lord Sainsbury of Preston Candover KG****Key to Committee members**

- ♦ Remuneration Committee
- Audit Committee
- \* Nomination Committee
- ♥ Corporate Responsibility and Sustainability Committee

♦ ● ♥ ♦ ♥ Denotes Chairman of Committee

# J Sainsbury plc: Operating Board



**1 Mike Coupe**  
**Chief Executive Officer**

See page 54.

**2 Kevin O'Byrne**  
**Chief Financial Officer**

See page 55.

**3 John Rogers**  
**Chief Executive Officer of Sainsbury's Argos**

See page 55.

**4 Tim Fallowfield**  
**Company Secretary & Corporate Services Director**

**Date of appointment:** September 2004

**Skills and experience:** Tim joined Sainsbury's in 2001 as Company Secretary and joined the Operating Board in 2004. In addition to his role as Company Secretary, Tim is responsible for the Corporate Services Division comprising Legal Services, Data Governance, Safety, Shareholder Services, Insurance and Central Security. He chairs the Group Safety Committee and the Data Governance Committee. Tim joined Sainsbury's from Exel plc, the global logistics company, where he was Company Secretary and Head of Legal Services. He began his career at the international law firm Clifford Chance and is a qualified solicitor.

**5 Peter Griffiths, OBE**  
**Chief Executive Officer of Sainsbury's Bank**

**Date of appointment:** May 2014

**Skills and experience:** Peter was appointed CEO of Sainsbury's Bank in November 2012 and joined the Operating Board in May 2014. Prior to joining Sainsbury's he was Group Chief Executive of Principality, the largest building society in Wales, growing it from the 13th largest building society in the UK to the 7th, during his decade in charge. He previously worked for NatWest, and was Chief Operating Officer at Morgan Chambers Plc. He is former Chairman of the CBI Wales and the Building Societies Association, and is a Fellow of UWIC and The Chartered Institute of Management. Peter was awarded an OBE in the Queen's Birthday Honours 2010, in recognition of his support for the Financial Services Industry.

**6 Jon Hartland****Acting Retail and Operations Director****Date of appointment:** October 2015

**Skills and experience:** Jon joined Sainsbury's in 1986 and held the position of Store Director for numerous stores until 1996. He then held a number of senior roles before becoming the Change Director in 2002 and later becoming the Central Retail Director. Jon was appointed Director for Non-Food Operations in 2011 and has been acting as the Retail and Operations Director role since October 2015. He sits on the GS1 apparel Europe board and was previously a Regional manager for Fine Fare (part of Associated British Foods plc).

**7 Paul Mills-Hicks****Food Commercial Director****Date of appointment:** May 2014

**Skills and experience:** Paul joined the Operating Board in May 2014 as Food Commercial Director having spent over ten years at Sainsbury's. He was closely involved in the formation and execution of the 'Making Sainsbury's Great Again' strategy. Following this he held a variety of roles in commercial, strategy and finance, most recently as Business Unit Director for Grocery. Prior to Sainsbury's, Paul was European Controller at Marks and Spencer Group plc and a Director at UBS Warburg.

**8 Angie Risley****Group HR Director****Date of appointment:** January 2013

**Skills and experience:** Angie was appointed Group HR Director and a member of the Operating Board in January 2013 with responsibility for human resources. She is also a Non-Executive Director of Serco Group plc and chairs their Remuneration Committee and is a Director of Sainsbury's Bank plc. Angie was most recently Group HR Director at Lloyds Banking Group and prior to this an Executive Director of Whitbread plc with responsibility for HR and Corporate Social Responsibility. She was a member of the Low Pay Commission.

**9 Richard Newsome****Acting Digital and Technology Director****Date of appointment:** January 2017

**Skills and experience:** Richard joined the Operating Board in January 2017, with responsibility for the Digital & Technology Division. He joined Sainsbury's in July 2014 as Director of Operations, from Rolls-Royce where he was responsible for Global IT Programme Delivery. Prior to that Richard had been UK IT Director for Cadbury and Kraft Foods, Client Director for Xansa's IT Outsourcing business, and had a long career in IT and Business Change at The Boots Company.

**Simon Roberts****Retail and Operations Director****Date of appointment:** Simon is due to join the Operating Board in July 2017.

# Corporate Governance



## Dear Shareholder

The Board this year has maintained its particular focus on the Company's strategic direction and on driving the creation of sustainable long-term value for shareholders. This is particularly important in a sector like ours which is experiencing significant change and which is highly competitive.

Over an extended period, the Board considered the potential attractions of Argos and was closely engaged this year with the acquisition of its owner, Home Retail Group plc (HRG), believing that this will accelerate the strategy announced in 2014. We are pleased with the pace of integration and the opportunities that Argos is providing. We are now a multi-channel, multi-product retailer with a market-leading digital offer and nationwide fast-track delivery capabilities.

Food is our core business and it is our priority to offer customers great quality and choice at fair prices which differentiates us in an increasingly competitive market. The Board reviews our supermarket business on a regular basis to ensure it is well positioned to meet the challenges of the current trading environment. Our focus is on creating the differentiated offer our customers want and achieving cost savings and efficiencies.

Another of our priorities has been the delivery of the growth strategy of Sainsbury's Bank. During the year we have had a number of opportunities to meet the Bank's management team and Board, to discuss progress and agree the key actions for the short and medium term.

Upon the completion of the HRG acquisition, we reviewed our senior management structure and made some important changes to the executive team. We take succession at Board and senior management level very seriously and believe that we have management of the highest calibre. We announced that John Rogers, our Chief Financial Officer since 2010, would be appointed to the key role of Chief Executive Officer of Sainsbury's Argos. In this role he will continue to drive the integration of Argos with Sainsbury's general merchandise business, and deliver the ongoing digital transformation across Sainsbury's Argos. John and the experienced Management Board at Sainsbury's Argos have made an excellent start in their new roles.

We welcomed Kevin O'Byrne as our new Chief Financial Officer in January 2017. Kevin has a wealth of retail and financial experience from his previous senior roles at Kingfisher, Dixons and Poundland and has a track record in growing businesses. We are sure that he will make a great contribution to the business and to the Board. We are also pleased that Simon Roberts is joining Sainsbury's as Retail and Operations Director on the Operating Board. Simon previously held senior positions at Boots and Marks & Spencer and we believe that he will have a major impact on our future success.

We are sorry that Mary Harris will be stepping down from the Board at this year's AGM having completed over nine years of service as a Non-Executive Director. I would like to thank Mary for her very valuable contribution over that time and particularly for her skilful leadership of the Remuneration Committee over recent years. I am pleased that Susan Rice will take over as Chairman of the Remuneration Committee on Mary's departure. A search for a new Non-Executive Director to join the Board is under way.

As a Board, we take governance very seriously and we regularly discuss and review our ways of working and our effectiveness. During the year, we asked Manchester Square Partners (MSP) to carry out a review of our effectiveness and are now working through an action plan, based on their feedback, to build on our strong foundations. We believe that Sainsbury's unique values and culture play a key role in our success and we were therefore particularly pleased with MSP's conclusion in this regard that "the Board embodies and leads by example on the behaviours and culture which Sainsbury's aims to drive throughout the organisation". Their review is described in detail on page 61.

We continue to have a mix of men, women and ethnic backgrounds on our Board. This diversity is in line with good governance and appropriate for both Sainsbury's and our customer base. We continue to focus on increasing our diversity and inclusivity at all levels of the business and I draw your attention to the detailed review on pages 39 and 65.

**David Tyler**  
**Chairman**

### Compliance Statement

The Board is committed to strong governance and, during the year, the Company has complied with all the provisions of the UK Corporate Governance Code (Governance Code). This report outlines how we have applied the Governance Code's main principles throughout the year.

Published by the Financial Reporting Council, the Governance Code is available at [www.frc.org.uk](http://www.frc.org.uk)

# Leadership

## How we are governed

The Board currently comprises three Executive Directors, the Chairman and six Non-Executive Directors. The Non-Executive Directors bring wide and varied commercial experience to the Board and committees. The Directors are subject to election by shareholders at the first AGM after their appointment and re-election at each AGM thereafter. All members of the Board, other than Mary Harris, will retire and seek election or re-election by shareholders at this year's AGM. John McAdam stepped down from the Board in July 2016 and Susan Rice succeeded him as Senior Independent Director.

In the period between John Rogers being appointed as Chief Executive Officer of Sainsbury's Argos in September 2016 and Kevin O'Byrne being appointed as Chief Financial Officer of the Company in January 2017, Ed Barker acted as Interim Chief Financial Officer and attended Board meetings and investor relations presentations in that capacity.

## Division of responsibilities

### Chairman, David Tyler

Responsible for leadership of the Board, ensuring its effectiveness in all aspects of its role and for setting the Board agenda. Ensures effective communication with shareholders and that the Board is aware of the views of major shareholders. Facilitates the contribution of the Non-Executive Directors through a culture of openness and debate, and ensures constructive relations between Executive and Non-Executive Directors.

### Chief Executive Officer, Mike Coupe

Responsible for the day-to-day management of the Group and executing the strategy, once agreed by the Board. Creates a framework of strategy, values, organisation and objectives to ensure the successful delivery of results, and allocates decision making and responsibilities accordingly. Manages the risk profile in line with the risk appetite identified and accepted by the Board. Takes a leading role, with the Chairman, in the relationship with all external agencies and in promoting Sainsbury's.

### Senior Independent Director, Susan Rice

Acts as a sounding board for the Chairman and as a trusted intermediary for the other Directors. Meets with the other Non-Executive Directors in the absence of the Chairman at least once a year in order to undertake a review of the Chairman's performance. Available to discuss with shareholders their views and any concerns that cannot be resolved through the normal channels of communication with the Chairman or the Executive Directors.

## Role of the Board and its committees

### Board

The Board is responsible for the long-term success of the Company, setting the Company's strategy, financial objectives and risk appetite, providing leadership to the business including on culture, values and ethics, monitoring the Company's overall financial performance and ensuring effective corporate governance and succession planning.

The matters reserved for the Board can be found on our website at [www.j-sainsbury.co.uk](http://www.j-sainsbury.co.uk)

### Operating Board

Day-to-day management of the Group is delegated to the Operating Board, which is chaired by Mike Coupe. The Operating Board has delegated certain powers to the Operating Board Committees, each of which has approved terms of reference setting out its areas of responsibility. John Rogers and Peter Griffiths represent the Sainsbury's Argos Management Board and the Sainsbury's Bank Board respectively on the Operating Board. The Operating Board held 12 scheduled meetings during the year. The responsibilities of each Director are set out on [pages 56 and 57](#).

### Committees

#### Audit Committee

The Audit Committee reviews the integrity of the financial information provided to shareholders, oversees the Company's system of internal controls and risk management, approves the internal and external audit process, and monitors the process for compliance with relevant laws, regulations and policies.

**i** More details on [page 68](#)

#### Remuneration Committee

The Remuneration Committee recommends and reviews the remuneration policy, ensuring it is aligned to the long-term success of the Company. It also approves the remuneration and benefits of Executive and Operating Board Directors.

**i** More details on [page 74](#)

#### Nomination Committee

The Nomination Committee reviews the balance of skills, knowledge, experience, independence and diversity of the Board and its Committees, and succession planning at Board and senior management levels.

**i** More details on [page 64](#)

#### Corporate Responsibility and Sustainability Committee

The Corporate Responsibility and Sustainability (CR&S) Committee reviews the broad CR&S strategy and the Company's progress on the key corporate responsibility initiatives including diversity, values and colleague and customer insights.

**i** More details on [page 66](#)

\*Terms of reference for each committee can be found on the website.

### Operating Board Committees

**Corporate Responsibility and Sustainability Steering Group**  
**Mike Coupe**

**Data Governance Committee**  
**Tim Fallowfield**

**Trading Board**  
**Paul Mills-Hicks**

**Investment Board**  
**Kevin O'Byrne**

**Group Safety Committee**  
**Tim Fallowfield**

**Diversity and Inclusivity Steering Group**  
**Angie Risley**

## Key areas of focus of the Board

The Board and Committees have a scheduled forward programme of meetings. This ensures that sufficient time is allocated to each key area and the Board's time together is used effectively. There is sufficient flexibility in the programme for specific items to be added to the agenda which enables the Board to focus on key matters relating to the business at the appropriate time.

The principal activities of the Board during the financial year included the following items, some of which were considered at each meeting, and others were reviewed periodically throughout the year:

| Item  |
|---|
| <b>Financial and Operational Performance</b><br>The Board reviewed and discussed: <ul style="list-style-type: none"> <li>— Annual budget and Corporate (five year) plan</li> <li>— CEO Report including a market and trading update</li> <li>— Performance against key targets of Sainsbury's, Sainsbury's Argos and Sainsbury's Bank</li> <li>— Customer insights and service standards</li> <li>— Financial items including Preliminary and Interim results and the Annual Report</li> <li>— Dividend Policy and recommendations</li> <li>— Treasury and tax policy</li> <li>— Pensions</li> </ul>        |
| <b>Strategy</b><br>At the strategy conference and on a regular basis throughout the year, the Board reviewed: <ul style="list-style-type: none"> <li>— The implementation of the agreed strategic plan, focusing particularly on the HRG acquisition and integration, the core supermarket strategy and Sainsbury's Bank</li> <li>— Potential further strategic initiatives</li> <li>— Regular market updates</li> <li>— Competitor performance</li> </ul>  |
| <b>Risk &amp; Governance</b><br>The Board reviewed and discussed risk and governance matters including: <ul style="list-style-type: none"> <li>— Reports from the Board committees – Audit, Remuneration, Nomination and CR&amp;S</li> <li>— Information security and data governance</li> <li>— Board Evaluation</li> <li>— Corporate Responsibility and Sustainability</li> <li>— Internal controls and risk management</li> <li>— Safety reports (health and safety, and food)</li> <li>— Public Affairs</li> <li>— Litigation</li> <li>— Investor relations and other stakeholder engagement</li> </ul> |
| <b>Colleagues</b><br>The Board received updates on: <ul style="list-style-type: none"> <li>— Talent, diversity and succession planning</li> <li>— Colleague pay</li> <li>— Significant reorganisations</li> <li>— HR Policy</li> </ul>  |

## Strategy

The Board continued to prioritise its reviews of the implementation of the agreed strategic plans, focusing particularly on the HRG acquisition, the core supermarket strategy and Sainsbury's Bank. A two day strategy conference, with the attendance of the Board and Operating Board, was held in October. The strategy conference was a key opportunity for the Board to discuss, challenge and focus on strategy, including in-depth reviews of the retail market, competition, pricing and promotions, customer insights, Sainsbury's Bank strategy and the five year corporate plan. The strategy conference is carefully structured to achieve a balance between presentations and time for debate and discussion. External advisers attended for part of the conference. During the year, the Board also received regular updates on progress against the strategy and, in July, it will agree the objectives and principal areas of focus for the next strategy conference.

## Home Retail Group acquisition

Given the strategic importance of the acquisition of HRG, the Board was fully engaged in planning, negotiating and approving the transaction, which is summarised below.

|   |   |  |
|---|---|--|
|    | <b>Planning</b>   | The Board had in depth discussions over several months about the benefits and potential long-term shareholder value that could be created through a potential acquisition of HRG. The Board provided challenge and guidance to the executive team. The Board's detailed review confirmed that the combination of the businesses was attractive in principle for shareholders and customers of both companies.  |
|    | <b>Negotiation</b>                                      | In November 2015, the Company approached HRG about the possibility of a combination of the two businesses. On 5 January 2016, Sainsbury's announced a possible offer for HRG. A sub-committee was established to oversee the negotiations and due diligence, and to ensure robust governance. The Board approved the terms and conditions of the offer.  |
|    | <b>Completing the deal and planning the integration</b> | On 2 April 2016, the HRG Board announced they would recommend Sainsbury's offer to their shareholders. During April to September, the Board had oversight of the progress of the transaction and supported the sub-committee in making decisions on a timely basis. Relevant documentation was reviewed and approved by the Board.<br><br>It was imperative that there was an organisational and operational plan in place to commence integration. The Board approved the appointment of John Rogers as Chief Executive Officer of Sainsbury's Argos on completion of the deal. |
|  | <b>Post completion and integration</b>                  | The acquisition completed on 2 September 2016. The integration of the Argos business into Sainsbury's started immediately. Regular updates on integration, synergies and trading performance and the emerging strategy of Sainsbury's Argos were considered by the Board. The Board took the opportunity to meet the management team and visit stores.   |

## Risk management

During the year David Keens, the Audit Committee Chairman, gave detailed updates to the Board following each Audit Committee meeting on risk management and internal controls and the specific matters considered by the Audit Committee. The Director of Internal Audit attends at least one Board meeting a year as part of the Board's overall review of the effectiveness of risk management and the system of internal controls. In addition, specific risks are regularly discussed. For instance, the Board receives an annual update and quarterly updates on health and safety, and food safety. One of the particular risks the Board also examined this year was data governance and information security and how the risks were being mitigated through a combination of people, process and technology change.

## Board operation and attendance

The Board held eight scheduled meetings during the year, including the two-day strategy conference held in October. A significant number of additional ad hoc meetings and conference calls were also convened to deal with specific matters, particularly in relation to key decisions concerning the acquisition of HRG.

The Board had a number of informal meetings during the year. These included informal meetings of the Board the day before most Board meetings, and meetings with individual members of the Operating Board and their leadership teams to receive updates on their specific areas of responsibility. In addition, the Chairman and Non-Executive Directors met without the Executive Directors being present, and the Non-Executive Directors also met without the Executive Directors or the Chairman being present.

All Directors were made aware of the key discussions and decisions of each of the four principal Committees by the Chairman of each Committee providing a detailed summary at the Board meeting following the relevant Committee meeting. Minutes of Board and Committee meetings were circulated to Directors shortly after those meetings took place.

The following table shows the attendance of Directors at scheduled Board and Committee meetings.

|               | Board | Audit | Remuneration | Nomination | CR&S |
|---------------|-------|-------|--------------|------------|------|
| Matt Brittin  | 8(8)  | 4(4)  |              | 4(4)       |      |
| Mike Coupe    | 8(8)  |       |              |            | 2(2) |
| Mary Harris   | 8(8)  |       | 5(5)         | 4(4)       | 1(2) |
| David Keens   | 8(8)  | 4(4)  |              | 4(4)       |      |
| Brian Cassin  | 7(8)  | 4(4)  |              | 4(4)       |      |
| Susan Rice    | 8(8)  | 1(1)  | 5(5)         | 4(4)       |      |
| John Rogers   | 8(8)  |       |              |            |      |
| Jean Tomlin   | 7(8)  |       | 5(5)         | 4(4)       | 2(2) |
| David Tyler   | 8(8)  |       |              | 4(4)       |      |
| Kevin O'Byrne | 2(2)  |       |              |            |      |
| John McAdam   | 3(3)  |       | 1(1)         |            |      |

Notes: Ed Barker attended two meetings in his capacity as Interim CFO. The maximum number of meetings held during the year that each Director could attend is shown in brackets. Brian Cassin and Jean Tomlin were each unable to attend one Board meeting due to prior business commitments.

On the rare occasions that a Director is unavoidably unable to attend a meeting, the Chairman briefs them before the meeting so that their comments and input can be taken into account at the meeting, and provides an update to them after the meeting.

## Effectiveness

### Board evaluation

#### Key findings from 2015/16 review

- 1 Build on the strong links with the Board of Sainsbury's Bank and the broader management team at the Bank.

The Board has had regular opportunities to review the progress of Sainsbury's Bank's growth strategy during the year. The September Board meeting was held at the Bank's offices in Edinburgh, giving the Board an opportunity to meet the Bank's Board, including the Chairman and Non-Executive Directors, and the senior management team who made detailed presentations.

- 2 Some specific items could be given more visibility at Board level, including the work to increase diversity at all levels across the business.

The Board received a detailed update on the Company's diversity and inclusivity priorities at the strategy conference in October, with further updates at CR&S Committee and Board meetings.

- 3 Continue to monitor the broader competitive landscape, given the extent of the multi-channel retail market and the pace of change.

The Board discussed the broader competition landscape at the strategy conference in October and frequently at Board meetings.

#### 2016/17 review

The Board agreed that the 2016/17 review should be carried out by an external facilitator. Three different suppliers took part in a tender process and the Board determined that Manchester Square Partners (MSP) should be appointed to conduct the evaluation exercise of the Board and its Committees. MSP had carried out the previous external review in 2013/14 – this continuity was felt to be advantageous in tracking any changes in the Board's effectiveness over that period. It was agreed that the review would explore a broad range of dimensions covering strategy, operational priorities, the Board's role, its structure and balance, succession, risk management and governance. These themes were developed into a full written set of questions to ensure that the objectives of the Board review were met.

The review was conducted from November 2016 to February 2017. MSP had access to the Board and strategy conference papers for the prior 12 months. Board members first completed a questionnaire and individual meetings were then held with all Directors, the Company Secretary, the Interim Chief Financial Officer, the Group HR Director, the Chief Executive Officer of Sainsbury's Bank and the audit partner from Ernst & Young. As part of the process MSP attended and observed a Board meeting. MSP presented the conclusions to the Board at a meeting convened for that purpose and the Board discussed the key points and agreed certain actions.

Following the presentation, the Senior Independent Director reviewed the Chairman's performance with the other Directors and met him to provide feedback. The Chairman provided feedback to each Director on their individual contributions to the Board and, with each of them, considered their development priorities.

MSP concluded that "the Board is functioning well and in line with first class corporate governance, the Board dynamics are excellent – this is a collegiate, consensual, cohesive and supportive but challenging Board with a high degree of mutual trust, respect and integrity".

**MSP highlighted a number of positive themes which had emerged from the evaluation, which include:**

- There is clarity and alignment on the role of the Board, the strategic priorities, key challenges and risks.
- All Non-Executive Directors feel the need to challenge constructively and believe the quality of debate is high and has become more robust.
- The Board provides strong leadership and support to the business and is successfully overseeing a period of significant change.
- There is a strong sense of shared values. The Board embodies and leads by example on the behaviours and culture which Sainsbury's aims to drive through the organisation.
- The pace has increased significantly, especially around strategy, decision making and execution.
- Risk is well monitored and managed.
- There are effective, efficient and thorough Board structures, processes and information flows.

**The Board identified the following actions:**

- Review the Board programme to continue to find sufficient time for strategy and deep dives on big topics, with integration of individual topics if possible.
- Develop more informative KPIs around digital activities and the competitive environment.
- Having discussed Mary Harris's plans to step down from the Board at the AGM, start the succession process for an additional Non-Executive Director.
- Extend the timings of Board visits to the other business locations or suppliers in order to allow more time for interaction.
- Find additional opportunities to meet the broader management teams.

It is anticipated that the 2018 Board evaluation exercise will be carried out internally.

**Induction**

We have a comprehensive and tailored induction programme in place for Directors in order for them to gain an understanding of all aspects of the Group, including our culture and values, strategy, sustainability, governance and the opportunities and challenges facing the business. The programme includes store and depot visits and meetings with other members of the Board, members of the Operating Board, senior management and external advisers. The programme is ongoing for Non-Executive Directors, who often meet members of the management team on an individual basis to continue to build up their knowledge of the Company or visit stores, depots and other business locations and also suppliers. Subsequent training is available on an ongoing basis to meet any particular needs.

During the year, Brian Cassin and Kevin O'Byrne joined the Board and John Rogers was appointed as Chief Executive Officer of Sainsbury's Argos. David Keens continued his induction following his appointment to the Board in April 2015.

**Brian Cassin**

Brian Cassin joined the Board on 1 April 2016. During his induction to date, Brian has met with members of the Board and had a series of one to one meetings with members of the Operating Board and senior management to get an insight into each of their areas of responsibility. He visited a number of stores including the new store at Nine Elms. He also attended a colleague listening group where he heard feedback from store colleagues and he met with external advisers to understand regulatory matters and obligations.

**David Keens**

David Keens joined the Board on 8 July 2015. He has had a comprehensive and tailored induction which has continued this year and included further visits

to operations around the Group which were particularly relevant to his role as the Chairman of the Audit Committee. For more information see page 68.

Kevin O'Byrne and John Rogers also have continuing comprehensive inductions consistent with the scale and profile of their new executive roles.

**Professional development, support and training**

We have a programme for meeting Directors' training and development requirements. The Board programme includes regular presentations from management and informal meetings to build their understanding of the business and sector. This year a number of Board meetings were held at offsite locations including:



**1 Marine Harvest**

The Board held its June meeting at Sainsbury's salmon supplier, Marine Harvest, at their Scottish office. Here the Board had the opportunity to meet with the Food Commercial Director, and the Trading Division leadership team and to discuss the overall trading strategy, including pricing and promotions, provenance and supplier relationships. The Board also received a presentation on Marine Harvest, met their management team and toured their facility. This has given the Board a greater understanding of Sainsbury's trading strategy, focus on differentiation, supplier relationship management and the relationship with Marine Harvest.

**2 Sainsbury's Bank**

The Board held their September meeting at Sainsbury's Bank in Edinburgh and met with Sainsbury's Bank Non-Executive Directors, Chairman, Executive Committee and senior management. They discussed the opportunities and challenges facing the financial services sector, received a detailed overview of the Bank's strategy including short and medium term plans and met the broader management team.

**3 Sainsbury's Argos**

The Board met the Sainsbury's Argos Management Board and senior management team, in Milton Keynes in November, and had the opportunity to discuss trading, integration and strategic plans, and to visit stores.

**4 The Online Fulfilment Centre in Bromley-by-Bow**

The Board discussed online strategy and toured the facility with the management team at the new Sainsbury's Online Fulfilment Centre in Bromley-by-Bow. The purpose built Online Fulfilment Centre is 185,000 sq. ft. and has the capacity to fulfil 25,000 customer online orders per week.

During the year the Company Secretary provided updates to the Board on relevant governance matters, Directors' duties and obligations, and new legislation and its impact on the Company including the new Market Abuse Regulations and the Green Paper on Corporate Governance Reforms. Both the Audit and Remuneration Committees received regular updates on relevant accounting and remuneration developments, trends and changing disclosure requirements from external advisers and management. The Chairman, in collaboration with the Company Secretary and management, ensured that all Directors were properly briefed on issues arising at Board meetings and that they had sufficient, reliable and timely access to relevant information. Directors have access to independent professional advice if necessary and to the advice of the Company Secretary in fulfilling their duties and responsibilities.

**Independence and conflicts of interest**

The Chairman satisfied the independence criteria of the Governance Code on his appointment to the Board and all the Non-Executive Directors are considered to be independent. Each of the Directors has a duty to avoid a situation where he/she has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the Company's interests. The Company's Articles of Association permit the Directors to authorise conflicts and potential conflicts, where appropriate. The Board has established procedures for the disclosure by Directors of any such conflicts, and also for the consideration and authorisation of these conflicts by the Board. In accordance with the Companies Act 2006, the Board considered and authorised each Director's potential conflicts of interest during the year.

Whenever a Director takes on additional external responsibilities, the Board considers any potential conflicts that may arise. The Board continues to monitor and review potential conflicts of interest on a regular basis. The Board has specifically considered the executive or non-executive roles that some of the Non-Executive Directors have with companies that may be suppliers to Sainsbury's. The Board is satisfied that the independence of the Directors who have executive or non-executive roles with other companies is not compromised.

Prior to appointment, each Non-Executive Director confirms that they will have sufficient time available to be able to discharge their responsibilities effectively. During the year, the Board reviewed, in advance, disclosures by Non-Executive Directors seeking to undertake additional commitments. The Board remains confident that individual members are able to devote sufficient time to undertake their responsibilities effectively.

## Relations with stakeholders

The Company is committed to maintaining good communications with stakeholders.

### Institutional shareholders

- Normal shareholder contact is the responsibility of Mike Coupe, Kevin O'Byrne and James Collins, Head of Investor Relations.
- The Chairman met with institutional shareholders and other large investors. The Senior Independent Director, Susan Rice, is also available to attend meetings as required.
- The Company met regularly with its large investors and institutional shareholders who, along with sell-side research analysts, were invited to presentations by the Company immediately after the announcement of the Company's interim and full-year results.
- Large investors and institutional shareholders also visited a number of stores and concessions.
- They are also invited to participate in conference calls following the announcement of the Company's trading statements. The content of these presentations and conference calls are webcast and are posted on the Company's website [www.j-sainsbury.co.uk/investor-centre](http://www.j-sainsbury.co.uk/investor-centre) so as to be available to all investors.
- While activity early in the year was constrained by Takeover Panel Rules relating to our offer for HRG, the Company met, through regular post-results roadshows, ad hoc meetings, conference attendances and site visits in the UK, US and Europe, a total of 187 shareholders and potential investors in 229 meetings over the course of the year.

### Feedback from institutional shareholders

- The Board received regular updates on the views of major investors and the Investor Relations programme at each Board meeting.
- Makinson Cowell provided investor relations consultancy services to the Company and external analysis to the Board on the views of institutional investors and sell-side analysts.
- Makinson Cowell additionally carried out an extensive Investor Study, covering share price performance, the share register, the Investor Relations programme and investor views on the retail market, communication, strategy and management. Key conclusions and recommendations arising from this survey were presented to the Board.
- Non-Executive Directors also received regular market reports and broker updates from the Company's Investor Relations department.
- Investors are increasingly interested in corporate responsibility matters, details of which can be found on pages 66 and 67. Information on countering bribery can be found on page 97.

### Private shareholders

- Our private shareholders are encouraged to access the Company's Interim and Annual Reports and presentations on our website. Other useful information such as announcements, historic dividend records and shareholder communications is also available on the website [www.j-sainsbury.co.uk/investors](http://www.j-sainsbury.co.uk/investors)

### AGM

- Shareholders had the opportunity to meet and question the Board at the AGM. There was a display of various aspects of the Company's activities and Mike Coupe made a business presentation. This year the AGM will be held on 5 July 2017.
- All resolutions proposed at the 2016 AGM were taken on a poll vote and were passed with significant majorities.

### Suppliers

The Board receive regular updates on the trading strategy, and supplier relationship management was a key area of focus of the June Board meeting held at Marine Harvest's facility in Scotland when Marine Harvest's management and the Trading Division Leadership team presented to the Board (page 62). The Company's compliance with the Grocery Supply Code of Practice is monitored by the Audit Committee (page 73) and David Keens met the Grocery Code Adjudicator in his role as Chairman of the Audit Committee. Supplier relationship management was also discussed by the CR&S Committee and in two CR&S stakeholder meetings, Mike Coupe and Jean Tomlin had the opportunity to hold discussions with key suppliers and other stakeholders.

### Colleagues

The CR&S Committee discussed insight on colleague engagement, and summaries of the key issues that were important to colleagues, at each of the meetings. It has been agreed that some of the Non-Executive Directors will meet colleagues from the National Great Place to Work Group to hear colleagues' views on matters which are at the top of their agenda and share with them some of the items on the Board agenda. This will enhance the link between the Non-Executive Directors and colleague representatives.

# Nomination Committee



## Dear Shareholder

The Nomination Committee has overseen the Board's succession planning during the year which has resulted in the appointments of John Rogers and Kevin O'Byrne to their new roles. We believe that they will carry out their responsibilities in a highly effective way, and that they will contribute significantly to our operational and strategic discussions, and complement the existing balance of skills and experience around the boardroom table.

Succession and diversity at Board and senior management levels are key aspects of our agenda. Our priorities over the year were as follows:

- To implement the succession plan for the Argos Chief Executive Officer role and ensure a smooth transition.
- To plan and implement the appointment of a new Chief Financial Officer.
- To support succession at Operating Board and senior management levels, including the appointment of Simon Roberts as Retail and Operations Director, and the appointment of a new management board for Sainsbury's Argos.
- To plan succession at Non-Executive level in light of Mary Harris' decision to step down from the Board at this year's AGM, following over nine years of service to the Company. A search process for a new Non-Executive Director is under way.
- To review our progress on becoming a more diverse and inclusive business. The Committee received a full update on the Company's progress at the strategy conference in October and Directors continue to receive regular updates at Board meetings.
- To oversee the Company's approach to resourcing the needs of the business, developing our colleagues and recruiting new talent.

The Committee is pleased with the progress made on these priorities during the year and believes that the new appointments at Board and senior level position the business well for the future.

*David Tyler*

**David Tyler**  
Chairman

### Succession planning

The Board takes succession planning for both Board members and senior management very seriously. All of the Non-Executive Directors are members of the Nomination Committee which is chaired by David Tyler. Mike Coupe is invited to attend meetings. During the year, the Committee held four formal meetings and there were regular updates on its various search processes and appointments.

At the strategy conference in October, the Committee reviewed succession plans, development and talent management for senior managers as well as progress on inclusivity throughout the business. In March 2017, following the Board evaluation, the Committee considered the balance, skills and diversity of the Board. As part of its succession planning the Committee agreed to start a search for a new Non-Executive Director in light of Mary Harris stepping down from the Board at the AGM, and discussed the preferred experience for the role specification. The Committee also approved the appointment of Susan Rice as Chairman of the Remuneration Committee in July 2017. Susan has been a member of the Remuneration Committee since September 2015.

Each of our Directors were recruited following a robust selection process which has been facilitated by independent executive search consultants. The Committee believes Sainsbury's has a good balance and diversity amongst Non-Executive Directors, with several having extensive experience of retail and consumer-facing businesses and other highly relevant skills derived from serving in a range of major executive and non-executive positions throughout their careers.

The Committee oversaw the two key appointments of John Rogers and Kevin O'Byrne during the year.

#### John Rogers

John was promoted to the role of Chief Executive Officer of Sainsbury's Argos upon completion of Sainsbury's acquisition of HRG in September 2016. John's experience goes beyond his most recent role as Chief Financial Officer. His vast experience as a leader in the business in strategy, digital, online, financial services and property since he joined Sainsbury's in 2005 made John the ideal candidate to lead Sainsbury's Argos.

As Chief Executive Officer he will continue to drive the integration of Argos with Sainsbury's general merchandise business, and deliver the ongoing digital transformation across Sainsbury's Argos.

#### Kevin O'Byrne

*Identify.* Using the agreed brief, the Committee reviewed and shared feedback on a list of internal and external candidates from independent executive search consultants Egon Zehnder International. The diverse list of candidates was appraised against the key competencies and experience required for the role.

*Interview.* Mike Coupe and Angie Risley (Group HR Director) led a series of interviews with the shortlisted candidates. Preferred candidates then met with David Tyler, David Keens and John Rogers following which the Committee met to discuss feedback.

*Select.* After further meetings with Non-Executive Directors, Kevin O'Byrne was recommended for appointment by the Committee. He was identified as the preferred candidate particularly due to his wealth of retail and finance experience, and his track record in growing businesses.

*Appoint.* Kevin's appointment as Chief Financial Officer was approved and announced on 7 November 2016 and took effect on 9 January 2017.

During the search process Ed Barker, Sainsbury's Director of Group Finance, was appointed Interim Chief Financial Officer from 5 September 2016 until 9 January 2017.

### Diversity and inclusivity

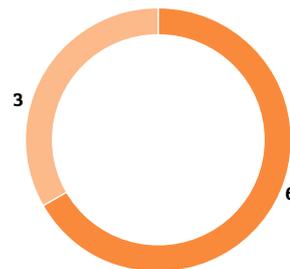
We want to be 'the most inclusive retailer'. We will achieve this aspiration by recruiting, retaining and developing diverse and talented people and creating an inclusive environment where everyone can be the best they can be and where diverse views are listened to. The Board is highly supportive of the initiatives to promote diversity and inclusivity throughout the business. For instance, Jean Tomlin attended Sainsbury's first Black, Asian, Minority Ethnic (BAME) event, delivering a key note speech to over 200 BAME colleagues about her career journey, experiences and challenges.

The Board receives regular updates on inclusivity and both the CR&S Committee and the Nomination Committee had detailed presentations on the range of priorities and the progress against them during the year. More about these initiatives and the progress being made can be found on page 39.

Our gender diversity statistics can be found in the table below. For most of the year, two members of the Operating Board (22%) were women, however following the departure of Sarah Warby in January 2017, the number fell to one.

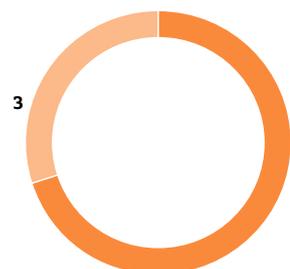
|  | Colleagues | Male         | Female        |
|--|------------|--------------|---------------|
| Board                                    | 10         | 7 (70%)      | 3 (30%)       |
| Operating Board                          | 9          | 8 (89%)      | 1 (11%)       |
| Divisional Directors and Senior Managers | 265        | 183 (69%)    | 82 (31%)      |
| Company                                  | 191,202    | 85,746 (45%) | 105,456 (55%) |

#### Board balance



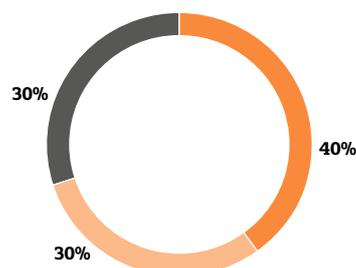
● Non-Executive Director ● Executive Directors

#### Board diversity



● Men ● Women

#### Board tenure



● 0-3 years ● 4-6 years ● 7-9 years

# Corporate Responsibility and Sustainability Committee



## Dear Shareholder,

Our vision is to be the most trusted retailer, where people love to work and shop, by living up to our values for customers, colleagues, suppliers, shareholders and wider society. This is critical to helping our customers to live well for less.

Throughout our 148-year history, we have always taken our responsibilities to society seriously. Today, the need for business to build trust by, for example, tax transparency or respecting human rights, is more important than ever. While we experience political change and uncertainty in some aspects of society, we know that we can still play an important role in supporting our customers in areas that matter to them.

Enabling people to live healthier lives, protecting the environment, supporting our colleagues and people who work throughout our supply chains and championing issues that affect our local communities, creates valuable opportunities to deepen our relationships with all our stakeholders while reducing risk.

As Chairman of the Board's Corporate Responsibility and Sustainability Committee, I oversee the governance of our Sustainability Plan which spans our five values: Respect for our environment, Living healthier lives, Sourcing with integrity, Great place to work, and Making a positive difference to our community.

Since we refreshed our Sustainability Plan in 2015, we have made significant progress in responding to changes in the world around us and deepening our understanding of the support our customers want from us.

For example, as part of our Respect for our environment value, we have continued to increase the impact of our *Waste less, Save more* campaign. This initiative was developed as a direct response to the findings in our Closer to Customers insight programme which revealed that customers wanted help with reducing food waste at home.

Many of our customers also want help to live healthier lives. Through our Living healthier lives value, we have reformulated more of our products to reduce salt, saturated fat and sugar, and we have continued to support young people in communities across the UK to do more exercise and eat more healthily through our flagship Active Kids scheme. Since its launch in 2005, we have invested more than £173 million in sports and cooking equipment and experiences for schools.

I am also particularly proud of the great progress we have made in Sourcing with integrity, towards developing sustainability standards across our key raw materials. The credibility and quality of this work relies on close partnership and co-creation with many independent, expert organisations around the world which help us to ensure we have world-class standards addressing economic, social and environmental issues. We place great value on these collaborations and I would like to thank all that have contributed to our journey.

As part of our Great place to work value, we strive to be the most inclusive retailer. During the year, we have launched our Embrace the Difference inclusion campaign internally with a host of engagement activities and training to support colleagues to embrace the differences they see in others. We're the largest employer to have reached the Investors in People Gold standard and the only retailer to achieve three consecutive Gold awards, and the feedback we received recognised that our values are a core part of our DNA. I was also pleased to see acknowledgment of our progress on gender, LGBT matters and apprenticeships – all underpinned by strong colleague advocacy and open communication that runs as a golden thread through our business.

As work to integrate and align activity across the Sainsbury's Group progresses in the year following the acquisition of HRG, we are identifying opportunities to have an even greater, positive impact on society. Despite this being a year of significant change for colleagues at Argos, some key activities, such as fundraising for Macmillan Cancer Support and the Irish Cancer Society – part of our Making a positive difference to our community value – have continued with real commitment. Building on this, we are confident that 2017/18 will be an exciting year for developing our approach to sustainability across the whole Group.

We continue to listen to all our stakeholders – customers, colleagues, suppliers and investors – to make sure we have the most relevant and effective strategy, leverage the knowledge and experience of experts and remain at the forefront of sustainability between now, 2020 and beyond. For me, what I am most proud of is how we work diligently across the organisation to deliver on our Sustainability Plan commitments and our values, day in and day out.

Further information about our approach can be found at [www.j-sainsbury.co.uk/investor-centre](http://www.j-sainsbury.co.uk/investor-centre), with quarterly updates also given as part of our broader trading statements.

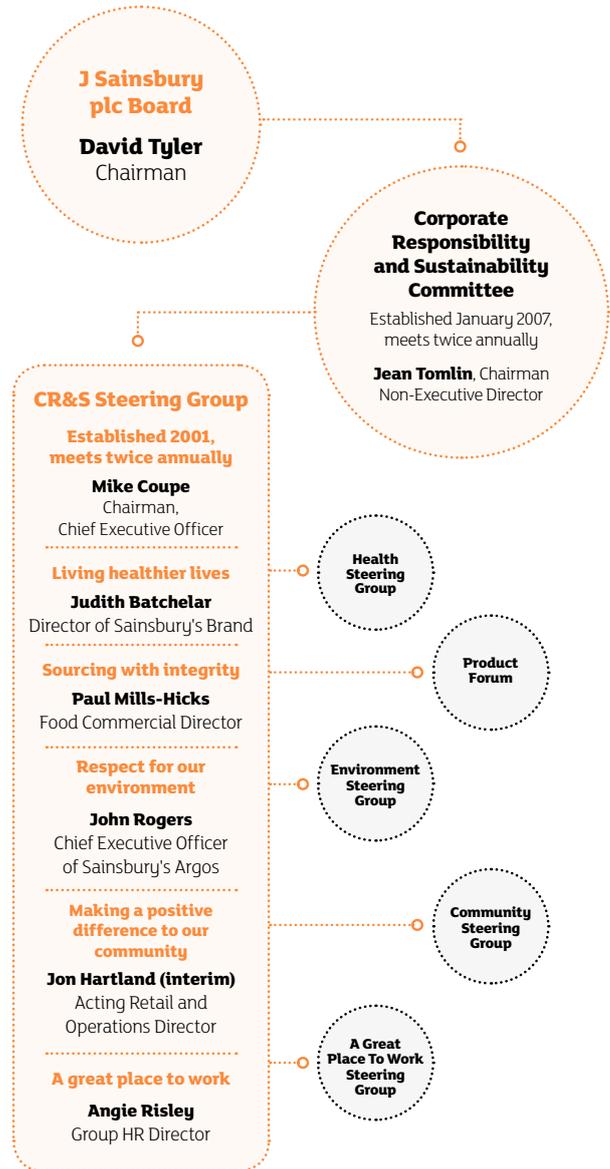
**Jean Tomlin**  
Chairman, Corporate Responsibility  
and Sustainability Committee

### Corporate Responsibility and Sustainability Committee

Our Corporate Responsibility and Sustainability (CR&S) Committee is chaired by Jean Tomlin and attended by its members Mary Harris and Mike Coupe. David Tyler also attends the meetings. It met twice during the year and discussed our progress across each of our five values as well as our Sustainability Plan as a whole. For example, it reviewed the development of the *Waste less, Save more* customer food waste initiative and plans for the integration of Home Retail Group sustainability activities into the wider Sainsbury's strategy. Through these meetings the CR&S Committee also receives regular updates on colleague and customer views on issues relating to our values and Sustainability Plan so that we can respond appropriately.

These formal Committee meetings were supported by two CR&S stakeholder meetings that were hosted by Jean Tomlin and Mike Coupe. Key external stakeholders, including representatives from the Government, industry, non-governmental organisations and key suppliers, joined us to discuss issues that relate to our values. Our Sourcing with integrity event focused on the role that Sainsbury's can play in supporting the UN Sustainable Development Goals and stakeholders at our Living healthier lives event discussed the findings of our latest Active Kids research and the challenges faced by 11-14 year olds in leading a healthier lifestyle. These events are an important way for us to hear new perspectives and be challenged on issues that are important for our business and society. We feed what we learn back into our teams so that we can respond through how we deliver our Sustainability Plan.

The Committee is supported by an internal CR&S governance structure whereby senior directors in the business have responsibility for each of our five values and sit on our CR&S Steering Group, chaired by Mike Coupe. The members of this biannual Steering Group are shown opposite.



# Audit Committee



## Dear Shareholder,

This year, the wide-ranging activities of the Committee have included the acquisition and integration of HRG, monitoring the transition of Sainsbury's Bank and the management of data security.

This is my second year on the Board and second report as Chairman of the Audit Committee. Building on the previous year, I have continued to visit Company operations around the Group, including data centres, business continuity facilities, online fulfilment services and supplier premises. There were further visits to Sainsbury's Bank in Edinburgh and to the newly acquired Argos Contact Centre in Widnes and Head Office in Milton Keynes. Retail store tours, both escorted and unannounced, are a regular feature.

The Committee provides oversight of the risk profile across the Group. This is undertaken by reviewing the principal risks and uncertainties and through regular updates from internal and external auditors. A new development this year has been the inclusion of Sainsbury's Argos into the Group risk management approach and into the activities of the Committee. The Company's principal risks and uncertainties are set out on pages 42 to 44.

We monitor the audit and risk activities of the operations of Sainsbury's Bank; including the continued transition from Lloyds Banking Group and recent integration of Argos Financial Services.

Data security and governance continues to be an area of focus for the Committee. Good progress is being made in identifying and managing data risks and in preparing for the introduction of new legislation in 2018.

This year's external Board evaluation process considered the role and effectiveness of the Committee. I am pleased to report that feedback relating to the Committee was positive and that we continue to provide the necessary support to the Board.

The significant financial and reporting matters considered by the Committee during the year are set out from page 69.

I am indebted to my co-Directors on the Committee for their time and insight during this past year. We, together with internal colleagues and external advisers, covered a wide range of topics and governance matters. Our intention is to continue in a similar, diligent manner over the coming year.

**David Keens**  
Chairman, Audit Committee

# Accountability

## Committee membership

The Audit Committee is chaired by David Keens, with Matt Brittin and Brian Cassin as its other members, all of whom are independent Non-Executive Directors. Susan Rice stepped down as a member of the Committee on 4 May 2016.

The Board has determined that David Keens has recent and relevant financial experience. The Committee as a whole has relevant retail sector experience – for instance, David Keens held the role of Group Finance Director of Next plc for 24 years.

## Attendees

The Chairman, Chief Executive Officer, Chief Financial Officer, Director of Internal Audit, Director of Group Finance, Company Secretary and Corporate Services Director, representatives from Sainsbury's Bank and the external auditor attended Audit Committee meetings.

## Committee activities

The key activities of the Committee during the year in fulfilling its responsibilities included reviewing, monitoring and approving the following:

### Financial reporting

- The integrity of the financial statements and any other formal announcement relating to financial performance
- The significant financial reporting issues and judgements contained in the financial statements
- The implementation of new accounting standards
- The Company's funding and liquidity position and its impact on the Company's financial and operational capabilities
- The assumptions and qualifications in support of the viability statement and going concern including stress testing against risk materialisation
- Assessment of whether the Annual Report is fair, balanced and understandable

### Risk management and internal controls

- Risk management updates including reviews of principal risks and uncertainties
- The Risk Management Policy
- Reports from the Audit and Risk Committees of Sainsbury's Bank and on all important operating and regulatory matters, including the transition of the Bank, its liquidity, cash flows, capital adequacy and risk management processes

### External audit

- The scope of the external audit plan and fee proposal
- The provision of non-audit fees in accordance with our policy
- The independence and objectivity of Ernst & Young
- The quality and effectiveness of Ernst & Young
- The reappointment of Ernst & Young as auditor

### Internal audit

- The internal controls framework
- Management's responsiveness to Internal Audit's findings and recommendations
- Changes to the Internal Audit Charter
- The scope of the internal audit plan
- The effectiveness of the Internal Audit function

### Other

- The integration of Sainsbury's Argos
- Whistleblowing
- The transition of Sainsbury's Bank
- Updates on data governance and information security
- The Company's compliance with the Grocery Supply Code of Practice
- Ongoing material litigation

- The Business Continuity Management Policy and the Code Compliance Officer Policy
- The FRC Audit Quality Review letter
- The Committee's revised terms of reference and its effectiveness

## Significant financial and reporting matters

An accounting and tax paper was prepared by management and presented to the Audit Committee four times during the year. This provided detail on the main financial reporting judgements and issues. Specific accounting papers were also prepared when considered necessary.

The Committee considered the following significant financial and reporting issues during the year:

### Impairment of financial and non-financial assets

The impairment of financial and non-financial assets was considered by the Committee, this is particularly appropriate in today's challenging marketplace. As disclosed in note 2 of the Notes to the Financial Statements, a review for impairment triggers is performed at each reporting date by considering if any current or future events suggest the recoverable value of certain assets may be less than their carrying value.

The Committee reviewed management's assessment of recoverable value and relevant judgements made. An impairment and onerous contract charge of £37 million was recognised in the year, as well as £57 million in relation to IT assets written off.

### Complex property transactions

There was one major property transaction in the year, being the opening of the Nine Elms store in August 2016.

The Committee has reviewed the concepts of this transaction in a previous year to ensure that all accounting and tax issues are identified and appropriately presented in the accounts, including whether amounts recognised reflect the overall substance of these transactions. Please refer to note 3 of the Notes to the Financial Statements for property profits recognised in the year.

### Pensions accounting

Following the acquisition of HRG during the year, the Group now holds two defined benefit schemes: the Sainsbury's defined benefit scheme and the HRG defined benefit scheme.

The Committee reviewed a summary of the key assumptions used in arriving at the valuations and obligations for both defined benefit pension schemes for the half-year and year-end reporting including inflation, discount and mortality rates. Benchmarking is assessed to ensure that the assumptions are appropriate.

Of particular note this year was the effect that the UK Referendum vote had on discount rates following a downward move in corporate bond yields, and the impact on the IAS 19 accounting deficit and therefore distributable reserves in the Group. The year-end reported discount rate was 2.7%, giving a consolidated IAS 19 pension deficit of £974 million before tax.

### Items excluded from underlying results

The European Securities and Markets Authority (ESMA) published guidelines on Alternative Performance Measures (APMs) which applied to relevant communications released on or after 3 July 2016. In light of the ESMA guidance, additional disclosure is now also included on the APMs used by Sainsbury's – please refer to page 190.

Items excluded from underlying results are reviewed by the Committee, and the Committee is satisfied that the Group's presentation of these items is clear and that further disclosure is included where appropriate.

### **Sainsbury's Bank reporting**

The Committee receives updates on the key agenda items discussed at the Bank's Audit Committee including accounting judgements and estimates and on all important operating and regulatory matters such as its liquidity, cash flows, capital adequacy and risk management processes. Representatives from the Bank Audit Committee and the Bank Internal Audit team attend meetings of the Committee at least twice a year.

During the year the accounting judgements and estimates reviewed by the Committee have included impairment assessments of the loans and advances due to Sainsbury's Bank customers, progress on the Bank transition, tax judgements and provisions and progress on the implementation of IFRS 9 "Financial instruments".

### **Supplier income**

Supplier income is considered by the Committee, and whilst the majority is calculated through a formulaic process, the Committee is satisfied with the controls in place to manage any areas of judgement and estimation.

The Committee ensures the Group provides adequate reporting, including income statement and balance sheet disclosures within the Financial Statements (from page 99) and is satisfied with the level of disclosure.

### **Acquisition of Home Retail Group**

On 2 September 2016, the Group acquired 100 per cent of the issued share capital of HRG, a listed company based in the United Kingdom. Significant work was undertaken to prepare for the integration of HRG, with the following areas in particular being considered by the Audit Committee:

- The approach to aligning the reporting dates of HRG and Sainsbury's
- The transfer of HRG financial services entities to Sainsbury's Bank
- Alignment of accounting policies between HRG and Sainsbury's
- Reviewed how the acquisition would impact the Group's IFRS 8 "Operating Segments" disclosures. Whilst an additional segment was identified, it was concluded that it met the aggregation criteria per IFRS 8 and the Group's reported segments therefore remained as Retail, Financial Services and Property Investment.
- Reviewed the accounting and financial reporting for the acquisition. This included reviewing the assumptions made in relation to valuing the assets and liabilities, which resulted in net assets acquired of £1,035 million and goodwill of £58 million. Refer to note 31 of the Notes to the Financial Statements for more information.
- The transition to Ernst & Young as auditors of Home Retail Group

### **Updates to accounting standards**

Management are currently preparing for the implementation of three new accounting standards:

- IFRS 9 "Financial Instruments" effective for the year commencing 11 March 2018
- IFRS 15 "Revenue" effective for the year commencing 11 March 2018
- IFRS 16 "Leases" effective for the year commencing 10 March 2019

We have reviewed impact assessments prepared by management on the transition to each of these accounting standards and the assumptions made. Additional disclosures in relation to each of these are included in note 1 of the Notes to the Financial Statements.

We note that within the External Audit report there is a risk associated with adjustments made to revenue. We have condensed this and have concluded that we have appropriate procedures and controls in place not to include this as a significant area of judgement.

### **Fair, balanced and understandable assessment**

The Board is required to confirm that the Annual Report and Financial Statements, taken as a whole, are fair, balanced and understandable (see page 100). To enable the Board to make this declaration, there is a year-end review process to ensure the Committee, and the Board as a whole, has access to all relevant information and, in particular, management's papers on significant issues faced by the business. The Committee received a paper from management detailing the approach taken in the preparation of the Annual Report and Financial Statements. The Audit Committee, and all other Board members, also received drafts of the Annual Report and Financial Statements in sufficient time to facilitate their review and enable them to challenge the disclosures if necessary. In addition, Ernst & Young reviewed the consistency between the narrative reporting of the Annual Report and the Financial Statements.

### **Viability statement**

The Committee has assessed whether three years continue to be an appropriate timeframe over which to make the viability statement. It was concluded that the current three year assessment period remains appropriate and this was reviewed and adopted by the Board.

The processes underpinning the assessment of the Group's longer-term prospects were reviewed.

The viability statement and our approach to assessing long-term viability can be found on page 45.

### **External auditor**

#### **Independence and objectivity of the external auditor**

The independence and objectivity of the external audit function is a fundamental safeguard to the interests of the Company's shareholders. In order to ensure their independence, the Audit Committee has overseen the Company's policy which restricts the engagement of Ernst & Young in relation to non-audit services.

The policy is designed to ensure that the provision of such services does not have an impact on the external auditor's independence and objectivity. It identifies certain types of engagement that the external auditor shall not undertake, including internal audit and actuarial services relating to the preparation of accounting estimates for the financial statements. It also requires that individual engagements above a certain fee level may only be undertaken with pre-approval from the Audit Committee, or if urgent, from the Committee Chairman and ratified by the subsequent meeting of the Committee. The policy also recognises that there are some types of work where a detailed understanding of the Company's business is advantageous. The policy is designed to ensure that the auditor is only appointed to provide a non-audit service where it is considered to be the most suitable supplier of the service.

The Audit Committee received a report on the non-audit services being provided and the cumulative total of non-audit fees. The cumulative non-audit fees are capped at 70% of the average of the audit fees for the Group for the preceding three year period.

The Audit Committee concluded that Ernst & Young remained objective and independent in their role as external auditors and that they continue to challenge management effectively.

The Audit Committee confirms that it has complied with the provision of the Statutory Audit Services Order 2014.

#### **Audit and professional fees paid to the external auditor**

The Audit Committee reviewed Ernst & Young's overall work plan, and approved their remuneration and terms of engagement. The majority of the non-audit work undertaken by Ernst & Young during 2016/17 was audit related assurance services and tax advisory services. These totalled £0.2 million. The total audit fees for the year in respect of the Group and subsidiaries were £1.9 million. For a breakdown on the fees please refer to note 5 of the Notes to the Financial Statements.

#### **Effectiveness of the external auditor**

Ernst & Young were appointed in July 2015 as the Company's auditor.

The Audit Committee reviewed Ernst & Young's effectiveness during the year. Additionally, a questionnaire was completed by the members of the Committee with feedback sought from key stakeholders including

the Interim Chief Financial Officer and Director of Group Finance. The questionnaire included evaluation of the audit partner and audit team, the approach to the audit, communications with the Committee, how Ernst & Young supported the work of the Audit Committee, and their independence and objectivity.

The Audit Committee concluded that Ernst & Young provided audit services efficiently and effectively and to a high quality. Areas for improvement or greater attention were discussed and shared with Ernst & Young and management.

**Appointment of the external auditor**

The Audit Committee has made a recommendation to the Board to reappoint Ernst & Young as the Company’s auditor for the 2017/18 financial year. Accordingly, a resolution proposing the reappointment will be tabled at the 2017 AGM.

**Audit Quality Review**

The Audit Quality Review team of the Financial Reporting Council (FRC) reviewed Ernst & Young’s audit of the Group’s Annual Report and Financial Statements 2016. The FRC have given us a copy of their report, which has been reviewed by the Committee and discussed with Ernst & Young. The report does not give the Committee any concerns over the quality, objectivity or independence of the audit.

**Risk management and internal controls**

The Board has overall responsibility for risk management and the system of internal controls and for reviewing their effectiveness. Certain of these responsibilities have been delegated to the Audit Committee as outlined below. The risk management process is designed to manage rather than eliminate the risk of failure to achieve the Company’s business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.

The risk management process and the system of internal controls have been in place for the whole year, up to the date of approval of the Annual Report and Financial Statements, and accord with the UK Financial Reporting Council’s Guidance on Risk Management, Internal Control and Related Financial and Business Reporting and the Governance Code.

The Board received updates on risk management and internal controls from the Chairman of the Audit Committee. All Committee papers and minutes were made available to the whole Board.

The Board also received reports relating to safety, other relevant risks, controls and governance. Any specific matters which could have affected the Company’s reputation were reported to the Board as they occurred.

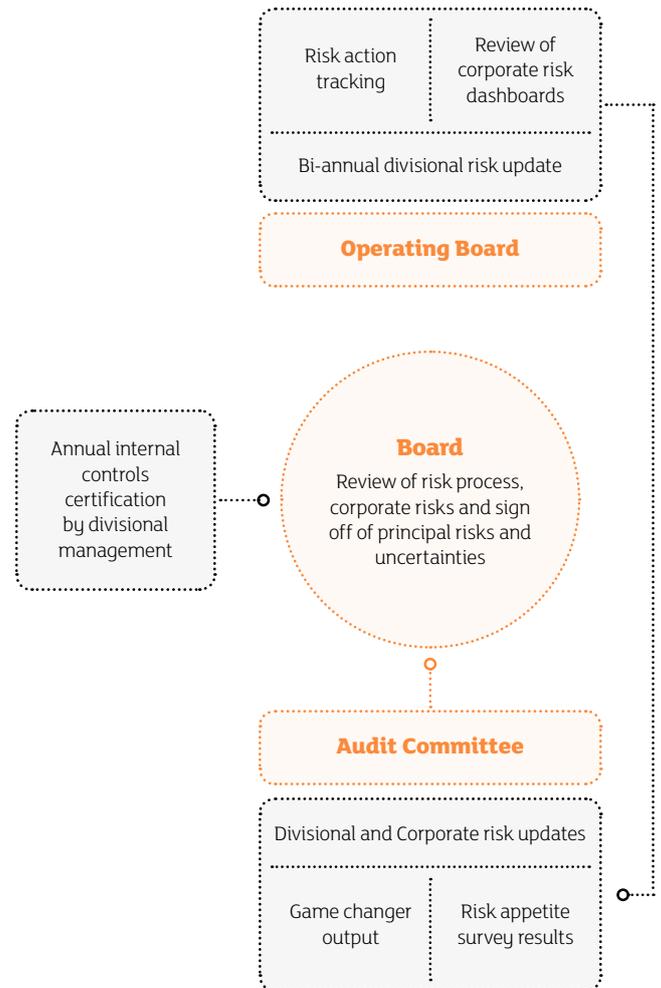
The Audit Committee has reviewed the effectiveness of the system of internal controls and has ensured that any required remedial action on any identified weaknesses has been, or is being taken.

The diagram on the right provides a high-level overview of the key risk management activities undertaken by the Operating Board, Audit Committee and Sainsbury’s divisional management that allow the Board to fulfil their obligations under the UK Corporate Governance Code and Companies Act 2006. The annual risk management process concludes with the Board’s robust assessment of the Company’s principal risks and uncertainties, including those that could threaten its business model, future performance, solvency and liquidity, and the completion of an annual internal controls certification.

**Corporate risk management process**

Accepting that risk is an inherent part of doing business, the risk management process is designed to identify key risks and to provide assurance that these risks are fully understood and managed in line with management’s risk appetite. The Audit Committee reviews the effectiveness of the risk management process at least annually.

The Operating Board maintains an overall corporate risk map which is reviewed twice a year by the Audit Committee and formally discussed with the Board. The risk map captures the most significant risks faced by the business and identifies the potential impact and likelihood at both a gross level (before consideration of mitigating controls) and net level (after consideration of mitigating controls). The Operating Board discusses and agrees the level of risk that the business is prepared to accept for each key



corporate risk. The target risk position is captured to reflect management’s risk appetite where this differs to the current net position. The Operating Board reviews the corporate risk dashboards during the year, comprised of key risk indicators, to ensure they identify any potential risk movements towards or away from their risk appetite. This enables the Operating Board to agree and monitor appropriate actions as required.

The risk management process is embedded at the Operating Board level and supported by a divisional risk management process. Operating Board members certify annually that they are responsible for managing their business objectives and internal controls so as to provide reasonable, but not absolute, assurance that the risks in their areas of responsibility are appropriately identified, evaluated and managed.

Internal Audit provides the Audit Committee with a risk management update twice a year which provides detail of the key risk activities undertaken at the divisional and corporate level.

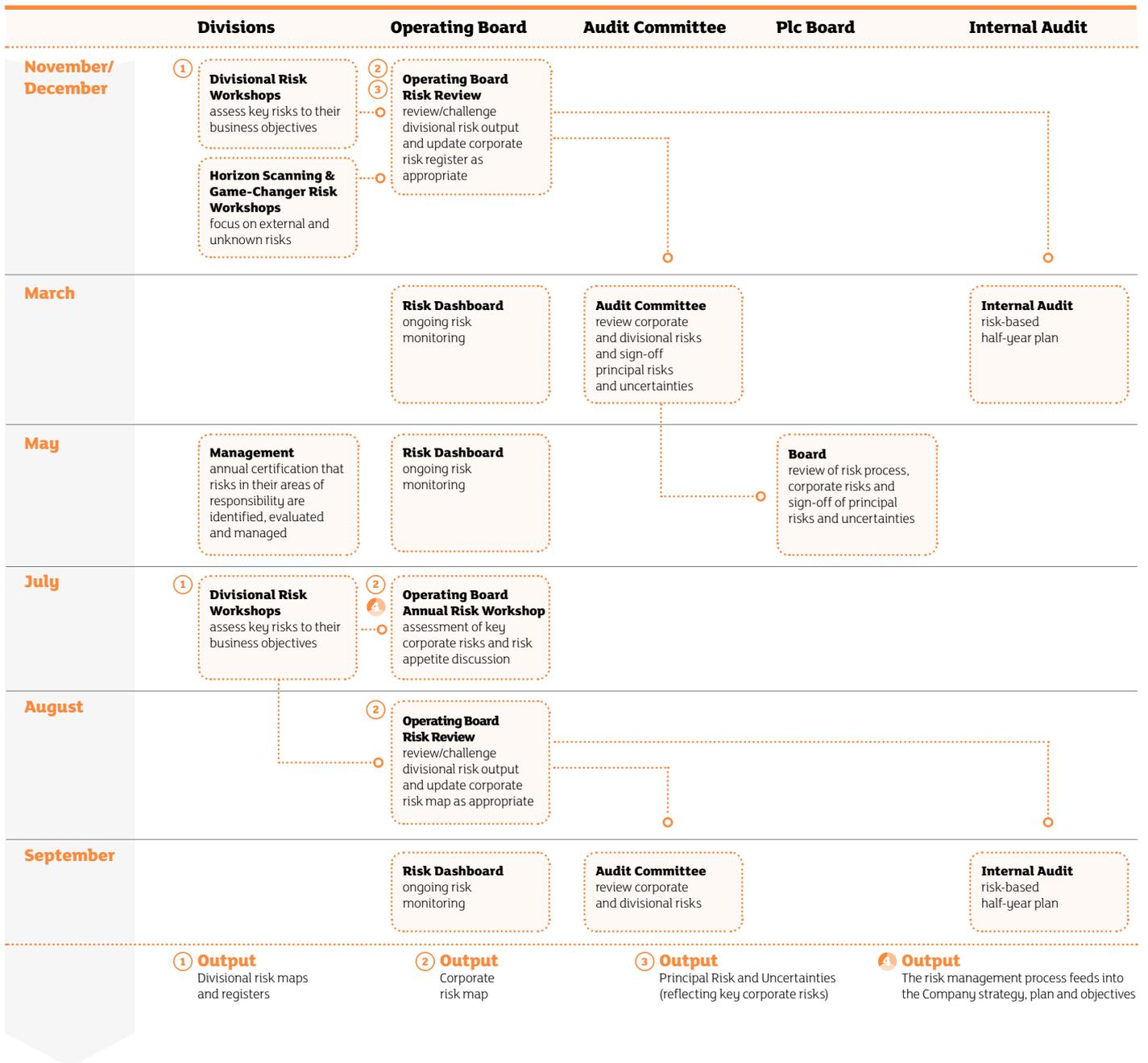
The risk management process is illustrated in the diagram on page 72. The specific risk activities undertaken in the financial year 2016/17 were as follows:

- Internal Audit facilitated risk workshops with each divisional leadership team to identify the key risks which may prevent the achievement of divisional objectives. Each divisional management team produced and maintained a divisional risk map and supporting risk register. The likelihood and impact of each key risk was evaluated at a gross level (before consideration of mitigating controls) and net level (after consideration of mitigating controls). Management’s risk appetite was reviewed and further actions to mitigate the risk were identified as required.
- The implementation of divisional risk actions were tracked by Internal Audit and reported to divisional leadership teams periodically. Risk action implementation rates are reviewed by the Operating Board regularly to monitor progress towards their risk appetite.

- Divisional management regularly reviews key divisional risks and the effectiveness and robustness of the mitigating controls as part of their normal business activities. Independent assurance over the controls is also provided through the delivery of the Internal Audit risk based plan.
- The Operating Board reviewed and challenged the output of the divisional risk process including new risks, risk movements and key risk themes. Where divisional risks are aligned to corporate risks the corporate risk map was updated as appropriate.
- Corporate risk dashboards comprised of key risk indicators have been developed to enable risk owners to identify any potential movements towards or away from their risk appetite. The Operating Board regularly reviewed the risk dashboards, reflecting any risk movements on the corporate risk map as required.
- Internal Audit facilitated a game-changer and horizon scanning risk workshop to identify external and uncertain risks over a five to ten year timeline. Key themes and outputs from this exercise were reviewed by the Operating Board to identify the potential impact on key corporate risks.

- Internal Audit provided independent assurance to management and the Committee as to the existence and effectiveness of the risk management process;
- Internal Audit conducted a risk appetite survey in December 2016 with the Operating Board to assess the extent to which consideration of risk appetite is embedded in the business. The output of the survey was presented to the Operating Board and Audit Committee for review and discussion; and
- The Board reviewed the risk management process and corporate risks at the year-end and approved the Company's principal risks and uncertainties (as set out on pages 42 to 44).

The risk management process is illustrated below:



### Internal controls

The system of internal control encompasses all controls, including those relating to financial reporting processes (including the preparation of the consolidated Group accounts), operational and compliance controls and those relating to risk management processes. It also includes the controls over Sainsbury's interests in joint ventures.

The Committee assesses the effectiveness of the internal controls systems on an ongoing basis, enabling a cumulative assessment to be made. The processes used during the year to support this assessment are as follows:

- Discussion and approval by the Board of the Company's strategy, plans and objectives, and the risks to achieving them
- Review and approval by the Board of budgets and forecasts, including those for both revenue and capital expenditure
- Regular reviews by management of the risks to achieving objectives and mitigating controls and actions
- Regular reviews by management and the Committee of the scope and results of the work of Internal Audit across the Company and of the implementation of their recommendations
- Regular reviews by the Committee of the scope and results of the work of the external auditors and of any significant issues arising
- Regular reviews by the Audit Committee of accounting policies and levels of delegated authority
- Regular reviews by the Board and the Committee of material fraudulent activity and any significant whistleblowing by colleagues or suppliers and actions being taken to remedy any control weaknesses

### Additional matters

#### Internal Audit

The Committee has regularly reviewed the Internal Audit department's resources, budget, work programme, results and management's implementation of required actions and its recommendations.

The Director of Internal Audit reports to the Committee Chairman and has direct access to all members of the Committee and the Chairman. She is given the opportunity after each meeting to meet with the Committee separately without management being present. She has regular meetings with all Committee members. The purpose, authority and responsibility of Internal Audit are defined in the Internal Audit Charter which the Committee reviews annually.

The effectiveness of the Internal Audit department is monitored and reviewed over the course of the year. The Committee has set KPIs which are used to assist it in reviewing the effectiveness of Internal Audit. The Director of Internal Audit reported against these KPIs twice during the year, highlighting any failure to achieve the target scores and explaining the reason therefore. In addition, an effectiveness questionnaire was completed by the Chairman of the Board and the members of each of the Committees and the Operating Board. The Committee concluded that Internal Audit continued to be effective.

#### Whistleblowing

The Company's whistleblowing procedures ensure that arrangements are in place to enable colleagues and suppliers to raise concerns about possible improprieties on a confidential basis. All issues raised have been investigated and appropriate actions taken. Any significant issues are highlighted to the Audit Committee.

#### Sainsbury's Bank

Sainsbury's Bank is a subsidiary of the Company which has an independent board responsible for setting the Bank's strategy, risk appetite and annual business plan as well as the day-to-day management of the business. The Board of the Bank has an independent Chairman and a majority of independent Non-Executive Directors.

The Bank will continue to provide to each Audit Committee an update on performance and the chairs of the Bank's Audit Committee and Risk Committee will present to the Audit Committee. There is alignment between the Sainsbury's Internal Audit function and their colleagues within Sainsbury's Bank equivalent team.

### Grocery Supply Code of Practice

In February 2010, a new Grocery Supply Code of Practice (GSCOP) was implemented following the recommendation of the Competition Commission. Each grocery retailer to which it applies had to appoint a Code Compliance Officer whose duties include hearing disputes between suppliers and the relevant retailer. Sainsbury's appointed the Director of Internal Audit as its Code Compliance Officer.

GSCOP requires that each grocery retailer (to which it applies) delivers an annual compliance report to the Groceries Code Adjudicator which has been approved by the Chairman of the Audit Committee. Furthermore, a summary of the compliance report must be included in our Annual Report and Financial Statements.

#### Summary annual compliance report

Sainsbury's has invested significant time and resource in providing comprehensive training to all relevant colleagues as required under GSCOP which is reinforced by online knowledge testing. Sainsbury's has also dedicated internal resource to provide all relevant colleagues with day-to-day advice and guidance. The Trading Division, in consultation with the Legal Services Department and the Code Compliance Officer, continues to assess the adequacy of policies and procedures in place to support GSCOP awareness and compliance.

A small number of alleged breaches of GSCOP have been received in the reporting period, which were dealt with within the Trading Division using our standard internal escalation procedure. The resolution of five of these alleged breaches was facilitated by the Code Compliance Officer during the reporting period.

# Annual Statement from the Remuneration Committee Chairman



## Dear Shareholder,

With changing customer expectations and a rapidly evolving business, the incentive pay outcomes for 2016/17 reflect our performance in the context of a volatile UK retail grocery market.

### Key remuneration decisions for 2016/17

Total remuneration for the Executive Directors has decreased by 11 to 16 per cent as a result of our incentive arrangements reflecting our performance during the year.

- *Annual bonus* – Our Executive Directors are committed to developing our strategy and driving the performance of our business in the challenging environment. The profit and sales targets set at the start of the year were not achieved. However, good progress was made on a number of key strategic, operational and customer initiatives and there was strong performance against individual objectives. In light of the overall results, the Committee determined that no cash annual bonus should be paid in respect of the year.
- *Deferred Share Award* – The Committee determined that awards under the DSA should be granted at 70 per cent of the maximum for all participants recognising, in particular, the continued performance of the business in relative terms and the significant achievements made on our strategic goals. This award is deferred into shares.
- *2014 Future Builder* – Following two consecutive years of no payout, an element of the 2014 Future Builder vested as a result of our performance against the cash flow and relative sales measures. A performance multiplier of 0.9x was applied to the core award for all participants resulting in vesting of 22.5 per cent of the maximum. Half vests in May this year and the remaining half will vest in May 2018 after a further holding period.

### 2017 Remuneration Policy

The previous policy was approved by shareholders in 2014 and, therefore, we are bringing a revised Remuneration Policy for shareholder approval at the 2017 AGM, in line with the regulatory requirement to renew our policy at least once every three years.

We have consulted extensively with our major shareholders regarding the new policy and as part of this review process we looked at alternative long-term incentive structures which could adapt to the dynamic nature of the grocery sector. While the Committee saw the merits of alternative structures, we recognised that shareholder views on these remain mixed at this stage. Consequently we have opted to maintain the key features of the Remuneration Policy previously approved by shareholders in 2014.

While the overall approach and pay levels remain unchanged, we have taken the opportunity to make a small number of technical changes to reflect evolving market and best practice. These include:

- Introduction of a two-year holding period for Future Builder awards, meaning that shares will not normally be released until five years after grant;
- Shareholding guidelines increased from 1.5 times to 2.0 times salary for Executive Directors (CEO will remain at 2.5 times);
- Reduction in retirement benefits for any future appointment from 30 per cent to 25 per cent; and
- Strengthened recovery provisions (malus and clawback).

It is important for senior executive pay to be performance-based and to encourage sustainable long-term value for our shareholders. It is also in shareholders' interests for the Company to be able to attract and retain the talented leaders required to deliver strong performance in challenging markets.

However, as a business with around 195,000 colleagues, we are also acutely aware of the wider context in which the Committee makes key decisions. We continue to consider wider colleague reward when determining pay arrangements for the Executive Directors, and this remains a fundamental part of our approach to pay. There is a strong focus on core values across the business, and this is reflected in the strategy. Taking a responsible and sustainable approach to business is a defining characteristic of the Sainsbury's culture and this extends to the approach to executive remuneration.

## Looking ahead

### Salary review

In line with our policy, we have followed our normal approach to the review of salaries for the Executive Directors and have awarded both Mike Coupe and John Rogers a salary increase of 1.5 per cent effective March 2017, in line with other management colleagues. Kevin O'Byrne, who joined the Board as Chief Financial Officer in January 2017, was not eligible for an increase given his start date.

### 2016 and 2017 Future Builder

As we communicated in last year's Report, the setting of performance criteria for the Future Builder award granted in May 2016 was delayed to ensure the measures and targets were relevant and meaningful in the context of the enlarged Group following the acquisition of Home Retail Group plc. The Committee ultimately decided that synergy targets should be added to the Future Builder to complement the existing Return on Capital Employed, Earnings Per Share, cash flow and costs savings measures. Details of these targets were published on our website during the year and are also set out in this year's Remuneration Report on page 83.

The Committee has decided to retain this performance framework for awards to be granted during 2017, based on performance through to March 2020. We have recalibrated the ROCE targets in order to provide realistic but stretching goals reflecting the current and future prospects of the business as well as the retail sector as a whole over the next three years. The cost saving and synergy ranges have also been updated based on stated objectives over the period. Overall these provide an appropriately stretching incentive for participants. Further detail of targets for 2017 awards are set out on page 82.

### The 2017 AGM

The Remuneration Committee remains firmly committed to the principle of pay for performance, ensuring that rewards for the senior leadership team are aligned with the experience of long-term shareholders, while also considering the pay and benefits of our wider workforce.

In line with the UK reporting regulations, the Directors' Remuneration Policy will be put to a binding vote and the Annual Report on Remuneration will be put to an advisory vote at the AGM on 5 July 2017.

Finally, as you will be aware, this is my last letter to you as Remuneration Committee Chairman as I am stepping down from the Board at the AGM. It has been a pleasure to work with an organisation such as Sainsbury's and I know that Susan Rice will be an excellent Remuneration Committee Chairman as she takes up the position from July 2017.



**Mary Harris**

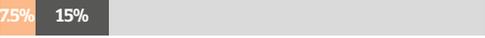
**Chairman, Remuneration Committee**

“

**The Remuneration Committee remains firmly committed to the principle of pay for performance, ensuring that rewards for the senior leadership team are aligned with the experience of long-term shareholders.”**

**Mary Harris**

## Summary of 2016/17 remuneration decisions

| Pay element   | 2016/17 decisions   |
|---|---|
| Salary  | <ul style="list-style-type: none"> <li>— Mike Coupe – £929,486 and John Rogers – £685,125 – salary increase of 1.5 per cent in March 2016, in line with other management and central colleagues.</li> <li>— Kevin O'Byrne – £625,000 – on appointment as Chief Financial Officer on 9 January 2017.</li> </ul>  |
| Annual bonus<br><b>No payout to the Executive Directors</b> | <ul style="list-style-type: none"> <li>— No payment was made in relation to the annual bonus for 2016/17, reflecting overall business performance. Full details of the bonus measures can be found on page 80.</li> <li>— For 2015/16 the bonus outturn was 76 per cent of the maximum for Mike Coupe and 78 per cent of the maximum for John Rogers.</li> </ul>  |
| Deferred Share Award<br><b>Award of 70 per cent of max</b>  | <ul style="list-style-type: none"> <li>— Performance assessed taking into account financial performance, returns to shareholders, relative performance against peers and strategic goals.</li> <li>— Financial targets partially met.</li> <li>— Good relative performance in terms of price, quality and service.</li> <li>— Dividend paid ahead of listed peers.</li> <li>— Significant progress against strategic goals; the acquisition of Home Retail Group plc has accelerated the Company's strategy.</li> <li>— For 2015/16 the DSA paid out at 80 per cent of the maximum.</li> </ul> <p><b>Deferred Share Award</b></p> <p><b>Award % of max</b> </p> |
| LTIP/Future Builder<br><b>Vesting 22.5 per cent of max</b>  | <ul style="list-style-type: none"> <li>— The Future Builder, based on performance to March 2017, will vest at 22.5 per cent of the maximum. Partial vesting was achieved under the cash flow and relative sales elements.</li> <li>— For the past two years, there has been no vesting of awards.</li> </ul> <p><b>Future Builder</b></p> <p><b>Weighting</b> </p> <p><b>Award % of max</b> </p> <p>● ROCE ● Cash flow ● Relative sales</p>   |

### Total Remuneration

|                                |                      | Mike Coupe<br>£000 |         | John Rogers<br>£000   |         | Kevin O'Byrne<br>£000 |
|--------------------------------|----------------------|--------------------|---------|-----------------------|---------|-----------------------|
|                                |                      | 2016/17            | 2015/16 | 2016/17               | 2015/16 | 2016/17 <sup>2</sup>  |
| <b>Fixed pay</b>               | Salary               | <b>929</b>         | 916     | <b>685</b>            | 650     | <b>108</b>            |
|                                | Benefits             | <b>17</b>          | 38      | <b>66<sup>1</sup></b> | 17      | <b>3</b>              |
|                                | Pension              | <b>279</b>         | 275     | <b>171</b>            | 163     | <b>27</b>             |
| <b>Performance-related pay</b> | Annual bonus         | –                  | 767     | –                     | 472     | –                     |
|                                | Deferred Share Award | <b>716</b>         | 806     | <b>432</b>            | 486     | –                     |
|                                | LTIP/Future Builder  | <b>408</b>         | –       | <b>245</b>            | –       | –                     |
| <b>Total pay</b>               |                      | <b>2,349</b>       | 2,802   | <b>1,599</b>          | 1,788   | <b>138</b>            |

1 John Rogers' benefits for 2016/17 include costs associated with accommodation in and travel to Milton Keynes following his appointment as CEO of Sainsbury's Argos.

2 Kevin O'Byrne was appointed on 9 January 2017.

## Summary of 2017/18 Remuneration Policy

This section summarises the key changes to the Remuneration Policy since it was last approved in 2014, and how it will be implemented for 2017/18. The full policy is set out on pages 88 to 94.

### Implementation for 2017/18

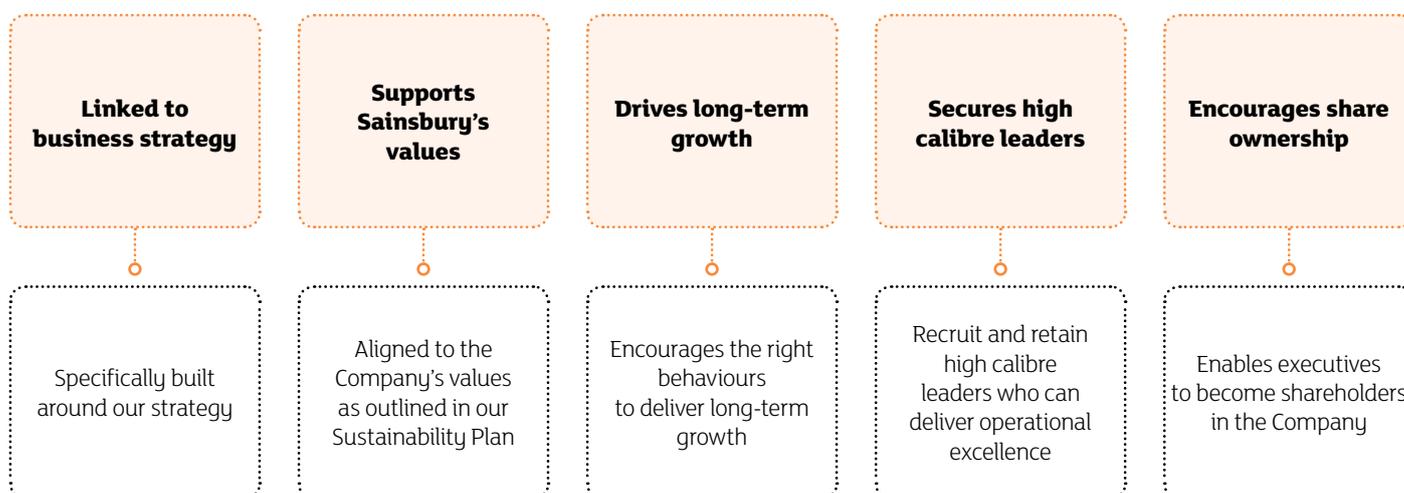
| Pay element  | Summary of policy  | Approach for 2017/18   |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
|--|--|--|----------------------------------|-----------|------------------------------------|----------------------------------|-----------------------------------|-----|----|-----|---|-----|-----|-----|--|-----|---------|---------|--|-----|-------|-------|---------------------------------------|-----|-------|-------|
| Salary<br><b>Increase in line with colleagues</b>                                      | Salaries are set taking into consideration a range of internal and external factors. Increases are normally in line with those for the wider workforce.  | Mike Coupe and John Rogers received salary increases of 1.5 per cent in March 2017 in line with other management and central colleagues. The 2017/18 salaries are:<br>— Mike Coupe – £943,428<br>— John Rogers – £695,402<br>— Kevin O'Byrne – £625,000  |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Benefits   | Range of benefits provided in line with market practice and reflecting individual circumstances.   | No changes to current arrangements.  |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Retirement benefits<br><b>Reduction in pension for future appointments</b>             | Participation in either the Company defined contribution plan and/or a cash salary supplement. The maximum value is 30 per cent of salary for existing Executive Directors. For new appointments the maximum value is being reduced under the new Policy from 30 per cent of salary to 25 per cent.  | No changes to salary supplement in lieu of pension for Mike Coupe (30 per cent of salary), John Rogers (25 per cent of salary) and Kevin O'Byrne (25 per cent of salary).  |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Annual bonus<br><b>No change to quantum and general structure</b>                      | Based on key financial and individual objectives measured over one year, with bonus payable in cash after the year-end. Maximum opportunity of up to 125 per cent of salary per annum.   | Performance is based on profit, sales, customer and individual performance. Profit accounts for at least half of the bonus.<br>The maximum bonus for 2017/18 is:<br>— Mike Coupe – 110 per cent of salary<br>— John Rogers – 90 per cent of salary<br>— Kevin O'Byrne – 90 per cent of salary  |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Deferred Share Award<br><b>No change to quantum and general structure</b>              | Recognises and rewards for delivery of short-term strategic and financial objectives which contribute towards long-term sustainable growth. Performance measured over one year, after which award made as share awards deferred for two financial years.<br>Maximum opportunity of up to 125 per cent of salary per annum.   | Performance over the financial year is based on financial performance, returns to shareholders, relative performance against peers and strategic goals. Financial performance and returns to shareholders account for over half of the DSA.<br>The maximum award for 2017/18 is:<br>— Mike Coupe – 110 per cent of salary<br>— John Rogers – 90 per cent of salary<br>— Kevin O'Byrne – 90 per cent of salary  |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| LTIP/Future Builder<br><b>Additional holding period</b><br><b>No change to quantum</b> | Recognises and rewards for delivery of Company performance and shareholder value over the longer term.<br>Awards dependent on performance measured over a period of at least three financial years.<br>For awards granted from 2017 onwards, a two-year holding period applies following the end of the three-year performance period.<br>Maximum award of up to 250 per cent of salary per annum. | Awards are structured as core awards, with a performance multiplier of up to four times. The 2017/18 awards are:<br>— Mike Coupe – core award of 62.5 per cent of salary (max 250 per cent)<br>— John Rogers – core award of 50 per cent of salary (max 200 per cent)<br>— Kevin O'Byrne – core award of 50 per cent of salary (max 200 per cent)<br>The targets for 2017 awards are as follows:   |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
|  |  | <table border="1"> <thead> <tr> <th>Measure</th> <th>Weighting</th> <th>Threshold target (1.0x core award)</th> <th>Maximum target (4.0x core award)</th> </tr> </thead> <tbody> <tr> <td>Return on capital employed (ROCE)</td> <td>20%</td> <td>8%</td> <td>11%</td> </tr> <tr> <td>Underlying basic earnings per share (EPS)</td> <td>20%</td> <td>23p</td> <td>30p</td> </tr> <tr> <td>Cumulative underlying cash flow from retail operations after capex (cash flow)</td> <td>20%</td> <td>£3,500m</td> <td>£5,150m</td> </tr> <tr> <td>Cumulative strategic cost savings (cost savings)</td> <td>20%</td> <td>£450m</td> <td>£550m</td> </tr> <tr> <td>HRG acquisition synergies (synergies)</td> <td>20%</td> <td>£160m</td> <td>£200m</td> </tr> </tbody> </table> | Measure                          | Weighting | Threshold target (1.0x core award) | Maximum target (4.0x core award) | Return on capital employed (ROCE) | 20% | 8% | 11% | Underlying basic earnings per share (EPS) | 20% | 23p | 30p | Cumulative underlying cash flow from retail operations after capex (cash flow) | 20% | £3,500m | £5,150m | Cumulative strategic cost savings (cost savings) | 20% | £450m | £550m | HRG acquisition synergies (synergies) | 20% | £160m | £200m |
| Measure  | Weighting  | Threshold target (1.0x core award)   | Maximum target (4.0x core award) |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Return on capital employed (ROCE)  | 20%  | 8%   | 11%                              |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Underlying basic earnings per share (EPS)  | 20%  | 23p  | 30p                              |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Cumulative underlying cash flow from retail operations after capex (cash flow)         | 20%  | £3,500m  | £5,150m                          |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Cumulative strategic cost savings (cost savings)                                       | 20%  | £450m  | £550m                            |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| HRG acquisition synergies (synergies)  | 20%  | £160m  | £200m                            |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Shareholding guidelines<br><b>Increased guidelines</b>                                 | The Executive Directors are required to build a significant shareholding in the Company. For the CEO this remains at 2.5 x salary, while for other Executive Directors this has increased to 2.0 x salary (from 1.5 x salary).<br>The shareholding guidelines are now aligned with the maximum grant levels for Future Builder awards.   |  |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |
| Recovery provisions<br><b>Strengthened provisions</b>                                  | The Executive Directors' incentive arrangements are subject to malus and clawback.   |  |                                  |           |                                    |                                  |                                   |     |    |     |   |     |     |     |  |     |         |         |  |     |       |       |                                       |     |       |       |

# Annual Report on Remuneration

## Remuneration principles

Our colleagues are a key part of the Company's strategy and our overall reward strategy supports this. Our objective is to have a fair, equitable and competitive total reward package that supports our vision of being the most trusted retailer where people love to work and shop, encourages colleagues to perform in ways that deliver great service for customers, drives sales and provides opportunities for colleagues to share in Sainsbury's success. This overall reward strategy is the foundation for the Remuneration Policy for senior executives.

The over-arching objectives of the Remuneration Policy are to ensure rewards are performance-based and encourage long-term shareholder value creation. The Remuneration Policy for senior executives is based on the following principles:



The Committee takes a rounded approach to pay and considers a variety of factors when determining, and subsequently implementing, the policy for senior executives. It believes it is important to exercise sound judgement at all stages during the process to ensure that executive pay levels appropriately reflect performance and are aligned with the interests of shareholders.

The Committee regularly reviews the overall structure of remuneration for senior executives to ensure that it continues to evolve and is aligned to the corporate plan and business goals as well as supporting the interests of shareholders. When reviewing remuneration arrangements, the Committee considers pay practices across the Company and the retail sector more generally, the impact on colleagues, the cost to the Company, stakeholder views (including shareholders, governance bodies and colleagues) and best practice.

## Single total figure of remuneration for Executive Directors (audited information)

The table below shows a single remuneration figure for all qualifying services for the 52 weeks to 11 March 2017, together with comparative figures for the 52 weeks to 12 March 2016.

|                          | Notes | Mike Coupe<br>£000 |         | John Rogers<br>£000 |         | Kevin O'Byrne<br>£000 |         |
|--------------------------|-------|--------------------|---------|---------------------|---------|-----------------------|---------|
|                          |       | 2016/17            | 2015/16 | 2016/17             | 2015/16 | 2016/17               | 2015/16 |
| Base salary              | 1     | <b>929</b>         | 916     | <b>685</b>          | 650     | <b>108</b>            |         |
| Benefits                 | 2     | <b>17</b>          | 38      | <b>66</b>           | 17      | <b>3</b>              |         |
| Pension                  |       | <b>279</b>         | 275     | <b>171</b>          | 163     | <b>27</b>             |         |
| <b>Total fixed pay</b>   |       | <b>1,225</b>       | 1,229   | <b>922</b>          | 830     | <b>138</b>            |         |
| Annual bonus             | 3     | –                  | 767     | –                   | 472     | –                     |         |
| Deferred Share Award     | 4     | <b>716</b>         | 806     | <b>432</b>          | 486     | –                     |         |
| Long-Term Incentive Plan | 5     | <b>408</b>         | –       | <b>245</b>          | –       | –                     |         |
| <b>Total</b>             |       | <b>2,349</b>       | 2,802   | <b>1,599</b>        | 1,788   | <b>138</b>            |         |

1 Kevin O'Byrne was appointed on 9 January 2017. His full-year salary will be £625,000.

2 Benefits include a combination of cash and non-cash benefits, valued at the taxable value. For Mike Coupe, John Rogers and Kevin O'Byrne this includes a cash car allowance (£15,250) and private medical cover. For John Rogers this also includes an annual travel allowance of £6,500 per annum and accommodation costs of £45,647 per annum in relation to a change of location to Milton Keynes following his appointment as CEO of Sainsbury's Argos. Also included is a value for Sharesave options based on a 20 per cent discount on the savings in the year.

3 Annual bonus relates to performance during the financial year, paid in May following the relevant year-end.

4 The Deferred Share Award relates to performance during the financial year, shares are granted in May following the relevant year-end and vest after a two-year deferral period.

5 The Long-Term Incentive Plan value relates to the Future Builder award vesting in May following the end of the relevant financial year, which is the third year of the performance period. 50 per cent of the shares are released in May after the end of the relevant performance period and the balance one year later. The figures include accrued dividends over the performance period. The 2015/16 awards lapsed. The 2016/17 awards are based on the average share price over the fourth quarter for 2016/17 of £2.632.

6 The Executive Directors are entitled to retain the fees earned from non-executive appointments outside the Company. Mike Coupe was appointed a Non-Executive Director of Greene King plc on 26 July 2011 and received £50,000 (2015/16: £45,744) for his services during 2016/17. John Rogers was appointed a Non-Executive Director of Travis Perkins plc on 1 November 2014 and received £57,052 (2015/16: £56,240) for his services during the year. Kevin O'Byrne was appointed as a Non-Executive Director of Land Securities plc on 1 April 2008 and received £15,041 for his services since his appointment as Chief Financial Officer on 9 January 2017.

### Base salary

|               | Salary as at 2016/17 year-end | Salary effective from 12 March 2017 |
|---------------|-------------------------------|-------------------------------------|
| Mike Coupe    | £929,486                      | £943,428                            |
| John Rogers   | £685,125                      | £695,402                            |
| Kevin O'Byrne | £625,000                      | £625,000                            |

When considering salaries the Committee takes account of a number of factors, with particular focus on the general level of salary increases awarded throughout the Company. The salary review for management and central colleagues in March 2017 was generally 1.5 per cent and for Sainsbury's hourly-paid retail colleagues in August 2016 was 4.0 per cent. Where relevant, the Committee also considers external market data on salary and total remuneration but the Committee applies judgement when considering such data. For 2017/18 both Mike Coupe and John Rogers will receive a salary increase of 1.5 per cent effective March 2017 in line with other management colleagues. Kevin O'Byrne, who joined the Board as CFO in January 2017, was not eligible for an increase given his start date.

### Pension

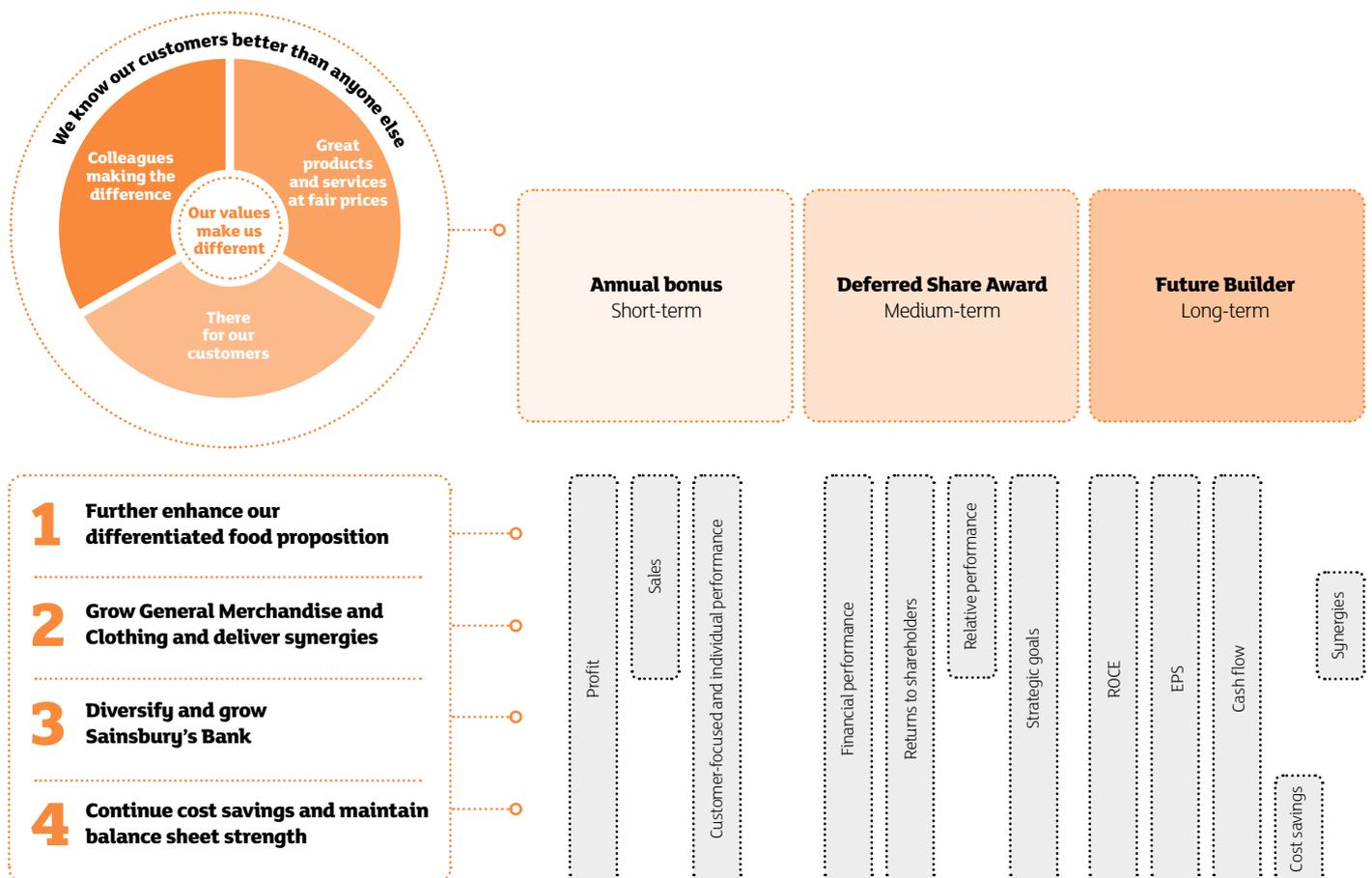
In lieu of pension plan participation, Mike Coupe receives a cash pension supplement of 30 per cent of salary and John Rogers and Kevin O'Byrne receive 25 per cent of salary. No Director has any entitlement to a Sainsbury's defined benefit pension.

### Benefits

For 2016/17 and 2017/18, benefits for Executive Directors include the provision of company car benefits, private medical cover, long-term disability insurance, life assurance and colleague discount. Benefits for John Rogers also include an annual travel allowance and accommodation costs in relation to a change of location to Milton Keynes following appointment as CEO of Sainsbury's Argos.

### Performance-related pay

The Committee believes it is important that a significant portion of the Executive Directors' package is performance-related and the performance conditions applying to incentive arrangements support the delivery of the Company's strategy and the long-term sustainable success of the Company. The specific metrics incorporated into the annual bonus, Deferred Share Award and Future Builder are built around the overall strategy and our key priorities.



The Board is of the opinion that the performance targets for the 2017/18 annual bonus and Deferred Share Award are commercially sensitive as the Company operates in a highly competitive, consumer-facing sector. The disclosure of targets would provide competitors with insights into the Company's strategic aims, budgeting and growth projections. However, in line with last year, the Company is retrospectively disclosing the financial performance targets set for the 2016/17 annual bonus in order to provide greater transparency. Consistent with previous years, detailed disclosure is provided in relation to the Deferred Share Award so that shareholders can understand the basis for payments. Targets for Future Builder awards have been disclosed on a prospective basis.

## Annual bonus

### 2017/18 policy

All bonus plans across the Company are aligned under a set of common principles. The Board and senior management plans are based on profit, sales, a customer-focused measure and individual performance. For the most senior executives, at least 50 per cent of the award is weighted towards the achievement of profit under the current structure. A performance gateway also has to be achieved in order to trigger a payment of any awards. The annual bonus is paid in cash after the year-end.

The profit and sales targets are set against the Company's expected performance and are subject to a rigorous process of challenge before the proposals are considered by the Board. The targets are set such that considerably stretching performance in excess of internal and external forecasts is required for maximum payout.

The customer-focused measure is based on a customer satisfaction index, which is a survey operated by a third party, that assesses the satisfaction of Sainsbury's customers shopping with us in-store or online. Individual performance objectives are set annually for each Executive Director and are reviewed by the Committee. These objectives cover a variety of financial and operational targets that contribute to the achievement of longer-term strategic goals; some of these objectives relate, either directly or indirectly, to the Company's value.

The maximum annual bonus award opportunity for the Chief Executive is 110 per cent of base salary and for the other Executive Directors is 90 per cent of base salary. The weighting of each measure is shown in the table below.

|   | Maximum opportunity as per cent of salary |                           |
|---|---|---------------------------|
|   | CEO                                       | Other Executive Directors |
| Profit                                      | 60%                                       | 45%                       |
| Sales                                       | 10%                                       | 10%                       |
| Customer-focused and individual performance | 40%                                       | 35%                       |
| <b>Total</b>                                | <b>110%</b>                               | <b>90%</b>                |

### 2016/17 annual bonus payment (audited information)

The performance measures for 2016/17 were the same as outlined above for 2017/18.

Overall financial results for the year were good in the context of a challenging and competitive trading environment. However, the profit and sales outcomes were below the threshold performance hurdles due to the stretch of the targets. The targets were set at the beginning of the financial year prior to the acquisition of Home Retail Group plc and so performance has been measured excluding the impact of the transaction to allow for a comparison on a like-for-like basis. The table below sets out the threshold and stretch profit and sales targets and the actual outcome for 2016/17.

|                     | Threshold | Stretch  | Actual   |
|---------------------|-----------|----------|----------|
| Profit <sup>1</sup> | £540m     | £640m    | £502m    |
| Sales <sup>2</sup>  | £25,919m  | £26,119m | £25,595m |

1 Underlying profit before tax, excluding Home Retail Group plc, and derived from Group Profit minus Argos business as usual profit and synergies.

2 Total sales including VAT and duty, including petrol sales, excluding Argos and Sainsbury's Bank. Petrol volumes and prices held constant to remove the effect of fuel volatility on sales.

Both Mike Coupe and John Rogers exceeded a number of their customer-focused and individual performance objectives set at the start of the year, with strong progress made on executing the key strategic priorities.

Following the end of the financial year, the Committee reviewed performance and determined that the business results in absolute terms did not warrant the payment of a cash bonus to the Executive Directors. While no bonus is payable to the Executive Directors, colleagues across the Group shared in a bonus of £78 million, reflecting their contribution throughout the year.

## Deferred Share Award

### 2017/18 policy

The Deferred Share Award (DSA) is used to drive performance against a diverse range of key financial and strategic scorecard measures, and rewards Executive Directors for achieving the short-term objectives that will directly lead to building the sustainable, long-term growth of the Company. These awards are made in shares to ensure further alignment with shareholders.

The DSA covers broadly the top 50 senior leaders in the Company, including Executive Directors. Performance is assessed in the round based on the Committee's judgement of performance against a number of measures within four broad categories. The categories and examples of the measures that will be reviewed for 2017/18 are set out below.

|                                    |  |
|------------------------------------|--|
| Financial performance              | <i>Profit, earnings per share, sales</i>                           |
| Returns to shareholders            | <i>Total shareholder return, dividend yield</i>                    |
| Relative performance against peers | <i>Market share, industry profit pool</i>                          |
| Strategic goals                    | <i>Proposition, channels, price, customers, colleagues, values</i> |

As outlined in our Remuneration Policy, at least 50 per cent of the award will be based on the delivery of financial performance and returns to shareholders. In addition, no shares will be awarded unless a performance gateway target is achieved.

Performance is assessed over one financial year, but any shares awarded are deferred for a further two financial years. The shares are subject to forfeiture if the participant resigns or is dismissed for cause prior to their release date. Dividends accrue on any shares that subsequently vest.

The maximum DSA award opportunity for the Chief Executive is 110 per cent of base salary and for the other Executive Directors is 90 per cent of base salary.

**2016/17 Deferred Share Award (audited information)**

Following the year-end, the Committee conducted a rigorous assessment of performance. Consistent with the underlying principles of the DSA, the Committee assessed achievements in the round and also considered the manner in which these performance goals had been delivered, in particular how the overall performance of the Company had contributed to its future sustainable growth and success.

2016/17 continued to be a challenging year for retailers and the Company only partially met its financial targets. However, the Company performed well against its peers in terms of price, quality, service and dividends paid. It also made significant progress against our strategic goals with the acquisition of Home Retail Group plc which will accelerate our strategy. The Committee, therefore, agreed that for 2016/17 awards would be made at 70 per cent of the maximum level, compared with 80 per cent last year. It also determined that the profit gateway for the plan was achieved. Although some of the specific measures and targets are commercially sensitive, the table below presents a selection of performance highlights which the Committee took into account within each of the four categories.

The table below sets out details of the awards and these are the figures set out in the DSA row of the single total figure table. The share award is made after the end of the 2016/17 financial year and the shares vest in March 2019 subject to continued employment.

|             | Maximum opportunity | Outcome            |            |
|-------------|---------------------|--------------------|------------|
|             | Per cent of salary  | Per cent of salary | Value £000 |
| Mike Coupe  | 110%                | 77%                | £716       |
| John Rogers | 90%                 | 63%                | £432       |

**2016/17 Deferred Share Award performance**

| Financial performance  | Returns to shareholders  | Relative performance against peers   |
|--|--|--|
| <ul style="list-style-type: none"> <li>— Underlying profit before tax of £581 million</li> <li>— Groceries Online sales growth of over eight per cent and order growth of around 12 per cent</li> <li>— General Merchandise (excluding Argos) sales growth of over two per cent</li> <li>— Clothing growth of over four per cent</li> <li>— Convenience sales growth of over six per cent</li> </ul> | <ul style="list-style-type: none"> <li>— Five-year Total Shareholder Return ahead of listed peers</li> <li>— Dividends paid to shareholders outperform listed peers and maintain dividend cover of 2.0x underlying earnings</li> <li>— Underlying basic EPS of 21.8 pence per share</li> </ul> | <ul style="list-style-type: none"> <li>— Competitive price position with lower regular prices</li> <li>— Market share performance in line with big four supermarket peers</li> <li>— Outperformance of product quality perception relative to our peers</li> </ul> |

**Strategic goals****1 Further enhance our differentiated food proposition**

- Successful completion of quality investment programme with over 3,000 own-brand products new or improved
- Successful implementation of simplified pricing strategy, reinvesting in everyday lower prices
- 151 Grocery click and collect sites now open
- Industry-leading service and availability, with 17 Grocer 33 wins and a third consecutive Investors in People Gold accreditation
- Outperformance of product quality perception relative to our peers

**2 Grow General Merchandise and Clothing and deliver synergies**

- Acquisition of Home Retail Group plc completed in September 2016
- Delivery of £7 million of synergies, against a target of £0 to £5 million
- Rolled out revised General Merchandise and Clothing format in 16 stores
- General Merchandise (excluding Argos) growth of over two per cent, Clothing growth of over four per cent
- Sixth largest clothing retailer by volume with eight million customers
- 39 Argos Digital stores opened this year in our supermarkets
- Rolled out 207 digital collection points, including 90 Argos Click and Collect counters
- Argos is the third most-visited e-commerce website in the UK

**3 Diversify and grow Sainsbury's Bank**

- Successful migration to new banking platform
- Successful integration of Argos Financial Services, enhancing the product portfolio for customers
- ATM estate growth of five per cent
- Website visits increased by 34 per cent
- Travel money transactions up 25 per cent
- Good financial performance with an operating profit of £62 million

**4 Continue cost savings and maintain balance sheet strength**

- £130 million of cost savings delivered and on track to deliver three-year target of £500 million
- Optimising store replenishment processes
- Better use of warehouse capacity
- Unlocking shareholder value from Pharmacy sale
- Net debt reduction of £349 million since 2016 from improved working capital and Home Retail Group plc acquisition

## Long-term incentives

### 2017/18 policy

The long-term incentive plan operated at Sainsbury's is known as Future Builder. Around 250 senior managers across the business participate in this arrangement. Awards were originally granted under the Long-Term Incentive Plan approved by shareholders in 2006. A renewed Long-Term Incentive Plan was approved by shareholders at the 2016 AGM, which is now being used.

Future Builder awards have been granted under the same structure for a number of years. A core award of shares is granted, generally calculated as a percentage of salary and scaled according to level of seniority. Vesting of the core award is dependent on performance against specific targets (common for all participants) tested at the end of a three-year performance period. The core awards can grow up to four times at stretch levels of performance.

Historically, awards have been structured so that half of any awards vest following the end of the performance period, with the remaining half vesting after a further year. For awards granted to Executive Directors from 2017 onwards, awards will normally be subject to a new two-year holding period following the end of the three-year performance period. This will result in future awards to Executive Directors normally only being released five years after grant.

The Remuneration Committee must be satisfied that the Company's underlying performance over the period justifies the level of vesting. Vesting will be reduced if the vesting outcome is not considered to be justified. At vesting, when making this judgement the Committee has scope to consider such factors as it deems relevant. The Committee believes that having a gateway is an important feature of the plan and mitigates the risk of unwarranted vesting outcomes. This gateway applies to all outstanding Future Builder awards.

### 2017 Future Builder awards (2017/18 to 2019/20 performance period)

Award levels will remain unchanged for the coming year. In 2017 Mike Coupe will receive a core award of 62.5 per cent of salary (maximum 250 per cent of salary) and the other Executive Directors will receive core awards of 50 per cent of salary (maximum 200 per cent of salary).

The 2017 awards will be subject to the same scorecard of metrics used for the 2016 awards. The Committee consulted with major shareholders regarding the targets for 2017 awards and the proposed target ranges were subsequently updated to reflect shareholder feedback. The cost savings and synergies targets for 2017 have been updated to align with the strategy communicated to shareholders for the period to March 2020. The ROCE targets have also been recalibrated in order to provide realistic but stretching goals reflecting the current and future prospects of the business as well as the retail sector as a whole over the next three years. Overall the Committee is of the view that these targets provide an appropriately stretching incentive for participants. The agreed measures, targets and weightings for 2017 awards are as follows:

| Measure  | Weighting | Threshold target<br>(1.0x core award) | Maximum target<br>(4.0x core award) |
|--|-----------|---------------------------------------|-------------------------------------|
| ROCE   | 20%       | 8%                                    | 11%                                 |
| Underlying basic EPS   | 20%       | 23p                                   | 30p                                 |
| Cumulative underlying cash flow from retail operations after capex | 20%       | £3,500m                               | £5,150m                             |
| Cumulative strategic cost saving                                   | 20%       | £450m                                 | £550m                               |
| Home Retail Group plc acquisition synergies                        | 20%       | £160m                                 | £200m                               |

### 2014 Future Builder (2014/15 to 2016/17 performance period) (audited information)

The 2014 Future Builder award was subject to ROCE, cash flow and relative sales performance targets, excluding Argos. In addition, a performance gateway must be achieved before any element could vest.

The following table sets out the extent to which each performance measure was achieved and this resulted in a performance multiplier of 0.9x which is applied to the core award, i.e. 22.5 per cent of the maximum available award vested.

|   | Weighting  | Threshold target<br>(1.0x core award) | Maximum target<br>(4.0x core award) | Achieved           | Multiplier achieved                      |
|---|--|---------------------------------------|-------------------------------------|--------------------|--|
| ROCE  | 50%  | 10.75%                                | 12.00%                              | 7.97% <sup>1</sup> | 0.0x                                     |
| Cumulative underlying cash flow from retail operations <sup>2</sup> | 30%  | £5,750m                               | £6,750m                             | £5,802m            | 0.3x                                     |
| Relative sales v IGD Index <sup>3</sup>                             | 20%  | Match Index                           | Index<br>+ 1.0% p.a.                | +0.6%              | 0.6x                                     |
| Performance gateway   | The Remuneration Committee must be satisfied that the Company's underlying performance over the period justifies the level of vesting. |                                       |                                     | Achieved           |  |
| <b>Total</b>  |  |                                       |                                     |                    | <b>0.9x<br/>out of a<br/>max of 4.0x</b> |

1 Figure relates to Group ROCE including Argos excluding pension fund deficit, while the targets exclude Argos.

2 Cumulative underlying cash flow from retail operations excluding Argos based on the reported cash flow generated from core retail operations over the performance period after adding back net rent and cash pension costs and adjusted for the cash impact of non-underlying items. Only core retail operations are included in recognition of the differences in cash generation between the retail business and Sainsbury's Bank.

3 Relative sales performance is measured using the IGD Index (IGD Market Track) adjusted to reflect the constituents at the start of the performance period. The Index measures growth in like-for-like sales (excluding fuel and Argos) across the market based on the performance of all of the Company's key competitors. This is an independent index of sales efficiency, which is viewed as a robust reference point for performance across the food retail sector.

**2015 Future Builder (2015/16 to 2017/18 performance period)**

Following the acquisition of Home Retail Group plc in September 2016, the targets will be assessed based on performance of the enlarged Group. After a detailed review, the Committee is satisfied that the targets originally set for this award remain appropriately stretching and that no adjustments are required. The Committee will continue to keep the targets under review in light of the acquisition of Home Retail Group plc. Appropriate disclosure of any adjustments necessary to ensure performance is assessed on a fair and consistent basis will be provided in next year's report.

| Measure  | Weighting | Threshold target<br>(1.0x core award) | Maximum target<br>(4.0x core award) |
|--|-----------|---------------------------------------|-------------------------------------|
| ROCE   | 25%       | 9%                                    | 12%                                 |
| Underlying basic EPS   | 25%       | 23p                                   | 30p                                 |
| Cumulative underlying cash flow from retail operations after capex | 25%       | £3,500m                               | £5,150m                             |
| Cumulative strategic cost saving                                   | 25%       | £450m                                 | £600m                               |

**2016 Future Builder awards (2016/17 to 2018/19 performance period)**

| Measure  | Weighting | Threshold target<br>(1.0x core award) | Maximum target<br>(4.0x core award) |
|--|-----------|---------------------------------------|-------------------------------------|
| ROCE   | 20%       | 9%                                    | 12%                                 |
| Underlying basic EPS   | 20%       | 23p                                   | 30p                                 |
| Cumulative underlying cash flow from retail operations after capex | 20%       | £3,500m                               | £5,150m                             |
| Cumulative strategic cost savings                                  | 20%       | £350m                                 | £450m                               |
| Home Retail Group acquisition synergies                            | 20%       | £100m                                 | £150m                               |

**Future Builder performance measures****ROCE**

- ROCE reflects the returns generated for shareholders and measures the efficiency of capital use.
- It is based on the underlying profit before interest and tax for the whole business, with Sainsbury's Bank fully consolidated, including the underlying share of post-tax profit from joint ventures. The capital employed figure excludes the impact of movements in the IAS 19 pension deficit.

**EPS**

- EPS directly reflects returns generated for shareholders.
- Underlying basic EPS is based on underlying profit after tax divided by the weighted average number of ordinary shares in issue during the year.

**Cash flow**

- Cash flow measures the total flow of cash in and out of the business as well as providing an assessment of underlying profitability.
- Cumulative underlying cash flow from retail operations after capital expenditure is based on the reported cash flow generated from core retail operations, including Sainsbury's Argos and Habitat, over the performance period after adding back net rent, cash pension costs and deducting core capital expenditure. Only core retail operations are included in recognition of the differences in cash generation between the retail business and Sainsbury's Bank.

**Cost savings**

- Cost savings is one of our key strategic targets and the level of savings targeted will require structural changes. This is a key long-term measure which is fundamental to delivering returns to shareholders.
- Cumulative strategic cost savings represents cost reductions over the performance period as a result of identified initiatives. It excludes Sainsbury's Bank and synergies.

**Synergies**

- Synergies represent the value driven from combining the J Sainsbury plc and Home Retail Group plc businesses since the acquisition in September 2016. The delivery of synergies was a key part of the deal.
- The target represents the EBITDA synergies delivered by the end of the three-year performance period.

### Share awards made during the financial year (audited information)

The following share awards were made to Executive Directors during the year. The Future Builder award levels are determined by the normal grant policy for the role and, in the case of the DSA, performance over the previous year.

|               | Scheme                      | Basis of award (maximum) | Face value | Percentage vesting at threshold performance | Number of shares | Performance period end date |
|---------------|-----------------------------|--------------------------|------------|---|------------------|-----------------------------|
| Mike Coupe    | Future Builder <sup>1</sup> | 250% of salary           | £2,323,715 | 20% of each element                         | 876,940          | 09/03/2019                  |
|               | DSA <sup>2</sup>            | 88% of salary            | £805,860   | n/a   | 304,121          | n/a                         |
| John Rogers   | Future Builder <sup>1</sup> | 200% of salary           | £1,370,250 | 20% of each element                         | 517,112          | 09/03/2019                  |
|               | DSA <sup>2</sup>            | 72% of salary            | £486,000   | n/a   | 183,410          | n/a                         |
| Kevin O'Byrne | Future Builder <sup>1</sup> | 200% of salary           | £1,250,000 | 20% of each element                         | 479,660          | 09/03/2019                  |
|               | DSA <sup>2</sup>            | –                        | –          | –   | –                | –                           |

1 The performance conditions applying to 2016 Future Builder awards are set out on page 83. The basis of award shows the maximum value, being four times the core award. The awards for Mike Coupe and John Rogers were made on 12 May 2016 and the number of shares has been calculated using the five-day average share price prior to grant (5 to 11 May 2016) of £2.6498. The award for Kevin O'Byrne was made on 26 January 2017 and the number of shares has been calculated using the five-day average share price prior to grant (19 to 25 January 2017) of £2.6060. Subject to performance, 50 per cent of the award vests on 12 May 2019 and 50 per cent 12 months later. The award is structured as a nil-cost option with an exercise period of up to two years.

2 The DSA was made on 12 May 2016 based on performance over the 2016/17 financial year. The award was made at 80 per cent of the maximum level (maximum of 110 per cent of salary for Mike Coupe and 90 per cent of salary for John Rogers). The number of shares has been calculated using the five-day average share price prior to grant (5 to 11 May 2016) of £2.6498. No further performance conditions apply. Awards become exercisable on 16 March 2018. The award is structured as a nil-cost option with an eight-year exercise period.

### Summary of remuneration arrangements for Kevin O'Byrne

Kevin O'Byrne was appointed as Chief Financial Officer of J Sainsbury plc on 9 January 2017 following John Rogers' appointment as CEO of Sainsbury's Argos.

Kevin was not eligible to receive a 2016/17 annual bonus or Deferred Share Award. He was awarded a 2016 Future Builder award with a maximum value of 200 per cent of salary shortly after appointment. The operation and structure of the award is in line with other participants and will vest at the normal time of 50 per cent in May 2019 and the remainder in May 2020. This performance based award is to compensate Kevin for remuneration forfeited on leaving his previous employment and is in line with our recruitment policy. The Committee is satisfied that this award is of comparable commercial value to the award which is being bought-out.

### Executive Directors' shareholdings and share interests (audited information)

The table below sets out details of the Executive Directors' shareholdings and a summary of their outstanding share awards at the end of the 2016/17 financial year. Further details of the movements of the Executive Directors' share awards during the year are set out on page 87.

|                            | Ordinary shares <sup>1</sup> |               |                         | Deferred Share Awards <sup>4</sup> | Scheme interests <sup>3</sup>  |  | SAYE  |
|----------------------------|------------------------------|---------------|-------------------------|------------------------------------|--|--|-------|
|                            | 12 March 2016                | 11 March 2017 | 2 May 2017 <sup>2</sup> |                                    | Future Builder awards with performance period completed <sup>5</sup> | Future Builder awards with performance period outstanding <sup>6</sup> |       |
| Mike Coupe                 | 1,068,515                    | 1,143,027     | 1,143,027               | 470,028                            | 0  | 2,305,556  | 4,518 |
| John Rogers                | 560,226                      | 660,145       | 660,232                 | 285,075                            | 0  | 1,318,524  | 6,302 |
| Kevin O'Byrne <sup>7</sup> | 0                            | 180,000       | 180,000                 | 0                                  | 0  | 479,660  | 0     |

1 Ordinary shares are beneficial holdings which include the Directors' personal holdings and those of their spouses and minor children. They also include the beneficial interests in shares which are held in trust under the Sainsbury's Share Purchase Plan.

2 The total includes shares purchased under the Sainsbury's Share Purchase Plan between 11 March 2017 and 2 May 2017.

3 Deferred Share Awards and Future Builder awards are structured as nil-cost options.

4 Relates to 2014/15 and 2015/16 Deferred Share Awards.

5 The 2012 and 2013 Future Builder awards lapsed and therefore no value is shown.

6 Relates to 2014, 2015 and 2016 Future Builder awards (maximum) where the performance period has not ended. As noted above, following the year-end, the 2014 award will vest at 22.5 per cent of maximum.

7 12 March 2016 figure relates to 9 January 2017 when Kevin O'Byrne joined the Board.

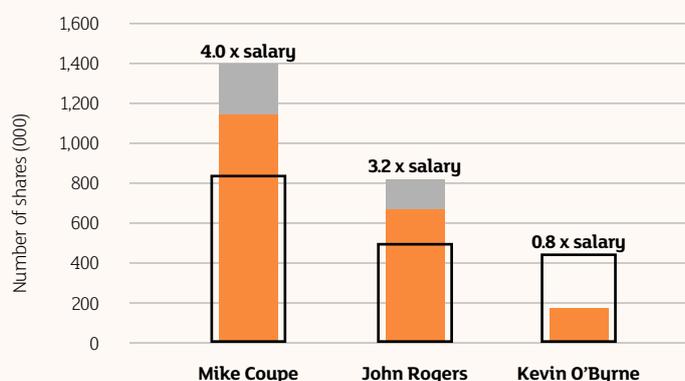
Note: The Executive Directors are potential beneficiaries of the Company's employee benefit trust, which is used to satisfy awards under the Company's employee share plans, and they are therefore treated as interested in the 1.0 million shares (2016: 7.9 million) held by the Trustees.

### Shareholding guidelines (audited information)

The Executive Directors are required to build up a specified level of shareholding in the Company. This is to create greater alignment of the Directors' interests with those of shareholders, in line with the objectives of the Remuneration Policy. The guidelines have been updated for the 2017 Directors' Remuneration Policy and continue to require the Chief Executive to have a holding of 2.5 times salary while the other Executive Directors are now required to hold 2.0 times salary. Directors are expected to build this shareholding within five years of appointment to the relevant role. In addition to shares held, share awards under the DSA and Future Builder awards where the performance period has ended count towards the guideline (on a net of tax basis).

Both Mike Coupe and John Rogers have shareholdings that meet and significantly exceed the current shareholding guideline. Kevin O'Byrne was appointed to the Board in January 2017 and will be expected to build his shareholding during the course of his tenure.

### Shareholding guidelines



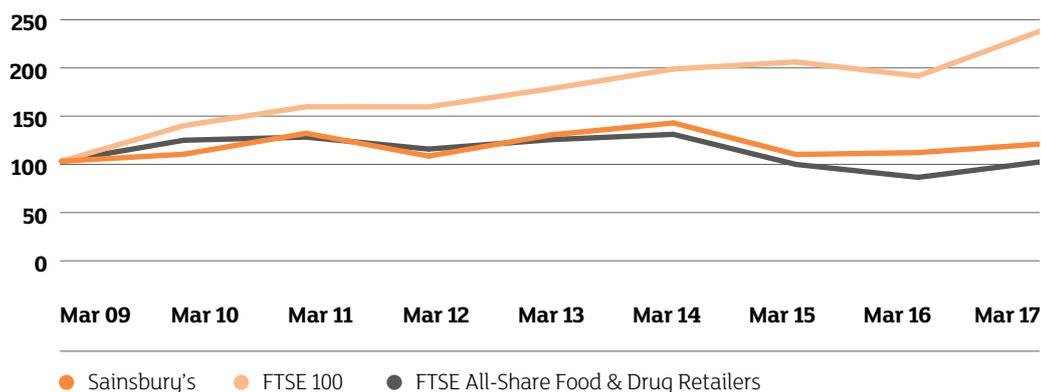
● Shareholding ● Share awards ○ Guidelines

Shareholding calculated using (i) salaries as at 11 March 2017, (ii) share total based on total of shareholding plus net of tax value (tax assumed to be 47 per cent) of share awards not subject to performance as at 11 March 2017 and (iii) the closing mid-market share price on 10 March 2017 of £2.664.

## Performance and CEO remuneration

The graph shows the TSR performance of an investment of £100 in J Sainsbury plc shares over the last eight years compared with an equivalent investment in the FTSE 100 Index. The FTSE 100 Index has been selected to provide an established and broad-based index. The graph also includes data for the FTSE All-Share Food & Drug Retailers Index. The Company is a constituent of both indices. The table details the total remuneration for the Chief Executive over this period.

### TSR performance since March 2009



|  | CEO                 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 | 2014/15 <sup>1</sup> | 2015/16 | 2016/17 |
|--|---------------------|---------|---------|---------|---------|---------|----------------------|---------|---------|
| Single figure remuneration £000            | M Coupe:<br>J King: | 4,441   | 4,380   | 3,471   | 4,366   | 3,906   | 1,507<br>405         | 2,802   | 2,349   |
| Bonus/DSA award as a percentage of maximum | M Coupe:<br>J King: | 92%     | 65%     | 61%     | 84%     | 73%     | 26%<br>0%            | 78%     | 35%     |
| LTIP vesting percentage of maximum         | M Coupe:<br>J King: | 80%     | 48%     | 43%     | 44%     | 40%     | 0%<br>0%             | 0%      | 22.5%   |

<sup>1</sup> Justin King's figures relate to the time he was Chief Executive during 2014/15. The figures for Mike Coupe relate to the whole of 2014/15; he was Chief Executive from 9 July 2014.

## All-employee share plans

The Company encourages share ownership and operates two all-employee share plans for colleagues, namely the Savings-Related Share Option Plan (Sharesave) and the All-Employee Share Ownership Plan, of which the Sainsbury's Share Purchase Plan (SSPP) is a part. Participation in Sharesave is conditional on three months' service. Executive Directors may participate in these plans in the same way as all other colleagues. Mike Coupe participates in Sharesave and John Rogers participates in SSPP. As these are all-employee plans there are no performance conditions. The Committee approves the adoption or amendment of these plans and awards to Executive Directors.

The 2011 Sharesave plan (five-year), with a £2.38 option price, and the 2013 Sharesave plan (three-year), with a £3.32 option price, came to an end on 1 March 2017 for over 11,500 colleagues. Colleagues could either take their savings or use the money to buy Sainsbury's shares at the option price. Using the market price on the date of the first exercise, the value of all the shares subject to the maturity was just over £19.3 million. The Company currently has over 32,500 colleagues participating in Sharesave with around 58,500 individual savings contracts.

## Percentage change in Chief Executive's remuneration

The table below shows how the percentage change in the Chief Executive's salary, benefits and bonus between 2015/16 and 2016/17 compares with the percentage change in the average of each of those components of pay for all our colleagues.

|                              | Salary<br>% change | Benefits<br>% change | Bonus<br>% change |
|------------------------------|--------------------|----------------------|-------------------|
| Chief Executive <sup>1</sup> | 1.5%               | 0%                   | n/a               |
| All colleagues <sup>2</sup>  | 4.0%               | 15.6%                | (37.9)%           |

<sup>1</sup> The bonus per cent change relates to the cash annual bonus and there was no payment in 2016/17.

<sup>2</sup> Figures relate to average based on number of full-time equivalent colleagues and the 2016/17 figures reflect the Home Retail Group plc acquisition.

## Dilution

The Company ensures that the level of shares granted under the Company's share plans and the means of satisfying such awards remains within best practice guidelines so that dilution from employee share awards does not exceed ten per cent of the Company's issued share capital for all-employee share plans and five per cent in respect of executive share plans in any ten-year rolling period. The Company monitors dilution levels on a regular basis and the Committee reviews these at least once a year. Up to 11 March 2017, an estimated 7.8 per cent of the Company's issued share capital has been allocated for the purposes of its all-employee share plans over a ten-year period, including an estimated 2.6 per cent over ten years in respect of its executive share plans. This is on the basis that all outstanding awards vest in full.

## Relative importance of spend on pay

The table below illustrates the year-on-year change in total colleague pay (being the aggregate staff costs as set out in note 28 to the financial statements) and distributions to shareholders (being declared dividends).

| Colleague pay |                            |          | Distribution to shareholders |               |          |
|---------------|----------------------------|----------|------------------------------|---------------|----------|
| 2015/16<br>£m | 2016/17 <sup>1</sup><br>£m | % change | 2015/16<br>£m                | 2016/17<br>£m | % change |
| 2,541         | 2,878                      | 13.3%    | 234                          | 232           | (0.9)%   |

<sup>1</sup> The 2016/17 figures reflect the Home Retail Group plc acquisition.

### Single total figure of remuneration for Non-Executive Directors (audited information)

The table below shows a single remuneration figure for all qualifying services for the 52 weeks to 11 March 2017 for each Non-Executive Director, together with comparative figures for the 52 weeks to 12 March 2016.

|                           | 2016/17                   |                               |               | 2015/16                   |                               |               |
|---------------------------|---------------------------|-------------------------------|---------------|---------------------------|-------------------------------|---------------|
|                           | Fees <sup>1</sup><br>£000 | Benefits <sup>2</sup><br>£000 | Total<br>£000 | Fees <sup>1</sup><br>£000 | Benefits <sup>2</sup><br>£000 | Total<br>£000 |
| David Tyler               | 500                       | 1                             | 501           | 495                       | 1                             | 496           |
| Matt Brittin              | 65                        | –                             | 65            | 64                        | –                             | 64            |
| Brian Cassin <sup>3</sup> | 62                        | 1                             | 63            | –                         | –                             | –             |
| Mary Harris               | 84                        | 3                             | 87            | 82                        | 4                             | 86            |
| David Keens <sup>4</sup>  | 84                        | 6                             | 90            | 68                        | –                             | 68            |
| John McAdam <sup>5</sup>  | 27                        | –                             | 27            | 82                        | –                             | 82            |
| Susan Rice                | 78                        | 15                            | 93            | 64                        | 14                            | 78            |
| Jean Tomlin               | 78                        | –                             | 78            | 76                        | 2                             | 78            |

1 Paid in relation to the year.

2 David Tyler received a non-cash benefit of private medical cover. The benefits for the other Non-Executive Directors relate to the reimbursement of travelling expenses to Board meetings held at the Company's registered office.

3 Brian Cassin was appointed to the Board on 1 April 2016.

4 David Keens was appointed to the Board on 29 April 2015.

5 John McAdam stepped down from the Board on 6 July 2016.

The Chairman receives an annual cash fee and benefits of private medical cover and a colleague discount card.

Non-Executive Directors receive a base annual cash fee; additional fees are paid to the Senior Independent Director and to the Chairmen of the Audit, Remuneration and Corporate Responsibility and Sustainability Committees. Non-Executive Directors receive no benefits other than a colleague discount card.

Details of the Board and Committee schedule of meetings and the number of meetings attended by the Directors are set out on page 61.

During the year, the Chairman and Non-Executive Directors' fees were reviewed, but no changes were made.

|  | Fees effective<br>from 27 September 2015 |
|--|--|
| Chairman fee   | £500,000                                 |
| Base fee   | £65,000                                  |
| Senior Independent Director fee (additional)                                       | £18,500                                  |
| Chairman of Remuneration Committee fee (additional)                                | £18,500                                  |
| Chairman of Audit Committee fee (additional)                                       | £18,500                                  |
| Chairman of Corporate Responsibility and Sustainability Committee fee (additional) | £13,000                                  |

The beneficial interest of the Non-Executive Directors, in post at the year-end, and their families in the shares of the Company are shown below.

|                           | Ordinary Shares <sup>1</sup> |               |            |
|---------------------------|------------------------------|---------------|------------|
|                           | 12 March 2016                | 11 March 2017 | 2 May 2017 |
| David Tyler               | 50,000                       | 75,000        | 75,000     |
| Matt Brittin              | 1,000                        | 14,090        | 14,090     |
| Brian Cassin <sup>2</sup> | –                            | 25,000        | 25,000     |
| Mary Harris               | 13,252                       | 27,446        | 27,446     |
| David Keens               | 100,000                      | 100,000       | 100,000    |
| Susan Rice                | 1,000                        | 4,000         | 4,000      |
| Jean Tomlin               | 1,315                        | 1,315         | 1,315      |

1 Ordinary shares are beneficial holdings which include the Directors' personal holdings and those of their spouses and minor children.

2 12 March 2016 figure relates to 1 April 2016 when Brian Cassin was appointed as a Director.

### Directors' appointment dates

|               |   |
|---------------|---|
| Mike Coupe    | 1 August 2007<br>(appointment as Chief Executive 9 July 2014) |
| John Rogers   | 19 July 2010  |
| Kevin O'Byrne | 9 January 2017  |
| David Tyler   | 1 October 2009 (Chairman from 1 November 2009)                |
| Matt Brittin  | 27 January 2011   |
| Brian Cassin  | 1 April 2016  |
| Mary Harris   | 1 August 2007   |
| David Keens   | 29 April 2015   |
| Susan Rice    | 1 June 2013   |
| Jean Tomlin   | 1 January 2013  |

### Governance – Remuneration Committee

#### Committee membership

The Remuneration Committee during the year comprised Mary Harris (Chairman), John McAdam (until 6 July 2016), Susan Rice and Jean Tomlin. All members of the Committee are independent Non-Executive Directors. Susan Rice will take over as Chairman at the AGM on 5 July 2017 having been a Committee member since September 2015.

#### Role and responsibilities of the Committee

The Committee complies with relevant regulations and considers the UK Corporate Governance Code and best practice when determining pay and policy. The specific responsibilities of the Committee include:

- Determining and agreeing with the Board the Remuneration Policy for the Chairman, Executive Directors and the Operating Board Directors;
- Setting individual remuneration arrangements for the Chairman, Executive Directors and Operating Board Directors;
- Reviewing and noting the remuneration trends across the Company;
- Approving the service agreements of each Executive Director, including termination arrangements; and
- Considering the achievement of the performance conditions under annual and long-term incentive/bonus arrangements.

The Committee's terms of reference are available on the Company's website [www.j-sainsbury.co.uk/investor-centre/corporate-governance](http://www.j-sainsbury.co.uk/investor-centre/corporate-governance).

Tim Fallowfield, Company Secretary, acts as secretary to the Committee. David Tyler, Mike Coupe, Angie Ritsley (Group HR Director), Sarah Desai (Head of Reward) and Ed Barker (Director of Group Finance) are invited to attend Committee meetings. The Committee considers their views when reviewing the remuneration of the Executive Directors and Operating Board Directors. Individuals who attend Remuneration Committee meetings are not present when their own remuneration is being determined.

The Committee typically meets four times each year, or more as required. The Committee has a calendar of standard items within its remit and in addition it held in-depth discussions on specific topics during the year. The key issues the Committee discussed during the year were remuneration arrangements in relation to changes on the Operating Board, the impact of the acquisition of Home Retail Group plc on incentives, a review of long-term incentive arrangements and the 2017 Directors' Remuneration Policy.

### Advisers to the Remuneration Committee

The Committee is authorised by the Board to appoint external advisers if it considers this beneficial. Over the course of the year, the Committee was supported by its appointed advisers, Deloitte LLP (Deloitte). Deloitte were reappointed by the Committee as advisers in 2013 following a competitive tender. During the year they provided advice to the Committee on a range of topics including remuneration trends, corporate governance, incentive plan design, incentive plan rules and the Remuneration Policy. Their consultants attended all of the Committee meetings. In relation to their advice, Deloitte received fees of circa £170,000 (fees are based on hours spent). During the year, Deloitte provided the Company with unrelated advice and consultancy regarding due diligence on the proposed acquisition of Home Retail Group plc, information technology, organisational structure, data analytics, taxation and matters relating to Sainsbury's Bank.

Deloitte are members of the Remuneration Consulting Group and, as such, operate under the Code of Conduct in relation to executive remuneration consulting in the UK. During the year, the Committee reviewed the advice provided by Deloitte and has confirmed that it has been objective and independent. The Committee has also determined that the Deloitte partner who provides remuneration advice to the Committee does not have any connections with the Company that may impact their independence. The Committee has reviewed the potential for conflicts of interest and judged that there were appropriate safeguards against such conflicts.

### Statement of voting at general meeting

The table below sets out the votes on the Annual Report on Remuneration at the 2016 AGM and the Directors' Remuneration Policy at the 2014 AGM. The Committee is keen to hear the views of all shareholders and continually reviews the Remuneration Policy and implementation.

|                                 | Votes for               | Votes against         | Votes abstained |
|---------------------------------|-------------------------|-----------------------|-----------------|
| Remuneration Report (2016 vote) | 98.77%<br>1,277 million | 1.23%<br>15.8 million | 36.0 million    |
| Remuneration Policy (2014 vote) | 99.15%<br>1,154 million | 0.85%<br>9.8 million  | 49.8 million    |

### Details of the Executive Directors' share awards and movements during the year (audited information)

The table below shows the conditional awards granted and exercised under each of the Company's share plans.

| Name                   | Award                                 | Date of grant           | Share price at date of award (pence) | Option price (pence) | Number of options held at 12 March 2016 | Number of options granted / dividend shares allocated during the year | Number of options released during the year | Number of options lapsed during the year | Date of exercise | Share price on exercise (pence) | Number of options exercised | Notional gain on exercise (£000) <sup>6</sup> | Number of options held at 11 March 2017 |
|------------------------|---------------------------------------|-------------------------|--------------------------------------|----------------------|---|---|--|--|------------------|---------------------------------|-----------------------------|---|---|
| Mike Coupe             | Long-Term Incentive Plan <sup>1</sup> | 16/05/2013              | 375                                  | Nil                  | 305,984                                 | –   | –  | 305,984                                  | –                | –                               | –                           | –   | –                                       |
|                        |                                       | 15/05/2014 <sup>4</sup> | 333                                  | Nil                  | 599,740                                 | –   | –  | –  | –                | –                               | –                           | –   | 599,740                                 |
|                        |                                       | 14/05/2015              | 269                                  | Nil                  | 828,880                                 | –   | –  | –  | –                | –                               | –                           | –   | 828,880                                 |
|                        |                                       | 12/05/2016              | 253                                  | Nil                  | –                                       | 876,936   | –  | –  | –                | –                               | –                           | –   | 876,936                                 |
|                        | Deferred Share Award <sup>2</sup>     | 15/05/2014              | 333                                  | Nil                  | 126,561                                 | 14,278  | 140,839                                    | –  | 05/05/2016       | 269                             | 140,839                     | 379   | –                                       |
|                        |                                       | 14/05/2015              | 269                                  | Nil                  | 165,907                                 | –   | –  | –  | –                | –                               | –                           | –   | 165,907                                 |
|                        |                                       | 12/05/2016              | 253                                  | Nil                  | –                                       | 304,121   | –  | –  | –                | –                               | –                           | –   | 304,121                                 |
| Sharesave <sup>3</sup> | 11/12/2013                            | 388                     | 332                                  | 4,518                | –                                       | –   | –  | –  | –                | –                               | –                           | 4,518   |   |
| <b>Total</b>           |                                       |                         |                                      | <b>2,031,590</b>     | <b>1,195,335</b>                        | <b>140,839</b>  | <b>305,984</b>                             |  |                  | <b>140,839</b>                  | <b>379</b>                  | <b>2,780,102</b>                              |   |
| John Rogers            | Long-Term Incentive Plan <sup>1</sup> | 19/05/2011              | 343                                  | Nil                  | 62,975                                  | –   | –  | –  | 05/05/2016       | 269                             | 62,975                      | 169   | –                                       |
|                        |                                       | 16/05/2013              | 375                                  | Nil                  | 271,056                                 | –   | –  | 271,056                                  | –                | –                               | –                           | –   | –                                       |
|                        |                                       | 15/05/2014              | 333                                  | Nil                  | 359,344                                 | –   | –  | –  | –                | –                               | –                           | –   | 359,344                                 |
|                        |                                       | 14/05/2015              | 269                                  | Nil                  | 442,068                                 | –   | –  | –  | –                | –                               | –                           | –   | 442,068                                 |
|                        | Deferred Share Award <sup>2</sup>     | 12/05/2016              | 253                                  | Nil                  | –                                       | 517,112   | –  | –  | –                | –                               | –                           | –   | 517,112                                 |
|                        |                                       | 15/05/2014              | 333                                  | Nil                  | 112,115                                 | 12,647  | 124,762                                    | –  | 05/05/2016       | 269                             | 124,762                     | 336   | –                                       |
|                        |                                       | 14/05/2015              | 269                                  | Nil                  | 101,665                                 | –   | –  | –  | –                | –                               | –                           | –   | 101,665                                 |
| Sharesave <sup>3</sup> | 09/12/2011                            | 297                     | 238                                  | 6,302                | –                                       | –   | –  | –  | –                | –                               | –                           | 6,302   |   |
| <b>Total</b>           |                                       |                         |                                      | <b>1,355,525</b>     | <b>713,169</b>                          | <b>124,762</b>  | <b>271,056</b>                             |  |                  | <b>187,737</b>                  | <b>505</b>                  | <b>1,609,901</b>                              |   |
| Kevin O'Byrne          | Long-Term Incentive Plan <sup>1</sup> | 26/01/2017 <sup>5</sup> | 261                                  | Nil                  | –                                       | 479,660   | –  | –  | –                | –                               | –                           | –   | 479,660                                 |
| <b>Total</b>           |                                       |                         |                                      |                      | <b>479,660</b>                          |   |  |  |                  |                                 |                             |   | <b>479,660</b>                          |

1 Details of the performance conditions applying to Future Builder awards are set out on pages 82 to 83. The LTIP share figures relate to the maximum that could be achieved.

2 See pages 80 to 81 for details of the Deferred Share Award, including performance conditions.

3 Sharesave is an all-employee share option plan and has no performance conditions as per HMRC Regulations.

4 Mike Coupe's 2014 Future Builder award was made in two parts on 15 May 2014 and 10 July 2014. The combined award is shown.

5 Details of Kevin O'Byrne's 2016 Future Builder are set out on page 84.

6 This is the notional gain on the date of exercise had all shares been sold.

## Directors' Remuneration Policy

The following section sets out our Directors' Remuneration Policy. This policy is subject to a binding shareholder vote at the AGM on 5 July 2017 and, if approved, will be effective from this date.

### Changes to the Remuneration Policy

Although the policy is being renewed, the key features remain unchanged from the policy previously approved by shareholders in 2014. As part of the review minor amendments have been made to reflect evolving market and best practice. These include:

- The introduction of a two-year holding period on Future Builder awards granted from 2017 onwards, which means future awards will normally be released five years after the grant date;
- Shareholding guidelines for Executive Directors, other than the CEO, are increased to 2.0 times salary, with the requirement for the CEO remaining at 2.5 times salary;
- Retirement benefits for any future appointment are reduced from 30 per cent to 25 per cent of salary; and
- Strengthened recovery provisions (malus and clawback).

### Policy Table for Executive Directors

The table below summarises each element of the policy for Executive Directors, with further details set out after the table.

| <b>Base salary</b>           |   |
|------------------------------|---|
| Purpose and link to strategy | Core element of remuneration used to attract and retain executives who can deliver our strategic objectives.  |
| Operation                    | Typically reviewed annually in March.<br>Consideration is given to a number of internal and external factors including business and individual performance, role, responsibilities, scope, market positioning, inflation and colleague pay increases.   |
| Opportunity                  | Salary increases (in percentage of salary terms) for Executive Directors will normally be within the range of those for the wider workforce. There is no maximum salary opportunity.<br>Where the Committee considers it necessary and appropriate, larger increases may be awarded in individual circumstances such as: <ul style="list-style-type: none"> <li>— A change in scope or responsibility;</li> <li>— If a new Executive Director is appointed at a lower rate and the salary is realigned over time as the individual gains experience in the role; or</li> <li>— Alignment to market level.</li> </ul> Salary levels effective for 2017/18: <ul style="list-style-type: none"> <li>— Mike Coupe – £943,428</li> <li>— John Rogers – £695,402</li> <li>— Kevin O'Byrne – £625,000</li> </ul> |
| Performance details          | None  |

| <b>Benefits</b>              |   |
|------------------------------|---|
| Purpose and link to strategy | Competitive benefits to assist in attracting and retaining executives.  |
| Operation                    | A range of benefits may be provided including, but not limited to, the provision of company car benefits (or cash equivalent), private medical cover, life assurance, long-term disability insurance, all-employee share plan participation and colleague discount.<br>The Committee keeps the benefits offered, the policies and the levels provided under regular review. |
| Opportunity                  | The value of benefits provided will be reasonable in the context of relevant market practice for comparable roles and taking into account any individual circumstances (e.g. relocation). There is no maximum monetary value.<br>Participation in any HMRC-approved all-employee share plan is limited to the maximum award levels permitted by the relevant legislation.   |
| Performance details          | None  |

| <b>Retirement benefits</b>   |  |
|------------------------------|--|
| Purpose and link to strategy | Provides an income following retirement and assists colleagues in building funds for their future.   |
| Operation                    | JS Self Invested Pension Plan (SIPP, a defined contribution plan) and/or a cash salary supplement.   |
| Opportunity                  | Maximum value of up to 30 per cent of salary per annum for existing Executive Directors, with a maximum value of up to 25 per cent of salary per annum for any new Executive Director appointments.<br>For new hires the nature and value of any pension provided will be, in the Committee's view, reasonable in the context of market practice for comparable roles and take account of both the individual's circumstances and the cost to the Company. |
| Performance details          | None   |

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**Annual bonus**

|                              |  |
|------------------------------|--|
| Purpose and link to strategy | Rewards performance on an annual basis against key financial and individual objectives.  |
| Operation                    | Performance measured over one year, bonus payable in cash after the year-end.<br>Bonus level determined by the Committee after the year-end based on performance against targets.<br>Measures and targets are reviewed annually.<br>Recovery provisions apply.   |
| Opportunity                  | Maximum opportunity of up to 125 per cent of salary per annum.<br>The level of threshold payment for performance varies depending on the performance measure, with payouts from zero per cent.<br>Full payout requires outperformance of stretch objectives. Maximum opportunity for 2017/18:<br>— Mike Coupe – 110 per cent of salary<br>— John Rogers – 90 per cent of salary<br>— Kevin O'Byrne – 90 per cent of salary |
| Performance details          | Based on a combination of financial (e.g. profit) and individual metrics.<br>A performance gateway must be achieved before any bonus payments can be made.<br>The detail of the measures, targets and weightings may be varied by the Committee year-on-year based on the Company's strategic goals. At least half of any award will be subject to financial measures.   |

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**Deferred Share Award (DSA)**

|                              |   |
|------------------------------|---|
| Purpose and link to strategy | Recognises and rewards for delivery of short-term strategic and financial objectives which contribute towards long-term sustainable growth.<br>Balance with annual bonus to ensure management remain mindful of long-term consequences of short-term actions.<br>Awards delivered in shares to provide further alignment with shareholders.   |
| Operation                    | Performance measured over one year, after which awards are made as conditional shares (or equivalent) deferred for two financial years.<br>After the year-end, performance is assessed in the round based on the Committee's judgement of performance achieved.<br>Measures and targets are reviewed annually in light of the strategic plan.<br>Dividends (or equivalents) may accrue on vested shares.<br>Recovery provisions apply.  |
| Opportunity                  | Maximum opportunity of up to 125 per cent of salary per annum.<br>No DSA grants are made unless threshold performance levels are reached, with full vesting requiring outperformance of stretch objectives.<br>Maximum opportunity for 2017/18:<br>— Mike Coupe – 110 per cent of salary<br>— John Rogers – 90 per cent of salary<br>— Kevin O'Byrne – 90 per cent of salary  |
| Performance details          | Basket of metrics covering four categories: financial performance, returns to shareholders, relative performance against peers and strategic goals.<br>A performance gateway must be achieved before any awards can be made.<br>The detail of the measures, targets and weightings may be varied by the Committee year-on-year based on the Company's strategic goals. At least half of any award will be based on the delivery of financial performance and returns to shareholders. |

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**Long-Term Incentive Plan (LTIP) – Future Builder**

|                              |  |
|------------------------------|--|
| Purpose and link to strategy | Recognises and rewards for delivery of Company performance and shareholder value over the longer term.<br>Share-based to provide greater alignment with shareholder interests.   |
| Operation                    | Awards of conditional share awards (or equivalent) with vesting dependent on performance measured over a period of at least three financial years.<br><br>Vested awards will normally be subject to a two-year holding period following the end of the performance period which means future awards will normally be released five years after the grant date.<br><br>The Committee reviews the metrics, targets and weightings prior to each grant to ensure that they remain appropriate.<br><br>Recovery provisions apply.<br><br>Dividends (or equivalents) may accrue on vested shares.   |
| Opportunity                  | Maximum award of up to 250 per cent of salary per annum in respect of any financial year.<br>Awards structured as core award (up to 62.5 per cent of salary per annum) with a performance multiplier of up to 4 times.<br>For achievements at threshold levels of performance, up to 25 per cent of maximum under each element may vest. Based on the current structure this is equivalent to a multiplier of 1 times the core award.<br>Award levels for 2017/18:<br>— Mike Coupe – core award of 62.5 per cent of salary<br>— John Rogers – core award of 50 per cent of salary<br>— Kevin O'Byrne – core award of 50 per cent of salary   |
| Performance details          | Based on a combination of financial and strategic measures appropriate within the context of the Company strategy and external environment over the relevant performance period.<br>A performance gateway must be achieved before any awards vest.<br>Prior to granting awards, the Committee will review the performance conditions and may opt to vary the metrics and weightings to ensure measures and targets remain aligned with its objectives. The Committee would seek to consult as appropriate with its major shareholders regarding any material changes.<br>Weightings for 2017/18 awards:<br>— ROCE – 20 per cent<br>— EPS – 20 per cent<br>— Cash flow – 20 per cent<br>— Cost savings – 20 per cent<br>— Synergies – 20 per cent |

**Shareholding guidelines**

|                              |  |
|------------------------------|--|
| Purpose and link to strategy | Alignment of Executive Directors with shareholders.  |
| Operation                    | Guidelines are Chief Executive 2.5 times salary, other Executive Directors 2.0 times salary.<br>Guideline expected to be met within five years of appointment. |

### Setting performance measures and targets

The Committee believes it is important that the performance conditions applying to incentive arrangements support the short and long-term corporate ambitions of the Company. We operate in a dynamic market with evolving challenges and the Committee reviews the performance measures and targets each year to ensure that they remain relevant and stretching. Further details of the performance measures are set out in the Annual Report on Remuneration.

The performance measures in the annual bonus and Deferred Share Award are selected as they are the key drivers of business performance. The targets for the annual bonus and DSA are set with reference to the corporate strategy and internal budgets as well as the external context (e.g. market forecasts). This approach seeks to ensure that the threshold and stretch targets are appropriately challenging.

The Future Builder performance measures focus on longer term growth and returns to shareholders, and a similar target-setting approach is used.

The Committee may vary or rebalance the weighting of the performance metrics for future annual bonus, DSA and Future Builder awards, in order to ensure that they remain aligned with the Company's strategic objectives. The Committee may also adjust the targets for awards or the calculation of performance measures and vesting outcomes for events not foreseen at the time the targets were set to ensure they remain a fair reflection of performance over the relevant period.

### Recovery provisions (malus and clawback) – preventing rewards for failure

The Remuneration Committee may operate recovery provisions (malus and clawback) on all incentive awards. The Committee may reduce or cancel an unvested award, or impose further conditions on an unvested award in the event of material mis-statement of financial results, serious reputational damage, serious misconduct or fraud.

In addition, in the circumstances outlined above, the Committee may clawback incentives, by requiring an Executive Director to make a repayment in relation to bonus payments and share awards. This provision would apply for up to two years following the end of the relevant performance period.

### Consideration of colleague pay and conditions

When considering remuneration arrangements for Executive Directors, the Committee takes into account, as a matter of course, the pay and conditions of colleagues throughout the Company.

In particular, the Committee receives regular updates of any major changes to the pay and benefits of colleagues generally and the Committee takes into account wider pay issues when determining Executive Directors' remuneration. When setting Executive Director salary increases the Committee considers the overall salary increase budget for management and the increase in rate of pay for hourly-paid colleagues, including the impact that implementing the National Living Wage has on colleague pay.

The Committee does not formally consult with colleagues on the setting of the policy but as a result of the Company's all-employee share plans, colleagues are able to become shareholders in the Company and can comment on the policy in the same way as other shareholders. Additionally, as mentioned in the Corporate Responsibility Report, we are looking at forums for our Non-Executive Directors and colleague representatives to discuss key business issues (including remuneration).

### Differences in Remuneration Policy for all colleagues

Many aspects of the Remuneration Policy for Executive Directors are consistent with the reward strategy for other colleagues across the Company. Below executive level, pay and benefits are scaled to reflect the nature of the role and based on the levels of pay in comparable roles in the market.

All colleagues, including colleagues at Sainsbury's Bank and Sainsbury's Argos, are entitled to base salary, benefits including pension and colleague discount. Eligible colleagues participate in our annual bonus plans which are aligned under a common set of principles with performance metrics tailored to different populations.

Senior executives expected to have the greatest influence on Company performance over time are eligible for participation in long-term incentive plans. All colleagues have the opportunity to become shareholders in the Company through our all-employee share plans.

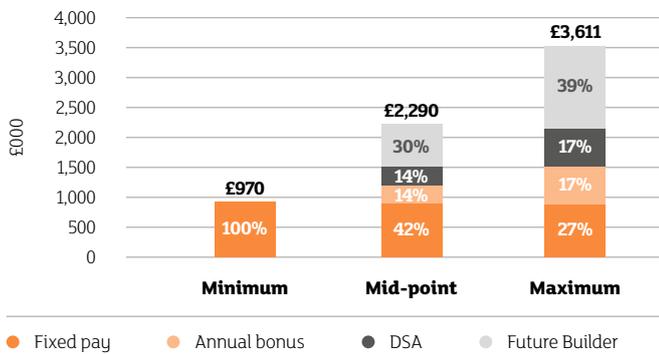
Participation in a pension plan is offered to all colleagues on a contributory basis, with the Company contribution varying by grade. Following auto-enrolment, we now have over 120,000 colleagues in our pension plans.

**Potential total remuneration opportunity under our pay policy**

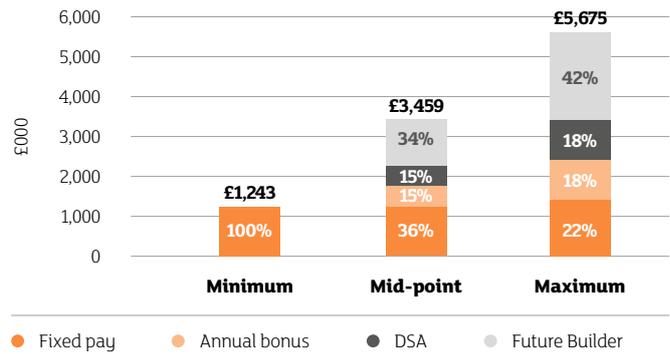
The Committee believes it is important that a significant portion of the package for Executive Directors is performance-related and delivered in shares to align their interests with shareholders. The balance between fixed pay (base salary, pension and benefits) and variable pay (annual bonus, Deferred Share Award and Future Builder) changes with performance. The variable proportion of total remuneration increases significantly for increased levels of performance. At least 60 per cent of the package is delivered through variable pay at mid-point performance and this proportion increases to at least three-quarters of the package at maximum levels of performance.

The charts show the total remuneration potential of the Executive Directors, in accordance with the Remuneration Policy, under three performance scenarios. In line with the regulations, the charts exclude the effect of share price movements.

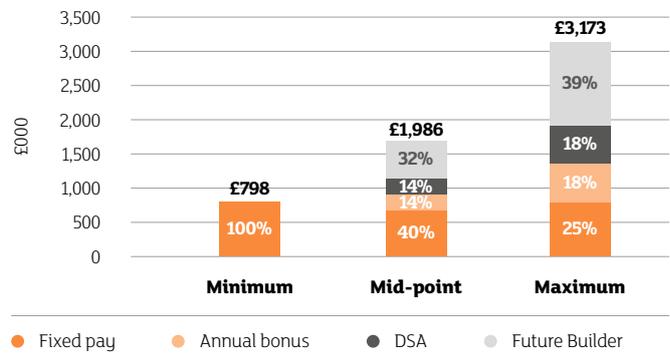
**John Rogers**



**Mike Coupe**



**Kevin O'Byrne**



|                             | Opportunity   | Minimum   | Mid-point          | Maximum            |
|-----------------------------|---|---|--------------------|--------------------|
| <b>Fixed pay</b>            |   | Salary – Mike Coupe £943,428; John Rogers £695,402; Kevin O'Byrne £625,000<br>Benefits – value in line with 2016/17<br>Pension – CEO 30% of salary; other Executive Directors 25% of salary |                    |                    |
| <b>Annual bonus</b>         | CEO – 110% of salary<br>Other Executive Directors – 90% of salary                           | Nil   | 50% of maximum     | 100% of maximum    |
| <b>Deferred Share Award</b> | CEO – 110% of salary<br>Other Executive Directors – 90% of salary                           | Nil   | 50% of maximum     | 100% of maximum    |
| <b>Future Builder</b>       | CEO – core award of 62.5% of salary<br>Other Executive Directors – core award 50% of salary | Nil   | Multiplier of 2.0x | Multiplier of 4.0x |

**Our approach to recruitment**

The Committee believes it is vital to be able to attract and recruit leaders of the calibre required to deliver our strategic objectives, while remaining mindful of the cost to the Company. When determining remuneration arrangements for new appointments, the Committee intends to pay no more than it believes is necessary to secure the required talent. The Committee will seek to align the remuneration package with the approved Remuneration Policy.

|                     |  |
|---------------------|--|
| <b>Fixed pay</b>    | Salary and benefits (including retirement benefits) would be determined in accordance with the Policy Table above. An alternative package may also be necessary where an individual fulfils an executive role on an interim basis.<br><br>In certain cases, the initial salary for a new appointment may be set at a lower level, with the intention of increasing the salary over time as the executive gains experience in the role.<br><br>Benefits may need to be tailored based on the individual circumstances (e.g. relocation, housing or travel allowances may be required).  |
| <b>Variable pay</b> | The maximum variable remuneration which may be offered to an executive will be no more than 500 per cent of salary (excluding any buy-out arrangements). This limit is consistent with the overall maximum set out in the Policy Table.<br><br>Within these limits and where appropriate the Committee may tailor the award (e.g. timeframe, form, performance criteria) based on the commercial circumstances.<br><br>Shareholders will be informed of the terms for any such arrangements.   |
| <b>Buy-outs</b>     | The Committee may need to buy-out remuneration terms forfeited on joining the Company. In such circumstances, the Committee will seek to ensure any buy-out is of comparable commercial value and capped as appropriate.<br><br>The quantum, form and structure of any buy-out arrangement will be determined by the Committee taking into account the terms of the previous arrangement being forfeited (e.g. form and structure of award, timeframe, performance criteria, likelihood of vesting, etc.). The buy-out may be structured as an award of cash or shares. However, the Committee will normally have a preference for replacement awards to be made in the form of shares and to be within the Company's existing incentive plans.<br><br>Where an executive is appointed from either within the Company or following corporate activity/reorganisation (e.g. acquisition of another company), the normal policy would be to honour any legacy arrangements in line with the original terms and conditions. |

On the appointment of a new Non-Executive Chairman or Non-Executive Director, the terms and fees will normally be consistent with the fee policy outlined later in the Directors' Remuneration Policy.

### Service contracts and policy for departing Executive Directors

The Company's policy is for Executive Directors' service contracts to be terminable on 12 months' notice by either party.

Contracts contain non-compete and non-solicit clauses with key suppliers and colleagues. The Company's normal practice is that Executive Directors may take up one non-executive role outside the Company, with approval from the Board, subject to the role being in a business that does not compete with the Company and with consideration of the time commitment. Directors are normally entitled to retain the fees earned from such appointments.

In the event of early termination without notice, any severance payment would be limited to one-year's salary and benefits (including pension), normally payable on a phased basis and subject to mitigation. Benefits payable may include certain one-off benefits in connection with termination such as legal costs and the costs of meeting any settlement agreement. There are no specific terms relating to a change of control.

The Executive Directors' service contracts are available for shareholders to view at the Company's registered office.

The Committee retains discretion to determine the exact termination terms of any Executive Director, having regard to all the relevant facts and circumstances available to them at the time. The table below sets out the general position and range of approaches in respect of incentive arrangements. In accordance with the terms of the relevant incentive plan rules, based on the circumstances of any departure the Committee has discretion to determine how an Executive Director should be categorised for each element and determine vesting levels accordingly based on the range shown below.

### Detailed provisions

Deferred Share Awards and Future Builder awards are subject to the terms of the relevant plan rules under which the award has been granted. It is expected that future awards would normally be granted under the LTIP rules approved by shareholders at the 2016 AGM. The Committee may adjust

or amend awards only in accordance with the provisions of the relevant plan rules. This includes making adjustments to awards to reflect one-off corporate events, such as a change in the Company's capital structure. In accordance with the plan rules, awards may be settled in cash rather than shares, where the Committee considers this appropriate.

On a change of control, Deferred Share Awards would be released or vest in full. Future Builder awards may vest taking account of relevant factors including progress against relevant performance conditions and may be pro-rated based on time.

In the event of a demerger or other significant distribution, Deferred Share Awards or Future Builder awards may be allowed to vest wholly or in part. A winding up, administration or a voluntary arrangement event would result in Deferred Share Awards being released or vesting in full and Future Builder awards would normally vest subject to achievement of the relevant performance conditions on the same time pro-rated basis as above.

In similar corporate events, awards under HMRC approved all-employee plans would vest in accordance with the standard approved terms.

The Committee may approve payments to satisfy commitments agreed prior to the implementation of this policy where such commitment was either; (i) made prior to the implementation of the 2014 Remuneration Policy; or (ii) agreed during the term of, and was consistent with, the 2014 Remuneration Policy. This includes previous incentive awards that are currently outstanding and unvested (e.g. prior year Deferred Share Awards). The structure of these legacy awards are generally consistent with the Policy Table but the performance conditions applying may be different. Further details of outstanding awards are set out in the Annual Report on Remuneration.

The Committee may also approve payments outside of this policy, in order to satisfy any legacy arrangements made to a colleague prior to (and not in contemplation of) promotion to the Board of Directors.

The Committee may make minor amendments to the Remuneration Policy to aid its operation or implementation without seeking shareholder approvals (e.g. for regulatory, exchange control, tax or administrative purposes or to take account of a change in legislation) provided that any such change is not to the material advantage of colleagues.

|   | 'Bad leaver'<br>(e.g. termination for cause, etc.)  | 'Good leaver'<br>(e.g. cessation due to ill-health, injury, etc.)  |
|---|---|--|
| Annual bonus                                      | No entitlement following date notice served.  | Bonus may be payable subject to performance. Awards normally pro-rated based on the period worked during the financial year, with payments usually occurring following the year-end.   |
| Deferred Share Award                              | No entitlement to current year's award following date notice served.<br>Unvested awards will lapse on notice. | Participants may be considered for an award, but normally must be employed and not under notice to receive current year's award.<br>Outstanding unvested awards normally do not lapse. Awards may be pro-rated for the proportion of the deferral period elapsed on cessation, unless the Committee determines otherwise. Awards may vest following cessation or at another date.<br>On death, unvested awards will be released and vest in full.  |
| Long-Term Incentive Plan<br>(i.e. Future Builder) | Unvested awards will lapse on notice.   | Unvested awards normally vest at the normal time subject to performance. Awards will normally be pro-rated by reference to the proportion of the performance period that has elapsed since cessation, unless the Committee determines otherwise.<br>On death, awards vest early on cessation with performance measured at this time. Awards are pro-rated by reference to the proportion of the performance period that has elapsed since cessation.<br>If the Director leaves in the first six months after the start of the performance period, the award normally lapses in full. |
| All-employee share plans                          | In line with HMRC rules.  |  |

### Remuneration Policy for the Non-Executive Chairman and Non-Executive Directors

The remuneration of the Non-Executive Chairman is determined by the Remuneration Committee and the remuneration of the Non-Executive Directors by the Non-Executive Chairman and Executive Directors. The Non-Executive Chairman and Non-Executive Directors receive fees and are eligible for certain benefits. Non-Executive roles are not entitled to any performance-related pay or pension.

The Non-Executive Chairman and Non-Executive Directors do not have service contracts. The Company's policy is to appoint the Non-Executive Chairman and Non-Executive Directors for an initial three-year period, which may be extended for a further term by mutual consent. The initial appointments and any subsequent reappointments are subject to annual election or re-election by shareholders.

Non-Executive Directors' appointments may be terminated at any time by serving three months' written notice by either party; six months' in the case of the Non-Executive Chairman. The Non-Executive Directors' letters of appointment are available for shareholders to view at the Company's registered office.

#### Non-Executive Director Remuneration Policy

|                                  |  |
|----------------------------------|--|
| Approach to setting remuneration | <p>The fees for Non-Executive Directors are set at a level which is considered appropriate to attract individuals with the necessary experience and ability to oversee the business. Fees may be paid in cash or shares.</p> <p>Typically reviewed annually in September.</p> <p>Judgement is used but consideration is given to a number of internal and external factors including responsibilities, market positioning, inflation and colleague pay increases.</p> <p>Where appropriate benefits may be provided such as private medical cover, annual medical assessment and colleague discount.</p> <p>Travel and other reasonable expenses (including any associated taxes) incurred in the course of performing their duties are reimbursed to Non-Executive Directors.</p> |
| Opportunity                      | <p>Fee opportunity reflects responsibility and time commitment.</p> <p>Additional fees are paid for further responsibilities such as chairing committees.</p> <p>The value of benefits provided will be reasonable in the market context and take account of the individual circumstances and benefits provided in comparable roles.</p> <p>Fee levels as at 12 March 2017:</p> <ul style="list-style-type: none"> <li>— Non-Executive Chairman – £500,000 per annum</li> <li>— Basic fee – £65,000 per annum</li> <li>— Senior Independent Director, Chair of Remuneration and Audit Committees additional fee – £18,500 per annum</li> <li>— Chairman of Corporate Responsibility and Sustainability Committee additional fee – £13,000 per annum</li> </ul>                     |

#### Consideration of shareholder views

The Remuneration Committee values the views of the Company's shareholders and guidance from shareholder representative bodies. The Committee proactively consults extensively with our major shareholders to ensure that their views are represented in discussions on remuneration matters. As part of the process for approaching the renewal of the policy, the Committee consulted with major shareholders on a range of topics including potential alternative incentive structures. The renewed policy reflects guidance received from major investors during the course of the engagement process.

The Directors' Remuneration Policy will be put to a binding vote and the Annual Report on Remuneration will be put to an advisory vote at the AGM on 5 July 2017. The Directors confirm that this report has been prepared in accordance with the Companies Act 2006 and reflects the provisions of the Large and Medium-sized Companies and Groups (Accounts & Reports) (Amendment) Regulations 2013.

Approved by the Board on 2 May 2017.



**Mary Harris**  
Chairman, Remuneration Committee

## Additional statutory information

### Dividends

Details on the payment of the final dividend can be found on page 51.

### Share capital and control

Except as described below in relation to the Company's employee share schemes, there are no restrictions on the voting rights attaching to the Company's ordinary shares or the transfer of securities in the Company; no person holds securities in the Company carrying special rights with regard to control of the Company; and the Company is not aware of any agreements between holders of securities that may result in restrictions in the transfer of securities or voting rights. Further details of the rights, restrictions and obligations attaching to the share capital of the Company, including voting rights, are contained in the Company's Articles of Association. The Articles of Association may only be changed with the agreement of shareholders.

Shares acquired through the Company's employee share plans rank *pari passu* with shares in issue and have no special rights. Where, under the Company's All Employee Share Ownership Plan, participants are beneficial owners of the shares but the Trustee is the registered owner, the voting rights are normally exercised by the registered owner at the direction of the participants. The J Sainsbury Employee Benefit Trusts and Home Retail Employee Share Trust waive their right to vote and to dividends on the shares they hold which are unallocated. Total dividends waived by the Trustees during the financial year amounted to £497,762. Some of the Company's employee share plans include restrictions on transfer of shares while the shares are held within the plan.

At the AGM held in July 2016, the Company was authorised by shareholders to purchase its own shares, within certain limits and as permitted by the Articles of Association. The Company made no purchases of its own shares during the year and no shares were acquired by forfeiture or surrender or made subject to a lien or charge.

All of the Company's employee share plans contain provisions relating to a change of control. On a change of control, options and awards granted to employees under the Company's share plans may vest and become exercisable, subject to the satisfaction of any applicable performance conditions at that time.

Certain of the Company's credit facilities and banking arrangements contain change of control clauses under which lenders may cancel their commitments and declare all outstanding amounts immediately due and payable. There are no other significant agreements that would take effect, alter or terminate upon a change of control following a takeover bid.

### Ordinary shares

Details of the changes to the ordinary issued share capital during the year are shown in note 19 of the Notes to the Financial Statements including shares allotted as a result of the HRG acquisition. At the date of this report, 2,188,900,863 ordinary shares of 28<sup>1</sup>/<sub>2</sub> pence have been issued, are fully paid up and are listed on the London Stock Exchange.

### Major interests in shares

As at 2 May 2017, the Company had been notified by the following investors of their interests in three per cent or more of the Company's shares. These interests were notified to the Company pursuant to DTR5 of the Disclosure Guidance and Transparency Rules:

|                    | Number of Ordinary Shares | % of voting rights |
|--------------------|---------------------------|--------------------|
| Qatar Holdings LLC | 481,746,132               | 22.01              |
| Deutsche Bank AG   | 109,650,100               | 5.01               |

### Directors' interests

The beneficial interests of the Directors and their families in the shares of the Company are shown in the Directors' Remuneration Report on pages 84 and 86.

During the year, no Director had any material interest in any contract of significance to the Group's business.

### Directors' indemnities

The Directors are entitled to be indemnified by the Company to the extent permitted by law and the Company's Articles of Association in respect of all losses arising out of or in connection with the execution of their powers, duties and responsibilities. The Company has executed deeds of indemnity for the benefit of each Director in respect of liabilities which may attach to them in their capacity as a Director of the Company. The Company purchased and maintained Directors' and Officers' liability insurance throughout 2016/17, which has been renewed for 2017/18. Neither the indemnities nor the insurance provide cover in the event that the Director is proved to have acted fraudulently.

### Employment

#### Employment policies

The Company values the different perspectives and experiences of all our colleagues. We are proud of our diverse workforce because every colleague's unique viewpoint helps us to innovate and to understand and embrace different customers' needs and wants. We are committed to providing equal opportunities for all colleagues and applicants, including during recruitment and selection, training and development, and promotion.

A Great Place to Work strategy is in place, underpinned by well-developed policies for the fair and equal treatment of all colleagues. Training is provided which ensures that policies are understood throughout the organisation. We have a workplace adjustments process in place for our colleagues who are living with a disability or long-term health condition which operates through the Government's Access to Work scheme. Workplace adjustments can be made at any point during a colleague's employment with us. See page 39 for further information on our diversity strategy.

### Colleague engagement

We deliver regular colleague communications which build trust in our corporate strategy, vision and values, enable our colleagues to do a good job, and provide information which matters to colleagues about their pay, benefits and career opportunities. We are committed to delivering news and information to our colleagues in a clear and timely way, and communicating change sensitively.

Colleagues receive information from their managers, as well as a range of internal communications including films and magazines and have access to a colleague intranet, and Yammer, our social platform. In addition, as we have detailed in the Great Place to Work section of this report on page 38, there are a number of ways for colleagues to have their say, from our colleague idea scheme, Message Mike, to Talking Shop when colleagues have an opportunity to meet members of our Operating Board and ask questions.

All colleagues receive a letter from our Chief Executive Officer every time we announce our results detailing our Company performance, and how our colleagues have played their part. Through our communication channels and messages from the Chief Executive Officer we have also set out Company milestones, explaining how every colleague can help to achieve them, and we celebrate our success when we reach them by rewarding colleagues with an increase in colleague discount.

### Human rights and modern slavery

The Company does not have a specific human rights policy but fairness and integrity are an important part of the responsible way we run our business, as shown by the values and policies described above and throughout this report. In addition, our customers want to be confident that the people who make and sell our products are not being exploited, or exposed to unsafe working conditions. Our commitment to sourcing with integrity is reflected in long-standing policies, processes and partnerships on ethical trade which seek to protect the rights of the people working in our supply chains. We are founding members of the Ethical Trading Initiative (ETI) and work closely with our suppliers, government agencies, non-profit organisations, unions and others to ensure that our standards are maintained.

This year sees the publication of our first statement in accordance with clause 54 of the Modern Slavery Act, 2015. It marks a development of our approach that sees us align across our entire business and supply chain, incorporating our own operations, from facilities management and logistics to Sainsbury's Bank and Sainsbury's Argos. In addition to maintaining our existing activities, we have taken a number of steps over this financial year to solidify our governance structure, processes and awareness-raising activities on the topic that will help us better identify and address worker exploitation. These include updates to our commercial terms and policies, enhancing our training, and a leading role in industry partnerships to develop a common standard for worker accommodation and a new certification scheme for labour providers.

We have been developing our updated risk-based approach in response to the growing intelligence on where slavery and trafficking risk exists across our industry. We are using enhanced data analytics capability and human rights expertise to create a next-generation diagnostic risk assessment tool that can be applied across the many and different areas of our business. We are confident that it will help us to implement an effective strategy and set of prevention and remediation activities, that are appropriate for each area of our business.

### Greenhouse gas emissions

In line with the GHG Protocol Corporate Accounting and Reporting Standard (revised edition), we have recalculated our Group base year due to the acquisition, within this reporting year, of HRG which includes Argos and Habitat.

This year we have disclosed the emissions performance of the combined Sainsbury's Group, Sainsbury's, Argos and Habitat. We have in addition, aligned scope and boundaries with legacy Sainsbury's reporting. All of the following figures are therefore reflective of these changes.

Sainsbury's has measured its greenhouse gas (GHG) footprint since 2005 and set a challenging target to reduce absolute emissions by 30 per cent by 2020, compared to our baseline (and 65 per cent relative to sales floor area).

Argos and Habitat have also set a target to reduce emissions by 40 per cent relative to sales floor area by 2020.

#### Location-based emissions

Versus 2005/06, in 2016/17 our:

- Sainsbury's Group emissions reduced by 11.9 per cent absolute and 41 per cent relative;
- Sainsbury's emissions reduced by 11.4 per cent absolute and 42.5 per cent relative; and
- Argos and Habitat emissions reduced by 15.9 per cent absolute and 26.5 per cent relative.

#### Sainsbury's Group

|  | GHG Emissions (tCO <sub>2</sub> e) |                  |                  |
|--|------------------------------------|------------------|------------------|
|  | 2005/06                            | 2015/16          | 2016/17          |
| <b>Total (tCO<sub>2</sub>e)</b>                          | <b>1,554,492</b>                   | <b>1,475,251</b> | <b>1,369,573</b> |
| Intensity measurement<br>(tCO <sub>2</sub> e/'000 sq ft) | 89.77                              | 57.37            | 53.00            |

#### Sainsbury's

| Emission source  | GHG Emissions (tCO <sub>2</sub> e) |                  |                  |
|--|------------------------------------|------------------|------------------|
|  | 2005/06                            | 2015/16          | 2016/17          |
| Combustion of fuel & operation of facilities (Scope 1)               | 536,694                            | 601,091          | 579,864          |
| Electricity, heat, steam and cooling purchased for own use (Scope 2) | 833,787                            | 722,512          | 634,960          |
| <b>Total (tCO<sub>2</sub>e)</b>                                      | <b>1,370,481</b>                   | <b>1,323,603</b> | <b>1,214,824</b> |
| Intensity measurement<br>(tCO <sub>2</sub> e/'000 sq ft)             | 90.37                              | 57.05            | 51.96            |

#### Argos and Habitat

| Emission source  | GHG Emissions (tCO <sub>2</sub> e) |                |                |
|--|------------------------------------|----------------|----------------|
|  | 2005/06                            | 2015/16        | 2016/17        |
| Combustion of fuel & operation of facilities (Scope 1)               | 101,563                            | 71,847         | 84,363         |
| Electricity, heat, steam and cooling purchased for own use (Scope 2) | 82,448                             | 79,801         | 70,386         |
| <b>Total (tCO<sub>2</sub>e)</b>                                      | <b>184,011</b>                     | <b>151,648</b> | <b>154,749</b> |
| Intensity measurement<br>(tCO <sub>2</sub> e/'000 sq ft)             | 85.55                              | 60.35          | 62.91          |

### Market-based emissions

The market-based emissions method reflects the emissions from the electricity that a company is using, which may be different from emissions for the electricity that is generated as a UK average. For example, different electricity suppliers emit more or less greenhouse gases depending on the energy source or technology, and companies who have invested in their own renewable or low carbon energy generation by this method can show the actual emissions level for the energy used.

Versus 2005/06, in 2016/17 our market based:

- Sainsbury's Group emissions reduced by 21.5 per cent absolute and 47.4 per cent relative;
- Sainsbury's emissions reduced by 22.2 per cent absolute and 49.6 per cent relative; and,
- Argos and Habitat emissions reduced by 16.3 per cent absolute and 26.8 per cent relative.

#### Sainsbury's Group

|  | GHG Emissions (tCO <sub>2</sub> e) |                  |                  |
|--|------------------------------------|------------------|------------------|
|  | 2005/06                            | 2015/16          | 2016/17          |
| <b>Total (tCO<sub>2</sub>e)</b>                          | <b>1,554,492</b>                   | <b>1,208,359</b> | <b>1,219,903</b> |
| Intensity measurement<br>(tCO <sub>2</sub> e/'000 sq ft) | 89.80                              | 46.99            | 47.21            |

#### Sainsbury's

| Emission source  | GHG Emissions (tCO <sub>2</sub> e) |                  |                  |
|--|------------------------------------|------------------|------------------|
|  | 2005/06                            | 2015/16          | 2016/17          |
| Combustion of fuel & operation of facilities (Scope 1)               | 536,694                            | 589,728          | 563,520          |
| Electricity, heat, steam and cooling purchased for own use (Scope 2) | 833,787                            | 541,102          | 502,298          |
| <b>Total (tCO<sub>2</sub>e)</b>                                      | <b>1,370,481</b>                   | <b>1,130,830</b> | <b>1,065,818</b> |
| Intensity measurement<br>(tCO <sub>2</sub> e/'000 sq ft)             | 90.37                              | 48.74            | 45.58            |

#### Argos and Habitat

| Emission source  | GHG Emissions (tCO <sub>2</sub> e) |               |                |
|--|------------------------------------|---------------|----------------|
|  | 2005/06                            | 2015/16       | 2016/17        |
| Combustion of fuel & operation of facilities (Scope 1)               | 101,563                            | 71,847        | 84,363         |
| Electricity, heat, steam and cooling purchased for own use (Scope 2) | 82,448                             | 5,682         | 69,722         |
| <b>Total (tCO<sub>2</sub>e)</b>                                      | <b>184,011</b>                     | <b>77,529</b> | <b>154,085</b> |
| Intensity measurement<br>(tCO <sub>2</sub> e/'000 sq ft)             | 85.55                              | 30.85         | 62.64          |

### Dual emissions reporting

Overall emissions have been presented to reflect both location and market based methodologies, affecting both Scope 1 and Scope 2 emissions.

Scope 1: 16 per cent of total natural gas usage is covered by Green Gas Certification (100 per cent Renewable Gas Guarantee of Origin Contract); therefore 16 per cent of natural gas emissions have been reported at zero emissions. All other Scope 1 market-based emissions have been calculated using UK Government's GHG Conversion Factors for Company Reporting 2016 for all sources.

Scope 2: 20 per cent of UK electricity is covered by a PPA, which meets all of the required quality criteria; therefore 20 per cent of UK electricity emissions have been reported at zero emissions. Remaining UK electricity has been reported at supplier-specific emissions rate. Non-UK electricity has been reported at local grid average.

### Electricity use

As a result of our ongoing investment in energy reduction initiatives:

- Sainsbury's Group absolute UK electricity consumption decreased year-on-year by 1.5 per cent and 11 per cent versus 2005/06 whilst adding 49.2 per cent more sales area;
- Sainsbury's absolute UK electricity consumption has decreased year-on-year by 1.4 per cent and 11.6 per cent versus 2005/06 whilst adding 54.2 per cent more sales area; and
- Argos and Habitat absolute UK electricity consumption decreased year-on-year by 1.5 per cent and 4.9 per cent versus 2005/06 whilst adding 14.4 per cent more space.

### Methodology

We have reported on all of the emission sources required under the Companies Act 2006 (Strategic Report and Directors' Reports) Regulations 2013. We have calculated and reported our emissions in line with the GHG Protocol Corporate Accounting and Reporting Standard (revised edition) and emission factors from UK Government's GHG Conversion Factors for Company Reporting 2016, and IEA 2014 for those overseas. The reporting period is the financial year 2016/17, the same as that covered by the Annual Report and Financial Statements. The boundaries of the GHG inventory are defined using the operational control approach. In general, the emissions reported are the same as those which would be reported based on a financial control boundary.

### Political donations

The Company made no political donations in 2016/17 (2015/16: £nil).

### Essential contracts

Sainsbury's has contractual and other arrangements with numerous third parties in support of its business activities. None of the arrangements is individually considered to be essential to the business of Sainsbury's.

### Taxation

The Company complies with relevant tax laws, regulations and obligations regarding the filing of tax returns, payment and collection of tax. Sainsbury's policy is not to undertake any tax planning schemes that seek to use so-called 'tax havens' for aggressive tax planning and for the purpose of tax avoidance.

The Group aims to develop an open, honest relationship with the tax authorities and involve them at an early stage should any complex tax issues arise. The taxation policy is reviewed annually by the Board. Tax is a key item on the Audit Committee agenda and is discussed quarterly where large or complex tax items will feature, together with compliance and key risk management updates.

All of Sainsbury's and Argos stores are based in the UK (with the exception of some Argos stores in the Republic of Ireland), as such, substantially all (more than 99 per cent) of our Group sales are generated and taxed in the UK.

### Branches

Details of branches of Group subsidiaries can be found in note 37 of the Notes to the Financial Statements.

### Post balance sheet events

There were no post balance sheet events.

### Financial risk management

The financial risk management and policies of the Group are disclosed in note 23 of the Notes to the Financial Statements.

### Ethical policies

The Company takes bribery extremely seriously and is committed to ensuring compliance with laws and regulations. Colleagues are expected to abide by a set of clearly communicated formal policies, such as the Ethical Supplier Policy and the Conflicts of Interest/Relationships at Work Policy. Training in support of these policies is provided to colleagues especially in the commercial divisions, firstly during their induction into the Company and thereafter through annual refreshers.

### Disclosure of information to the auditor

Each of the Directors has confirmed that, so far as he/she is aware, there is no relevant audit information of which the auditor is unaware. Each Director has taken all steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information.

### Directors' Report

The Directors' Report comprises pages 01 to 73, 95 to 98 and 100 of this Annual Report and Financial Statements. The following information is also incorporated into the Directors' Report:

| Information requirement                        | Location within Annual Report       |
|--|-------------------------------------|
| Interest capitalised                           | See note 10                         |
| Publication of unaudited financial information | Leverage ratio, see note 23         |
| Details of any long-term incentive schemes     | See Remuneration Report and note 30 |
| Shareholder waiver of dividends                | See note 22                         |
| Shareholder waiver of future dividends         | See note 22                         |

Other information requirements set out in LR 9.8.4R are not applicable to the Company.

By order of the Board

**Tim Fallowfield**

**Company Secretary and Corporate Services Director**

2 May 2017

# Financial Statements

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## Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and Financial Statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Group and the Company as at the end of the financial year, and of the profit or loss of the Group for the financial year. Under that law, the Directors have prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and have elected to prepare the Parent Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice, including FRS 101 'Reduced Disclosure Framework' (UK Accounting Standards and applicable law). 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 the Company and of the profit or loss of the Group for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether IFRSs as adopted by the European Union and applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Group and Company financial statements respectively; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's and the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Having taken all the matters considered by the Board and brought to the attention of the Board during the year into account, we are satisfied that the Annual Report and Financial Statements, taken as a whole, is fair, balanced and understandable.

The Board believes that the disclosures set in this Annual Report provide the information necessary for shareholders to assess the Group's performance, business model and strategy.

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the Directors, whose names and functions are listed on pages 54 to 55, confirms that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- the Strategic Report and Directors' Report contained in the Annual Report and Financial Statements include a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

By order of the Board

**Tim Fallowfield**  
**Company Secretary and Corporate Services Director**  
 2 May 2017

# Independent auditors' report to the members of J Sainsbury plc

## Our opinion on the financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent company's affairs as at 11 March 2017 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including FRS 101 "Reduced Disclosure Framework"; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

## What we have audited

J Sainsbury plc's financial statements for the 52 weeks ended 11 March 2017 comprise:

| Group   | Parent company                                    |
|---|---|
| Consolidated income statement                     | Balance sheet                                     |
| Group statement of comprehensive income           | Statement of changes in equity                    |
| Group balance sheet                               | Related notes 1 to 12 to the financial statements |
| Group cash flow statement                         |   |
| Group statement of changes in equity              |   |
| Related notes 1 to 37 to the financial statements |   |

The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 "Reduced Disclosure Framework".

## Overview of our audit approach

### Risks of material misstatement

- Supplier arrangements
- Aspects of revenue recognition
- HRG acquisition purchase price allocation
- Financial Services customer receivables impairment
- IT environment

### Audit scope

- We performed a full scope audit of the complete financial information of the following components: J Sainsbury plc, Sainsbury's and Argos trading entities and Sainsbury's Bank. We performed audit procedures on specific balances including for the property companies, joint ventures and the insurance company due to the size and risk of certain individual balances within these components.
- The components where we performed full or specific audit procedures accounted for 92 per cent of profit before tax before items noted below, 99 per cent of revenue and 96 per cent of total assets.

### Materiality

- Overall Group materiality is £34 million which represents 5.1 per cent of profit before tax before items noted below.

## Our assessment of risk of material misstatement

We identified the risks of material misstatement described below as those that had the greatest effect on our overall audit strategy, the allocation of resources in the audit and the direction of the efforts of the audit team. In addressing these risks, we have performed the procedures below which were designed in the context of the financial statements as a whole and, consequently, we do not express any opinion on these individual areas.

### Changes from the prior year

The Group acquired Home Retail Group plc in the year and we have reflected this in our risk assessment, the results of which are below.

We have identified similar risks of material misstatements in Home Retail Group compared to the pre-existing Sainsbury's Group. We have therefore included the risks relating to legacy Home Retail Group components Argos and Argos Financial Services together where appropriate in the risks below and we have adopted a similar audit strategy where possible.

We have designated Argos as a full scope component and performed audit procedures on specific balances including in the Argos Financial Services and Argos Asia entities.

**Risk****Supplier arrangements**

Refer to the Audit Committee Report (page 68); Accounting policies (page 114); and note 2 of the Consolidated Financial Statements (page 114)

The Group receives material discounts from suppliers, referred to as supplier arrangements. Complex supplier arrangements recognised in the income statement for the financial year are £343 million (2015/16: £371 million). These arrangements are described in note 2 to the financial statements.

We focused our audit procedures on the areas where management applies judgement, where the processing is either manual or more complex and where the quantum of agreements is high.

**Our response to the risk**

- We walked through the controls in place within the supplier arrangements process. We were able to take a controls-reliance approach over certain aspects of the process, testing the key controls.
- We selected a sample of suppliers to whom we sent confirmations across all 'deal' types to confirm key deal input terms. We did not receive any responses where suppliers disagreed with the deal terms recorded. Where we did not receive a response from the supplier, we performed alternative procedures, including obtaining evidence of initiation and settlement of the arrangement.
- We tested the existence and valuation of balance sheet amounts recognised in accounts receivable and as a contra-asset in accounts payable by reviewing post period end settlement. We also performed a 'look-back' analysis of prior period balance sheet amounts to check that these amounts were appropriately recovered.
- We tested the settlement of a sample of supplier arrangements recognised in the income statement, which included settlement in cash or by off-set to accounts payable.
- Using data extracted from the accounting system, we tested the appropriateness of journal entries and other adjustments to supplier arrangements to corroborating evidence.
- We tested deals recorded post period end and obtained the supplier agreement to validate that the deal was correctly recorded post period end.
- We read management's disclosure in respect of supplier arrangements amounts recorded in the income statement and balance sheet to confirm completeness and accuracy of amounts disclosed.

**What we concluded to the Audit Committee**

Supplier arrangement amounts are appropriately recognised in the income statement and balance sheet.

**Risk****Aspects of revenue recognition**

Refer to the Audit Committee Report (page 68); Accounting policies (page 120); and note 4 of the Consolidated Financial Statements (page 117)

Our assessment is that the vast majority of the Group's revenue transactions are non-complex, with no judgement applied over the amount recorded. We focused our work on the manual adjustments that are made to revenue.

Our procedures were designed to address the risk of manipulation of accounting records and the ability to override controls.

**Our response to the risk**

- We obtained a detailed understanding of these manual adjustments. Due to the manual nature of these adjustments, we performed substantive audit procedures.
- We used our computer-aided analytics tools to identify those revenue journals for which the corresponding entry was not cash. These entries include Nectar points, coupons and vouchers.
- We obtained corroborating evidence for such corresponding entries. For the Nectar points adjustment we obtained evidence from the administrator of the scheme. For third party coupons and vouchers we obtained evidence of collection and settlement.
- Using data extracted from the accounting system, we tested the appropriateness of journal entries impacting revenue, as well as other adjustments made in the preparation of the financial statements. We considered unusual journals such as those posted outside expected hours, or by unexpected individuals, and for large or unusual amounts.

**What we concluded to the Audit Committee**

Adjustments to revenue have been appropriately recognised.

**Risk****Financial Services customer receivables impairment**

Refer to the Audit Committee Report (page 68); Accounting policies (page 133); and note 15b of the Consolidated Financial Statements (page 133)

Financial Services customer receivables, through either credit cards, loans or Argos store cards, are significant. Total amounts recognised at 28 February 2017 are £4,602 million (2016: £3,344 million). The provision for impairment is £89 million (2016: £79 million). There is judgement in the assumptions applied to calculate the loan provisions against outstanding balances.

**Our response to the risk**

The audit of Sainsbury's Bank was completed by a component auditor from another audit firm. We agreed an audit strategy with the component auditor in advance of their testing and we reviewed the results of their work. The primary team performed the specific scope audit of Argos Financial Services. The audit strategy for both Sainsbury's Bank and Argos Financial Services included the following:

- The loan impairment methodology was reviewed to confirm it was consistent with both the IFRS requirements and that previously applied.
- The completeness and accuracy of the data from underlying systems that were used in the impairment models were tested.
- Key assumptions including the probability of default and the size of the loss if default occurred were assessed against internal and external evidence. The key assumptions within the models were compared to knowledge of assumptions used in the banking sector and also with internal historical trends, concluding that, based on the evidence obtained, management's conclusions were supportable.
- Changes to the modelling assumptions were assessed to confirm these were appropriate and in line with accounting standards.
- The accuracy of prior year impairment reserves was considered to assess the quality of management's estimation process.

**What we concluded to the Audit Committee**

The provision for impairment of Financial Services receivables due from customers is appropriately recognised.

## Risk

### HRG acquisition purchase price allocation

Refer to the Audit Committee Report (page 68); Accounting policies (page 169); and note 31 of the Consolidated Financial Statements (page 169)

The Group acquired Home Retail Group plc during the year. The provisional business combination fair values are outlined in note 31 to the financial statements.

We focused our risk on the areas where management applies judgement in the accounting and valuation of the acquired assets and liabilities, for example in calculation of the Argos brand.

#### Our response to the risk

- Our audit of the fair values of the acquired assets and liabilities was subject to full scope audit procedures by the primary team.
- We walked through the controls in place within the purchase price accounting process and understood management's process to be in line with IFRS 3 Business Combinations.
- We corroborated management's assumptions by comparing to relevant available information assisted by our business valuation specialists. In particular, we challenged the discount rate and the useful economic life of the Argos brand.
- We tested the prospective financial information utilised in the calculation of the valuations based on the viewpoint of a market participant as defined by IFRS 13 Fair Value Measurement.
- We evaluated the adequacy of the business combination disclosures to the requirements in IFRS 3.

#### What we concluded to the Audit Committee

The provisional purchase price allocation is appropriately recognised.

## Risk

### The IT environment

The IT systems across the Group are complex and there are varying levels of integration between them. The systems are vital to the ongoing operations of the business and to the integrity of the financial reporting process.

For Sainsbury's Bank the key system relating to the customer loan receivable impairment, as described above, is provided by an external party.

#### Our response to the risk

- We held discussions with management to understand the IT environment and walked through the key financial processes to understand where IT systems were integral to the Group's controls over financial reporting. From this we identified which IT systems to include in the scope for our detailed IT testing.
- We assessed the IT general controls environment for the key systems impacting the accurate recording of transactions and the presentation of the financial statements.
- We designed our IT audit procedures to assess the IT environment, including an assessment of controls over changes made to the system and controls over appropriate access to the systems.
- Where we found that adequate IT general controls were not in place, we performed additional substantive testing to mitigate the risk of material misstatement.
- Sainsbury's Bank's auditors received a report from the auditors on the general control environment of the outsourced systems and followed up on matters arising, performing further procedures as necessary. We discussed the remediation work performed by Sainsbury's Bank's auditors and reviewed their work.

#### What we concluded to the Audit Committee

We have not identified any misstatements in the financial statements due to the limitations of the IT environment.

## The scope of our audit

### Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each entity within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the Group and effectiveness of Group-wide controls, changes in the business environment and other factors such as recent Internal Audit results when assessing the level of work to be performed at each entity.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts of the components of the Group in the Group financial statements, we selected the head office company, J Sainsbury plc, Sainsbury's and Argos trading entities and Sainsbury's Bank components to perform full scope procedures. These represent the principal business units within the Group based on their size and risk characteristics.

For other entities including Argos Financial Services, the property companies, Argos Asia, joint ventures and insurance components we performed audit procedures on specific accounts which we considered had the potential for the greatest impact on the significant accounts in the financial statements either because of the size of these accounts or their risk profile.

The audit scope of these components may not have included testing of all significant accounts of the component but will have contributed to the coverage of significant accounts tested for the Group.

Of the remaining balances, none are individually greater than 5 per cent of the Group's profit before tax excluding items noted below. For these accounts, we performed other procedures, including analytical review, testing of consolidation journals and intercompany eliminations to respond to any potential risks of material misstatement to the Group financial statements.

### Involvement with component teams

In establishing our overall approach to the Group audit, we determined the type of work needed to be undertaken at each of the components by us, as the primary audit engagement team, or by component auditors from other EY network firms operating under our instruction. Of the full scope components, audit procedures were performed on the head office company, J Sainsbury plc, Sainsbury's and Argos trading entities and consolidation of the Group by the primary team. The work at the specific scope locations was performed by EY components in Hong Kong, the Isle of Man and the primary team.

For the Sainsbury's Bank full scope component, where the work was performed by auditors from another audit firm, we instructed the component auditor to perform specified procedures in response to our risk assessment. During the current period's audit cycle, the Senior Statutory Auditor visited Sainsbury's Bank and held discussions with management. The team discussed the audit approach with the component team and significant issues arising from their work, reviewing key audit working papers on risk areas. The closing discussion was attended by the primary team. This, together with the additional procedures performed at Group level, gave us appropriate evidence for our opinion on the Group financial statements.

### Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

**Materiality**

*The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.*

We determined materiality for the Group to be £34 million, which is 5.1 per cent of profit before tax excluding the items described below. We believe that this materiality basis provides us with the best assessment of the requirements of the users of the financial statements. This is consistent with the approach taken in the prior period.

|                       |  |        |
|-----------------------|--|--------|
| <b>Starting basis</b> | Profit before tax                          | £503m  |
| <b>Adjustments</b>    | Net impairment and onerous contract charge | £37m   |
|                       | Argos transaction and integration costs    | £53m   |
|                       | Sainsbury's Bank transition costs          | £60m   |
|                       | Business rationalisation                   | (£72m) |
|                       | IT write-offs                              | £57m   |
|                       | Restructuring costs                        | £33m   |
| <b>Materiality</b>    | Profit before tax excluding adjustments    | £671m  |
|                       | Materiality (5.1% of materiality basis)    | £34m   |

**Performance materiality**

*The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.*

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was approximately 75 per cent (2015/16: 50 per cent) of our planning materiality, namely £25 million (2015/16: £15 million). The reason for the change is that we have assessed the risk of material misstatement to be lower now this is no longer our first audit.

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current period, the range of performance materiality allocated to components was £5 million to £19 million (2015/16: £3 million to £11 million).

**Reporting threshold**

*An amount below which identified misstatements are considered as being clearly trivial.*

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £1.7 million (2015/16: £1.5 million), which is set at 5 per cent of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

**Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

**Respective responsibilities of Directors and auditor**

As explained more fully in the Statement of Directors' responsibilities set out on page 100, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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.

**Opinion on other matters prescribed by the Companies Act 2006**

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and based on the work undertaken in the course of the audit;
- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements;

## Matters on which we are required to report by exception

|  |   |                                  |
|--|---|----------------------------------|
| <b>ISAs (UK and Ireland) reporting</b> | <p>We are required to report to you if, in our opinion, financial and non-financial information in the Annual Report is:</p> <ul style="list-style-type: none"> <li>— materially inconsistent with the information in the audited financial statements; or</li> <li>— apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or</li> <li>— otherwise misleading.</li> </ul> <p>In particular, we are required to report whether we have identified any inconsistencies between our knowledge acquired in the course of performing the audit and the Directors' statement that they consider the Annual Report and Accounts taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the entity's performance, business model and strategy; and whether the Annual Report appropriately addresses those matters that we communicated to the Audit Committee that we consider should have been disclosed.</p> | We have no exceptions to report. |
| <b>Companies Act 2006 reporting</b>    | <p>In light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have identified no material misstatements in the Strategic Report or Directors' Report.</p> <p>We are required to report to you if, in our opinion:</p> <ul style="list-style-type: none"> <li>— 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</li> <li>— the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or</li> <li>— certain disclosures of Directors' remuneration specified by law are not made; or</li> <li>— we have not received all the information and explanations we require for our audit.</li> </ul>  | We have no exceptions to report. |
| <b>Listing Rules review</b>            | <p>We are required to review:</p> <ul style="list-style-type: none"> <li>— the Directors' statement in relation to going concern, set out on page 45, and longer-term viability, set out on page 45; and</li> <li>— the part of the Corporate Governance Statement relating to the Company's compliance with the provisions of the UK Corporate Governance Code specified for our review.</li> </ul>  | We have no exceptions to report. |

## Statement on the Directors' assessment of the principal risks that would threaten the solvency or liquidity of the entity

|  |  |  |
|--|--|--|
| <b>ISAs (UK and Ireland) reporting</b> | <p>We are required to give a statement as to whether we have anything material to add or to draw attention to in relation to:</p> <ul style="list-style-type: none"> <li>— the Directors' confirmation in the Annual Report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity;</li> <li>— the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated;</li> <li>— the Directors' statement in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements; and</li> <li>— the Directors' explanation in the Annual Report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.</li> </ul> | We have nothing material to add or to draw attention to. |
|--|--|--|

### Nigel Jones

#### (Senior statutory auditor)

for and on behalf of Ernst & Young LLP,  
Statutory Auditor London  
2 May 2017

- 1 The maintenance and integrity of the J Sainsbury plc website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
- 2 Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

# Consolidated income statement

for the 52 weeks to 11 March 2017

|   | Note | 2017<br>£m      | 2016<br>£m |
|---|------|-----------------|------------|
| <b>Revenue</b>  | 4    | <b>26,224</b>   | 23,506     |
| Cost of sales   |      | <b>(24,590)</b> | (22,050)   |
| <b>Gross profit</b>                                       |      | <b>1,634</b>    | 1,456      |
| Administrative expenses                                   | 5    | <b>(1,207)</b>  | (850)      |
| Other income  | 5    | <b>215</b>      | 101        |
| <b>Operating profit</b>                                   |      | <b>642</b>      | 707        |
| Finance income  | 6    | <b>34</b>       | 19         |
| Finance costs   | 6    | <b>(136)</b>    | (167)      |
| Share of post-tax loss from joint ventures and associates | 12   | <b>(37)</b>     | (11)       |
| <b>Profit before tax</b>                                  |      | <b>503</b>      | 548        |
| Analysed as:  |      |                 |            |
| Underlying profit before tax                              | 3    | <b>581</b>      | 587        |
| Non-underlying items                                      | 3    | <b>(78)</b>     | (39)       |
|   |      | <b>503</b>      | 548        |
| Income tax expense  | 7    | <b>(126)</b>    | (77)       |
| <b>Profit for the financial year</b>                      |      | <b>377</b>      | 471        |
| <b>Earnings per share</b>                                 | 8    | <b>pence</b>    | pence      |
| Basic   |      | <b>17.5</b>     | 23.9       |
| Diluted   |      | <b>16.5</b>     | 22.5       |
| Underlying basic  |      | <b>21.8</b>     | 24.2       |
| Underlying diluted  |      | <b>20.4</b>     | 22.8       |

The notes on pages 111 to 177 form an integral part of these financial statements.

# Consolidated statement of comprehensive income

for the 52 weeks to 11 March 2017

|   | Note | 2017<br>£m   | 2016<br>£m |
|---|------|--------------|------------|
| <b>Profit for the financial year</b>  |      | <b>377</b>   | 471        |
| <b>Items that will not be reclassified subsequently to the income statement</b> |      |              |            |
| Remeasurement on defined benefit pension schemes                                | 29   | <b>(407)</b> | 121        |
| Current tax relating to items not reclassified                                  | 7    | <b>41</b>    | –          |
| Deferred tax relating to items not reclassified                                 | 7    | <b>28</b>    | (36)       |
|   |      | <b>(338)</b> | 85         |
| <b>Items that may be reclassified subsequently to the income statement</b>      |      |              |            |
| Currency translation differences  | 20   | <b>5</b>     | 2          |
| Available-for-sale financial assets fair value movements                        |      |              |            |
| Attributable to Group   |      | <b>10</b>    | (1)        |
| Items reclassified from available-for-sale assets reserve                       | 20   | <b>(1)</b>   | –          |
| Cash flow hedges effective portion of fair value movements                      |      |              |            |
| Attributable to Group   | 20   | <b>115</b>   | 4          |
| Attributable to joint ventures and associates                                   | 20   | –            | 1          |
| Items reclassified from cash flow hedge reserve                                 | 20   | <b>(87)</b>  | 7          |
| Current tax relating to items that may be reclassified                          | 7    | <b>(1)</b>   | –          |
| Deferred tax relating to items that may be reclassified                         | 7    | <b>5</b>     | 3          |
|   |      | <b>46</b>    | 16         |
| <b>Total other comprehensive (expense)/income for the year (net of tax)</b>     |      | <b>(292)</b> | 101        |
| <b>Total comprehensive income for the year</b>                                  |      | <b>85</b>    | 572        |

The notes on pages 111 to 177 form an integral part of these financial statements.

# Consolidated balance sheet

At 11 March 2017 and 12 March 2016

|  | Note | 2017<br>£m     | 2016<br>£m |
|--|------|----------------|------------|
| <b>Non-current assets</b>                                      |      |                |            |
| Property, plant and equipment                                  | 10   | <b>10,006</b>  | 9,764      |
| Intangible assets  | 11   | <b>742</b>     | 329        |
| Investments in joint ventures and associates                   | 12   | <b>237</b>     | 327        |
| Available-for-sale financial assets                            | 13   | <b>435</b>     | 340        |
| Other receivables  | 15a  | <b>69</b>      | 103        |
| Amounts due from Financial Services customers                  | 15b  | <b>1,916</b>   | 1,649      |
| Derivative financial instruments                               | 24   | <b>10</b>      | 17         |
|  |      | <b>13,415</b>  | 12,529     |
| <b>Current assets</b>  |      |                |            |
| Inventories  | 14   | <b>1,775</b>   | 968        |
| Trade and other receivables                                    | 15a  | <b>574</b>     | 508        |
| Amounts due from Financial Services customers                  | 15b  | <b>2,686</b>   | 1,695      |
| Available-for-sale financial assets                            | 13   | <b>100</b>     | 48         |
| Derivative financial instruments                               | 24   | <b>94</b>      | 51         |
| Cash and cash equivalents                                      | 25b  | <b>1,083</b>   | 1,143      |
|  |      | <b>6,312</b>   | 4,413      |
| Assets held for sale   | 16   | <b>10</b>      | 31         |
|  |      | <b>6,322</b>   | 4,444      |
|  |      | <b>19,737</b>  | 16,973     |
| <b>Current liabilities</b>                                     |      |                |            |
| Trade and other payables                                       | 17a  | <b>(3,741)</b> | (3,077)    |
| Amounts due to Financial Services customers and other deposits | 17b  | <b>(4,284)</b> | (3,173)    |
| Borrowings   | 27   | <b>(172)</b>   | (223)      |
| Derivative financial instruments                               | 24   | <b>(22)</b>    | (43)       |
| Taxes payable  |      | <b>(219)</b>   | (158)      |
| Provisions   | 18   | <b>(135)</b>   | (46)       |
|  |      | <b>(8,573)</b> | (6,720)    |
| Liabilities held for sale                                      | 16   | <b>–</b>       | (4)        |
|  |      | <b>(8,573)</b> | (6,724)    |
|  |      | <b>(2,251)</b> | (2,280)    |
| <b>Net current liabilities</b>                                 |      |                |            |
| <b>Non-current liabilities</b>                                 |      |                |            |
| Other payables   | 17a  | <b>(304)</b>   | (269)      |
| Amounts due to Financial Services customers and other deposits | 17b  | <b>(637)</b>   | (582)      |
| Borrowings   | 27   | <b>(2,039)</b> | (2,190)    |
| Derivative financial instruments                               | 24   | <b>(38)</b>    | (69)       |
| Deferred income tax liability                                  | 7    | <b>(172)</b>   | (237)      |
| Provisions   | 18   | <b>(128)</b>   | (129)      |
| Retirement benefit obligations                                 | 29   | <b>(974)</b>   | (408)      |
|  |      | <b>(4,292)</b> | (3,884)    |
|  |      | <b>6,872</b>   | 6,365      |
| <b>Net assets</b>  |      |                |            |
| <b>Equity</b>  |      |                |            |
| Called up share capital  | 19   | <b>625</b>     | 550        |
| Share premium account  | 19   | <b>1,120</b>   | 1,114      |
| Capital redemption reserve                                     | 20   | <b>680</b>     | 680        |
| Merger reserve   | 19   | <b>568</b>     | –          |
| Other reserves   | 20   | <b>193</b>     | 155        |
| Retained earnings  | 22   | <b>3,190</b>   | 3,370      |
|  |      | <b>6,376</b>   | 5,869      |
| Perpetual capital securities                                   | 21   | <b>248</b>     | 248        |
| Perpetual convertible bonds                                    | 21   | <b>248</b>     | 248        |
|  |      | <b>6,872</b>   | 6,365      |

The notes on pages 111 to 177 form an integral part of these financial statements.

The financial statements on pages 106 to 177 were approved by the Board of Directors on 2 May 2017, and are signed on its behalf by:

**Mike Coupe** Chief Executive  
**Kevin O'Byrne** Chief Financial Officer

# Consolidated cash flow statement

for the 52 weeks to 11 March 2017

|  | Note | 2017<br>£m   | 2016<br>£m |
|--|------|--------------|------------|
| <b>Cash flows from operating activities</b>                              |      |              |            |
| Cash generated from operations   | 25a  | <b>1,323</b> | 624        |
| Interest paid  |      | <b>(95)</b>  | (108)      |
| Corporation tax paid   |      | <b>(75)</b>  | (124)      |
| <b>Net cash generated from operating activities</b>                      |      | <b>1,153</b> | 392        |
| <b>Cash flows from investing activities</b>                              |      |              |            |
| Purchase of property, plant and equipment                                |      | <b>(634)</b> | (646)      |
| Purchase of intangible assets  |      | <b>(110)</b> | (34)       |
| Proceeds from disposal of property, plant and equipment                  |      | <b>55</b>    | 109        |
| Receipt of advance disposal proceeds                                     |      | –            | 125        |
| Acquisition of subsidiaries, net of cash acquired                        | 31   | <b>101</b>   | –          |
| Capital return to Home Retail Group plc shareholders                     | 31   | <b>(226)</b> | –          |
| Share issuance costs on acquisition of Home Retail Group plc             | 31   | <b>(3)</b>   | –          |
| Investment in joint ventures   | 12   | <b>(16)</b>  | (18)       |
| Disposal of subsidiaries   |      | –            | (1)        |
| Interest received  | 12   | <b>18</b>    | 19         |
| Dividends and distributions received                                     |      | <b>65</b>    | 46         |
| <b>Net cash used in investing activities</b>                             |      | <b>(750)</b> | (400)      |
| <b>Cash flows from financing activities</b>                              |      |              |            |
| Proceeds from issuance of ordinary shares                                |      | <b>6</b>     | 8          |
| Drawdown of short-term borrowings  |      | <b>448</b>   | –          |
| Repayment of short-term borrowings                                       |      | <b>(492)</b> | (95)       |
| Repayment of long-term borrowings  |      | <b>(130)</b> | (238)      |
| Proceeds from the issue of perpetual capital securities                  | 21   | –            | 247        |
| Proceeds from the issue of perpetual convertible bonds                   | 21   | –            | 247        |
| Purchase of own shares   |      | –            | (20)       |
| Repayment of capital element of obligations under finance lease payments |      | <b>(37)</b>  | (30)       |
| Interest elements of obligations under finance lease payments            |      | <b>(8)</b>   | (9)        |
| Dividends paid on ordinary shares  | 9    | <b>(230)</b> | (234)      |
| Dividends paid on perpetual securities                                   | 21   | <b>(23)</b>  | (4)        |
| <b>Net cash used in financing activities</b>                             |      | <b>(466)</b> | (128)      |
| <b>Net decrease in cash and cash equivalents</b>                         |      |              |            |
|  |      | <b>(63)</b>  | (136)      |
| Opening cash and cash equivalents  |      | <b>1,140</b> | 1,276      |
| Effects of foreign exchange rates  |      | –            | –          |
| <b>Closing cash and cash equivalents</b>                                 | 25b  | <b>1,077</b> | 1,140      |

The notes on pages 111 to 177 form an integral part of these financial statements.

# Consolidated statement of changes in equity

for the 52 weeks to 11 March 2017

|  | Note   | Called up share capital<br>£m | Share premium account<br>£m | Capital redemption and other reserves<br>£m | Merger reserve<br>£m | Retained earnings<br>£m | Total equity before perpetual securities<br>£m | Perpetual capital securities<br>£m | Perpetual convertible bonds<br>£m | Total equity<br>£m |
|--|--------|-------------------------------|-----------------------------|---|----------------------|-------------------------|--|------------------------------------|-----------------------------------|--------------------|
| <b>At 13 March 2016</b>  |        | 550                           | 1,114                       | 835   | –                    | 3,370                   | 5,869  | 248                                | 248                               | 6,365              |
| Profit for the year  | 21, 22 | –                             | –                           | –   | –                    | 359                     | 359  | 12                                 | 6                                 | 377                |
| Other comprehensive income/(expense)   | 20, 22 | –                             | –                           | 46  | –                    | (338)                   | (292)  | –                                  | –                                 | (292)              |
| <b>Total comprehensive income for the year ended 11 March 2017</b>   |        | –                             | –                           | 46  | –                    | 21                      | 67   | 12                                 | 6                                 | 85                 |
| Transactions with owners:  |        |                               |                             |   |                      |                         |  |                                    |                                   |                    |
| Dividends  | 9, 22  | –                             | –                           | –   | –                    | (232)                   | (232)  | –                                  | –                                 | (232)              |
| Acquisition of subsidiaries  | 19, 22 | 75                            | –                           | –   | 568                  | (3)                     | 640  | –                                  | –                                 | 640                |
| Adjustment to consideration in respect of share options (note 31)  | 31     | –                             | –                           | –   | –                    | 3                       | 3  | –                                  | –                                 | 3                  |
| Distribution to holders of perpetual securities (net of tax)   | 21     | –                             | –                           | –   | –                    | –                       | –  | (12)                               | (6)                               | (18)               |
| Amortisation of convertible bond equity component  | 20, 22 | –                             | –                           | (8)   | –                    | 8                       | –  | –                                  | –                                 | –                  |
| Share-based payment (net of tax)   | 30     | –                             | –                           | –   | –                    | 32                      | 32   | –                                  | –                                 | 32                 |
| Purchase of own shares   | 22     | –                             | –                           | –   | –                    | (9)                     | (9)  | –                                  | –                                 | (9)                |
| Allotted in respect of share option schemes  | 19, 22 | –                             | 6                           | –   | –                    | –                       | 6  | –                                  | –                                 | 6                  |
| <b>At 11 March 2017</b>  |        | <b>625</b>                    | <b>1,120</b>                | <b>873</b>                                  | <b>568</b>           | <b>3,190</b>            | <b>6,376</b>                                   | <b>248</b>                         | <b>248</b>                        | <b>6,872</b>       |
| At 15 March 2015   |        |                               |                             |   |                      |                         |  |                                    |                                   |                    |
|  |        | 548                           | 1,108                       | 826   | –                    | 3,057                   | 5,539  | –                                  | –                                 | 5,539              |
| Profit for the year  | 21, 22 | –                             | –                           | –   | –                    | 452                     | 452  | 13                                 | 6                                 | 471                |
| Other comprehensive income   | 22     | –                             | –                           | 16  | –                    | 85                      | 101  | –                                  | –                                 | 101                |
| Total comprehensive income for the year ended 12 March 2016  |        | –                             | –                           | 16  | –                    | 537                     | 553  | 13                                 | 6                                 | 572                |
| Transactions with owners:  |        |                               |                             |   |                      |                         |  |                                    |                                   |                    |
| Dividends  | 9, 22  | –                             | –                           | –   | –                    | (234)                   | (234)  | –                                  | –                                 | (234)              |
| Issue of perpetual subordinated capital securities and perpetual subordinated convertible bonds (net of tax) | 21     | –                             | –                           | –   | –                    | –                       | –  | 248                                | 248                               | 496                |
| Distributions to holders of perpetual subordinated convertible bonds (net of tax)                            | 21     | –                             | –                           | –   | –                    | –                       | –  | (13)                               | (6)                               | (19)               |
| Amortisation of convertible bond equity component  | 20, 22 | –                             | –                           | (7)   | –                    | 7                       | –  | –                                  | –                                 | –                  |
| Share-based payment (net of tax)   | 30     | –                             | –                           | –   | –                    | 23                      | 23   | –                                  | –                                 | 23                 |
| Purchase of own shares   | 22     | –                             | –                           | –   | –                    | (20)                    | (20)   | –                                  | –                                 | (20)               |
| Allotted in respect of share option schemes  | 19, 22 | 2                             | 6                           | –   | –                    | –                       | 8  | –                                  | –                                 | 8                  |
| <b>At 12 March 2016</b>  |        | <b>550</b>                    | <b>1,114</b>                | <b>835</b>                                  | <b>–</b>             | <b>3,370</b>            | <b>5,869</b>                                   | <b>248</b>                         | <b>248</b>                        | <b>6,365</b>       |

The notes on pages 111 to 177 form an integral part of these financial statements.

# Notes to the consolidated financial statements

## 1 Basis of preparation

J Sainsbury plc is a public limited company (the 'Company') incorporated in the United Kingdom, whose shares are publicly traded on the London Stock Exchange. The Company is domiciled in the United Kingdom and its registered address is 33 Holborn, London EC1N 2HT, United Kingdom.

The financial year represents the 52 weeks to 11 March 2017 (prior financial year 52 weeks to 12 March 2016). The consolidated financial statements for the 52 weeks to 11 March 2017 comprise the financial statements of the Company and its subsidiaries (the 'Group') and the Group's share of the post-tax results of its joint ventures and associates.

The Group's principal activities are Food, General Merchandise & Clothing retailing and Financial Services.

The Group's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and International Financial Reporting Interpretations Committee (IFRIC) and with those parts of the Companies Act 2006 applicable to companies reporting under IFRSs.

The financial statements are presented in sterling, rounded to the nearest million (£m) unless otherwise stated. They have been prepared on a going concern basis under the historical cost convention, except for derivative financial instruments, defined benefit scheme assets, investment properties and available-for-sale financial assets that have been measured at fair value.

Significant accounting policies have been included in the relevant notes to which the policies relate, and those relating to the financial statements as a whole can be read further below. Significant accounting policies have been applied consistently to all periods presented in the financial statements. As part of the acquisition of Home Retail Group plc an exercise has been performed to ensure that the accounting policies within both businesses are aligned. Based on this review, there have been no material changes to existing accounting policies from those disclosed in this Annual Report.

### Basis of consolidation

The consolidated financial statements of the Group consist of the financial statements of the ultimate parent company J Sainsbury plc, all entities controlled by the Company and the Group's share of its interests in joint ventures and associates.

#### a) Subsidiaries

Subsidiaries are all entities (including structured entities) over which the Group has control. This is when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The results of subsidiaries are included in the income statement from the date of acquisition or, in the case of disposals, up to the effective date of disposal. Intercompany transactions and balances between Group companies are eliminated upon consolidation.

Sainsbury's Property Scottish Partnership and Sainsbury's Property Scottish Limited Partnership are two partnerships the Group has an interest in, which are fully consolidated into these Group accounts. The Group has taken advantage of the exemption conferred by Regulation 7 of the Partnerships ('Accounts') Regulations 2008 and has therefore not appended the accounts of these qualifying partnerships to these accounts. Separate accounts for these partnerships are not required to be, and have not been, filed at Companies House.

#### b) Joint ventures and associates

The Group applies IFRS 11 to all joint arrangements. Under IFRS 11, investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations of each investor. The Group has assessed the nature of its joint arrangements and determined them to be joint ventures. The Group's share of the post-tax results of its joint ventures and associates is included in the income

statement using the equity method of accounting. Where the Group transacts with a joint venture or associate, profits and losses are eliminated to the extent of the Group's interest in the joint venture or associate.

Investments in joint ventures and associates are carried in the Group balance sheet at historical cost plus post-acquisition changes in the Group's share of net assets of the entity, less any provision for impairment.

Associates are entities over which the Group has significant influence but not control.

Investment properties held by the Group are those contained within its joint ventures with Land Securities Group PLC and The British Land Company PLC. These are properties held for capital appreciation and/or to earn rental income. They are initially measured at cost, including related transaction costs. After initial recognition at cost, they are carried at their fair values based on market value determined by professional valuers at each reporting date. The difference between the fair value of an investment property at the reporting date and its carrying amount prior to re-measurement is included within the income statement but is excluded from underlying profit in order to provide a clear and consistent presentation of the underlying performance of the Group's ongoing business for shareholders.

### Foreign currencies

The consolidated financial statements are presented in sterling, which is the ultimate parent company's functional currency.

#### a) Foreign operations

On consolidation, assets and liabilities of foreign operations are translated into sterling at year-end exchange rates. The results of foreign operations are translated into sterling at average rates of exchange for the year.

#### b) Foreign currency transactions

Transactions denominated in foreign currencies are translated at the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement.

### Amendments to published standards

#### Effective for the Group and Company in these financial statements:

The Group has considered the following amendments to published standards that are effective for the Group for the financial year beginning 13 March 2016 and concluded that they are either not relevant to the Group or that they do not have a significant impact on the Group's financial statements. These standards and interpretations have been endorsed by the European Union.

- Annual Improvements to IFRSs 2012–2014 Cycle
- Amendments to IAS 16, 'Property, plant and equipment' and IAS 38, 'Intangible assets' which clarifies acceptable methods of depreciation and amortisation
- Amendments to IFRS 11, 'Joint arrangements' on the accounting for acquisitions of interests in joint operations
- Amendments to IAS 16 and IAS 41, 'Bearer Plants'
- Amendments to IAS 1, 'Presentation of financial statements' which clarifies existing IAS 1 requirements
- Amendments to IAS 27, 'Consolidated and separate financial statements' which allow an entity to use the equity method as described in IAS 28 to account for its investments in subsidiaries
- Amendments to IFRS 10, 'Consolidated financial statements', IFRS 12, 'Disclosure of interests in other entities' and IAS 28, 'Investments in associates and joint ventures' on applying the consolidation exception

## 1 Basis of preparation continued

### Standards and revisions effective for future periods:

The following standards and revisions will be effective for future periods:

- IFRS 9, 'Financial instruments'
- IFRS 15, 'Revenue from contracts with customers'
- IFRS 16, 'Leases'
- Amendments to IAS 7 'Statement of cash flows' on the disclosures in financial statements

IAS 7 is expected to impact disclosures only. The remaining standards have been considered in turn below:

#### IFRS 9 'Financial Instruments'

IFRS 9 will supersede IAS 39 in its entirety, and is effective for accounting periods commencing on or after 1 January 2018. For Sainsbury's, the effective date is the financial year commencing 11 March 2018. Any changes to recognition and measurement will be applied retrospectively by adjusting the opening balance sheet at that time. There is no requirement to restate comparative amounts.

The core areas addressed within IFRS 9 are as follows:

- Classification and measurement of financial assets and liabilities
- Impairment of financial assets
- Hedge accounting

The Group does not expect any material changes in relation to the classification and measurement of financial assets and liabilities, nor for hedge accounting other than additional disclosure requirements. The most significant impact on the Group is likely to be in relation to impairment of financial assets as outlined below.

#### Impairment of financial assets

Financial assets which are measured at amortised cost or fair value through other comprehensive income under IFRS 9 will be subject to the new impairment provisioning requirements of the standard, and it is this area which has the most impact on the Group in relation to loans and advances to customers within Financial Services.

Financial Services' current impairment policy under IAS 39 is to recognise losses only when an impairment event has been observed, and where an impairment event has arisen but has not yet been identified through observation of a specific impairment trigger. As a result, losses are generally not recognised when credit risk deteriorates, and only materialise when the deterioration results in an impairment event.

IFRS 9 introduces a three stage 'expected credit loss (ECL)' model which is forward looking and which generally will result in earlier recognition of credit losses. It is no longer necessary for an impairment event to have occurred before credit losses are recognised.

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**Stage 1** As soon as a financial instrument is originated or purchased, 12-month expected credit losses must be recognised in profit and loss and an impairment allowance will be established

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**Stage 2** If the credit risk increases significantly (and the resulting credit quality is not considered to be low credit risk) full lifetime expected credit losses will be provided for

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**Stage 3** Financial assets will move into Stage 3 when they are considered to be credit impaired, i.e. when one or more events have occurred that have a detrimental impact on the estimated future cash flows of the asset

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#### Implementation approach

The Group's implementation project has been in place since early 2015 (and has been expanded to incorporate subsidiaries acquired as part of the J Sainsbury's acquisition of Home Retail Group). The primary objectives of the project are to: define accounting policies in compliance with the standard; deliver the necessary data, system and operational changes; and update the credit provisioning models and overall governance framework. The project is being jointly led by Sainsbury's Bank's Finance and Credit Risk functions, with support from external professional advisers. The project has a steering committee in place to provide appropriate oversight and governance; and a Technical Working Group to ensure that policy decisions and approaches are appropriate and in line with industry practice.

The Bank has defined its approach and methodology for ECL provisioning under IFRS 9, and has been developing models to comply with the new requirements.

Key judgemental areas still to be concluded on include the determination of 'significant increase in credit risk' (which is the key concept for moving from 12-month ECL to lifetime ECL), and the approach to modelling future economic scenarios.

Until the ECL models are fully developed, the Group is unable to quantify the impact of transition to IFRS 9. Furthermore, the mapping of the three IFRS 9 impairment stages to regulatory treatment (specific versus general credit risk adjustments) is not clear at this time, pending further guidance from regulators. The Basel Committee for Banking Supervision (BCBS) has proposed a transitional approach to the impact of IFRS 9 on regulatory capital, whereby the Day 1 impact on CET1 capital may be spread over several years. The decision on whether or not to apply such an approach has been delegated to individual regulatory jurisdictions. The Group will fully consider the impact of IFRS 9 on the Bank's regulatory capital once these proposals have been finalised within the European Union.

#### IFRS 15 'Revenue from Contracts with Customers'

IFRS 15 'Revenue' will replace IAS 18 'Revenue' and IAS 11 'Construction Contracts' for accounting periods commencing on or after 1 January 2018. For Sainsbury's, the effective date is the financial year commencing 11 March 2018. Any changes to recognition and measurement will be applied retrospectively by adjusting the opening balance sheet at that time. There is no requirement to restate comparative amounts.

The core principle of the standard is that an entity will recognise revenue at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring promised goods or services to a customer.

To apply this principle, entities must follow the five-step model below:

- 1 Identify the contract(s) with a customer – written, oral or implied by an entity's customary business practices.
- 2 Identify the performance obligations in the contract(s) – evaluate the terms in the contract to identify all the promised goods or services and then determine which of these will be treated as separate performance obligations. They are separate if the customer can benefit from the good or service on its own (i.e. it is distinct).
- 3 Determine the transaction price – the amount that an entity expects to be entitled to in exchange for transferring goods or services to a customer, excluding amounts collected on behalf of third parties.
- 4 Allocate the transaction price to the performance obligations – generally in proportion to their stand-alone selling prices.
- 5 Recognise revenue when (or as) the entity satisfies each performance – when control of a promised good or service transfers to the customer.

The Group has performed a detailed impact assessment during the year, identifying all current sources of revenue and analysing the accounting requirements for each under IFRS 15. Currently the Group does not expect any material changes to either revenue or profit as a result of adopting IFRS 15.

## 1 Basis of preparation continued

### IFRS 16 'Leases'

IFRS 16 'Leases' will replace IAS 17 'Leases' for accounting periods commencing on or after 1 January 2019. For Sainsbury's, the effective date is the financial year commencing 10 March 2019. The core principal of the standard is to provide a single lessee accounting model, requiring lessees to recognise a right-of-use asset and lease liability for all leases unless the term is less than 12 months or the underlying asset has a low value. IFRS 16's approach to lessor accounting is mostly unchanged from IAS 17.

The transition to IFRS 16 will have a material impact on the balance sheet as all operating leases will need to be recognised on the balance sheet. Furthermore, rental expense in the income statement will be replaced with depreciation and interest expense.

The Group's implementation project commenced in 2016 to ensure all leases acquired as part of the Home Retail Group transaction were also captured. The primary objectives of the project are to: define accounting policies in compliance with the standard; identify all leases within the Group; capture the necessary data for each lease, including discount rates; determine a transition approach; understand and implement necessary system and operational changes; and update the Group's leasing strategy and overall governance framework. The project is being led by Group Finance with support from external professional advisers. The project has a steering committee in place to provide appropriate oversight and governance; and a Technical Working Group to ensure that policy decisions and approaches are appropriate and in line with industry practice.

The Group is currently in the process of developing updated accounting policies (including the application of practical expedients) and is assessing the information requirements for each lease.

A key area still to be concluded on is the transition approach. Whilst the impact of transition is likely to be material, the Group is unable to quantify the effect of transition at this time.

## 2 Significant accounting judgements, estimates and assumptions

The preparation of financial statements in conformity with IFRSs requires the use of judgements, estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Those which are significant to the Group are discussed separately below:

### Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, which have the most significant effect on the amounts recognised in the consolidated financial statements:

#### a) Non-current assets and liabilities held for sale

At each balance sheet date management assesses whether any assets, whose carrying amount will be recovered through a sale transaction rather than continued use, meet the definition of held for sale. Where there is an active plan in place to locate a buyer, management consider such assets to meet the criteria to be classified as held for sale if they are available for immediate sale and the sale is highly probable.

For more information on the assets and liabilities held for sale, refer to note 16.

#### b) Operating lease commitments

The Group is party to commercial property leases on a number of its stores. At inception of each lease, the terms and conditions of the arrangements are evaluated to assess whether the lease terms constitute a major part of the economic life of the assets and whether the present value of the minimum lease payments amount to substantially all of the fair value of the commercial property. Where there is no evidence of this, management concludes that all the significant risks and rewards of ownership do not transfer to the Group and these leases are accounted for as operating leases. Further information about committed operating lease payments is included in note 32.

#### c) Consolidation of structured entities

A structured entity is one in which Sainsbury's does not hold the majority interest but for which management has concluded that voting rights are not the dominant factor in deciding who controls the entity. In making such an assessment, management considers the terms of the arrangement to assess who has responsibility for the management of the entity and its assets. Where Sainsbury's has this responsibility, it is deemed that the Group controls the entity and it is fully consolidated into the Group accounts. The structured entities applicable to the Group are Sainsbury's Property Scottish Partnership and Sainsbury's Property Scottish Limited Partnership.

#### d) Aggregation of operating segments

Management has determined the operating segments based on the information provided to the Operating Board (the Chief Operating Decision Maker for the Group) to make operational decisions on the management of the Group. Following the acquisition of Home Retail Group plc in September 2016, four operating segments were identified as follows:

- Retail – Food
- Retail – General Merchandise & Clothing
- Financial Services
- Property Investment

Management has considered the economic characteristics, similarity of products, production processes, customers, sales methods and regulatory environment of its two Retail segments. In doing so it has been concluded that they should be aggregated into one 'Retail' segment in the financial statements. This aggregated information provides users the financial information needed to evaluate the business and the environment in which it operates.

### Estimates and assumptions

The areas where estimates and assumptions are significant to the financial statements are as described below. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

#### a) Business combinations

As part of the acquisition of Home Retail Group, the identifiable assets and liabilities acquired, including intangible assets and contingent liabilities, were recognised at their fair value in accordance with IFRS 3 'Business combinations'. The determination of the fair values on acquired assets and liabilities is based to a considerable extent, on management's judgement. In particular, the valuation of £179 million for the acquired Argos brand was sensitive to management's assessment of useful economic life (UEL), which was estimated to be ten years. A movement of plus or minus one year on the UEL would have resulted in a brand asset movement of £25 million/£(28) million.

#### b) Impairment of assets

The Group is required to assess whether goodwill has suffered any impairment loss, based on the recoverable amount of the cash-generating unit (CGU) or group of CGUs to which it is allocated. The recoverable amounts of the CGUs have been determined based on value in use calculations and these calculations require the use of estimates in relation to future cash flows and suitable discount rates, as disclosed in note 11. Actual outcomes could vary from these estimates.

Financial and non-financial assets are subject to impairment reviews based on whether current or future events and circumstances suggest that their recoverable amount may be less than their carrying value. Recoverable amount is based on the higher of the value in use and fair value less costs to dispose. Value in use is calculated from expected future cash flows using suitable discount rates and includes management assumptions and estimates of future performance.

## 2 Significant accounting judgements, estimates and assumptions continued

Impairment loss calculations on loans and advances within Financial Services (note 15(b)) involve the estimation of future cash flows of financial assets, based on observable data at the balance sheet date and historical loss experience for assets with similar credit risk characteristics. This will typically take into account the level of arrears, security, past loss experience and default levels. These calculations are undertaken on a portfolio basis using various statistical modelling techniques.

Impairment models are continually reviewed to ensure data and assumptions are appropriate, with the most material assumption being around expected loss rates. The accuracy of any such impairment calculation will be affected by unexpected changes to the economic situation, and assumptions which differ from actual outcomes. As such, judgement is applied when determining the levels of provisioning.

### c) Post-employment benefits

The Group operates two defined benefit schemes for its employees – the Sainsbury's Defined Benefit Scheme and the Home Retail Group Defined Benefit Scheme. The present value of the schemes' liabilities recognised at the balance sheet date and the net financing charge recognised in the income statement are dependent on interest rates of high quality corporate bonds. Other key assumptions within this calculation are based on market conditions or estimates of future events, including mortality rates, as set out in note 29. The carrying value of the retirement benefit obligations will be impacted by changes to any of the assumptions used, however is most sensitive to changes in the discount rate. Sensitivities to movements in the discount rate are included in note 29.

### d) Provisions

Provisions have been made for onerous leases, onerous contracts, dilapidations, restructuring, insurance and long service awards. These provisions are estimates and the actual costs and timing of future cash flows are dependent on future events and market conditions. Any difference between expectations and the actual future liability will be accounted for in the period when such determination is made. The carrying amount of provisions will be impacted by changes in the discount rate. Details of provisions are set out in note 18.

### e) Income taxes

The Group recognises expected liabilities for tax based on an estimation of the likely taxes due, which requires significant judgement as to the ultimate tax determination of certain items. Where the actual liability arising from these items differs from these estimates, such differences will have an impact on income tax and deferred tax provisions in the period when such determination is made. Detail of the tax charge and deferred tax are set out in note 7.

### f) Determining fair values

The fair values of financial assets and liabilities are based on prices available from the market on which the instruments are traded. Where market values are not available, the fair values of financial assets and liabilities have been calculated by discounting expected future cash flows at prevailing interest rates. The fair values of short-term deposits, trade receivables, overdrafts and payables are assumed to approximate to their book values.

### g) Supplier arrangements

Supplier incentives, rebates and discounts, collectively known as 'supplier arrangements', represent a material deduction to cost of sales and administrative expenses and directly affect the Group's reported margin. The arrangements can be complex, with amounts spanning multiple products over different time periods, and there can be multiple triggers and discounts. The accrued value at the reporting date is included in trade receivables or trade payables, depending on the right of offset. The four key types are as follows:

- Discounts and supplier incentives – these represent the majority of all supplier arrangements and are linked to individual unit sales. The incentive is typically based on an agreed sum per item sold on promotion for a period and therefore is considered part of the purchase price of that product.
- Fixed amounts – these are agreed with suppliers primarily to support

in-store activity including promotions, such as utilising specific space. These involve a degree of judgement and estimation in ensuring the appropriate cut-off of arrangements for fixed amounts which span period-end. These require judgement to determine when the terms of the arrangement are satisfied and that amounts are recognised in the correct period.

- Supplier rebates – these are typically agreed on an annual basis, aligned with the Group's financial year. The rebate amount is linked to pre-agreed targets such as sales volumes and requires estimates of the amount earned up to the balance sheet date, for each relevant supplier contract. Where agreements span a financial period-end, estimations are required of projected turnover and judgement may also need to be applied to determine the rebate level earned as agreements may involve multiple tiers. In order to minimise any risk arising from estimation, supplier confirmations are obtained to agree the value to be recognised at year-end, prior to it being invoiced. Rebates represent the smallest element of the Group's supplier arrangements and by aligning the agreements to the Group's financial year, where possible, the judgements required are minimised.
- Marketing and advertising income – income which is directly linked to the cost of producing the Argos catalogue is recognised once agreed with the supplier and when the catalogue is made available to the Group which is the point at which the catalogue costs are recognised.

Of the above categories, fixed amounts, supplier rebates and marketing and advertising income involve a level of judgement and estimation. The amounts recognised in the income statement for these three categories in the financial year are as follows:

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| Fixed amounts (within cost of sales)                                     | <b>204</b> | 302        |
| Supplier rebates (within cost of sales)                                  | <b>87</b>  | 69         |
| Marketing and advertising income<br>(included within operating expenses) | <b>52</b>  | –          |
| <b>Total supplier arrangements</b>                                       | <b>343</b> | 371        |

Of the above amounts, the following was outstanding and held on the balance sheet at year-end:

|   | 2017<br>£m | 2016<br>£m |
|---|------------|------------|
| <b>Within current trade receivables</b> |            |            |
| Supplier arrangements due               | <b>29</b>  | 6          |
| <b>Within current trade payables</b>    |            |            |
| Supplier arrangements due               | <b>25</b>  | 39         |
| Accrued supplier arrangements           | <b>13</b>  | 25         |

### 3 Non-GAAP performance measures

In order to provide shareholders with additional insight in to the underlying performance of the business, items recognised in reported profit or loss before tax which, by virtue of their size and or nature, do not reflect the Group's underlying performance are excluded from the Group's underlying results.

These adjusted items are as follows:

|  | 2017<br>£m  | 2016<br>£m |
|--|-------------|------------|
| <b>Underlying profit before tax</b>                                | <b>581</b>  | 587        |
| <b>Property related</b>  |             |            |
| Profit on disposal of properties                                   | <b>98</b>   | 101        |
| Investment property fair value movements                           | <b>(25)</b> | (18)       |
| Net impairment and onerous contract charge                         | <b>(37)</b> | (1)        |
| <b>Argos</b>   |             |            |
| Transaction costs relating to the acquisition of Home Retail Group | <b>(22)</b> | (12)       |
| Argos integration costs  | <b>(27)</b> | –          |
| Homebase separation  | <b>(4)</b>  | –          |
| <b>Sainsbury's Bank transition</b>                                 | <b>(60)</b> | (59)       |
| <b>Focus</b>   |             |            |
| Business rationalisation   | <b>72</b>   | (3)        |
| IT write-offs  | <b>(57)</b> | –          |
| <b>Restructuring costs</b>   | <b>(33)</b> | (15)       |
| <b>Other</b>   |             |            |
| Perpetual securities coupons                                       | <b>23</b>   | 15         |
| Non-underlying finance movements                                   | <b>10</b>   | (22)       |
| Acquisition adjustments  | <b>8</b>    | 3          |
| Defined benefit scheme financing charge and scheme expenses        | <b>(24)</b> | (28)       |
| <b>Total adjustments</b>   | <b>(78)</b> | (39)       |
| <b>Profit before tax</b>   | <b>503</b>  | 548        |

#### Property related

- Profit on disposal of properties for the financial year comprised £101 million for the Group (2016: £100 million) and £(3) million for the property joint ventures (2016: £1 million) included within other income.
- Net impairment and onerous contract charge comprises £19 million within property, plant and equipment (note 10) and onerous lease provisions of £18 million.

#### Argos

- Argos integration costs for the year of £(27) million were part of the previously announced £(130) million required over the three years in order to achieve the synergies of £160 million.
- The Homebase separation and restructuring costs for the year of £(4) million were part of the previously announced £(75) million upon the sale of Homebase.

#### Sainsbury's Bank transition

- Sainsbury's Bank transition costs of £(60) million (2016: £(59) million) were part of the previously announced costs incurred in transitioning to a new, more flexible banking platform as part of the previously announced New Bank Programme.

#### Focus

- Business rationalisation includes £98 million profit on disposals of the Pharmacy business (included within other income) offset by £(26) million of costs incurred closing non-core businesses to enable the Group to focus on its strategy. This included the closure of Netto, Sainsbury's Entertainment and Phoneshops.
- The Group incurred £(57) million in relation to the cessation of non-core IT projects. This includes £(36) million in property, plant and equipment (note 10), £(19) million in intangibles (note 11) and £(2) million other directly attributable costs.

#### Restructuring costs

- Internal restructuring costs of £(33) million relate to changes in store colleague structures and working practices.

#### Other

- The coupons on the perpetual subordinated capital securities and the perpetual subordinated convertible bonds are accounted for as equity in line with IAS 32 'Financial Instruments: Presentation', however are accrued on a straight-line basis and included as an expense within underlying profit before tax.
- Non-underlying finance movements for the financial year comprised £12 million for the Group (2016: £(20) million) and £(2) million for the joint ventures (2016: £(2) million).
- Acquisition adjustments of £8 million (2016: £3 million) reflect the unwind of fair value adjustments arising from the Sainsbury's Bank and Home Retail Group acquisitions.
- Comprises pension financing charge of £(16) million (2016: £(22) million) and defined benefit scheme expenses of £(8) million (2016: £(6) million).

The tax impact of adjusted items is included within note 7.

### 3 Non-GAAP performance measures continued

#### Cash flow statement

The table below shows the impact of non-underlying items on the Group cash flow statement:

|  | 2017<br>£m   | 2016<br>£m  |
|--|--------------|-------------|
| <b>Cash flows from operating activities</b>                    |              |             |
| Defined benefit scheme financing charge and scheme expenses    | (8)          | (6)         |
| Sainsbury's Bank transition                                    | (47)         | (53)        |
| Business rationalisation                                       | (5)          | –           |
| Argos integration costs  | (12)         | –           |
| Transaction costs relating to acquisition of Home Retail Group | (22)         | (12)        |
| Homebase separation  | (2)          | –           |
| Restructuring costs  | (19)         | (19)        |
| <b>Cash used in operating activities</b>                       | <b>(115)</b> | <b>(90)</b> |
| <b>Cash flows from investing activities</b>                    |              |             |
| Profit on disposal of properties                               | 55           | 109         |
| Business rationalisation (sale of Pharmacy business)           | (4)          | 125         |
| <b>Cash generated from investing activities</b>                | <b>51</b>    | <b>234</b>  |
| <b>Net cash flows</b>  | <b>(64)</b>  | <b>144</b>  |

## 4 Segment reporting

### Background

The Group's businesses are organised into four operating segments:

- Retail – Food;
- Retail – General Merchandising & Clothing;
- Financial Services (Sainsbury's Bank plc and Argos Financial Services entities); and
- Property Investments (The British Land Company PLC joint venture and Land Securities Group PLC joint venture).

As discussed in note 2, the Food and General Merchandise & Clothing segments have been aggregated into a Retail segment in the financial statements. The Operating Board assesses the performance of all segments on the basis of underlying profit before tax. All material operations and assets are in the UK. The year ended 11 March 2017 includes 27 weeks of Home Retail Group results.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Segment capital expenditure is the total cost incurred during the period to acquire segment assets that are expected to be used for more than one period.

|   | Retail<br>£m   | Financial<br>Services<br>£m | Property<br>Investment<br>£m | Group<br>£m     |
|---|----------------|-----------------------------|------------------------------|-----------------|
| <b>52 weeks to 11 March 2017</b>                      |                |                             |                              |                 |
| <b>Segment revenue</b>                                |                |                             |                              |                 |
| Retail sales to external customers                    | 25,824         | –                           | –                            | 25,824          |
| Financial Services to external customers              | –              | 407                         | –                            | 407             |
| <b>Underlying revenue</b>                             | <b>25,824</b>  | <b>407</b>                  | <b>–</b>                     | <b>26,231</b>   |
| Acquisition adjustment fair value unwind <sup>1</sup> | –              | (7)                         | –                            | (7)             |
| <b>Revenue</b>  | <b>25,824</b>  | <b>400</b>                  | <b>–</b>                     | <b>26,224</b>   |
| <b>Underlying operating profit</b>                    |                |                             |                              |                 |
| Underlying finance income                             | 18             | –                           | –                            | 18              |
| Underlying finance costs <sup>2</sup>                 | (137)          | –                           | –                            | (137)           |
| Underlying share of post-tax loss from joint ventures | –              | –                           | 12                           | 12              |
| <b>Underlying profit before tax</b>                   | <b>507</b>     | <b>62</b>                   | <b>12</b>                    | <b>581</b>      |
| Non-underlying expense (note 3)                       |                |                             |                              | (78)            |
| <b>Profit before tax</b>                              |                |                             |                              | <b>503</b>      |
| Income tax expense (note 7)                           |                |                             |                              | (126)           |
| <b>Profit for the financial period</b>                |                |                             |                              | <b>377</b>      |
| <b>Assets</b>   |                |                             |                              |                 |
| Investment in joint ventures                          | 4              | –                           | 233                          | 237             |
| <b>Segment assets</b>                                 | <b>13,654</b>  | <b>5,850</b>                | <b>233</b>                   | <b>19,737</b>   |
| <b>Segment liabilities</b>                            | <b>(7,762)</b> | <b>(5,103)</b>              | <b>–</b>                     | <b>(12,865)</b> |
| <b>Other segment items</b>                            |                |                             |                              |                 |
| Capital expenditure <sup>3</sup>                      | 741            | 58                          | –                            | 799             |
| Depreciation expense <sup>4</sup>                     | 593            | 7                           | –                            | 600             |
| Amortisation expense <sup>5</sup>                     | 18             | 10                          | –                            | 28              |
| Net impairment and onerous contract charge            | 37             | –                           | –                            | 37              |
| Share-based payments                                  | 30             | 2                           | –                            | 32              |

1 Represents fair value unwind on loans and advances to customers resulting from the Sainsbury's Bank and Home Retail Group Financial Services acquisitions.

2 The coupons on the perpetual capital securities and the perpetual convertible bonds are accounted for as equity in line with IAS 32 'Financial Instruments: Presentation', however are accrued on a straight-line basis and included as an expense within underlying finance costs, as detailed in note 3.

3 Retail capital expenditure consists of property, plant and equipment additions of £683 million and intangible asset additions of £58 million. Financial Services capital expenditure consists of property, plant and equipment additions of £12 million and intangible asset additions of £46 million.

4 Depreciation within the Retail segment includes a £6 million charge in relation to the unwind of fair value adjustments recognised on acquisition of HRG.

5 Amortisation expense within the Retail segment includes £32 million income in relation to the unwind of fair value adjustments recognised on acquisition of HRG. Amortisation expense within the Financial Services segment includes £6 million charge in relation to the unwind of fair value adjustments recognised on acquisition of Sainsbury's Bank.

## 4 Segment reporting continued

|  | Retail<br>£m | Financial<br>Services<br>£m | Property<br>Investment<br>£m | Group<br>£m |
|--|--------------|-----------------------------|------------------------------|-------------|
| <b>52 weeks to 12 March 2016</b>                               |              |                             |                              |             |
| <b>Segment revenue</b>   |              |                             |                              |             |
| Retail sales to external customers                             | 23,168       | –                           | –                            | 23,168      |
| Financial Services to external customers                       | –            | 327                         | –                            | 327         |
| <b>Underlying revenue</b>                                      | 23,168       | 327                         | –                            | 23,495      |
| Acquisition adjustment fair value unwind <sup>1</sup>          | –            | 11                          | –                            | 11          |
| <b>Revenue</b>   | 23,168       | 338                         | –                            | 23,506      |
| <b>Underlying operating profit</b>                             |              |                             |                              |             |
| Underlying finance income                                      | 19           | –                           | –                            | 19          |
| Underlying finance costs <sup>2</sup>                          | (140)        | –                           | –                            | (140)       |
| Underlying share of post-tax (loss)/profit from joint ventures | (7)          | –                           | 15                           | 8           |
| <b>Underlying profit before tax</b>                            | 507          | 65                          | 15                           | 587         |
| Non-underlying expense (note 3)                                |              |                             |                              | (39)        |
| <b>Profit before tax</b>                                       |              |                             |                              | 548         |
| Income tax expense (note 7)                                    |              |                             |                              | (77)        |
| <b>Profit for the financial period</b>                         |              |                             |                              | 471         |
| <b>Assets</b>  |              |                             |                              |             |
| Investment in joint ventures                                   | 16           | –                           | 311                          | 327         |
| <b>Segment assets</b>  | 12,115       | 4,531                       | –                            | 16,646      |
| <b>Segment liabilities</b>                                     | (6,727)      | (3,881)                     | –                            | (10,608)    |
| <b>Other segment items</b>                                     |              |                             |                              |             |
| Capital expenditure <sup>3</sup>                               | 654          | 35                          | –                            | 689         |
| Depreciation expense   | 552          | 7                           | –                            | 559         |
| Amortisation expense <sup>4</sup>                              | 14           | 11                          | –                            | 25          |
| Net impairment and onerous contract charges <sup>5</sup>       | (1)          | –                           | –                            | (1)         |
| Share-based payments   | 22           | 1                           | –                            | 23          |

1 Represents fair value unwind on loans and advances to customers resulting from the Sainsbury's Bank acquisition.

2 The coupons on the perpetual capital securities and the perpetual convertible bonds are accounted for as equity in line with IAS 32 'Financial Instruments: Presentation', however are accrued on a straight-line basis and included as an expense within underlying finance costs, as detailed in note 3.

3 Retail capital expenditure consists of property, plant and equipment additions of £635 million and intangible asset additions of £19 million. Financial Services capital expenditure consists of property, plant and equipment additions of £20 million and intangible asset additions of £15 million.

4 Amortisation expense within the Financial Services segment includes £10 million of intangible asset amortisation arising from Sainsbury's Bank acquisition fair value adjustments.

5 Net impairment and onerous contract charge includes a £9 million impairment reversal recognised against property, plant and equipment as detailed in note 10.

## 4 Segment reporting continued

### Cash flow

|   | APM<br>reference | 2017<br>Retail<br>£m | 2017<br>Financial<br>Services<br>£m | 2017<br>Group<br>£m | 2016<br>Retail<br>£m | 2016<br>Financial<br>Services<br>£m | 2016<br>Group<br>£m |
|---|------------------|----------------------|-------------------------------------|---------------------|----------------------|-------------------------------------|---------------------|
| <b>Cash flows from operating activities</b>                                       |                  |                      |                                     |                     |                      |                                     |                     |
| Cash generated from/(used in) operations (note 25a)                               |                  | 929                  | 394                                 | 1,323               | 1,024                | (400)                               | 624                 |
| Interest paid   | A                | (95)                 | –                                   | (95)                | (108)                | –                                   | (108)               |
| Corporation tax (paid)/received   |                  | (87)                 | 12                                  | (75)                | (124)                | –                                   | (124)               |
| <b>Net cash generated from/(used in) operating activities</b>                     |                  | <b>747</b>           | <b>406</b>                          | <b>1,153</b>        | 792                  | (400)                               | 392                 |
| <b>Cash flows from investing activities</b>                                       |                  |                      |                                     |                     |                      |                                     |                     |
| Purchase of property, plant and equipment excluding strategic capital expenditure |                  | (530)                | (12)                                | (542)               | (593)                | (53)                                | (646)               |
| Purchase of strategic capital expenditure   | B                | (92)                 | –                                   | (92)                | –                    | –                                   | –                   |
| Purchase of property, plant and equipment   |                  | (622)                | (12)                                | (634)               | (593)                | (53)                                | (646)               |
| Purchase of intangible assets   |                  | (58)                 | (52)                                | (110)               | (34)                 | –                                   | (34)                |
| Proceeds from disposal of property, plant and equipment                           | B                | 55                   | –                                   | 55                  | 109                  | –                                   | 109                 |
| Receipt of advance disposal proceeds  |                  | –                    | –                                   | –                   | 125                  | –                                   | 125                 |
| Acquisition of subsidiaries   | C                | (447)                | –                                   | (447)               | –                    | –                                   | –                   |
| Cash acquired upon acquisition of subsidiaries                                    | C                | 548                  | –                                   | 548                 | –                    | –                                   | –                   |
| Capital return to Home Retail Group plc shareholders                              | C                | (226)                | –                                   | (226)               | –                    | –                                   | –                   |
| Share issuance costs on acquisition of Home Retail Group plc                      | C                | (3)                  | –                                   | (3)                 | –                    | –                                   | –                   |
| Investment in joint ventures  | E                | (16)                 | –                                   | (16)                | (18)                 | –                                   | (18)                |
| Disposal of subsidiaries  | E                | –                    | –                                   | –                   | (1)                  | –                                   | (1)                 |
| Interest received   | A                | 18                   | –                                   | 18                  | 19                   | –                                   | 19                  |
| Dividends and distributions received <sup>1</sup>                                 | B                | 65                   | –                                   | 65                  | 46                   | –                                   | 46                  |
| <b>Net cash used in investing activities</b>                                      |                  | <b>(686)</b>         | <b>(64)</b>                         | <b>(750)</b>        | (347)                | (53)                                | (400)               |
| <b>Cash flows from financing activities</b>                                       |                  |                      |                                     |                     |                      |                                     |                     |
| Proceeds from issuance of ordinary shares   | E                | 6                    | –                                   | 6                   | 8                    | –                                   | 8                   |
| Drawdown of short-term borrowings   | D                | 448                  | –                                   | 448                 | –                    | –                                   | –                   |
| Repayment of short-term borrowings  | D                | (492)                | –                                   | (492)               | (95)                 | –                                   | (95)                |
| Repayment of long-term borrowings   | D                | (130)                | –                                   | (130)               | (238)                | –                                   | (238)               |
| Proceeds from the issue of perpetual capital securities and bonds                 |                  | –                    | –                                   | –                   | 494                  | –                                   | 494                 |
| Purchase of own shares  | E                | –                    | –                                   | –                   | (20)                 | –                                   | (20)                |
| Repayment of capital element of obligations under finance lease payments          | D                | (37)                 | –                                   | (37)                | (30)                 | –                                   | (30)                |
| Interest elements of obligations under finance lease payments                     | A                | (8)                  | –                                   | (8)                 | (9)                  | –                                   | (9)                 |
| Dividends paid on ordinary shares   |                  | (230)                | –                                   | (230)               | (234)                | –                                   | (234)               |
| Dividends paid on perpetual securities  | A                | (23)                 | –                                   | (23)                | (4)                  | –                                   | (4)                 |
| <b>Net cash used in financing activities</b>                                      |                  | <b>(466)</b>         | –                                   | <b>(466)</b>        | (128)                | –                                   | (128)               |
| <b>Intra group funding</b>  |                  |                      |                                     |                     |                      |                                     |                     |
| Bank capital injections   |                  | (130)                | 130                                 | –                   | (137)                | 137                                 | –                   |
| HRG acquisition and AFS loan book refinancing                                     | C                | 585                  | (585)                               | –                   | –                    | –                                   | –                   |
| <b>Net cash generated from/(used in) intra group funding</b>                      |                  | <b>455</b>           | <b>(455)</b>                        | –                   | (137)                | 137                                 | –                   |
| <b>Net increase/(decrease) in cash and cash equivalents</b>                       |                  | <b>50</b>            | <b>(113)</b>                        | <b>(63)</b>         | 180                  | (316)                               | (136)               |
| Elimination of net decrease in Sainsbury's Bank cash and cash equivalents         |                  |                      |                                     | 113                 |                      |                                     | 316                 |
| Decrease in debt  |                  |                      |                                     | 211                 |                      |                                     | 363                 |
| Fair value and other non-cash movements   |                  |                      |                                     | 88                  |                      |                                     | (26)                |
| <b>Movement in net debt</b>   |                  |                      |                                     | <b>349</b>          |                      |                                     | 517                 |
| Opening net debt  |                  |                      |                                     | (1,826)             |                      |                                     | (2,343)             |
| <b>Closing net debt</b>   |                  |                      |                                     | <b>(1,477)</b>      |                      |                                     | (1,826)             |

1 Included within dividends and distributions received of £65 million is £55 million of dividends received from property investment joint ventures.

## 4 Segment reporting continued

Cash flows from operating activities are reconciled as follows:

|   | 2017<br>Retail<br>£m | 2017<br>Financial<br>Services<br>£m | 2017<br>Group<br>£m | 2016<br>Retail<br>£m | 2016<br>Financial<br>Services<br>£m | 2016<br>Group<br>£m |
|---|----------------------|-------------------------------------|---------------------|----------------------|-------------------------------------|---------------------|
| Profit/(loss) before tax <sup>1</sup>                             | 516                  | (13)                                | 503                 | 539                  | 9                                   | 548                 |
| Net finance costs   | 102                  | –                                   | 102                 | 148                  | –                                   | 148                 |
| Share of post-tax loss from joint ventures (note 12) <sup>1</sup> | 37                   | –                                   | 37                  | 11                   | –                                   | 11                  |
| Operating profit/(loss)   | 655                  | (13)                                | 642                 | 698                  | 9                                   | 707                 |
| Adjusted for:   |                      |                                     |                     |                      |                                     |                     |
| Depreciation/amortisation expense                                 | 611                  | 17                                  | 628                 | 566                  | 18                                  | 584                 |
| Non-cash adjustments arising from acquisitions (note 3)           | 5                    | 7                                   | 12                  | –                    | (13)                                | (13)                |
| Financial Services impairment losses on loans and advances        | –                    | 33                                  | 33                  | –                    | 15                                  | 15                  |
| Profit on disposal of properties                                  | (101)                | –                                   | (101)               | (100)                | –                                   | (100)               |
| Loss on disposal of intangibles                                   | 22                   | 14                                  | 36                  | –                    | –                                   | –                   |
| Profit on disposal of Pharmacy business                           | (98)                 | –                                   | (98)                | –                    | –                                   | –                   |
| Impairment charge/(reversal) of property, plant & equipment       | 55                   | –                                   | 55                  | (9)                  | –                                   | (9)                 |
| Foreign exchange differences                                      | (7)                  | –                                   | (7)                 | 24                   | –                                   | 24                  |
| Share-based payments expense                                      | 30                   | 2                                   | 32                  | 23                   | –                                   | 23                  |
| Retirement benefit obligations                                    | (112)                | –                                   | (112)               | (76)                 | –                                   | (76)                |
| Exceptional pension contributions                                 | (199)                | –                                   | (199)               | (125)                | –                                   | (125)               |
| <b>Operating cash flows before changes in working capital</b>     | <b>861</b>           | <b>60</b>                           | <b>921</b>          | 1,001                | 29                                  | 1,030               |
| Decrease/(increase) in working capital                            | 68                   | 334                                 | 402                 | 23                   | (429)                               | (406)               |
| <b>Cash generated from/(used in) operations</b>                   | <b>929</b>           | <b>394</b>                          | <b>1,323</b>        | 1,024                | (400)                               | 624                 |

1 Includes £(18) million relating to the Property Investment segment.

## 5 Operating profit

### Accounting policies

#### Revenue

Revenue consists of sales through retail outlets and online and, in the case of Financial Services, interest receivable, fees and commissions and excludes Value Added Tax. Revenue is recognised when the significant risks and rewards of goods and services have been passed to the buyer and it can be measured reliably.

#### a) Retail – sale of goods

Sales through retail outlets are shown net of returns, the cost of Nectar reward points issued and redeemed, colleague discounts, vouchers and sales made on an agency basis. Commission income is recognised in revenue based on the terms of the contract.

Sales of in-store goods are generally recognised at the point of cash receipt. Where Nectar credits such as vouchers or loyalty points are provided as part of the sales transaction, the amount allocated to the credits is deferred and recognised when the credits are redeemed and the Group fulfils its obligations to supply the credit. For delivered goods, sales are recognised when the goods have been delivered.

#### b) Other income

Other income generally consists of profits and losses on disposal of assets. Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term.

#### c) Financial Services interest receivable

Interest income is recognised in the income statement for all instruments measured at amortised cost using the effective interest method. This calculation takes into account all amounts that are integral to the yield as well as incremental transaction costs. The effective interest rate is the rate that discounts the expected future cash flows over the expected life of the financial instrument to the net carrying amount of the financial asset or liability at initial recognition.

#### d) Financial Services fees and commissions

Fees and commissions that are not integral to the effective interest rate calculation relate primarily to certain credit card and storecard fees, ATM interchange fees, insurance introduction commission and warranty commission receivable. These are recognised in the income statement on an accruals basis as services are provided. Where in the case of insurance commissions the income comprises an initial commission and profit share, both are recognised on completion of the service to the extent reliably measurable. Where there is a risk of potential claw back, an appropriate element of the commission receivable is deferred and amortised over the clawback period. Where the relevant contract requires Financial Services to perform future services in respect of the income receivable, initial commission is recognised on completion of the service provided, with an element deferred to reflect services yet to be performed in future periods.

#### e) Financial Services other operating income

Margin from the sale of travel money, representing the difference between the cost price and the selling price, is recognised when the sale to the customer takes place within other operating income.

#### Cost of sales

Cost of sales consists of all costs that are directly attributable to the point of sale including warehouse, transportation costs and all the costs of operating retail outlets. In the case of Financial Services, cost of sales includes interest expense on operating activities, calculated using the effective interest method.

## 5 Operating profit continued

Operating profit is stated after charging/(crediting) the following items:

|   | 2017<br>£m   | 2016<br>£m |
|---|--------------|------------|
| Employee costs (note 28)                                      | <b>2,878</b> | 2,541      |
| Depreciation expense (note 10) <sup>1</sup>                   | <b>600</b>   | 559        |
| Amortisation expense (note 11) <sup>2</sup>                   | <b>28</b>    | 25         |
| Profit on disposal of properties (note 3) <sup>3</sup>        | <b>(101)</b> | (100)      |
| Operating lease rentals                                       |              |            |
| – land and buildings  | <b>625</b>   | 532        |
| – other leases  | <b>80</b>    | 73         |
| – sublease payments receivable                                | <b>(53)</b>  | (49)       |
| Foreign exchange (gains)/losses                               | <b>(7)</b>   | 24         |
| Impairment losses on loans and advances                       | <b>33</b>    | 15         |
| Impairment and onerous contract charges (note 3) <sup>4</sup> | <b>(37)</b>  | (1)        |
| IT write-offs (note 3)  | <b>(57)</b>  | –          |

1 Depreciation expense includes £6 million (2016: £nil) in relation to the unwind of acquisition adjustments.

2 Amortisation expense includes £32 million income (2016: £nil) in relation to the unwind of fair value adjustments recognised on acquisition of HRG, and a £6 million charge (2016: £10 million charge) in relation to the unwind of fair value adjustments recognised on acquisition of Sainsbury's Bank.

3 Included within other income of £215 million, along with gain on sale of Pharmacy business of £98 million (note 3).

4 Includes an impairment reversal of £19 million (2016: £9 million reversal) recognised against property, plant and equipment as detailed in note 10.

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| <b>Auditors' remuneration</b>  |            |            |
| Fees payable to the Company's auditors for the audit of the parent company and consolidated financial statements | <b>0.8</b> | 0.3        |
| Fees payable to the Company's auditors for other services:   |            |            |
| The audit of the Company's subsidiaries  | <b>0.9</b> | 0.4        |
| Audit related assurance services   | <b>0.1</b> | 0.1        |
| Tax advisory, tax compliance and other non-audit fees  | <b>0.1</b> | 0.0        |
| <b>Total fees</b>  | <b>1.9</b> | 0.8        |

The increase in auditors' remuneration is as a result of the acquisition of Home Retail Group during the year.

## 6 Finance income and finance costs

### Accounting policies

Finance income and costs, excluding those arising from Financial Services, are recognised in the income statement for financial assets and liabilities measured at amortised cost using the effective interest method. For Financial Services, finance income and finance costs are recognised in revenue and cost of sales.

Interest paid and interest received for the purpose of the cash flow statement relates to retail only, with Financial Services interest paid and interest received included in the net operating cash flow.

The coupons on the perpetual capital securities and perpetual convertible bonds are accounted for as dividends in accordance with IAS 32 'Financial Instruments: Presentation' and hence are not a finance cost.

|  | 2017<br>£m   | 2016<br>£m |
|--|--------------|------------|
| Interest on bank deposits and other financial assets | 18           | 19         |
| Finance fair value movements <sup>1</sup>            | 16           | –          |
| <b>Finance income</b>                                | <b>34</b>    | 19         |
| Borrowing costs:                                     |              |            |
| Secured borrowings                                   | (81)         | (88)       |
| Unsecured borrowings                                 | (30)         | (30)       |
| Obligations under finance leases                     | (8)          | (9)        |
| Provisions – amortisation of discount (note 18)      | (6)          | (5)        |
|  | <b>(125)</b> | (132)      |
| Other finance costs:                                 |              |            |
| Interest capitalised – qualifying assets (note 10)   | 7            | 7          |
| Finance fair value movements <sup>1</sup>            | –            | (20)       |
| IAS 19 pension financing charge (note 29)            | (16)         | (22)       |
| Interest expense on Pharmacy sale advance proceeds   | (2)          | –          |
|  | <b>(11)</b>  | (35)       |
| <b>Finance costs</b>                                 | <b>(136)</b> | (167)      |

1 Finance fair value movements relate to net fair value movements on derivative financial instruments not designated in a hedging relationship.

## 7 Taxation

### Accounting policies

#### Current tax

Current tax is accounted for on the basis of tax laws enacted or substantively enacted at the balance sheet date. Current tax is charged or credited to the income statement, except when it relates to items charged to equity or other comprehensive income.

#### Deferred tax

Deferred tax is accounted for on the basis of temporary differences arising from differences between the tax base and accounting base of assets and liabilities.

Deferred tax is recognised for all temporary differences, except to the extent where it arises from the initial recognition of an asset or a liability in a transaction that is not a business combination and, at the time of transaction, affects neither accounting profit nor taxable profit. It is determined using tax rates (and laws) that have been enacted or substantively 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 tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Deferred tax is charged or credited to the income statement, except when it relates to items charged or credited directly to equity or other comprehensive income.

Deferred tax is provided on temporary differences associated with investments in subsidiaries, branches and joint ventures except where the Group is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

### Income tax expense

|   | 2017<br>£m   | 2016<br>£m |
|---|--------------|------------|
| Current tax expense:                                |              |            |
| Current year UK tax                                 | 124          | 105        |
| Over-provision in prior years                       | (11)         | (17)       |
| <b>Total current tax expense</b>                    | <b>113</b>   | 88         |
| Deferred tax charge/(credit):                       |              |            |
| Origination and reversal of temporary differences   | 17           | 17         |
| Under-provision in prior years                      | 14           | 7          |
| Revaluation of deferred tax balances                | (18)         | (35)       |
| <b>Total deferred tax charge/(credit)</b>           | <b>13</b>    | (11)       |
| <b>Total income tax expense in income statement</b> | <b>126</b>   | 77         |
| Analysed as:  |              |            |
| Underlying tax                                      | 135          | 122        |
| Non-underlying tax                                  | (9)          | (45)       |
| <b>Total income tax expense in income statement</b> | <b>126</b>   | <b>77</b>  |
| Underlying tax rate                                 | <b>23.2%</b> | 20.8%      |
| Effective tax rate                                  | <b>25.0%</b> | 14.1%      |

## 7 Taxation continued

The effective tax rate of 25.0 per cent (2016: 14.1 per cent) is higher than (2016: lower than) the standard rate of corporation tax in the UK. The differences are explained below:

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| <b>Profit before tax</b>   | <b>503</b> | 548        |
| Income tax at UK corporation tax rate of 20.0% (2016: 20.05%)      | <b>101</b> | 110        |
| Effects of underlying items:                                       |            |            |
| Disallowed depreciation on UK properties                           | <b>27</b>  | 26         |
| Over-provision in prior years                                      | <b>(1)</b> | (1)        |
| Revaluation of deferred tax balances                               | <b>(9)</b> | (20)       |
| Other  | <b>2</b>   | (1)        |
| Effects of non-underlying items: <sup>1</sup>                      |            |            |
| Profit on disposal of properties                                   | <b>(8)</b> | (21)       |
| Investment property fair value movements                           | <b>5</b>   | 4          |
| Net impairment and onerous contract charge                         | <b>6</b>   | –          |
| Transaction costs relating to the acquisition of Home Retail Group | <b>4</b>   | 3          |
| Argos integration costs  | <b>1</b>   | –          |
| Homebase separation  | <b>1</b>   | –          |
| Business rationalisation   | –          | 1          |
| IT write-offs  | <b>1</b>   | –          |
| Non-underlying finance movements                                   | <b>1</b>   | –          |
| Under/(over) provision in prior years                              | <b>4</b>   | (9)        |
| Revaluation of deferred tax balances                               | <b>(9)</b> | (15)       |
| <b>Total income tax expense in income statement</b>                | <b>126</b> | 77         |

1 Disclosed where the tax on non-underlying items differs from the statutory rate.

The main rate of UK corporation tax is reducing from 20 per cent to 19 per cent effective from 1 April 2017. A further reduction in the corporation tax rate to 17 per cent, rather than 18 per cent, effective from 1 April 2020 was substantively enacted in the year, so its effect is reflected in these financial statements. Deferred tax on temporary differences and tax losses as at the balance sheet date is calculated at the substantively enacted rates at which the temporary differences and tax losses are expected to reverse.

Income tax charged or (credited) to equity and/or other comprehensive income during the year is as follows:

|   | Retirement<br>benefit<br>obligations <sup>1</sup><br>£m | Fair value<br>movements <sup>1</sup><br>£m | Perpetual<br>security<br>coupons <sup>2</sup><br>£m | Total<br>£m |
|---|---|--|---|-------------|
| <b>52 weeks to 11 March 2017</b>                                |   |  |   |             |
| Current tax recognised in equity or other comprehensive income  | <b>(41)</b>   | <b>1</b>                                   | <b>(5)</b>  | <b>(45)</b> |
| Deferred tax recognised in equity or other comprehensive income | <b>(28)</b>   | <b>(5)</b>                                 | –   | <b>(33)</b> |
| Income tax charged/(credited)                                   | <b>(69)</b>   | <b>(4)</b>                                 | <b>(5)</b>  | <b>(78)</b> |
| <b>52 weeks to 12 March 2016</b>                                |   |  |   |             |
| Current tax recognised in equity or other comprehensive income  | –   | –  | (6)   | (6)         |
| Deferred tax recognised in equity or other comprehensive income | 36  | (3)  | –   | 33          |
| Income tax charged/(credited)                                   | 36  | (3)  | (6)   | 27          |

1 Recognised in other comprehensive income.

2 Recognised in equity.

The current and deferred tax in relation to the Group's defined benefit pension scheme's remeasurements, available-for-sale fair value movements and perpetual securities coupons have been charged or credited through other comprehensive income where appropriate.

## 7 Taxation continued

### Deferred tax

The movements in deferred income tax assets and liabilities during the financial year, prior to the offsetting of the balances within the same tax jurisdiction, are shown below.

|  | Accelerated capital allowances<br>£m | Capital losses<br>£m | Fair value movements<br>£m | Rolled over capital gains<br>£m | Retirement benefit obligations<br>£m | Share-based payments<br>£m | Other<br>£m        | Total<br>£m        |
|--|--------------------------------------|----------------------|----------------------------|---------------------------------|--------------------------------------|----------------------------|--------------------|--------------------|
| At 13 March 2016   | (159)                                | 51                   | (25)                       | (95)                            | 19                                   | 7                          | (35)               | (237)              |
| Acquisition of subsidiaries  | (19)                                 | –                    | (28)                       | –                               | 82                                   | 1                          | 9                  | 45                 |
| Prior year adjustment to income statement                                      | (16)                                 | (12)                 | –                          | 15                              | –                                    | –                          | (1)                | (14)               |
| Prior year adjustment to equity or other comprehensive income                  | –                                    | –                    | 9                          | –                               | –                                    | –                          | –                  | 9                  |
| Credit/(charge) to income statement  | 21                                   | (7)                  | (2)                        | (10)                            | (6)                                  | –                          | (13)               | (17)               |
| (Charge)/credit to equity or other comprehensive income                        | –                                    | –                    | (6)                        | –                               | 40                                   | –                          | –                  | 34                 |
| Rate change adjustment to income statement                                     | 7                                    | (1)                  | 2                          | 6                               | 1                                    | –                          | 3                  | 18                 |
| Rate change adjustment to equity or other comprehensive income                 | –                                    | –                    | 2                          | –                               | (12)                                 | –                          | –                  | (10)               |
| <b>At 11 March 2017</b>  | <b>(166)</b>                         | <b>31</b>            | <b>(48)</b>                | <b>(84)</b>                     | <b>124</b>                           | <b>8</b>                   | <b>(37)</b>        | <b>(172)</b>       |
| At 15 March 2015   | (162)                                | 52                   | (29)                       | (97)                            | 57                                   | 6                          | (42)               | (215)              |
| Prior year adjustment to income statement                                      | (10)                                 | 1                    | 1                          | –                               | –                                    | –                          | 1                  | (7)                |
| (Charge)/credit to income statement  | (5)                                  | 4                    | –                          | (8)                             | (12)                                 | 2                          | 2                  | (17)               |
| Charge to equity or other comprehensive income                                 | –                                    | –                    | –                          | –                               | (24)                                 | –                          | –                  | (24)               |
| Rate change adjustment to income statement                                     | 18                                   | (6)                  | –                          | 10                              | 10                                   | (1)                        | 4                  | 35                 |
| Rate change adjustment to equity or other comprehensive income                 | –                                    | –                    | 3                          | –                               | (12)                                 | –                          | –                  | (9)                |
| At 12 March 2016   | (159)                                | 51                   | (25)                       | (95)                            | 19                                   | 7                          | (35)               | (237)              |
|  |                                      |                      |                            |                                 |                                      |                            | <b>2017<br/>£m</b> | <b>2016<br/>£m</b> |
| Total deferred income tax liabilities  |                                      |                      |                            |                                 |                                      |                            | <b>(335)</b>       | (314)              |
| Total deferred income tax assets   |                                      |                      |                            |                                 |                                      |                            | <b>163</b>         | 77                 |
| <b>Net deferred income tax liability recognised in non-current liabilities</b> |                                      |                      |                            |                                 |                                      |                            | <b>(172)</b>       | (237)              |

Deferred income tax assets have been recognised in respect of all temporary differences and tax losses giving rise to deferred income tax assets because it is probable that these assets will be recovered. Deferred income tax assets and liabilities are only offset where there is a legally enforceable right of offset and the deferred income tax assets and the deferred income tax liabilities relate to income taxes levied by the same taxation authority.

## 8 Earnings per share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the year, excluding those held by the Employee Share Ownership Plan trusts (note 22), which are treated as cancelled. For diluted earnings per share, the earnings attributable to the ordinary shareholders are adjusted by the interest on the senior convertible bonds (net of tax) and by the coupons on the perpetual subordinated convertible bonds (net of tax).

The weighted average number of ordinary shares in issue is adjusted to assume conversion of all potentially dilutive 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 year and the number of shares that would be issued if all senior convertible bonds and perpetual subordinated convertible bonds are assumed to be converted.

Underlying earnings per share is provided by excluding the effect of any non-underlying items as defined in note 3. This alternative measure of earnings per share is presented to reflect the Group's underlying trading performance.

## 8 Earnings per share continued

All operations are continuing for the periods presented.

|  | 2017<br>million | 2016<br>million |
|--|-----------------|-----------------|
| Weighted average number of shares in issue                                   | <b>2,049.0</b>  | 1,920.8         |
| Weighted average number of dilutive share options                            | <b>18.2</b>     | 14.6            |
| Weighted average number of dilutive senior convertible bonds                 | <b>137.7</b>    | 131.4           |
| Weighted average number of dilutive subordinated perpetual convertible bonds | <b>75.1</b>     | 41.4            |
| Total number of shares for calculating diluted earnings per share            | <b>2,280.0</b>  | 2,108.2         |

|   | £m          | £m  |
|---|-------------|-----|
| Profit for the financial period (net of tax)                        | <b>377</b>  | 471 |
| Less profit attributable to:  |             |     |
| Holders of perpetual capital securities                             | <b>(12)</b> | (8) |
| Holders of perpetual convertible bonds                              | <b>(6)</b>  | (4) |
| Profit for the financial year attributable to ordinary shareholders | <b>359</b>  | 459 |

|   | £m         | £m  |
|---|------------|-----|
| Profit for the financial period attributable to ordinary shareholders | <b>359</b> | 459 |
| Add interest on senior convertible bonds (net of tax)                 | <b>12</b>  | 11  |
| Add coupon on subordinated perpetual convertible bonds (net of tax)   | <b>6</b>   | 4   |
| Diluted earnings for calculating diluted earnings per share           | <b>377</b> | 474 |

|   | £m         | £m   |
|---|------------|------|
| Profit for the financial year attributable to ordinary shareholders of the parent       | <b>359</b> | 459  |
| Adjusted for non-underlying items (note 3)  | <b>78</b>  | 39   |
| Tax on non-underlying items   | <b>(9)</b> | (45) |
| Add back coupons on perpetual securities (net of tax) <sup>1</sup>                      | <b>18</b>  | 12   |
| Underlying profit after tax attributable to ordinary shareholders of the parent         | <b>446</b> | 465  |
| Add interest on convertible bonds (net of tax)  | <b>12</b>  | 11   |
| Add coupon on subordinated perpetual convertible bonds (net of tax)                     | <b>6</b>   | 4    |
| Diluted underlying profit after tax attributable to ordinary shareholders of the parent | <b>464</b> | 480  |

|                             | Pence<br>per<br>share | Pence<br>per<br>share |
|-----------------------------|-----------------------|-----------------------|
| Basic earnings              | <b>17.5</b>           | 23.9                  |
| Diluted earnings            | <b>16.5</b>           | 22.5                  |
| Underlying basic earnings   | <b>21.8</b>           | 24.2                  |
| Underlying diluted earnings | <b>20.4</b>           | 22.8                  |

<sup>1</sup> Underlying earnings per share calculation is based on underlying profit after tax attributable to ordinary shareholders. Therefore the coupons on the perpetual securities (note 21) are added back.

## 9 Dividends

|   | 2017<br>Pence per<br>share | 2016<br>Pence per<br>share | 2017<br>£m | 2016<br>£m |
|---|----------------------------|----------------------------|------------|------------|
| Amounts recognised as distributions to ordinary shareholders in the year: |                            |                            |            |            |
| Final dividend of prior financial year                                    | <b>8.1</b>                 | 8.2                        | <b>155</b> | 157        |
| Interim dividend of current financial year                                | <b>3.6</b>                 | 4.0                        | <b>77</b>  | 77         |
|   | <b>11.7</b>                | 12.2                       | <b>232</b> | 234        |

After the balance sheet date on 2 May 2017, a final dividend of 6.6 pence per share (2016: 8.1 pence per share) was proposed by the Directors in respect of the 52 weeks to 11 March 2017. This results in a total final proposed dividend of £144 million (2016: £155 million), a decrease of 7.1 per cent on the previous year. Subject to shareholders' approval at the Annual General Meeting, the dividend will be paid on 7 July 2017 to the shareholders on the register at 12 May 2017. The proposed final dividend has not been included as a liability at 11 March 2017.

Of the above dividend of £232 million, £2 million remained unpaid at the year-end.

## 10 Property, plant and equipment

### Accounting policies

#### a) Land and buildings

Land and buildings are held at historical cost less accumulated depreciation and any recognised provision for impairment. Capital work in progress is held at cost less any recognised provision for impairment. Cost includes the original purchase price of the asset and the costs to bringing the asset to its working condition for intended use. This includes capitalised borrowing costs.

#### b) Fixtures and equipment

Fixtures, equipment and vehicles are held at cost less accumulated depreciation and any recognised provision for impairment. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition and its intended use.

#### c) Depreciation

Depreciation is calculated to write down the cost of the assets to their residual values, on a straight-line basis, using the following rates:

- Freehold buildings and leasehold properties – 50 years, or the lease term if shorter
- Fixtures, equipment and vehicles – three to 15 years
- Freehold land is not depreciated

Capital work in progress is not depreciated.

Gains and losses on disposal are determined by comparing proceeds less any associated costs of disposal with the asset's carrying amount and are recognised within operating profit.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

### Impairment of non-financial assets

At each reporting date, the Group reviews the carrying amounts of its property, plant and equipment to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset, being the higher of its fair value less costs to dispose and its value in use, is estimated in order to determine the extent of the impairment loss.

Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit (CGU) to which the asset belongs. For Retail property, plant and equipment, the CGU is deemed to be each trading store or store pipeline development site. Non-store assets, including depots and IT assets, are reviewed separately, whilst Financial Services is deemed a separate CGU.

Any impairment loss is recognised in the income statement in the year in which it occurs. Where an impairment loss subsequently reverses due to a change in the original estimate, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, or its original carrying value less notional accumulated depreciation if lower.

### Capitalisation of interest

Borrowing costs that are directly attributable to the acquisition or construction of qualifying assets are capitalised to the cost of the asset, gross of tax relief.

### Leased assets

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership to the Group. All other leases are classified as operating leases. For property leases, the land and building elements are treated separately to determine the appropriate lease classification.

#### a) Finance leases

Assets funded through finance leases are capitalised as property, plant and equipment and depreciated over the shorter of their estimated useful lives or the lease term. The amount capitalised is the lower of the fair value of the asset or the present value of the minimum lease payments during the lease term. The resulting lease obligations are included in liabilities net of finance charges. Finance costs on finance leases are charged directly to the income statement.

#### b) Lease incentives

Lease incentives primarily include up-front cash payments or rent-free periods. Lease incentives are capitalised and spread over the period of the lease term.

#### c) Leases with predetermined fixed rental increases

The Group has a number of leases with predetermined fixed rental increases. These rental increases are accounted for on a straight-line basis over the term of the lease.

## 10 Property, plant and equipment continued

|  | Land and buildings<br>£m | Fixtures and equipment<br>£m | Total<br>£m   |
|--|--------------------------|------------------------------|---------------|
| <b>Cost</b>                                    |                          |                              |               |
| At 13 March 2016                               | <b>10,114</b>            | <b>5,145</b>                 | <b>15,259</b> |
| Acquisition of subsidiaries (note 31)          | <b>111</b>               | <b>151</b>                   | <b>262</b>    |
| Additions                                      | <b>301</b>               | <b>394</b>                   | <b>695</b>    |
| Disposals                                      | <b>(71)</b>              | <b>(607)</b>                 | <b>(678)</b>  |
| Transfer to assets held for resale             | <b>(11)</b>              | <b>–</b>                     | <b>(11)</b>   |
| Exchange differences                           | <b>1</b>                 | <b>1</b>                     | <b>2</b>      |
| <b>At 11 March 2017</b>                        | <b>10,445</b>            | <b>5,084</b>                 | <b>15,529</b> |
| <b>Accumulated depreciation and impairment</b> |                          |                              |               |
| At 13 March 2016                               | <b>2,313</b>             | <b>3,182</b>                 | <b>5,495</b>  |
| Depreciation expense for the year              | <b>193</b>               | <b>407</b>                   | <b>600</b>    |
| Impairment loss for the year <sup>1</sup>      | <b>17</b>                | <b>38</b>                    | <b>55</b>     |
| Disposals                                      | <b>(28)</b>              | <b>(599)</b>                 | <b>(627)</b>  |
| Transfer to assets held for resale             | <b>(1)</b>               | <b>–</b>                     | <b>(1)</b>    |
| Exchange differences                           | <b>–</b>                 | <b>1</b>                     | <b>1</b>      |
| <b>At 11 March 2017</b>                        | <b>2,494</b>             | <b>3,029</b>                 | <b>5,523</b>  |
| <b>Net book value at 11 March 2017</b>         | <b>7,951</b>             | <b>2,055</b>                 | <b>10,006</b> |
| <b>Capital work-in-progress included above</b> | <b>213</b>               | <b>86</b>                    | <b>299</b>    |
| <b>Cost</b>                                    |                          |                              |               |
| At 15 March 2015                               | 9,932                    | 4,922                        | 14,854        |
| Additions                                      | 259                      | 396                          | 655           |
| Disposals                                      | (152)                    | (173)                        | (325)         |
| Transfer to assets held for resale             | 75                       | –                            | 75            |
| At 12 March 2016                               | 10,114                   | 5,145                        | 15,259        |
| <b>Accumulated depreciation and impairment</b> |                          |                              |               |
| At 15 March 2015                               | 2,249                    | 2,957                        | 5,206         |
| Depreciation expense for the year              | 166                      | 393                          | 559           |
| Impairment reversal for the year               | (9)                      | –                            | (9)           |
| Disposals                                      | (97)                     | (168)                        | (265)         |
| Transfer to assets held for resale             | 4                        | –                            | 4             |
| At 12 March 2016                               | 2,313                    | 3,182                        | 5,495         |
| <b>Net book value at 12 March 2016</b>         | <b>7,801</b>             | <b>1,963</b>                 | <b>9,764</b>  |
| <b>Capital work-in-progress included above</b> | <b>259</b>               | <b>83</b>                    | <b>342</b>    |

<sup>1</sup> Comprises an impairment reversal of £17 million which was recognised on land where there has been an increase in the market value during the year, and an impairment charge of £72 million recognised on assets where impairment indicators existed. Net charge of £55 million comprises £36 million of non-core IT assets, and £19 million of other fixed asset impairments, both as detailed in note 3.

## 10 Property, plant and equipment continued

### Interest capitalised

Interest capitalised included in additions amounted to £7 million (2016: £7 million) for the Group. Accumulated interest capitalised included in the cost of property, plant and equipment net of disposals amounted to £352 million (2016: £348 million) for the Group. The capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation is 4.0 per cent (2016: 4.0 per cent).

### Security

Property, plant and equipment pledged as security is as follows:

|   | 2017<br>Number of<br>properties | 2017<br>Net book<br>value<br>£bn | 2016<br>Number of<br>properties | 2016<br>Net book<br>value<br>£bn |
|---|---------------------------------|----------------------------------|---------------------------------|----------------------------------|
| Loan due 2018 and loan due 2031           | 125                             | 2.6                              | 125                             | 2.6                              |
| Revolving credit facility                 | 60                              | 1.3                              | 60                              | 1.4                              |
| Sainsbury's Property Scottish partnership | 24                              | 0.6                              | 24                              | 0.6                              |
| Other                                     | 16                              | 0.3                              | 16                              | 0.3                              |
|   | <b>225</b>                      | <b>4.8</b>                       | 225                             | 4.9                              |

### Analysis of assets held under finance leases

|   | 2017<br>Land and<br>buildings<br>£m | 2017<br>Fixtures and<br>equipment<br>£m | 2017<br>Total<br>£m | 2016<br>Land and<br>buildings<br>£m | 2016<br>Fixtures and<br>equipment<br>£m | 2016<br>Total<br>£m |
|---|-------------------------------------|---|---------------------|-------------------------------------|---|---------------------|
| Cost                                    | 82                                  | 1                                       | 83                  | 82                                  | –                                       | 82                  |
| Accumulated depreciation and impairment | (33)                                | –                                       | (33)                | (30)                                | –                                       | (30)                |
| Net book value                          | 49                                  | 1                                       | 50                  | 52                                  | –                                       | 52                  |

## 11 Intangible assets

### Accounting policies

#### a) Goodwill

Goodwill represents the excess of the fair value of the consideration of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill is considered to have an indefinite useful life. Goodwill is tested for impairment annually and again whenever indicators of impairment are detected and is carried at cost less any provision for impairment.

#### b) Computer software

Computer software is carried at cost less accumulated amortisation and any provision for impairment. Externally acquired computer software and software licences are amortised on a straight-line basis over their useful economic lives of five to ten years. Costs relating to development of computer software for internal use are capitalised once the recognition criteria of IAS 38, 'Intangible Assets' are met. Other development expenditures that do not meet these criteria are expensed as incurred. When the software is available for its intended use, these costs are amortised on a straight-line basis over their useful economic lives of five to ten years within administrative expenses.

#### c) Acquired intangible assets

Intangible assets acquired in a business combination are recognised at fair value at the acquisition date. Intangible assets with finite useful economic lives are carried at cost less accumulated amortisation and any provision for impairment and are amortised on a straight-line basis over their estimated useful economic lives, ranging from three to ten years, within administrative expenses.

### Impairment of non-financial assets

At each reporting date, the Group reviews the carrying amounts of its intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset, being the higher of its fair value less costs to dispose and its value in use, is estimated in order to determine the extent of the impairment loss.

Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit (CGU) to which the asset belongs. For retail goodwill, the CGU is deemed to be each retail chain of stores acquired. Non-store assets, including IT assets, are reviewed separately, whilst Financial Services is deemed a separate CGU.

Any impairment loss is recognised in the income statement in the year in which it occurs. Where an impairment loss, other than an impairment loss on goodwill, subsequently reverses due to a change in the original estimate, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, or its original carrying value less notional accumulated depreciation if lower.

## 11 Intangible assets continued

|                                       | Goodwill<br>£m | Computer<br>software<br>£m | Acquired<br>intangibles<br>£m | Other<br>£m | Total<br>£m |
|---------------------------------------|----------------|----------------------------|-------------------------------|-------------|-------------|
| <b>Cost</b>                           |                |                            |                               |             |             |
| At 13 March 2016                      | 142            | 231                        | 39                            | 10          | 422         |
| Reclassification                      | –              | 10                         | –                             | (10)        | –           |
| Acquisition of subsidiaries (note 31) | 58             | 143                        | 179                           | –           | 380         |
| Additions                             | –              | 104                        | –                             | –           | 104         |
| Disposals                             | (7)            | (59)                       | –                             | –           | (66)        |
| <b>At 11 March 2017</b>               | <b>193</b>     | <b>429</b>                 | <b>218</b>                    | <b>–</b>    | <b>840</b>  |

### Accumulated amortisation and impairment

|                                   |          |           |           |          |           |
|-----------------------------------|----------|-----------|-----------|----------|-----------|
| At 13 March 2016                  | 4        | 59        | 29        | 1        | 93        |
| Reclassification                  | –        | 1         | –         | (1)      | –         |
| Amortisation expense for the year | –        | 13        | 15        | –        | 28        |
| Disposals                         | –        | (23)      | –         | –        | (23)      |
| <b>At 11 March 2017</b>           | <b>4</b> | <b>50</b> | <b>44</b> | <b>–</b> | <b>98</b> |

### Net book value at 11 March 2017

**189      379      174      –      742**

### Cost

|                                    |     |     |    |      |      |
|------------------------------------|-----|-----|----|------|------|
| At 15 March 2015                   | 143 | 197 | 39 | 49   | 428  |
| Additions                          | –   | 34  | –  | –    | 34   |
| Disposals                          | (1) | –   | –  | –    | (1)  |
| Transfer to assets held for resale | –   | –   | –  | (39) | (39) |
| At 12 March 2016                   | 142 | 231 | 39 | 10   | 422  |

### Accumulated amortisation and impairment

|                                    |   |    |    |      |      |
|------------------------------------|---|----|----|------|------|
| At 15 March 2015                   | 4 | 44 | 19 | 36   | 103  |
| Amortisation expense for the year  | – | 15 | 10 | –    | 25   |
| Transfer to assets held for resale | – | –  | –  | (35) | (35) |
| At 12 March 2016                   | 4 | 59 | 29 | 1    | 93   |

### Net book value at 12 March 2016

138      172      10      9      329

Goodwill comprises the following:

|                         | 2017<br>£m | 2016<br>£m |
|-------------------------|------------|------------|
| Jacksons Stores Limited | 47         | 53         |
| Home Retail Group plc   | 58         | –          |
| Sainsbury's Bank plc    | 45         | 45         |
| Bells Stores Limited    | 16         | 17         |
| Other                   | 23         | 23         |
|                         | <b>189</b> | <b>138</b> |

The goodwill balances above are allocated to the respective cash-generating units (CGUs) or group of CGUs within the Retail or Financial Services segment. The CGUs to which goodwill has been allocated and the level at which it is monitored in the retailing segment are deemed to be the respective acquired retail chains of stores, whilst Financial Services is a separate CGU.

The value of the goodwill was tested for impairment during the current financial year by means of comparing the recoverable amount of each CGU or group of CGUs with the carrying value of its goodwill. The calculation of the Retail CGU's value in use is calculated on the cash flows expected to be generated by the stores using the latest budget and forecast data. Board approved cash flow projections for five years are used and then extrapolated out assuming flat cash flows and discounted at a pre-tax rate of nine per cent (2016: nine per cent) over the earlier of a 25 year period (being the estimated average remaining useful life of a freehold store) or lease length for leasehold stores. Financial Services CGU's value in use is calculated using Board approved cash flows discounted at a pre-tax rate of nine per cent (2016: nine per cent) over a five year period with a terminal value.

Based on the operating performance of the CGUs, an impairment of goodwill of £nil million was identified in the current financial year (2016: £nil million). The valuations indicate sufficient headroom such that a reasonably possible change to key assumptions would not result in any impairment of goodwill.

Additions to acquired intangibles arose from the acquisition of HRG and relates to the Argos brand. This is being amortised over ten years.

## 12 Investments in joint ventures and associates

### Accounting policies

The Group applies IFRS 11 to all joint arrangements. Under IFRS 11, investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations of each investor. The Group has assessed the nature of its joint arrangements and determined them to be joint ventures. The Group's share of the post-tax results of its joint ventures and associates is included in the income statement using the equity method of accounting. Where the Group transacts with a joint venture or associate, profits and losses are eliminated to the extent of the Group's interest in the joint venture or associate.

Investments in joint ventures and associates are carried in the Group balance sheet at historical cost plus post-acquisition changes in the Group's share of net assets of the entity, less any provision for impairment.

Associates are entities over which the Group has significant influence but not control.

The Group's principal joint venture is:

|   | Statutory year-end | Share of ordinary allotted capital | Country of registration or incorporation |
|---|--------------------|------------------------------------|--|
| BL Sainsbury Superstores Limited (British Land property investment) | 31 March           | 50%                                | England                                  |

A full list of the Group's joint ventures is included in note 37. Joint ventures with a different year-end date to the Group are reported to include the results up to 28 February 2017, the nearest month-end to the Group's year-end. Adjustments are made for the effects of significant transactions or events that occurred between 28 February and the Group's balance sheet date.

|  | British Land £m | Other joint ventures £m | Total £m    |
|--|-----------------|-------------------------|-------------|
| At 13 March 2016                                     | <b>275</b>      | <b>52</b>               | <b>327</b>  |
| Additions <sup>1</sup>                               | –               | <b>18</b>               | <b>18</b>   |
| Dividends and distributions received <sup>2</sup>    | <b>(54)</b>     | <b>(11)</b>             | <b>(65)</b> |
| Share of retained loss:                              |                 |                         |             |
| Underlying profit after tax                          | <b>12</b>       | –                       | <b>12</b>   |
| Investment property fair value movements             | <b>(23)</b>     | <b>(2)</b>              | <b>(25)</b> |
| Finance fair value movements                         | <b>(2)</b>      | –                       | <b>(2)</b>  |
| Share of loss on disposal of properties <sup>3</sup> | <b>(5)</b>      | –                       | <b>(5)</b>  |
| Other non-underlying joint venture items             | –               | <b>(19)</b>             | <b>(19)</b> |
| Share of retained loss                               | <b>(18)</b>     | <b>(21)</b>             | <b>(39)</b> |
| Disposals to the Group <sup>3</sup>                  | <b>2</b>        | –                       | <b>2</b>    |
| Share of joint venture loss after tax                | <b>(16)</b>     | <b>(21)</b>             | <b>(37)</b> |
| Disposals from the Group                             | –               | <b>(6)</b>              | <b>(6)</b>  |
| <b>At 11 March 2017</b>                              | <b>205</b>      | <b>32</b>               | <b>237</b>  |
| At 15 March 2015                                     | 288             | 71                      | 359         |
| Additions  | –               | 18                      | 18          |
| Dividends and distributions received <sup>2</sup>    | (9)             | (37)                    | (46)        |
| Share of retained profit: <sup>4</sup>               |                 |                         |             |
| Underlying profit after tax                          | 13              | (3)                     | 10          |
| Investment property fair value movements             | (18)            | –                       | (18)        |
| Finance fair value movements                         | (2)             | –                       | (2)         |
| Share of profit on sale of properties                | 2               | (1)                     | 1           |
| Share of joint venture loss after tax                | (5)             | (4)                     | (9)         |
| Disposals from the Group                             | –               | 4                       | 4           |
|  | 274             | 52                      | 326         |
| Movements in other comprehensive income (note 20)    | 1               | –                       | 1           |
| <b>At 12 March 2016</b>                              | <b>275</b>      | <b>52</b>               | <b>327</b>  |

1 Additions of £18 million include a non-cash element of £2 million.

2 The dividends and distributions received in cash include £nil million (2016: £13 million) return of partner capital.

3 Total joint venture property losses of £(3) million as per note 3.

4 In addition to the above, in the prior year a £(2) million share of joint venture losses was recognised in relation to joint ventures with a carrying value of £nil.

## 12 Investments in joint ventures and associates continued

The total assets, liabilities, income and expenses of the Group's principal joint venture BL Sainsbury Superstores Limited are detailed below:

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| Non-current assets   | 769        | 946        |
| Current assets (excluding cash and cash equivalents)       | –          | 2          |
| Cash and cash equivalents                                  | 3          | 65         |
| Current liabilities  | (24)       | (28)       |
| Non-current liabilities                                    | (324)      | (417)      |
| Joint venture net assets                                   | 424        | 568        |
| Group share of joint venture net assets                    | 212        | 284        |
| Goodwill   | 5          | 5          |
| Unrealised profit on disposal of properties as above       | (12)       | –          |
| Group share of joint venture net assets as disclosed above | 205        | 289        |
| Revenue  | 48         | 55         |
| Other expenses   | (61)       | (41)       |
| Other income   | –          | 3          |
| Interest expenses  | (20)       | (24)       |
| Joint venture loss before tax                              | (33)       | (7)        |
| Analysed as:   |            |            |
| Underlying profit before tax                               | 27         | 30         |
| Investment property fair value movements                   | (45)       | (36)       |
| Finance fair value movements                               | (3)        | 3          |
| Loss on disposals of properties                            | (12)       | (4)        |
|  | (33)       | (7)        |
| Income tax expense   | (3)        | (3)        |
| Joint venture loss after tax                               | (36)       | (10)       |
| Other comprehensive income                                 | –          | 1          |
| Total comprehensive expense                                | (36)       | (9)        |

The joint venture had no other contingent liabilities nor capital commitments other than those disclosed in notes 33 and 35.

## 13 Available-for-sale financial assets

### Accounting policies

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories (fair value through profit or loss and loans and receivables). They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date. Subsequent to initial recognition at fair value plus transaction costs, these assets are recorded at fair value at each period end with the movements recognised in other comprehensive income until derecognition or impaired at which time the cumulative gain or loss previously recognised in other comprehensive income reserves is recognised in the income statement. Dividends on available-for-sale equity instruments are recognised in the income statement when the entity's right to receive payment is established. Interest on available-for-sale debt instruments is recognised using the effective interest method.

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| <b>Non-current</b>                               |            |            |
| Equity:  |            |            |
| Unlisted equity investment                       | 2          | 3          |
| Other financial assets                           | 161        | 146        |
| Debt:  |            |            |
| Interest bearing financial assets                | 39         | 35         |
| Financial Services related investment securities | 233        | 156        |
|  | 435        | 340        |
| <b>Current</b>                                   |            |            |
| Debt:  |            |            |
| Financial Services related investment securities | 100        | 48         |
|  | 535        | 388        |

The other financial asset predominantly represents the Group's beneficial interest in a commercial property investment pool. The fair value of the other financial asset is based on discounted cash flows assuming a property rental growth rate of 0.5 per cent (2016: 0.6 per cent) and a weighted average cost of capital of nine per cent (2016: nine per cent). There were no disposals or impairment provisions on available-for-sale financial assets in either the current or the previous financial year.

## 14 Inventories

### Accounting policies

Inventories comprise goods held for resale and properties held for resale or in the course of development and are valued on a weighted average cost basis and carried at the lower of cost and net realisable value. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution. Cost includes all direct expenditure and other appropriate attributable costs incurred in bringing inventories to their present location and condition.

|                        | 2017<br>£m   | 2016<br>£m |
|------------------------|--------------|------------|
| Goods held for resale  | 1,774        | 967        |
| Development properties | 1            | 1          |
|                        | <b>1,775</b> | 968        |

The amount of inventories recognised as an expense and charged to cost of sales for the 52 weeks to 11 March 2017 was £19,483 million (2016: £17,210 million).

## 15 Receivables

### (a) Trade and other receivables

#### Accounting policies

Trade receivables are non-interest bearing and are on commercial terms. Other receivables have both non-interest and interest bearing receivables. Trade and other receivables are stated at their carrying amounts and are written off when management deems them uncollectable or forgiven.

|                                | 2017<br>£m | 2016<br>£m |
|--------------------------------|------------|------------|
| <b>Non-current</b>             |            |            |
| Other receivables              | 59         | 92         |
| Prepayments and accrued income | 10         | 11         |
|                                | <b>69</b>  | 103        |
| <b>Current</b>                 |            |            |
| Trade receivables              | 106        | 96         |
| Other receivables              | 312        | 305        |
|                                | <b>418</b> | 401        |
| Prepayments and accrued income | 156        | 107        |
|                                | <b>574</b> | 508        |

Current other receivables of £312 million (2016: £305 million), which include £165 million (2016: £170 million) of bank funds in the course of settlement, are generally non-interest bearing. The carrying amounts of trade and other receivables are denominated in sterling.

The Group's exposure to credit risk arising from its retail operations is minimal given that the customer base is large and unrelated and that the overwhelming majority of customer transactions are settled through cash or secure electronic means. New parties wishing to obtain credit terms with the Group are credit checked prior to invoices being raised and credit limits are determined on an individual basis.

### (b) Amounts due from Financial Services customers

#### Accounting policies

Loans and advances are initially recognised at fair value and subsequently held at amortised cost, using the effective interest method, less provision for impairment and recognised on the balance sheet when cash is advanced. For the Financial Services portfolios of loans, such as credit card lending and personal loans, impairment provisions are calculated for groups of assets, otherwise impairment is identified at a counterparty specific level following objective evidence that a financial asset is impaired. Such evidence may include a missed interest or principal payment or the breach of a banking covenant. Provisioning on unsecured balances identified as being in arrears is calculated based on past experience, with regularly updated assumptions. The present value of estimated cash flows recoverable is determined after taking into account any security held. The amount of impairment is calculated by comparing the present value of the cash flows discounted at the loan's original effective interest rate with the balance sheet carrying value. If impaired, the carrying value is adjusted and the difference charged to the income statement and a provision recognised in the balance sheet.

The written down value of the impaired loan is compounded back to the net realisable balance over time using an effective interest rate. This is reported through interest receivable within the income statement and represents the unwinding of the discount.

A write-off is made when all or part of a loan or advance is deemed uncollectable or forgiven. Write-offs are charged against previously established provisions for impairment or directly to the income statement. Subsequent recoveries of amounts written off decrease the charge for loan impairment in the income statement.

## 15 Receivables continued

An allowance for impairment losses is also maintained in respect of assets which are impaired at the balance sheet date but which have not been identified as such, based on historical loss experience and other relevant factors. This includes analysis of the likelihood of a particular balance to move into an arrears status within a defined period of time and application of an appropriate loss rate. The emergence period into an arrears state represents the average time elapsed between the loss trigger event and default. The methodology and assumptions used are regularly reviewed to reduce any differences between estimates and actual results.

|                                  | 2017<br>£m   | 2016<br>£m |
|----------------------------------|--------------|------------|
| <b>Non-current</b>               |              |            |
| Loans and advances to customers  | 1,948        | 1,680      |
| Impairment of loans and advances | (32)         | (31)       |
|                                  | <b>1,916</b> | 1,649      |
| <b>Current</b>                   |              |            |
| Loans and advances to customers  | 2,743        | 1,743      |
| Impairment of loans and advances | (57)         | (48)       |
|                                  | <b>2,686</b> | 1,695      |

Loans and advances to customers accrue interest at the effective interest rate. Financial Services has pledged the rights to £678 million (2016: £468 million) of its personal loans book with the Bank of England for £260 million (2016: £240 million) of Treasury Bills under the Funding for Lending Scheme and £155 million of funding (2016: £nil) under the Indexed Long-Term Repo Facility. Funding for Lending Treasury Bills can then be converted to cash as a source of future funding to the Bank. As at 11 March 2017, there was £nil (2016: £nil) borrowings drawn down.

Financial Services has assigned the beneficial interest in £378 million (2016: £379 million) of its personal loans book to a Special Purpose Entity for use as collateral in securitisation transactions, facilitating £311 million (2016: £300 million) of drawings.

Refer to note 23 for details on Financial Services credit risk.

### (c) Provision for impairment of loans and advances

|                          | 2017<br>£m  | 2016<br>£m  |
|--------------------------|-------------|-------------|
| Opening provision        | (79)        | (87)        |
| Additional provisions    | (33)        | (15)        |
| Utilisation of provision | 24          | 22          |
| Amortisation of discount | (1)         | 1           |
| <b>Closing provision</b> | <b>(89)</b> | <b>(79)</b> |

The Group acquired Home Retail Group plc during the year. The loan book fair value acquired was £615 million net of provisions. Gross provisions at the date of acquisition were £66 million which are not shown in the table above in line with IFRS 3 'Business Combinations'.

### (d) Major counterparties

The Group has two major counterparties totalling £55 million (2016: two major counterparties totalling £43 million). No major counterparty balances are considered overdue or impaired.

## 16 Assets and liabilities held for sale

### Accounting policies

Assets and liabilities are classified as held for sale if their carrying amount is to be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable within one year from the date of classification and the assets and liabilities are available-for-sale in their present condition. Assets held for sale are stated at the lower of the carrying amount and fair value less costs to dispose.

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| <b>Assets held for sale</b>                |            |            |
| Retail segment properties                  | 10         | 9          |
| Assets related to Pharmacy business:       |            |            |
| Fixed assets                               | –          | 3          |
| Intangible assets                          | –          | 4          |
| Inventory                                  | –          | 15         |
|  | <b>10</b>  | <b>31</b>  |
| <b>Liabilities held for sale</b>           |            |            |
| Liabilities relating to Pharmacy business: |            |            |
| Creditors                                  | –          | 4          |
|  | –          | 4          |

All of the Company's assets and liabilities held for sale at 12 March 2016 were sold during the current financial year.

## 17 Payables

### (a) Trade and other payables

#### Accounting policies

The Group's policy on payment of creditors is to agree terms of payment prior to commencing trade with a supplier and to abide by those terms on the timely submission of satisfactory invoices.

Accruals and deferred income/gains includes accounting for leases with fixed rental increases and lease incentives on a straight-line basis over the term of the lease.

|                                    | 2017<br>£m   | 2016<br>£m |
|------------------------------------|--------------|------------|
| <b>Current</b>                     |              |            |
| Trade payables                     | 2,685        | 2,082      |
| Other payables                     | 571          | 590        |
| Accruals and deferred income/gains | 485          | 405        |
|                                    | <b>3,741</b> | 3,077      |
| <b>Non-current</b>                 |              |            |
| Other payables                     | 19           | 6          |
| Accruals and deferred income/gains | 285          | 263        |
|                                    | <b>304</b>   | 269        |

#### Foreign currency risk

The Group has net euro denominated trade payables of £17 million (2016: £11 million) and US dollar denominated trade payables of £64 million (2016: £49 million).

### (b) Amounts due to Financial Services customers and banks

#### Accounting policies

With the exception of fixed rate bonds, amounts due to Financial Services customers are generally repayable on demand and accrue interest at retail deposit rates.

|                           | 2017<br>£m   | 2016<br>£m |
|---------------------------|--------------|------------|
| <b>Current</b>            |              |            |
| Customer accounts         | 3,885        | 3,026      |
| Other deposits            | 278          | 29         |
| Senior secured loan notes | 121          | 118        |
|                           | <b>4,284</b> | 3,173      |
| <b>Non-current</b>        |              |            |
| Customer accounts         | 216          | 182        |
| Other deposits            | 231          | 219        |
| Senior secured loan notes | 190          | 181        |
|                           | <b>637</b>   | 582        |

Financial Services, via its subsidiary undertakings, has entered a £400 million asset backed commercial paper securitisation of consumer loans. Of this facility, £311 million had been drawn as at 11 March 2017 (12 March 2016: £300 million). Interest on the notes is repayable at a floating rate linked to three-month LIBOR and their contractual repayment is determined by cash flows on the relevant personal loans included in the collateral pool.

Other deposits of £509 million (2016: £248 million) relate to deposits from wholesale counterparties.

## 18 Provisions

#### Accounting policies

Provisions are recognised when there is a present legal or constructive obligation as a result of a past event, for which it is probable that an outflow of economic benefit will be required to settle the obligation and where the amount can be reliably estimated. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

The need for provisions for onerous leases, measured net of expected rental income, is assessed when the leased property becomes vacant and is no longer used in the operations of the business or when the leased property relates to an unprofitable trading store. Provisions for dilapidation costs are recognised on a lease-by-lease basis.

Provisions for onerous contracts are recognised where expected cash outflows exceed the anticipated future benefits. The amounts provided are based on the Group's best estimate of the likely committed outflow net of anticipated future benefits and after any impairment of pipeline development site assets where applicable.

The costs of long service awards are accrued over the period the service is provided by the employee when it is probable that settlement will be required and they are capable of being measured reliably. Liabilities recognised in respect of long-term employee benefits are measured at the present value of the estimated future cash outflows to be made by the Group in respect of services provided by employees up to the reporting date.

A restructuring provision is recognised when the Group has developed a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement the plan or announcing its main features to those affected by it. The measurement of a restructuring provision includes only the direct expenditures arising from the restructuring.

## 18 Provisions continued

|                                | Onerous leases and onerous contracts<br>£m | Long service awards<br>£m | Restructuring<br>£m | Other provisions<br>£m | Total<br>£m |
|--------------------------------|--|---------------------------|---------------------|------------------------|-------------|
| At 13 March 2016               | 96   | 4                         | 2                   | 73                     | 175         |
| Acquisition of subsidiaries    | –  | –                         | 18                  | 86                     | 104         |
| Additional provisions          | 32   | –                         | 33                  | 26                     | 91          |
| Unused amounts reversed        | (5)  | –                         | –                   | (5)                    | (10)        |
| Utilisation of provision       | (29)                                       | –                         | (16)                | (58)                   | (103)       |
| Amortisation of discount       | 6  | –                         | –                   | –                      | 6           |
| <b>At 11 March 2017</b>        | <b>100</b>                                 | <b>4</b>                  | <b>37</b>           | <b>122</b>             | <b>263</b>  |
| At 15 March 2015               | 88   | 7                         | 10                  | 16                     | 121         |
| Reclassification from accruals | –  | –                         | –                   | 68                     | 68          |
| Additional provisions          | 23   | –                         | 11                  | 14                     | 48          |
| Unused amounts reversed        | (2)  | (2)                       | (3)                 | (1)                    | (8)         |
| Utilisation of provision       | (18)                                       | (1)                       | (16)                | (24)                   | (59)        |
| Amortisation of discount       | 5  | –                         | –                   | –                      | 5           |
| At 12 March 2016               | 96   | 4                         | 2                   | 73                     | 175         |

|               | 2017<br>£m | 2016<br>£m |
|---------------|------------|------------|
| Disclosed as: |            |            |
| Current       | 135        | 46         |
| Non-current   | 128        | 129        |
|               | <b>263</b> | <b>175</b> |

The onerous lease provision covers residual lease commitments of up to an average of 32 years (2016: 28 years), after allowance for existing or anticipated sublet rental income.

Long service awards are accrued over the period the service is provided by the employee.

Insurance provisions of £80 million (2016: £57 million) are included within other provisions.

## 19 Called up share capital, share premium and merger reserve

### Accounting policies

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

|  | 2017<br>million | 2016<br>million | 2017<br>£m | 2016<br>£m |
|--|-----------------|-----------------|------------|------------|
| <b>Called up share capital</b>   |                 |                 |            |            |
| Allotted and fully paid ordinary shares 28 <sup>4</sup> / <sub>p</sub> | 2,188           | 1,924           | 625        | 550        |
| <b>Share premium account</b>   |                 |                 |            |            |
| Share premium  |                 |                 | 1,120      | 1,114      |

The movements in the called up share capital, share premium and merger reserve are set out below:

|   | Number of ordinary shares<br>million | Ordinary shares<br>£m | Share premium account<br>£m | Merger reserve<br>£m |
|---|--------------------------------------|-----------------------|-----------------------------|----------------------|
| At 13 March 2016                            | 1,924                                | 550                   | 1,114                       | –                    |
| Acquisition of subsidiaries <sup>1</sup>    | 261                                  | 75                    | –                           | 568                  |
| Allotted in respect of share option schemes | 3                                    | –                     | 6                           | –                    |
| <b>At 11 March 2017</b>                     | <b>2,188</b>                         | <b>625</b>            | <b>1,120</b>                | <b>568</b>           |
| At 15 March 2015                            | 1,919                                | 548                   | 1,108                       | –                    |
| Allotted in respect of share option schemes | 5                                    | 2                     | 6                           | –                    |
| At 12 March 2016                            | 1,924                                | 550                   | 1,114                       | –                    |

<sup>1</sup> 261 million new J Sainsbury plc shares of 28<sup>4</sup>/<sub>p</sub> nominal value each were issued (being 0.321 new J Sainsbury plc shares per existing Home Retail Group plc share); fair value of the consideration is based on a J Sainsbury plc share price of £2.4610 as of 2 September 2016. This is accounted for as £75 million in share capital, plus the premium arising from the consideration in excess of the nominal amount of shares issued of £568 million, which is recognised in merger reserve as the transaction qualified for merger relief.

## 20 Capital redemption and other reserves

|  | Currency translation reserve<br>£m | Available-for-sale assets<br>£m | Cash flow hedge<br>£m | Convertible bond reserve<br>£m | Total other reserves<br>£m | Capital redemption reserve<br>£m |
|--|------------------------------------|---------------------------------|-----------------------|--------------------------------|----------------------------|----------------------------------|
| At 13 March 2016   | <b>3</b>                           | <b>126</b>                      | <b>(3)</b>            | <b>29</b>                      | <b>155</b>                 | <b>680</b>                       |
| Currency translation differences   | <b>5</b>                           | –                               | –                     | –                              | <b>5</b>                   | –                                |
| Available-for-sale financial assets fair value movements (net of tax)    | –                                  | <b>18</b>                       | –                     | –                              | <b>18</b>                  | –                                |
| Items reclassified from available-for-sale asset reserve                 | –                                  | <b>(1)</b>                      | –                     | –                              | <b>(1)</b>                 | –                                |
| Cash flow hedges effective portion of fair value movements (net of tax): |                                    |                                 |                       |                                |                            |                                  |
| Attributable to Group  | –                                  | –                               | <b>111</b>            | –                              | <b>111</b>                 | –                                |
| Items reclassified from cash flow hedge reserve                          | –                                  | –                               | <b>(87)</b>           | –                              | <b>(87)</b>                | –                                |
| Amortisation of convertible bond – equity component                      | –                                  | –                               | –                     | <b>(8)</b>                     | <b>(8)</b>                 | –                                |
| <b>At 11 March 2017</b>  | <b>8</b>                           | <b>143</b>                      | <b>21</b>             | <b>21</b>                      | <b>193</b>                 | <b>680</b>                       |
| At 15 March 2015   | 1                                  | 124                             | (15)                  | 36                             | 146                        | 680                              |
| Currency translation differences   | 2                                  | –                               | –                     | –                              | 2                          | –                                |
| Available-for-sale financial assets fair value movements (net of tax)    | –                                  | 2                               | –                     | –                              | 2                          | –                                |
| Cash flow hedges effective portion of fair value movements (net of tax): |                                    |                                 |                       |                                |                            |                                  |
| Attributable to Group  | –                                  | –                               | 4                     | –                              | 4                          | –                                |
| Attributable to joint ventures (note 12)                                 | –                                  | –                               | 1                     | –                              | 1                          | –                                |
| Items reclassified from cash flow hedge reserve                          | –                                  | –                               | 7                     | –                              | 7                          | –                                |
| Amortisation of convertible bond – equity component                      | –                                  | –                               | –                     | (7)                            | (7)                        | –                                |
| At 12 March 2016   | 3                                  | 126                             | (3)                   | 29                             | 155                        | 680                              |

The currency translation reserve represents the cumulative foreign exchange differences on the translation of the net assets of the Group's foreign operations from their functional currency to the presentation currency of the parent.

The available-for-sale assets reserve represents the fair value gains and losses on the available-for-sale financial assets held by the Group. The cash flow hedge reserve represents the cumulative effective fair value gains and losses on cash flow hedges in the Group.

The convertible bond reserve represents the equity component of the £450 million convertible bond issued in November 2014.

The capital redemption reserve arose on the redemption of B shares. Shareholders approved a £680 million return of share capital, by way of a B share scheme, at the Company's Extraordinary General Meeting on 12 July 2004. The final redemption date for B shares was 18 July 2007 and all transactions relating to the B shares have now been completed.

## 21 Perpetual securities

### Accounting policies and key information

Perpetual securities (perpetual capital securities and perpetual convertible bonds) are issued securities that qualify for recognition as equity. Accordingly any periodic returns are accounted for as dividends and recognised directly in equity and as a liability at the time it becomes obligated to pay the periodic return. Any associated tax impacts are recognised directly in equity.

On 30 July 2015 the Group issued £250 million of perpetual subordinated capital securities and £250 million of perpetual subordinated convertible bonds, collectively known as perpetual securities. Costs directly associated with the issue of £6 million were offset against the value of the proceeds. The securities are perpetual with no fixed redemption date. Holders of the perpetual securities do not benefit from any put option rights however the Group does have the right to call the perpetual subordinated capital securities at their principal amount on 30 July 2020, and the perpetual subordinated convertible bonds on 30 July 2021. The perpetual subordinated convertible bonds may be converted into ordinary shares of the Company at the option of the holders at any time up to 23 July 2021 at a conversion price of 327.4615 pence.

The Group has the right to defer coupons on the perpetual securities on any coupon payment date where the Company has not either paid a dividend on its ordinary shares or bought back ordinary shares (excluding shares bought to satisfy employee share schemes) within the previous 12 month period. The coupon rate on the perpetual subordinated capital securities increases after the fifth anniversary and for the perpetual subordinated convertible bonds after the sixth anniversary.

The next coupon date on the perpetual securities is 30 July 2017. As the Company paid a dividend to ordinary shareholders in the 12 months prior to this date (in January 2017), the periodic distributions of £7 million for the perpetual subordinated capital securities and £16 million for the perpetual subordinated convertible bonds have been recognised in the financial year.

## 21 Perpetual securities continued

|  | Perpetual capital securities<br>£m | Perpetual convertible bonds<br>£m |
|--|------------------------------------|-----------------------------------|
| At 13 March 2016   | 248                                | 248                               |
| Distributions to holders of perpetual securities   | (16)                               | (7)                               |
| Current tax relief on distributions to holders of perpetual securities                     | 4                                  | 1                                 |
| Profit for the year attributable to holders of perpetual securities                        | 12                                 | 6                                 |
| <b>At 11 March 2017</b>  | <b>248</b>                         | <b>248</b>                        |
| At 15 March 2015   |                                    |                                   |
| Issue of £250 million 2.875% perpetual subordinated convertible bonds (net of issue costs) | –                                  | 247                               |
| Issue of £250 million 6.5% perpetual subordinated capital securities (net of issue costs)  | 247                                | –                                 |
| Current tax relief on issue costs  | 1                                  | 1                                 |
| Distributions to holders of perpetual securities   | (16)                               | (7)                               |
| Current tax relief on distributions to holders of perpetual securities                     | 3                                  | 1                                 |
| Profit for the year attributable to holders of perpetual securities                        | 13                                 | 6                                 |
| At 12 March 2016   | 248                                | 248                               |

## 22 Retained earnings

|   | Own shares<br>£m | Profit and loss account<br>£m | Total retained earnings<br>£m |
|---|------------------|-------------------------------|-------------------------------|
| At 13 March 2016  | (21)             | 3,391                         | 3,370                         |
| Profit for the year   | –                | 359                           | 359                           |
| Remeasurements on defined benefit pension schemes (net of tax)    | –                | (338)                         | (338)                         |
| Dividends paid  | –                | (232)                         | (232)                         |
| Acquisition of subsidiaries                                       | –                | (3)                           | (3)                           |
| Adjustment to consideration in respect of share options (note 31) | –                | 3                             | 3                             |
| Amortisation of convertible bond-equity component                 | –                | 8                             | 8                             |
| Share-based payment (net of tax)                                  | –                | 32                            | 32                            |
| Purchase of own shares  | (9)              | –                             | (9)                           |
| Allotted in respect of share option schemes                       | 19               | (19)                          | –                             |
| <b>At 11 March 2017</b>   | <b>(11)</b>      | <b>3,201</b>                  | <b>3,190</b>                  |
| At 15 March 2015  | (18)             | 3,075                         | 3,057                         |
| Profit for the year   | –                | 452                           | 452                           |
| Remeasurements on defined benefit pension schemes (net of tax)    | –                | 85                            | 85                            |
| Dividends paid  | –                | (234)                         | (234)                         |
| Share-based payment (net of tax)                                  | –                | 23                            | 23                            |
| Purchase of own shares  | (20)             | –                             | (20)                          |
| Allotted in respect of share option schemes                       | 17               | (17)                          | –                             |
| Amortisation of convertible bond – equity component               | –                | 7                             | 7                             |
| At 12 March 2016  | (21)             | 3,391                         | 3,370                         |

### Own shares held by Employee Share Ownership Plan (ESOP) trusts

The Group owns 4,303,928 (2016: 7,857,148) of its ordinary shares of 28<sup>1</sup>/<sub>2</sub> pence nominal value each. At 12 March 2016, the total nominal value of the own shares was £1.2 million (2016: £2.2 million).

All shares (2016: all shares) are held by Group trusts for the Executive Share Plans. All Group trusts waive the rights to the dividends receivable in respect of the shareholder under the above schemes.

The cost of the own shares is deducted from equity in the Group financial statements. The market value of the own shares at 11 March 2017 was £11 million (2016: £21 million).

## 23 Financial risk management

The principal financial risks faced by the Group relate to liquidity risk, counterparty credit risk, foreign currency risk, interest rate risk, commodity risk and capital risk.

Financial risk management is managed by a central treasury department in accordance with policies and guidelines which are reviewed and approved by the Board of Directors. The risk management policies are designed to minimise potential adverse effects on the Group's financial performance by identifying financial exposures and setting appropriate risk limits and controls. The risk management policies also ensure sufficient liquidity is available to the Group to meet foreseeable financial obligations and that cash assets are invested safely.

Financial risk management with respect to Financial Services is separately managed within the Financial Services' governance structure. The risks are more fully described in the Financial Services section below.

The Group uses forward contracts to hedge foreign exchange and commodity exposures, and cross currency swap contracts and interest rate swap contracts to hedge interest rate exposures. The use of financial derivatives is governed by Board approved policies which prohibits the use of derivative financial instruments for speculative purposes.

### Liquidity risk

Liquidity risk is the risk that the Group could be unable to meet its financial obligations as they fall due.

The principal operational cash flow of the Group is largely stable and predictable reflecting the low business risk profile of the food retail sector and the cyclical profile of the non-food retail sector. Cash flow forecasts are produced to assist management in identifying future liquidity requirements. The Group's liquidity policy sets a minimum funding headroom of £400 million in excess of forecast net debt over a rolling 12 month time horizon. The Group manages its liquidity risk by maintaining a core of long-dated borrowings, pre-funding future cash flow commitments and holding contingent committed credit facilities.

The Group maintains a contingent committed revolving credit facility of £1,150 million. The £1,150 million facility is split into two tranches, a £500 million Facility (A) maturing in May 2019 and a £650 million Facility (B) maturing in May 2020. As at 11 March 2017, £nil had been drawn (2016: £nil).

The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period to the contractual maturity date. The amounts disclosed in the tables are the contractual undiscounted cash flows or an estimate of cash flows in respect of floating interest rate liabilities.

| Group  | Less than<br>one year<br>£m | One to<br>two years<br>£m | Two to<br>five years<br>£m | More than<br>five years<br>£m |
|--|-----------------------------|---------------------------|----------------------------|-------------------------------|
| <b>At 11 March 2017</b>  |                             |                           |                            |                               |
| <b>Non-derivative financial liabilities</b>                        |                             |                           |                            |                               |
| Secured loans:   |                             |                           |                            |                               |
| Loan due 2018  | (137)                       | (575)                     | –                          | –                             |
| Loan due 2031 <sup>1</sup>   | (66)                        | (68)                      | (219)                      | (777)                         |
| Unsecured loans:   |                             |                           |                            |                               |
| Bank overdraft   | (6)                         | –                         | –                          | –                             |
| Bank loans due 2019 <sup>2</sup>                                   | (4)                         | (4)                       | (202)                      | –                             |
| Convertible bond due 2019  | (6)                         | (6)                       | (453)                      | –                             |
| Finance lease obligations <sup>2</sup>                             | (31)                        | (34)                      | (32)                       | (206)                         |
| Trade and other payables   | (3,741)                     | –                         | –                          | –                             |
| Amounts due to Financial Services customers and banks <sup>5</sup> | (4,365)                     | (364)                     | (293)                      | –                             |
| <b>Derivative contracts – net settled</b>                          |                             |                           |                            |                               |
| Commodity contracts  | 3                           | –                         | –                          | –                             |
| Interest rate swaps in hedging relationships <sup>1,4</sup>        | (5)                         | (4)                       | (9)                        | (5)                           |
| Other interest rate swaps <sup>4</sup>                             | (1)                         | –                         | –                          | –                             |
| <b>Derivative contracts – gross settled</b>                        |                             |                           |                            |                               |
| Foreign exchange forwards – outflow <sup>3</sup>                   | (1,327)                     | (92)                      | –                          | –                             |
| Foreign exchange forwards – inflow <sup>3</sup>                    | 1,405                       | 97                        | –                          | –                             |
| Commodity contracts – outflow                                      | (15)                        | (15)                      | (37)                       | (29)                          |
| Commodity contracts – inflow                                       | 12                          | 12                        | 27                         | 29                            |

### Assumptions:

- Cash flows relating to debt and swaps linked to inflation rates have been calculated using a RPI of 1.3 per cent for the year ended 11 March 2017, 2.6 per cent for the year ending 10 March 2018 and 3.6 per cent for future years (2016: RPI of 1.1 per cent for the year ended 12 March 2016, 1.3 per cent for the year ended 11 March 2017, and 3.0 per cent for future years).
- Cash flows relating to debt bearing a floating interest rate have been calculated using prevailing interest rates as at 11 March 2017 and 12 March 2016.
- Cash flows in foreign currencies have been translated using spot rates as at 11 March 2017 and 12 March 2016.
- The swap rate that matches the remaining term of the interest rate swap as at 11 March 2017 has been used to calculate the floating rate cash flows over the life of the interest rate swaps shown above (2016: 12 March 2016).
- Cash flows relating to amounts due to Sainsbury's Bank customers and banks are calculated using contractual terms and interest rates for fixed rate instruments. Where balances are contractually repayable on demand, behavioural assumptions are applied to estimate the interest payable on those balances. These are shown as due within one year.

## 23 Financial risk management continued

|   | Less than one<br>year<br>£m | One to two<br>years<br>£m | Two to five<br>years<br>£m | More than five<br>years<br>£m |
|---|-----------------------------|---------------------------|----------------------------|-------------------------------|
| <b>At 12 March 2016</b>                             |                             |                           |                            |                               |
| <b>Non-derivative financial liabilities</b>         |                             |                           |                            |                               |
| Secured loans:                                      |                             |                           |                            |                               |
| Loan due 2018                                       | (134)                       | (137)                     | (575)                      | –                             |
| Loan due 2031                                       | (64)                        | (66)                      | (210)                      | (817)                         |
| Unsecured loans:                                    |                             |                           |                            |                               |
| Bank overdraft                                      | (3)                         | –                         | –                          | –                             |
| Bank loans due 2016                                 | (39)                        | –                         | –                          | –                             |
| Bank loans due 2019                                 | (4)                         | (4)                       | (207)                      | –                             |
| Convertible bond due 2019                           | (6)                         | (6)                       | (458)                      | –                             |
| Finance lease obligations                           | (46)                        | (30)                      | (56)                       | (209)                         |
| Trade and other payables                            | (2,939)                     | (6)                       | –                          | –                             |
| Amounts due to Sainsbury's Bank customers and banks | (3,223)                     | (232)                     | (375)                      | –                             |
| <b>Derivative contracts – net settled</b>           |                             |                           |                            |                               |
| Commodity contracts                                 | (5)                         | –                         | –                          | –                             |
| Interest rate swaps in hedging relationships        | (8)                         | (10)                      | (5)                        | –                             |
| Other interest rate swaps                           | (1)                         | (1)                       | –                          | –                             |
| <b>Derivative contracts – gross settled</b>         |                             |                           |                            |                               |
| Foreign exchange forwards – outflow                 | (562)                       | (74)                      | –                          | –                             |
| Foreign exchange forwards – inflow                  | 585                         | 74                        | –                          | –                             |
| Commodity contracts – outflow                       | (15)                        | (15)                      | (43)                       | (37)                          |
| Commodity contracts – inflow                        | 9                           | 9                         | 26                         | 29                            |
| Cross currency swaps – outflow                      | 45                          | –                         | –                          | –                             |
| Cross currency swaps – inflow                       | (40)                        | –                         | –                          | –                             |

## 23 Financial risk management continued

The year-on-year increase in foreign exchange projected cash outflows and inflows is largely as a result of the acquisition of Home Retail Group.

Further information relating to liquidity risk in Financial Services is more fully described in the separate section on Financial Services financial risk factors below.

### Counterparty credit risk

Counterparty credit risk is the risk of a financial loss arising from counterparty default or non-performance in respect of the Group's holdings of cash and cash equivalents, derivative financial assets, deposits with banks, investments in marketable securities, trade and other receivables and loans and advances to customers. The Group considers its maximum credit risk to be £6,967 million (2016: £5,554 million), equivalent to the Group's total financial assets, and of this amount £5,620 million relates to Financial Services (2016: £4,326 million).

The Group (excluding Financial Services) sets counterparty limits for each of its banking and investment counterparties based on their credit ratings, the minimum unsecured long-term credit rating accepted by the Group is BBB+ (Standard & Poor's and Fitch) or Baa1 (Moody's) or, in the case of sterling liquidity funds, AAA or Aaa/MR1+ from Moody's. In the event of a split credit rating, the lower rating applies.

The table below analyses the Group's cash and cash equivalents by credit exposure excluding bank balances, store cash, cash in transit and cash at ATMs:

| Counterparty                                   | Long-term rating | Group 2017<br>£m | Group 2016<br>£m |
|--|------------------|------------------|------------------|
| Financial institutions – Money market funds    | AAAm/Aaa         | 294              | 330              |
| Financial institutions – Money market deposits | AAAm/Aaa         | 9                | 50               |
| Financial institutions – Money market deposits | AA+/Aa1 to A/A2  | 100              | 100              |
| UK Government Treasury Bills                   | AA+/Aa1 to A/A2  | –                | 20               |
| Deposits at central banks                      | AA+/Aa1          | 241              | 269              |

Management does not expect any losses arising from non-performance of deposit counterparties.

Interest rate swaps, forward contracts and commodity contracts for difference are used by the Group to hedge interest rate, foreign currency and fuel exposures. The table below analyses the fair value of the Group's derivative financial assets by credit exposure, excluding any collateral held.

| Counterparty                | Long-term rating   | Group 2017<br>£m | Group 2016<br>£m |
|-----------------------------|--------------------|------------------|------------------|
| Interest rate swaps         | AA+/Aa1 to A/A2    | 25               | 48               |
| FX forward contracts        | AA+/Aa1 to A/A2    | 65               | 17               |
| FX forward contracts        | A/A3- to BBB+/Baa1 | 11               | 3                |
| FX forward contracts        | BBB-               | 1                | –                |
| Commodity forward contracts | AA+/Aa1 to A/A2    | 2                | –                |

The foreign currency forward contracts entered into with a BBB- counterparty relate to historic operating practices within Home Retail Group plc. This exposure will be reduced through natural hedging in 2017.

Further information relating to counterparty credit risk in Financial Services is more fully described in the section on Financial Services financial risk factors below.

### Offsetting of financial assets and liabilities

The following table sets out the Group's financial assets and financial liabilities that are subject to counterparty offsetting or a master netting agreement. The master netting agreements regulate settlement amounts in the event either party defaults on their obligations.

|                                  | Gross amounts of recognised financial assets and liabilities<br>£m | Amounts offset in the balance sheet<br>£m | Net amounts recognised in the balance sheet<br>£m | Balances subject to a contractual right of offset<br>£m | Amounts not offset in balance sheet | Cash collateral pledged<br>£m | Net amounts<br>£m |
|----------------------------------|--|---|---|---|-------------------------------------|-------------------------------|-------------------|
| <b>At 11 March 2017</b>          |  |   |   |   |                                     |                               |                   |
| Derivative financial assets      | 104  | –   | 104   | (2)   | –                                   | –                             | 102               |
| Derivative financial liabilities | (60)   | –   | (60)  | 2   | 19                                  | –                             | (39)              |
| Cash and cash equivalents        | 1,083  | –   | 1,083   | –   | –                                   | –                             | 1,083             |
| Bank overdrafts                  | (6)  | –   | (6)   | –   | –                                   | –                             | (6)               |
| Trade and other payables         | (1,705)  | 60  | (1,645)   | –   | –                                   | –                             | (1,645)           |
|                                  | (584)  | 60  | (524)   | –   | 19                                  | –                             | (505)             |
| <b>At 12 March 2016</b>          |  |   |   |   |                                     |                               |                   |
| Derivative financial assets      | 68   | –   | 68  | (7)   | –                                   | –                             | 61                |
| Derivative financial liabilities | (112)  | –   | (112)   | 7   | 13                                  | –                             | (92)              |
| Cash and cash equivalents        | 1,143  | –   | 1,143   | –   | –                                   | –                             | 1,143             |
| Bank overdrafts                  | (3)  | –   | (3)   | –   | –                                   | –                             | (3)               |
| Trade and other payables         | (1,785)  | 114                                       | (1,671)   | –   | –                                   | –                             | (1,671)           |
|                                  | (689)  | 114                                       | (575)   | –   | 13                                  | –                             | (562)             |

### 23 Financial risk management continued

The Group holds certain financial derivatives which are subject to credit support agreements. Under these agreements cash collateral is posted by one party to the other party should the fair value of the financial derivative exceed a pre-agreed level. As at 11 March 2017, the Group held no collateral against financial derivative assets (2016: nil).

Financial Services has derivatives that are governed by the International Swaps and Derivatives Association and their associated credit support annex bilateral agreements whereby if the fair value exceeds a pre-agreed level, cash collateral is exchanged. As at 11 March 2017, Financial Services and its subsidiary undertakings had provided collateral of £19 million (2016: £13 million) against the derivatives.

The Group also operates a cash pooling arrangement and collective net overdraft facility with its main clearing bank. As at 11 March 2017, the Group had £6 million (2016: £3 million) under this facility.

#### Foreign currency risk

Currency risk is the risk of increased costs arising from unexpected movements in exchange rates impacting the Group's foreign currency denominated supply contracts.

The Group's currency risk policy seeks to limit the impact of fluctuating exchange rates on the Group's income statement by requiring highly probable foreign currency cash flows to be hedged. Highly probable future cash flows, which may be either contracted or un-contracted, are hedged on a layered basis using foreign currency forward contracts.

The Group has exposure to currency risk on balances held in foreign currency denominated bank accounts, which may arise due to short-term timing differences on maturing hedges and underlying supplier payments.

The Group considers that a ten per cent movement in exchange rates against sterling is a reasonable measure of volatility. The impact of a ten per cent movement in the exchange rate of US dollar and euro versus sterling as at the balance sheet date, with all other variables held constant, is summarised in the table below:

|              | 2017<br>Change in<br>exchange<br>rate impact<br>on post-tax<br>profit<br>+/-10%<br>£m | 2017<br>Change in<br>exchange<br>rate impact<br>on cash<br>flow hedge<br>reserve<br>+/-10%<br>£m | 2016<br>Change in<br>exchange<br>rate impact<br>on post-tax<br>profit<br>+/-10%<br>£m | 2016<br>Change in<br>exchange<br>rate impact<br>on cash<br>flow hedge<br>reserve<br>+/-10%<br>£m |
|--------------|---|--|---|--|
| <b>Group</b> |   |  |   |  |
| USD/GBP      | <b>12/(15)</b>  | <b>(114)/139</b>   | 3/(4)   | (48)/59  |
| EUR/GBP      | <b>(2)/2</b>  | <b>(10)/13</b>   | 3/(4)   | (9)/11   |

The year-on-year increase in foreign exchange related sensitivities is largely as a result of the acquisition of Home Retail Group.

#### Interest rate risk

Interest rate risk is the risk of increased costs or lower income arising from unexpected movements in interest rates and inflation rates impacting on the Group's borrowing and investment portfolios. The Group's interest rate policy seeks to limit the impact of fluctuating interest and inflation rates by maintaining a diversified mix of fixed rate, floating rate and variable capped rate liabilities.

Interest on financial instruments is classified as fixed rate if interest re-sets on the borrowings are less frequent than once every 12 months. Interest on financial instruments is classified as floating rate if interest re-sets on the borrowings occur every 12 months or more frequently. Floating rate instruments are considered variable capped rate if the nominal interest rate is subject to a cap.

## 23 Financial risk management continued

The mix of the Group's financial assets and liabilities at the balance sheet date was as follows:

| Group   | Fixed<br>£m    | Floating<br>£m | Variable<br>capped<br>£m | Total<br>£m    |
|---|----------------|----------------|--------------------------|----------------|
| <b>At 11 March 2017</b>                               |                |                |                          |                |
| Interest bearing available-for-sale financial assets  | 334            | 39             | –                        | 373            |
| Amounts due from Financial Services customers         | 2,862          | 1,740          | –                        | 4,602          |
| Cash and cash equivalents                             | 423            | 660            | –                        | 1,083          |
| Borrowings  | (1,108)        | (205)          | (761)                    | (2,074)        |
| Finance lease obligations                             | (88)           | (50)           | –                        | (138)          |
| Amounts due to Financial Services customers and banks | (770)          | (4,151)        | –                        | (4,921)        |
| Derivative effect:                                    |                |                |                          |                |
| Interest rate swaps                                   | (2,437)        | 2,437          | –                        | –              |
| Inflation linked swaps                                | (400)          | –              | 400                      | –              |
| <b>Total</b>  | <b>(1,184)</b> | <b>470</b>     | <b>(361)</b>             | <b>(1,075)</b> |
| <b>At 12 March 2016</b>                               |                |                |                          |                |
| Interest bearing available-for-sale financial assets  | –              | 35             | –                        | 35             |
| Amounts due from Financial Services customers         | 2,507          | 837            | –                        | 3,344          |
| Cash and cash equivalents                             | 475            | 668            | –                        | 1,143          |
| Borrowings  | (1,202)        | (238)          | (798)                    | (2,238)        |
| Finance lease obligations                             | (114)          | (61)           | –                        | (175)          |
| Amounts due to Financial Services customers and banks | (410)          | (3,345)        | –                        | (3,755)        |
| Derivative effect:                                    |                |                |                          |                |
| Interest rate swaps                                   | (2,160)        | 2,160          | –                        | –              |
| Inflation linked swaps                                | (400)          | –              | 400                      | –              |
| <b>Total</b>  | <b>(1,304)</b> | <b>56</b>      | <b>(398)</b>             | <b>(1,646)</b> |

Further information relating to interest rate risk in Financial Services is more fully described in the section on Financial Services financial risk factors below.

### (i) Cash flow sensitivity for floating rate instruments

The Group considers that a 100 basis point movement in interest rates is a reasonable measure of volatility. The sensitivity of floating rate balances to a change of 100 basis points in the interest rate (or such lesser amount as would result in a zero rate of interest) at the balance sheet date is shown below:

|                                   | 2017<br>Impact on<br>post-tax<br>loss<br>£m | 2017<br>Impact on<br>cash flow<br>hedge<br>reserve<br>£m | 2016<br>Impact on<br>post-tax<br>profit<br>£m | 2016<br>Impact on<br>cash flow<br>hedge<br>reserve<br>£m |
|-----------------------------------|---|--|---|--|
| Change in floating rate +/-100bps | (10)/5                                      | 2/(2)  | (7)/5   | 3/(3)  |

### (ii) Cash flow sensitivity for variable capped rate liabilities

The Group holds £761 million of capped inflation-linked borrowings (2016: £798 million) of which £400 million (2016: £400 million) have been swapped into fixed rate borrowings using inflation rate swaps maturing April 2017 to April 2019.

The Group considers that a 100 basis point movement in the RPI rate is a reasonable measure of volatility. The sensitivity of variable capped balances to a change of 100 basis points in the RPI rate at the balance sheet date is shown below:

|                                   | 2017<br>Impact on<br>post-tax<br>loss<br>£m | 2017<br>Impact on<br>cash flow<br>hedge<br>reserve<br>£m | 2016<br>Impact on<br>post-tax<br>profit<br>£m | 2016<br>Impact on<br>cash flow<br>hedge<br>reserve<br>£m |
|-----------------------------------|---|--|---|--|
| Change in floating rate +/-100bps | (3)/3                                       | 2/(2)  | (3)/3   | 6/(6)  |

## Commodity risk

Commodity risk is the risk of increased costs arising from unexpected movements in commodity prices impacting the Group's own use consumption of electricity, gas and diesel.

The Group hedges own use consumption of electricity and gas with forward purchases under flexible purchasing arrangements with its suppliers. The Group uses a combination of purchasing agreements and financial derivatives to hedge fuel exposures on a layered basis using contracts for difference.

The Group considers a ten per cent movement in commodity prices a reasonable measure of volatility.

## 23 Financial risk management continued

|  | 2017<br>Impact on<br>cash flow<br>hedge<br>reserve<br>£m | 2017<br>Impact on<br>cash flow<br>hedge<br>reserve<br>£m |
|--|--|--|
| Change in the fair value of electricity, diesel and gas price +/-10% | <b>2/(2)</b>   | 1/(1)  |

### Capital risk management

The Group defines capital as total equity plus net debt.

The Board's capital objective is to maintain a strong and efficient capital base to support the Group's strategic objectives, provide optimal returns for shareholders and safeguard the Group's status as a going concern. There has been no change to capital risk management policies during the year.

The Board monitors a broad range of financial metrics including return on capital employed, balance sheet gearing and fixed charge cover.

The Board can manage the Group's capital structure by diversifying the debt portfolio, adjusting the size and timing of dividends paid to shareholders, recycling capital through sale and leaseback transactions, issuing new shares or repurchasing shares in the open market and flexing capital expenditure.

From time-to-time the Company purchases its own shares in the market for the purpose of issuing shares under the Group's share option programmes; however the Group does not operate a defined share buy-back plan.

Part of the Group's capital risk management is to ensure compliance with the general covenants included in the Group's various borrowing facilities. There have been no breaches of general covenants in the financial year ended 11 March 2017.

## 23 Financial risk management continued

Information relating to Financial Services capital risk management is detailed below.

### Financial Services

Sainsbury's Bank (including Argos Financial Services) has identified a set of primary risk types (see table) that are overseen by a dedicated second line function. These risks are actively managed through primary risk policies and supporting policy standards that clearly articulate the rules, boundaries and measures by which the risks are controlled and help each colleague to understand their individual responsibilities. Our risk reporting processes provide a detailed and aggregated view of these risks to facilitate an active review and management process within defined risk appetite.

Financial Primary Risk

| Primary Risk   | Approach and mitigating actions  |
|--|--|
| <p><b>Liquidity and Funding Risk</b><br/>Holding insufficient resources to meet obligations as they fall due or only being able to access them at an excessive cost.<br/><i>Example:</i> A sudden and significant withdrawal of savings balances due to market uncertainty.</p>                  | <ul style="list-style-type: none"> <li>— Liquidity and Funding policy aligned to risk appetite, with targets for key ratios and coverage of stress outflows.</li> <li>— Key liquidity and funding ratios are monitored and reported on a daily basis with triggers in place for escalation.</li> <li>— Regular reviews of the Internal Liquidity Adequacy Assessment Process (ILAAP), funding plan and Liquidity Contingency Plan to support resilience.</li> </ul>            |
| <p><b>Market Risk</b><br/>The risk that the Bank's earnings and value would be reduced as result of adverse change to market parameters.<br/><i>Example:</i> Changes in the level and volatility of movement in interest rates and foreign exchange rates.</p>                                   | <ul style="list-style-type: none"> <li>— The Bank has a detailed market risk policy, which sets out its market risk limit structure. Earnings and market value sensitivity is reported on a regular basis to ALCO.</li> <li>— All new banking products or amendments to the terms of existing products are reviewed from an interest rate risk perspective to ensure compliance with existing risk appetite.</li> </ul>  |
| <p><b>Retail Credit Risk</b><br/>Losses arising from a retail customer failing to meet their capital or interest repayment obligations as they fall due.<br/><i>Example:</i> Adverse changes in UK macro-economic factors impacting on the credit quality of the Bank's assets.</p>              | <ul style="list-style-type: none"> <li>— Credit Risk policy aligned with risk appetite limits.</li> <li>— Robust credit decisioning tools use multiple sources of credit reference agency data in decisions and monitoring.</li> <li>— Effective credit risk governance and committee framework.</li> <li>— Regular reporting framework in place, including reference to external benchmarking.</li> <li>— Stress testing applied, early warning triggers in place.</li> </ul> |
| <p><b>Wholesale Credit Risk</b><br/>Losses arising from institutional counterparties failing to meet their contractual cash flow obligations.<br/><i>Example:</i> Downgrades in the credit rating of counterparties.</p>   | <ul style="list-style-type: none"> <li>— Counterparty limits are in place to control exposure levels.</li> <li>— Key ratios are monitored and reported on a daily basis with triggers in place for escalation.</li> <li>— Regular monitoring of credit ratings migration and CDS pricing of the Bank's key counterparties.</li> </ul>  |
| <p><b>Capital Adequacy Risk</b><br/>Holding an insufficient level or quality of capital for normal or stress requirements, or an inefficient deployment of capital.<br/><i>Example:</i> Adverse changes in the economy could deplete capital resources and/or increase capital requirements.</p> | <ul style="list-style-type: none"> <li>— Capital policy aligned to risk appetite, with a range set for normal conditions along with stress minimums.</li> <li>— Capital adequacy is monitored and reported on a daily basis with triggers in place for escalation.</li> <li>— The annual Internal Capital Adequacy Assessment Process (ICAAP) determines the adequacy of capital resources as well as mitigating actions.</li> </ul>   |

Further detail on each of these risks is shown below:

### Liquidity and funding risk

Liquidity risk is the risk that the Bank cannot meet its payment obligations as they fall due, or can only do so at extreme cost. We seek to ensure that we can meet our financial obligations at all times, even under liquidity stress conditions.

The annual Internal Liquidity Adequacy Assessment Process (ILAAP) enables the Bank to:

- (1) demonstrate that it understands the liquidity risks it is running
- (2) assess its liquidity needs under various stress scenarios and
- (3) put in place appropriate controls to mitigate liquidity risks.

In meeting its internal limits as well as PRA requirements, the Bank maintains a stock of high quality liquid assets that can be readily monetised by outright sale or repurchase agreement to meet the Bank's obligations to depositors and other creditors.

The Bank's Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) are regularly monitored and forecast alongside cash flow and funding ratios. We prepare long-term and short-term forecasts to assess liquidity requirements, taking into account factors such as ATM cash management, contractual maturities and customer deposit patterns (stable or less stable deposits) as well as outflows regarding pipelines and commitments. These reports support daily liquidity management, with early warning indicators reviewed on a daily basis and appropriate triggers for escalation and action in line with the risk appetite, Liquidity and Funding Policy and Liquidity Contingency Plan. Asset encumbrance ratios and risk indicators for wholesale funding concentrations by type (total/secured/unsecured), maturity, sector, geography and counterparty are also regularly monitored and reported to ALCO.

## 23 Financial risk management continued

### Market risk

Market risk is the risk that the value of the Bank's assets, liabilities, capital and earnings are exposed to the adverse change of the market risk drivers. The Bank's market risks include Interest Rate Risk in the Banking Book (IRRBB) and Foreign Exchange (FX) Risk. The Bank does not have a trading book.

#### Interest rate risk

IRRBB arises from interest rates movements which impact present value and timing of future cash flows resulting in changes to the underlying value of a bank's assets, liabilities and off-balance sheet instruments and hence its economic value. Interest rates movements also affect a bank's earnings by altering interest-sensitive income and expenses, affecting its net interest income.

The main types of interest rate risk faced by the Bank are:

- a) Re-pricing gap risk: the risk arising from timing differences in the interest rate changes of bank assets and liabilities (e.g. fixed rate personal loans and instant access savings accounts).
- b) Yield curve risk: the risk arising from changes in the slope and shape of the yield curve.
- c) Basis risk: risk arising from imperfect correlation between different interest rate indices (e.g. administered rate on savings products and treasury assets linked to LIBOR).
- d) Prepayment risk: the risk arising from the timing of customer prepayments which differ from planning and hedging assumptions.
- e) Pipeline risk: the risk of a customer drawing down, or not, a product at a rate which is unfavourable for the Bank.

Interest risk exposure is actively managed within limits that are aligned with the Bank's risk appetite by using financial instruments such as interest rate swaps and by taking into account natural hedges between assets and liabilities. The hedging strategies are implemented to ensure the Bank remains within its limits and that it takes advantage of natural hedging opportunities between fixed rate assets and liabilities with similar re-pricing characteristics.

In order to measure the exposure to interest rate risk under various interest rates shock scenarios, the Bank uses both economic value and earnings-based metrics: Market Value Sensitivity and Earnings at Risk. These metrics are monthly monitored and reported to ALCO.

For interest rate risk measurement, products are allocated within re-pricing gap analysis based on their nearest re-pricing date (all non-maturing deposits are assumed to re-price in month one) and personal loans are allocated according to behavioural repayment profile.

#### Foreign exchange risk

The Bank is exposed to FX risk through its holding of cash denominated in foreign currencies, primarily euro and US dollar, within its Travel Money bureaux in J Sainsbury's stores. Starting February 2017 the FX positions are hedged on a daily basis.

### Credit risk

Credit risk is the risk of financial loss arising from the failure of customers or other counterparties to settle their financial obligations to the Bank.

#### Retail credit risk

Management of credit risk in respect of retail customers makes use of automated credit decisioning techniques (both scorecards and policy rules) for new applications. In addition, behavioural scoring is used to assess the conduct of customers' accounts on an on-going basis, for example granting extensions to limits. Underwriting is undertaken by specialist teams in operational areas to complement these processes. The Retail Credit Risk Committee ensures that appropriate policies are established and adhered to and this is subject to further oversight from the Board Risk Committee. Internal Audit teams carry out regular reviews of credit risk processes and policies are reviewed and re-approved on an annual basis.

#### Wholesale and derivative credit risk

The Bank invests its liquidity resources in eligible investment securities that qualify for the regulatory Liquidity Coverage Ratio (LCR) and internal Operational Liquidity Pool (OLP). These investments include the Bank of England's (BoE) reserve account, UK government securities (gilts or Treasury bills), multilateral development bank securities, government guaranteed agency securities UK regulated covered bond programmes and asset backed securities.

Limits are established for all counterparty and asset class exposures based on their respective credit quality and market liquidity. Consideration is also given to geographical region and the strength of relevant sovereign credit ratings. Derivatives are subject to the same credit risk control procedures as are applied to other wholesale market instruments and the credit risk arising from mark to market derivative valuations is mitigated by daily margin calls, posting cash collateral to cover exposures. Daily monitoring is undertaken by the Bank's Treasury department, including early warning indicators with appropriate triggers for escalation.

## 23 Financial risk management continued

The table below shows the maximum exposure to credit risk for the components of the balance sheet, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through the use of collateral agreements.

|  | 2017<br>£m   | 2016<br>£m |
|--|--------------|------------|
| <b>Credit risk exposures relating to on balance sheet items</b>  |              |            |
| Loans and advances to customers                                  |              |            |
| Unsecured  | <b>4,564</b> | 3,301      |
| Secured  | <b>38</b>    | 43         |
| Cash and balances with central banks                             | <b>420</b>   | 423        |
| Loans and advances to banks                                      | <b>33</b>    | 25         |
| Derivative financial instruments                                 | <b>1</b>     | –          |
| Investment securities  | <b>333</b>   | 317        |
| Other assets   | <b>231</b>   | 206        |
| <b>Credit risk exposures relating to off balance sheet items</b> |              |            |
| Loans commitment and other related liabilities                   | <b>98</b>    | 77         |
| Treasury bills drawn under FLS                                   | <b>260</b>   | 240        |
| <b>Total credit risk exposures</b>                               | <b>5,978</b> | 4,632      |

### Credit quality per class of financial asset

Loans and advances to customers are summarised as follows:

|                                     | 2017<br>£m   | 2016<br>£m |
|-------------------------------------|--------------|------------|
| Impaired                            | <b>146</b>   | 106        |
| Past due but not impaired           | <b>50</b>    | 13         |
| Neither past due nor impaired       | <b>4,485</b> | 3,291      |
| Gross                               | <b>4,681</b> | 3,410      |
| Less: allowance for impairment      | <b>(89)</b>  | (79)       |
| Less: hedging fair value adjustment | <b>10</b>    | 13         |
| <b>Net book value</b>               | <b>4,602</b> | 3,344      |

## 23 Financial risk management continued

### Credit quality analysis

|  | Unsecured<br>lending<br>£m | Secured<br>lending<br>£m | Total<br>£m |
|--|----------------------------|--------------------------|-------------|
| <b>11 March 2017</b>                             |                            |                          |             |
| <b>Past due and impaired</b>                     |                            |                          |             |
| Less than three months, but impaired             | 2                          | –                        | 2           |
| Past due three to six months                     | 16                         | 2                        | 18          |
| Past due six to 12 months                        | –                          | –                        | –           |
| Past due over 12 months                          | –                          | –                        | –           |
| Recoveries                                       | 126                        | –                        | 126         |
| Possession                                       | –                          | –                        | –           |
| Total gross impaired loans                       | 144                        | 2                        | 146         |
| <b>Past due but not impaired</b>                 |                            |                          |             |
| Past due less than three months but not impaired | 49                         | 1                        | 50          |
| Total gross past due but not impaired            | 49                         | 1                        | 50          |
| <b>Neither past due nor impaired</b>             |                            |                          |             |
| Not impaired                                     | 4,450                      | 35                       | 4,485       |
| Total gross neither past due nor impaired        | 4,450                      | 35                       | 4,485       |
| Total gross amount due                           | 4,643                      | 38                       | 4,681       |

12 March 2016

|  |       |    |       |
|--|-------|----|-------|
| <b>Past due and impaired</b>                     |       |    |       |
| Less than three months, but impaired             | 2     | –  | 2     |
| Past due three to six months                     | 8     | –  | 8     |
| Past due six to 12 months                        | –     | 1  | 1     |
| Past due over 12 months                          | –     | –  | –     |
| Recoveries                                       | 95    | –  | 95    |
| Total gross impaired loans                       | 105   | 1  | 106   |
| <b>Past due but not impaired</b>                 |       |    |       |
| Past due less than three months but not impaired | 12    | 1  | 13    |
| Total gross past due but not impaired            | 12    | 1  | 13    |
| <b>Neither past due nor impaired</b>             |       |    |       |
| Not impaired                                     | 3,251 | 40 | 3,291 |
| Total gross neither past due nor impaired        | 3,251 | 40 | 3,291 |
| Total gross amount due                           | 3,368 | 42 | 3,410 |

Mortgages held over residential properties represent the only collateral held by the Bank for retail exposures. The market value of collateral held for impaired loans and loans past due but not impaired was £7 million (2016: £7 million). The fair value of collateral held against possession cases was £nil (2016: £nil).

### Financial Services capital resources (unaudited)

The following table analyses the regulatory capital resources under both transitional and end point measures of CRD IV (for which there is no difference in the case of the Bank). CRD IV regulations are being phased in over a five year period from 2013 – 2018. From a prudential perspective, the Bank is monitored and supervised on a consolidated basis with its subsidiary, Home Retail Group Card Services Limited, from the point of acquisition of Argos Financial Services onwards. The Bank has obtained an individual consolidation waiver from the PRA, which allows the Bank to monitor its capital position on a consolidated basis only. Therefore, the 28 February 2017 capital position shown below is on a regulatory consolidated basis, but the comparative shows the Bank standalone position.

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| Common Equity Tier 1 (CET 1) capital:      |            |            |
| Ordinary share capital                     | 566        | 436        |
| Allowable reserves                         | 148        | 167        |
| Regulatory adjustments                     | (147)      | (118)      |
| Total Common Equity Tier 1 (CET 1) capital | 567        | 485        |
| Tier 1 capital                             | 567        | 485        |

Regulatory capital is calculated under the Capital Requirements Regulations and Capital Requirements Directive (collectively known as CRD IV) as enacted in the UK. Common Equity Tier 1 (CET 1) capital includes ordinary share capital, other reserves, losses and regulatory deductions. The Bank does not currently hold any Tier 2 capital.

## 23 Financial risk management continued

The movement of CET 1 capital during the financial year is analysed as follows:

|  | 2017<br>£m  | 2016<br>£m |
|--|-------------|------------|
| At 1 March 2017/1 March 2016                 | <b>485</b>  | 354        |
| Share capital issued                         | <b>130</b>  | 137        |
| Verified profit attributable to shareholders | <b>(4)</b>  | 6          |
| Verified losses of subsidiary undertakings   | <b>(17)</b> | –          |
| Other reserve movements                      | <b>2</b>    | 2          |
| Increase in intangible assets                | <b>(29)</b> | (14)       |
| At 28 February 2017/29 February 2016         | <b>567</b>  | 485        |

### Leverage ratio (unaudited)

The leverage ratio is defined as the ratio of Tier 1 capital to adjusted assets, which is measured below on a regulatory consolidated basis. The denominator represents the total non-risk weighted assets of the regulatory group (Bank and Home Retail Group Card Services Limited) adjusted for certain off balance sheet exposures, assets and regulatory deductions and provides a non-risk-weighted 'backstop' capital measure. The leverage ratio is planned to become a Pillar 1 measure from 1 January 2018. The leverage ratio is calculated below as at 28 February 2017 – this represents both transitional and end point CRD IV measures. The Bank's leverage ratio of 8.6 per cent exceeds the minimum Basel leverage ratio of 3 per cent.

|  | 2017<br>£m   | 2016<br>£m |
|--|--------------|------------|
| <b>Components of the leverage ratio</b>                              |              |            |
| Total assets as per published financial statements                   | <b>5,794</b> | 4,499      |
| Uplift on consolidation of subsidiary undertakings                   | <b>42</b>    | –          |
| Exposure value for derivatives and securities financing transactions | <b>269</b>   | 6          |
| Off balance sheet exposures: unconditionally cancellable (10%)       | <b>633</b>   | 336        |
| Off balance sheet: other (100%)                                      | <b>20</b>    | 260        |
| Other adjustments  | <b>(168)</b> | (136)      |
|  | <b>6,590</b> | 4,965      |
| Tier 1 capital   | <b>567</b>   | 485        |
| Leverage ratio   | <b>8.6%</b>  | 9.8%       |

### Capital management

The Bank manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of its activities. During the period to 28 February 2017, the Bank received planned injections of £130 million of ordinary share capital to support the increased capital requirements resulting from: the acquisition of Argos Financial Services and forecast costs and deductible intangible assets generated through the development of flexible banking platforms. Capital adequacy is monitored on an on-going basis by senior management, the ALCO, the Executive Risk Committee and the Board Risk Committee. Our submissions to the PRA in the year have shown that the Bank has complied with all externally imposed capital requirements. The Bank's capital ratio of 13.3 per cent exceeds internal and regulatory thresholds.

Sainsbury's Bank plc, as the principal regulated entity within Financial Services, will disclose Pillar 3 information as required by the Capital Requirements Regulations and PRA prudential sourcebook on the J Sainsbury plc external website.

## 24 Financial instruments

### Accounting policies

#### a) Financial assets

The Group classifies its financial assets in the following categories: at fair value through profit or loss (FVTPL), loans and receivables, and available-for-sale (AFS). AFS investments are initially measured at fair value including transaction costs and are recognised at the trade date. Financial assets held at FVTPL are initially recognised at fair value and transaction costs are expensed.

'Financial assets at FVTPL' include financial assets held for trading and those designated at FVTPL at inception. FVTPL are derivatives classified as held for trading unless they are accounted for as an effective hedging instrument. 'Financial assets at FVTPL' are recorded at fair value, with any fair value gains or losses recognised in the income statement in the period in which they arise.

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date. Subsequent to initial recognition at fair value plus transaction costs, these assets are recorded at fair value at each period end with the movements recognised in other comprehensive income until derecognition or impaired at which time the cumulative gain or loss previously recognised in other comprehensive income reserves are recycled is recognised in the income statement. Dividends on AFS equity instruments are recognised in the income statement when the entity's right to receive payment is established. Interest on AFS debt instruments is recognised using the effective interest method.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Group has no intention of trading these loans and receivables and include amounts due from Financial Services customers and amounts due from other banks. Subsequent to initial recognition at fair value plus transaction costs, these assets are carried at amortised cost less impairment using the effective interest method. Income from these financial assets is calculated on an effective yield basis and is recognised in the income statement.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership.

Within Financial Services, securities sold subject to standard sale and repurchase agreements ('repos') are not derecognised where the Bank retains substantially all the risks and rewards of ownership by virtue of the predetermined repurchase price. The counterparty liability is included in other deposits.

#### b) Impairment of financial assets

An assessment of whether there is objective evidence of impairment is carried out for all financial assets or groups of financial assets at the balance sheet date. An assessment of impairment may be of individual assets ('individual impairment') or of a portfolio of assets ('collective impairment') where indicators arise. A financial asset or a group of financial assets is considered to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

For individual impairment, the principal loss event is one or more missed payments, although other loss events can also be taken into account, including arrangements in place to pay less than the contractual payments, fraud and bankruptcy or other financial difficulty indicators. An assessment of collective impairment will be made of financial assets with similar risk characteristics. For these assets, portfolio loss experience is used to provide objective evidence of impairment.

Where there is objective evidence that an impairment loss exists on loans and receivables, impairment provisions are made to reduce the carrying value of financial assets to the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

For financial assets carried at amortised cost, the charge to the income statement reflects the movement in the level of provisions made, together with amounts written off net of recoveries in the year.

In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the asset below its cost is considered in determining whether the asset is impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss is removed from equity and recognised in the income statement.

Impairment losses recognised in the income statement on equity instruments are not reversed. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement.

Interest will continue to accrue on all financial assets, based on the written down carrying value based on the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. To the extent that a provision may be increased or decreased in subsequent periods, the recognition of interest will be based on the latest balance net of provision.

#### c) Financial Services loans and advances including impairment

For Financial Services portfolios of loans, such as credit card lending, storecard lending and personal loans, impairment provisions are calculated for groups of assets, otherwise impairment is identified at a counterparty specific level following objective evidence that a financial asset is impaired. Such evidence may include a missed interest or principal payment or the breach of a banking covenant. Provisioning on unsecured balances identified as being in arrears is calculated based on past experience, with regularly updated assumptions. The present value of estimated cash flows recoverable is determined after taking into account any security held. The amount of impairment is calculated by comparing the present value of the cash flows discounted at the loan's original effective interest rate with the balance sheet carrying value. If impaired, the carrying value is adjusted and the difference charged to the income statement and a provision recognised in the balance sheet.

The written down value of the impaired loan is compounded back to its net realisable balance over time using an effective interest rate. This is reported through interest receivable within the income statement and represents the unwinding of the discount.

A write-off is made when all or part of a claim is deemed uncollectable or forgiven. Write-offs are charged against previously established provisions for impairment or directly to the income statement. Subsequent recoveries of amounts written off decrease the charge for loan impairment in the income statement.

## 24 Financial instruments continued

An allowance for impairment losses is also maintained in respect of assets which are impaired at the balance sheet date but which have not been identified as such, based on historical loss experience and other relevant factors. This includes analysis of the likelihood of a particular balance to move into an arrears status within a defined period of time and application of an appropriate loss rate. The emergence period into an arrears state represents the average time elapsed between the loss trigger event and default. The methodology and assumptions used are regularly reviewed to reduce any differences between estimates and actual results.

Interest-bearing bank loans, overdrafts, other deposits and amounts due to Sainsbury's Bank customers are recorded initially at fair value, which is generally the proceeds received, net of direct issue costs. Subsequently, these liabilities are held at amortised cost using the effective interest method.

### d) Financial liabilities

Financial liabilities charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accrual basis in the income statement using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

The fair value of the liability component of a convertible bond is determined using the market interest rate for an equivalent non-convertible bond. This amount is recorded as a liability on an amortised cost basis until extinguished on conversion or maturity of the bonds. The remainder of the proceeds are allocated to the conversion option which is recognised in shareholders' equity, net of income tax effects and is not subsequently remeasured.

Issue costs are apportioned between the liability and the equity components of the convertible bonds based on their carrying amounts at the date of issue.

Financial liabilities are derecognised when the obligation under the liability is discharged, cancelled or expires.

### e) Fair value estimation

The methods and assumptions applied in determining the fair values of financial assets and financial liabilities are disclosed below in the financial disclosure section.

### f) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. The legally enforceable right must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy of the company or the counterparty.

## Derivative financial instruments and hedge accounting

The Group uses derivative financial instruments to hedge its exposure to foreign exchange, interest rate and commodity risks. All derivative financial instruments are initially measured at fair value on the contract date and are also measured at fair value at subsequent reporting dates. Where derivatives do not qualify for hedge accounting, any changes in the fair value of the derivative financial instrument are recognised in the income statement as finance income or costs as they arise.

To qualify for hedge accounting, the Group documents, at the inception of the hedge, the hedging risk management strategy, the relationship between the hedging instrument and the hedged item or transaction, the nature of the risks being hedged and an assessment of the effectiveness of the hedging relationship to ensure it is highly effective on an ongoing basis.

Where a derivative does qualify for hedge accounting, any changes in fair value are recognised depending on the nature of the hedge relationship and the item being hedged as follows:

### a) Cash flow hedges

Hedge relationships are classified as cash flow hedges where the derivative financial instruments hedge the Group's exposure to variability in cash flows resulting from a highly probable forecasted transaction. These include the exchange rate risk of inventory purchases denominated in foreign currency, as well as the commodity risk on purchases of power and fuel. Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cash flows are recognised directly in other comprehensive income and the ineffective portion is recognised immediately in the income statement.

If the cash flow hedge of a firm commitment or forecast transaction results in the recognition of a non-financial asset or liability, then, at the time the asset or liability is recognised, the associated gains or losses on the derivative that had previously been recognised in other comprehensive income are included in the initial measurement of the asset or liability.

### b) Fair value hedges

Hedge relationships are classified as fair value hedges where the derivative financial instruments hedge the change in the fair value of a financial asset or liability due to movements in interest rates. The changes in fair value of the hedging instrument are recognised in the income statement. The hedged item is also adjusted for changes in fair value attributable to the hedged risk, with the corresponding adjustment made in the income statement.

### c) Portfolio fair value hedging

During the period Sainsbury's Bank used portfolio fair value hedging as a risk management tool for hedging interest rate risk on the personal loans portfolio. Portfolio fair value hedging allows the designation of the whole or part of a portfolio of assets or liabilities with similar risk exposures. The hedged item can be designated based on expected maturities to match the hedging derivative maturity.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. At that time, any cumulative gain or loss on the hedging instrument recognised in other comprehensive income is retained in equity until the forecasted transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in other comprehensive income is transferred to the income statement for the period.

## 24 Financial instruments continued

The fair value of derivative financial instruments has been disclosed in the balance sheet as follows:

|              | 2017        |                 | Group               |                         |
|--------------|-------------|-----------------|---------------------|-------------------------|
|              | Asset<br>£m | Liability<br>£m | 2016<br>Asset<br>£m | 2016<br>Liability<br>£m |
| Non-current  | 10          | (38)            | 17                  | (69)                    |
| Current      | 94          | (22)            | 51                  | (43)                    |
| <b>Total</b> | <b>104</b>  | <b>(60)</b>     | 68                  | (112)                   |

The fair value and notional amount of derivatives analysed by hedge type are as follows:

|   | 2017             |                |                  |                | 2016             |                |                  |                |
|---|------------------|----------------|------------------|----------------|------------------|----------------|------------------|----------------|
|   | Asset            |                | Liability        |                | Asset            |                | Liability        |                |
|   | Fair value<br>£m | Notional<br>£m |
| <b>Fair value hedges</b>                                |                  |                |                  |                |                  |                |                  |                |
| Interest rate swaps                                     | 8                | 774            | (22)             | 2,386          | 18               | 620            | (22)             | 2,291          |
| <b>Cash flow hedges</b>                                 |                  |                |                  |                |                  |                |                  |                |
| Interest rate swaps                                     | –                | –              | (4)              | 100            | –                | –              | (4)              | 100            |
| Inflation rate swaps                                    | –                | –              | (2)              | 400            | –                | –              | (10)             | 400            |
| Foreign exchange forward contracts                      | 77               | 1,301          | (2)              | 119            | 20               | 453            | (2)              | 156            |
| Commodity contracts                                     | 3                | 21             | –                | –              | –                | –              | (6)              | 21             |
| <b>Derivatives not in a formal hedging relationship</b> |                  |                |                  |                |                  |                |                  |                |
| Interest rate swaps                                     | 16               | 341            | (15)             | 295            | 30               | 386            | (27)             | 327            |
| Cross currency and foreign exchange swaps               | –                | –              | –                | –              | –                | –              | (7)              | 71             |
| Commodity contracts                                     | –                | –              | (15)             | 15             | –                | –              | (34)             | 15             |
| <b>Total</b>  | <b>104</b>       | <b>2,437</b>   | <b>(60)</b>      | <b>3,315</b>   | 68               | 1,459          | (112)            | 3,381          |

The notional and fair value of foreign exchange forward contracts has increased on consolidation of the Home Retail Group plc.

### Fair value hedges

#### Interest rate swaps

The Group holds a £160 million portfolio of interest rate swaps (2016: £206 million) to hedge a portion of fixed rate borrowings maturing in April 2018. Under the terms of the swaps, the Group receives fixed rate interest and pays floating rate interest.

Financial Services holds a £3,000 million portfolio of interest rate swaps accounted for as fair value hedges (2016: £2,705 million). Interest rate swaps are transacted to hedge Financial Services customer assets, fixed interest treasury instruments and non-interest bearing items (including reserves) through a combination of pay and receive fixed swaps (£2,354 million and £646 million respectively (2016: £2,350 million and £355 million respectively)). All derivatives are designated into effective fair value hedge accounting relationships.

For the year to 11 March 2017, the fair value movement in the Group's interest rate swaps resulted in a charge to the income statement of £7 million (2016: £6 million). The fair value movement in the underlying fixed rate borrowings and Sainsbury's Bank loans and advances to customers resulted in a credit to the income statement of £6 million (2016: £6 million).

### Cash flow hedges

#### Interest rate swaps

The Group holds a £400 million (2016: £400 million) portfolio of inflation rate swaps to hedge a portion of the inflation linked secured loan due 2031. Under the terms of the swaps, the Group receives annual RPI inflation (subject to a cap at five per cent and floor at nil per cent) and pays fixed rate interest.

The Group holds a £100 million (2016: £100 million) portfolio of interest rate swaps to hedge £100 million of a £200 million floating rate bank loan due 2019. Under the terms of the swaps, the Group receives floating rate interest and pays fixed rate interest.

As at 11 March 2017, an unrealised loss of £4 million (2016: loss of £13 million) is included in other comprehensive income in respect of the swaps designated as cash flow hedges. This loss will be transferred to the income statement over the next 24 months.

#### Foreign exchange forward contracts

The Group holds a portfolio of foreign exchange forward contracts to hedge its future foreign currency trading liabilities. As at 11 March 2017 the Group had forward purchased a net €135 million (2016: €127 million) and sold sterling with maturities from March 2017 to July 2018 (2016: March 2016 to February 2017) and forward purchased US\$1,521 million (2016: US\$763 million) and sold sterling with maturities from March 2017 to June 2018 (2016: March 2016 to June 2017).

As at 11 March 2017, an unrealised profit of £28 million (2016: £16 million) is included in other comprehensive income in respect of the forward contracts. This profit will be transferred to the income statement over the next 15 months. During the year a credit to the income statement of £83 million was transferred from the cash flow hedge equity reserve and included in cost of sales (2016: £12 million credit).

## 24 Financial instruments continued

### Commodity forward contracts

The Group holds a portfolio of commodity forward contracts to hedge its own use fuel consumption over the next 24 months.

At 11 March 2017, an unrealised gain of £3 million (2016: loss of £5 million) is included in other comprehensive income in respect of the commodity contracts. This gain will be transferred to the income statement over the next 24 months.

### Derivatives not in a hedge relationship

Some of the Group's derivative contracts do not qualify for hedge accounting and are therefore not designated in a hedging relationship. In addition, where gains or losses on a derivative contract economically offset the losses or gains on an underlying transaction, the derivative is not designated as being in a hedging relationship.

### Interest rate and foreign exchange swaps

The Group holds a £295 million (2016: £327 million) portfolio of interest rate swaps at fair value through profit or loss to convert floating rate obligations into fixed rates. Under the terms of the swaps the Group receives floating rate interest and pays fixed rate interest. Offsetting these swaps the Group holds a £341 million (2016: £386 million) portfolio of interest rate swaps at fair value through profit or loss, to convert fixed rate obligations into floating rate interest. Under the terms of the swaps the Group receives fixed rate interest and pays floating rate interest.

### Commodity forward contracts

Commodity forward contracts at fair value through profit and loss relate to the Group's long-term fixed price power purchase agreements with independent producers.

### Fair value

Set out below is a comparison of the carrying amount and the fair value of financial instruments that are carried in the financial statements at a value other than fair value. The fair values of financial assets and liabilities are based on prices available from the market on which the instruments are traded. Where market values are not available, the fair values of financial assets and liabilities have been calculated by discounting expected future cash flows at prevailing interest rates. The fair values of short-term deposits, trade receivables, other receivables, overdrafts and payables are assumed to approximate to their book values.

|   | Group<br>Carrying<br>amount<br>£m | Group<br>Fair value<br>£m |
|---|-----------------------------------|---------------------------|
| <b>At 11 March 2017</b>                                     |                                   |                           |
| <b>Financial assets</b>                                     |                                   |                           |
| Amounts due from Financial Services customers <sup>1</sup>  | 4,602                             | 4,640                     |
| <b>Financial liabilities</b>                                |                                   |                           |
| Loans due 2018 <sup>2</sup>                                 | (680)                             | (706)                     |
| Loans due 2031  | (761)                             | (1,062)                   |
| Bank overdrafts   | (6)                               | (6)                       |
| Bank loans due 2019   | (199)                             | (199)                     |
| Convertible bond due 2019                                   | (427)                             | (473)                     |
| Obligations under finance leases                            | (138)                             | (138)                     |
| Amounts due to Financial Services customers and other banks | (4,921)                           | (4,924)                   |
| <b>At 12 March 2016</b>                                     |                                   |                           |
| <b>Financial assets</b>                                     |                                   |                           |
| Amounts due from Financial Services customers <sup>1</sup>  | 3,344                             | 3,337                     |
| <b>Financial liabilities</b>                                |                                   |                           |
| Amounts due to Group entities                               | –                                 | –                         |
| Loans due 2018 <sup>2</sup>                                 | (780)                             | (824)                     |
| Loans due 2031  | (799)                             | (896)                     |
| Bank overdrafts   | (3)                               | (3)                       |
| Bank loans due 2016   | (39)                              | (39)                      |
| Bank loans due 2019   | (199)                             | (199)                     |
| Convertible bond due 2019                                   | (418)                             | (473)                     |
| Obligations under finance leases                            | (175)                             | (175)                     |
| Amounts due to Financial Services customers and other banks | (3,755)                           | (3,757)                   |

1 Included within a portfolio fair value hedging relationship with £3,000 million (2016: £2,705 million) of interest rate swaps.

2 Includes £160 million accounted for as a fair value hedge (2016: £206 million).

## 24 Financial instruments continued

The fair value of financial assets as disclosed in the table above as at 11 March 2017 was £4,640 million (2016: £3,337 million). The fair value of the financial assets has been calculated by discounting cash flows at prevailing interest rates and is within Level 2 of the fair value hierarchy. The fair value of financial liabilities was £7,508 million (2016: £6,366 million) of which £473 million (2016: £473 million) has been determined using market values and is within Level 1 of the fair value hierarchy. The remaining £7,035 million (2016: £5,893 million) has been calculated by discounting cash flows at prevailing interest rates and is within Level 2 of the fair value hierarchy.

### Fair value measurements recognised in the balance sheet

The following table provides an analysis of financial instruments that are recognised at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are derived from quoted market prices (unadjusted) in active markets for identical assets or liabilities at the balance sheet date. This level includes listed equity securities and debt instrument on public exchanges;
- Level 2 fair value measurements are derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). The fair value of financial instruments is determined by discounting expected cash flows at prevailing interest rates; and
- Level 3 fair value measurements are derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

| Group                                      | Level 1<br>£m | Level 2<br>£m | Level 3<br>£m | Total<br>£m |
|--|---------------|---------------|---------------|-------------|
| <b>At 11 March 2017</b>                    |               |               |               |             |
| <b>Available-for-sale financial assets</b> |               |               |               |             |
| Interest bearing financial assets          | –             | 39            | –             | 39          |
| Other financial assets                     | –             | 13            | 148           | 161         |
| Investment securities                      | 333           | –             | –             | 333         |
| <b>Financial assets</b>                    |               |               |               |             |
| Derivative financial assets                | –             | 104           | –             | 104         |
| <b>Financial liabilities</b>               |               |               |               |             |
| Derivative financial liabilities           | –             | (45)          | (15)          | (60)        |

At 12 March 2016

### Available-for-sale financial assets

|                                   |     |    |     |     |
|-----------------------------------|-----|----|-----|-----|
| Interest bearing financial assets | –   | 35 | –   | 35  |
| Other financial assets            | –   | –  | 146 | 146 |
| Investment securities             | 203 | –  | 1   | 204 |

### Financial assets

|                             |   |    |   |    |
|-----------------------------|---|----|---|----|
| Derivative financial assets | – | 68 | – | 68 |
|-----------------------------|---|----|---|----|

### Financial liabilities

|                                  |   |      |      |       |
|----------------------------------|---|------|------|-------|
| Derivative financial liabilities | – | (78) | (34) | (112) |
|----------------------------------|---|------|------|-------|

The increase in derivative financial assets and liabilities is as a result of the consolidation of Home Retail Group plc.

Reconciliation of Level 3 fair value measurements of financial assets and liabilities:

|   | Available-for-sale financial assets<br>£m | Commodity derivatives<br>£m | Investment securities<br>£m | Total<br>£m |
|---|---|-----------------------------|-----------------------------|-------------|
| <b>52 weeks to 11 March 2017</b>              |   |                             |                             |             |
| At 12 March 2016                              | 146                                       | (34)                        | 1                           | 113         |
| In finance cost in the Group income statement | –   | 19                          | (1)                         | 18          |
| In other comprehensive income                 | 2   | –                           | –                           | 2           |
| <b>At 11 March 2017</b>                       | <b>148</b>                                | <b>(15)</b>                 | <b>–</b>                    | <b>133</b>  |

|   | Available-for-sale financial assets<br>£m | Commodity derivatives<br>£m | Investment securities<br>£m | Total<br>£m |
|---|---|-----------------------------|-----------------------------|-------------|
| <b>52 weeks to 12 March 2016</b>              |   |                             |                             |             |
| At 14 March 2015                              | 145                                       | (14)                        | –                           | 131         |
| In finance cost in the Group income statement | –   | (20)                        | –                           | (20)        |
| In other comprehensive income                 | 1   | –                           | 1                           | 2           |
| <b>At 12 March 2016</b>                       | <b>146</b>                                | <b>(34)</b>                 | <b>1</b>                    | <b>113</b>  |

## 24 Financial instruments continued

The available-for-sale financial assets relate to the Group's beneficial interest in a property investment pool. The net present value of the Group's interest in the various freehold reversions owned by the property investment pool has been derived by assuming a property growth rate of 0.5 per cent per annum (2016: 0.6 per cent) and a discount rate of nine per cent (2016: nine per cent), (see note 13). The sensitivity of this balance to changes of one per cent in the assumed rate of property rental growth and one per cent in the discount rate holding other assumptions constant is shown below:

|                           | 2017<br>Change in<br>growth rate<br>+/-1.0%<br>£m | 2017<br>Change in<br>discount<br>rate +/-1.0%<br>£m | 2016<br>Change in<br>growth rate<br>+/-1.0%<br>£m | 2016<br>Change in<br>discount rate<br>+/-1.0%<br>£m |
|---------------------------|---|---|---|---|
| Available-for-sale assets | <b>13/(13)</b>                                    | <b>(8)/9</b>  | 15/(14)   | (9)/10  |

The Group has entered into several long-term fixed price Power Purchase agreements with independent producers. Included within derivative financial liabilities is £15 million (2016: £34 million) relating to these agreements. The Group values its Power Purchase agreements as the net present value of the estimated future usage at the contracted fixed price less the market implied forward energy price discounted at the prevailing swap rate. The Group also makes an assumption regarding expected energy output based on the historical performance and the producer's estimate of expected electricity output. The sensitivity of this balance to changes of 20 per cent in the assumed rate of energy output and 20 per cent in the implied forward energy prices holding other assumptions constant is shown below:

|                                  | 2017<br>Change<br>in volume<br>+/-20.0%<br>£m | 2017<br>Change in<br>electricity<br>forward<br>price +/-<br>20.0%<br>£m | 2016<br>Change<br>in volume<br>+/- 20.0%<br>£m | 2016<br>Change in<br>electricity<br>forward price<br>+/- - 20.0%<br>£m |
|----------------------------------|---|---|--|--|
| Derivative financial instruments | <b>(3)/3</b>                                  | <b>12/(13)</b>  | (7)/7  | 13/(14)  |

### Financial assets and liabilities by category

Set out below are the accounting classification of each class of financial assets and liabilities as at 11 March 2017 and 12 March 2016.

| Group   | Loans and<br>receivables<br>£m | Available-<br>for-sale<br>£m | Fair value<br>through<br>profit<br>or loss<br>£m | Derivatives<br>used for<br>hedging<br>£m | Other<br>financial<br>liabilities<br>£m | Total<br>£m    |
|---|--------------------------------|------------------------------|--|--|---|----------------|
| <b>At 11 March 2017</b>                               |                                |                              |  |  |   |                |
| Cash and cash equivalents                             | <b>1,083</b>                   | –                            | –  | –  | –                                       | <b>1,083</b>   |
| Trade and other receivables                           | <b>477</b>                     | –                            | –  | –  | –                                       | <b>477</b>     |
| Amounts due from Financial Services customers         | <b>4,602</b>                   | –                            | –  | –  | –                                       | <b>4,602</b>   |
| Available-for-sale financial assets                   | –                              | <b>535</b>                   | –  | –  | –                                       | <b>535</b>     |
| Trade and other payables                              | –                              | –                            | –  | –  | <b>(3,741)</b>                          | <b>(3,741)</b> |
| Current borrowings                                    | –                              | –                            | –  | –  | <b>(172)</b>                            | <b>(172)</b>   |
| Non-current borrowings                                | –                              | –                            | –  | –  | <b>(2,039)</b>                          | <b>(2,039)</b> |
| Amounts due to Financial Services customers and banks | –                              | –                            | –  | –  | <b>(4,921)</b>                          | <b>(4,921)</b> |
| Derivative financial instruments                      | –                              | –                            | <b>(14)</b>                                      | <b>58</b>                                | –                                       | <b>44</b>      |
|   | <b>6,162</b>                   | <b>535</b>                   | <b>(14)</b>                                      | <b>58</b>                                | <b>(10,873)</b>                         | <b>(4,132)</b> |

| Group   | Loans and<br>receivables<br>£m | Available-<br>for-sale<br>£m | Fair value<br>through profit<br>or loss<br>£m | Derivatives<br>used for<br>hedging<br>£m | Other<br>financial<br>liabilities<br>£m | Total<br>£m |
|---|--------------------------------|------------------------------|---|--|---|-------------|
| At 12 March 2016                                      |                                |                              |   |  |   |             |
| Cash and cash equivalents                             | 1,143                          | –                            | –   | –  | –                                       | 1,143       |
| Trade and other receivables                           | 493                            | –                            | –   | –  | –                                       | 493         |
| Amounts due from Financial Services customers         | 3,344                          | –                            | –   | –  | –                                       | 3,344       |
| Available-for-sale financial assets                   | –                              | 388                          | –   | –  | –                                       | 388         |
| Trade and other payables                              | –                              | –                            | –   | –  | (2,945)                                 | (2,945)     |
| Current borrowings                                    | –                              | –                            | –   | –  | (223)                                   | (223)       |
| Non-current borrowings                                | –                              | –                            | –   | –  | (2,190)                                 | (2,190)     |
| Amounts due to Financial Services customers and banks | –                              | –                            | –   | –  | (3,755)                                 | (3,755)     |
| Derivative financial instruments                      | –                              | –                            | (38)  | (6)                                      | –                                       | (44)        |
|   | 4,980                          | 388                          | (38)  | (6)                                      | (9,113)                                 | (3,789)     |

## 25 Notes to the cash flow statements

### Accounting policies

#### Cash and cash equivalents

Cash and bank balances comprise cash in hand and at bank, deposits at central banks, investments in money market funds and deposits and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

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

#### (a) Reconciliation of operating profit to cash generated from operations

|  | 2017<br>£m   | 2016<br>£m |
|--|--------------|------------|
| Profit before tax  | 503          | 548        |
| Net finance costs  | 102          | 148        |
| Share of post-tax loss from joint ventures (note 12)                         | 37           | 11         |
| Operating profit   | 642          | 707        |
| Adjustments for:   |              |            |
| Depreciation expense   | 600          | 559        |
| Amortisation expense   | 28           | 25         |
| Non-cash adjustments arising from acquisitions (note 3) <sup>1</sup>         | 12           | (13)       |
| Financial Services impairment losses on loans and advances                   | 33           | 15         |
| Profit on disposal of properties   | (101)        | (100)      |
| Loss on disposal of intangibles  | 36           | –          |
| Profit on disposal of Pharmacy business                                      | (98)         | –          |
| Impairment charge/(release) of property, plant and equipment                 | 55           | (9)        |
| Foreign exchange differences   | (7)          | 24         |
| Share-based payments expense   | 32           | 23         |
| Retirement benefit obligations <sup>2</sup>                                  | (311)        | (201)      |
| Operating cash flows before changes in working capital                       | 921          | 1,030      |
| Changes in working capital:  |              |            |
| (Increase)/decrease in inventories   | (6)          | 12         |
| Increase in current available-for-sale financial assets                      | (126)        | (202)      |
| Decrease/(increase) in trade and other receivables                           | 37           | (25)       |
| Increase in amounts due from Financial Services customers and other deposits | (681)        | (318)      |
| Increase/(decrease) in trade and other payables                              | 36           | (16)       |
| Increase in amounts due to Financial Services customers and other deposits   | 1,166        | 95         |
| (Decrease)/increase in provisions and other liabilities                      | (24)         | 48         |
| <b>Cash generated from operations</b>  | <b>1,323</b> | <b>624</b> |

1 This excludes £26 million income (2016: £10 million charge) relating to acquisition adjustment unwinds included with amortisation in this note, and a £6 million charge for acquisition adjustment unwinds included in depreciation (2016: £nil).

2 The adjustment for retirement benefit obligations reflects the difference between the defined benefit pension scheme expenses of £8 million (2016: £6 million), and the cash contributions of £319 million made by the Group to the defined benefit scheme (2016: £207 million).

#### (b) Cash and cash equivalents

For the purposes of the cash flow statements, cash and cash equivalents comprise the following:

|                                      | 2017<br>£m   | 2016<br>£m   |
|--------------------------------------|--------------|--------------|
| Cash in hand and bank balances       | 439          | 374          |
| Money market funds and deposits      | 403          | 480          |
| Treasury bills                       | –            | 20           |
| Deposits at central banks            | 241          | 269          |
| Cash and bank balances               | 1,083        | 1,143        |
| Bank overdrafts (note 27)            | (6)          | (3)          |
| <b>Net cash and cash equivalents</b> | <b>1,077</b> | <b>1,140</b> |

## 26 Analysis of net debt

|  | Retail         | Financial Services | Group <sup>1</sup> | Retail     | Financial Services | Group <sup>1</sup> |
|--|----------------|--------------------|--------------------|------------|--------------------|--------------------|
|  | 2017<br>£m     | 2017<br>£m         | 2017<br>£m         | 2016<br>£m | 2016<br>£m         | 2016<br>£m         |
| <b>Non-current assets</b>                            |                |                    |                    |            |                    |                    |
| Interest bearing available-for-sale financial assets | 39             | –                  | 39                 | 35         | –                  | 35                 |
| Available-for-sale investment securities             | –              | 233                | 233                | –          | 156                | 156                |
| Derivative financial instruments                     | 9              | 1                  | 10                 | 13         | 4                  | 17                 |
|  | <b>48</b>      | <b>234</b>         | <b>282</b>         | 48         | 160                | 208                |
| <b>Current assets</b>                                |                |                    |                    |            |                    |                    |
| Cash and cash equivalents                            | 630            | 453                | 1,083              | 577        | 566                | 1,143              |
| Available-for-sale investment securities             | –              | 100                | 100                | –          | 48                 | 48                 |
| Derivative financial instruments                     | 94             | –                  | 94                 | 51         | –                  | 51                 |
|  | <b>724</b>     | <b>553</b>         | <b>1,277</b>       | 628        | 614                | 1,242              |
| <b>Current liabilities</b>                           |                |                    |                    |            |                    |                    |
| Bank overdrafts                                      | (6)            | –                  | (6)                | (3)        | –                  | (3)                |
| Borrowings   | (143)          | –                  | (143)              | (182)      | –                  | (182)              |
| Finance leases                                       | (23)           | –                  | (23)               | (38)       | –                  | (38)               |
| Derivative financial instruments                     | (19)           | (3)                | (22)               | (41)       | (2)                | (43)               |
|  | <b>(191)</b>   | <b>(3)</b>         | <b>(194)</b>       | (264)      | (2)                | (266)              |
| <b>Non-current liabilities</b>                       |                |                    |                    |            |                    |                    |
| Borrowings   | (1,924)        | –                  | (1,924)            | (2,053)    | –                  | (2,053)            |
| Finance leases                                       | (115)          | –                  | (115)              | (137)      | –                  | (137)              |
| Derivative financial instruments                     | (19)           | (19)               | (38)               | (48)       | (21)               | (69)               |
|  | <b>(2,058)</b> | <b>(19)</b>        | <b>(2,077)</b>     | (2,238)    | (21)               | (2,259)            |
| <b>Total net debt</b>                                | <b>(1,477)</b> | <b>765</b>         | <b>(712)</b>       | (1,826)    | 751                | (1,075)            |

1 The perpetual capital securities and perpetual convertible bonds are accounted for as equity in accordance with IAS 32 'Financial Instruments: Presentation' and therefore are not included within net debt.

## 27 Borrowings

|                           | 2017<br>Current<br>£m | 2017<br>Non-current<br>£m | 2017<br>Total<br>£m | 2016<br>Current<br>£m | 2016<br>Non-current<br>£m | 2016<br>Total<br>£m |
|---------------------------|-----------------------|---------------------------|---------------------|-----------------------|---------------------------|---------------------|
| Loan due 2018             | 108                   | 572                       | 680                 | 101                   | 679                       | 780                 |
| Loan due 2031             | 34                    | 727                       | 761                 | 41                    | 758                       | 799                 |
| Bank overdrafts           | 6                     | –                         | 6                   | 3                     | –                         | 3                   |
| Bank loans due 2016       | –                     | –                         | –                   | 39                    | –                         | 39                  |
| Bank loans due 2019       | –                     | 199                       | 199                 | –                     | 199                       | 199                 |
| Convertible bond due 2019 | 1                     | 426                       | 427                 | 1                     | 417                       | 418                 |
| Finance lease obligations | 23                    | 115                       | 138                 | 38                    | 137                       | 175                 |
| <b>Total borrowings</b>   | <b>172</b>            | <b>2,039</b>              | <b>2,211</b>        | 223                   | 2,190                     | 2,413               |

### a) Loan due 2018 and Loan due 2031

Secured loans are secured on 125 (2016: 125) supermarket properties (note 10) and comprise loans from two finance companies, Eddystone Finance plc and Longstone Finance plc:

- a fixed rate amortising loan from Eddystone Finance plc with an outstanding principal value of £670 million (2016: £764 million) at a weighted average rate of 4.54 per cent and carrying amount of £680 million (2016: £780 million) with a final repayment date of April 2018; and
- an inflation linked amortising loan from Longstone Finance plc with an outstanding principal value of £743 million (2016: £779 million) at a fixed real rate of 2.36 per cent where principal and interest are uplifted annually by RPI subject to a cap at five per cent and floor at nil per cent with a carrying amount of £761 million (2016: £798 million) with a final repayment date of April 2031.

## 27 Borrowings continued

The Group has entered into interest rate swaps to convert £160 million (2016: £206 million) of the £670 million (2016: £764 million) loan due 2018 from fixed to floating rates of interest. These transactions have been accounted for as fair value hedges (note 24). In previous years, £572 million of fixed to floating rate swaps accounted for as fair value hedges were de-designated from their fair value hedging relationship. The fair value adjustment of the debt previously hedged by these swaps will be amortised over the remaining life of the loans, resulting in an amortisation charge to the income statement in the current financial year of £1 million (2016: £1 million).

The Group has entered into inflation swaps to convert £400 million (2016: £400 million) of the £743 million (2016: £779 million) loan due 2031 from RPI linked interest to fixed rate interest for periods maturing April 2017 to April 2019. These transactions have been designated as cash flow hedges (note 24).

The principal activity of Eddystone Finance plc and Longstone Finance plc is the issuing of commercial mortgage backed securities and applying the proceeds towards the secured loans due 2018 and 2031 with the Group as summarised above.

SFM Corporate Services Limited holds all the issued share capital of Eddystone Finance Holdings Limited and Longstone Finance Holdings Limited on trust for charitable purposes. Eddystone Finance Holdings Limited beneficially owns all the issued share capital of Eddystone Finance plc and Longstone Finance Holdings Limited beneficially owns all the issued share capital of Longstone Finance plc. As the Group has no interest, power or bears any risk over these entities they are not included in the Group consolidation.

### b) Bank overdrafts

Bank overdrafts are repayable on demand and bear interest at a spread above Bank of England base rate.

### c) Revolving credit facility

The Group maintains a secured contingent committed revolving credit facility of £1,150 million. This facility is structured on a dual tranche basis with a £500 million Facility (A) due May 2019 and a £650 million Facility (B) due May 2020. As at 11 March 2017, £nil had been drawn (2016: £nil).

The revolving credit facility incurs commitment fees at market rates and drawdowns bear interest at a margin above LIBOR.

### d) Bank loans due 2016

During September 2016, the Group repaid upon maturity a €50 million loan due September 2016 at floating rates of interest. The €50 million floating rate loan had been swapped into a £44 million floating rate loan using a cross currency swap.

### e) Bank loans due 2019

On 5 May 2015, the Group amended its £200 million unsecured bank loan due August 2019 into a secured corporate £200 million bank loan due August 2019 at a floating rate of interest. £100 million of this has been swapped into a fixed rate liability. The £100 million portion of the loan and associated interest rate swap has been designated as a cash flow hedge.

### f) Convertible bond due 2019

In November 2014, the Group issued £450 million of unsecured convertible bonds due November 2019. The bonds pay a coupon of 1.25 per cent payable semi-annually. Each bond is convertible into ordinary shares of J Sainsbury plc at any time up to 21 November 2019 at a conversion price of 321.47 pence.

The net proceeds of the convertible bond have been split as at 11 March 2017 into a liability component of £427 million and an equity component of £23 million. The equity component represents the fair value of the embedded option to convert the bond into ordinary shares of the Company.

|   | 2017<br>£m | 2016<br>£m |
|---|------------|------------|
| Liability component brought forward           | 418        | 410        |
| Interest expense                              | 13         | 13         |
| Interest paid                                 | (6)        | (6)        |
| Other <sup>1</sup>                            | 2          | 1          |
| Liability component as at the end of the year | 427        | 418        |

1 Other relates to fees.

## 27 Borrowings continued

### g) Finance lease obligations

|  | Minimum<br>lease<br>payments<br>2017<br>£m | Minimum<br>lease<br>payments<br>2016<br>£m | Present<br>value of<br>minimum<br>lease<br>payments<br>2017<br>£m | Present<br>value of<br>minimum<br>lease<br>payments<br>2016<br>£m |
|--|--|--|---|---|
| <b>Obligations under finance leases:</b> |  |  |   |   |
| Less than 1 year                         | <b>31</b>                                  | 46   | <b>23</b>   | 38  |
| Within 2 and 5 years inclusive           | <b>66</b>                                  | 87   | <b>41</b>   | 63  |
| After 5 years                            | <b>207</b>                                 | 209  | <b>74</b>   | 74  |
|  | <b>304</b>                                 | 342  | <b>138</b>  | 175   |
| Less: future finance charges             | <b>(166)</b>                               | (167)                                      |   |   |
| Present value of lease obligations       | <b>138</b>                                 | 175  |   |   |
| Disclosed as:                            |  |  |   |   |
| Current                                  | <b>23</b>                                  | 38   |   |   |
| Non-current                              | <b>115</b>                                 | 137  |   |   |
|  | <b>138</b>                                 | 175  |   |   |

Finance leases have effective interest rates ranging from 4.3 per cent to 8.5 per cent (2016: 4.3 per cent to 8.5 per cent). The average remaining lease term is 72 years (2016: 66 years).

## 28 Employee costs

|  | 2017<br>£m   | 2016<br>£m |
|--|--------------|------------|
| Employee costs for the Group during the year amounted to:    |              |            |
| Wages and salaries, including bonus and termination benefits | <b>2,579</b> | 2,272      |
| Social security costs  | <b>165</b>   | 148        |
| Pension costs – defined contribution schemes                 | <b>102</b>   | 98         |
| Share-based payments expense (note 30)                       | <b>32</b>    | 23         |
|  | <b>2,878</b> | 2,541      |

|  | 2017<br>Number<br>000s | 2016<br>Number<br>000s |
|--|------------------------|------------------------|
| The average number of employees, including Directors, during the year was: |                        |                        |
| Full-time  | <b>51.9</b>            | 48.0                   |
| Part-time  | <b>130.0</b>           | 114.7                  |
|  | <b>181.9</b>           | 162.7                  |
| Full-time equivalent   | <b>118.7</b>           | 108.3                  |

Details of key management compensation can be found in note 36 and within the Directors' Remuneration Report on pages 74 to 94.

## 29 Retirement benefit obligations

### Accounting policies

In respect of defined benefit pension schemes, the surplus or deficit recognised in the balance sheet represents the difference between the fair value of the plan assets and the present value of the defined benefit obligation at the balance sheet date. The defined benefit obligation is actuarially calculated on an annual basis using the projected unit credit method. Plan assets are recorded at fair value.

Actuarial gains and losses are reported in the statement of other comprehensive income as incurred, and comprise both the effects of changes in actuarial assumptions and experience adjustments arising because of differences between the previous actuarial assumptions and what has actually occurred.

The income statement charge consists of a financing charge, which is the net of interest cost on pension scheme liabilities and interest income on plan assets and defined benefit pension scheme expenses.

The financing charge is determined by applying the discount rate used to measure the defined benefit obligation to the pension scheme liabilities and plan assets at the beginning of the financial year.

The Group contributions to defined contribution pension schemes are charged to the income statement as incurred. Any contributions unpaid at the balance sheet date are included as an accrual as at that date. The Group has no further payment obligations once the contributions have been paid.

### Background

At 11 March 2017, retirement benefit obligations relate to two defined benefit schemes, the Sainsbury's Pension Scheme and from 2 September 2016, the Home Retail Group Pension Scheme (the 'Schemes') as well as two unfunded pension liabilities relating to senior former employees of Sainsbury's and Home Retail Group.

The retirement benefit obligations at the year-end have been calculated by KPMG, as actuarial advisers to the Group, using the projected unit credit method and based on adjusting the position at the date of the previous triennial valuations (see below) for known events and changes in market conditions as allowed under IAS 19, 'Employee benefits'.

### Sainsbury's Pension Scheme

The Scheme is governed by a Trustee board, and the assets of the Scheme are held separately from the Group's assets. The Scheme is an HMRC Registered pension scheme, subject to UK legislation with oversight from the Pensions Regulator. The governance of the Scheme is the responsibility of the Trustee; the Trustee comprises 11 directors – five selected from members, five appointed by the Company and one Independent Chairman who is selected by the Company in consultation with the Trustee. In accordance with legislation, the Trustee consults with the Company regarding the Scheme's investment strategy and agrees an appropriate funding plan with the Company.

The Scheme has three different benefit categories: Final Salary, Career Average and Cash Balance. For Final Salary and Career Average members, benefits at retirement are determined by length of service and salary. For Cash Balance members, benefits are determined by the accrued retirement account credits.

The Scheme was closed to new employees on 31 January 2002 and closed to future benefit accrual on 28 September 2013. The Scheme is also used to pay life assurance benefits to current (including new) colleagues. The assets of the Scheme are valued at bid price and are held separately from the Group's assets.

The Scheme was subject to a triennial actuarial valuation, carried out by Willis Towers Watson for the Trustee, as at 14 March 2015 on the projected unit basis. On the basis of the assumptions agreed, the actuarial deficit at 14 March 2015 was £740 million, an increase of £148 million from the March 2012 deficit of £592 million.

A Recovery Plan was agreed in September 2016 which included:

- Two special contributions of £125 million paid in August 2015 and August 2016
- Deficit contributions increasing to £65 million a year until March 2021
- The interest in the property partnership to continue, of up to £600 million payable in 2030 if there is a deficit at that time.

The Scheme continues to receive annual coupons from the property partnership which are based on the average weighted discount rate used in the triennial valuation and so are effectively reset every three years. These coupons will reduce from 2017/18 to £19 million a year.

## 29 Retirement benefit obligations continued

### Home Retail Group Pension Scheme

The Scheme is governed by a Trustee board, and the assets of the Scheme are held separately from the Group's assets. The Scheme is an HMRC Registered pension scheme, subject to UK legislation with oversight from the Pensions Regulator. The governance of the Scheme is the responsibility of the Trustee; the Trustee comprises six directors – two selected from members, four appointed by the Company including an Independent Chairman. In accordance with legislation, the Trustee consults with the Company regarding the Scheme's investment strategy and agrees an appropriate funding plan with the Company.

The Scheme was closed to new employees in 2009 and closed to future benefit accrual in January 2013. The Scheme is used to pay life assurance benefits only to current (including new) colleagues. Pension benefits were based on service and final salary. The assets of the Scheme are valued at bid price and are held separately from the Group's assets.

The Home Retail Group defined benefit pension scheme was subject to a Trustees' triennial valuation as at 31 March 2015. This was carried out by Willis Towers Watson for the Trustee. On the basis of the assumptions agreed, the actuarial deficit as at 31 March 2015 was £315 million, an increase of £157 million from the March 2012 deficit of £158 million.

A Recovery Plan was agreed and implemented on acquisition which included:

- An immediate payment on acquisition by Sainsbury's of £50 million
- Deficit contributions of £40 million a year, £10 million payable each quarter, until October 2021
- Security over £80 million of freehold property (to be completed in the year ending 10 March 2018)
- A parent guarantee of £470 million which reduces over time in line with deficit contributions paid and will be reset at following triennial valuations

As part of the sale of Homebase by Home Retail Group, it was agreed with the Trustee that a cash contribution of £50 million would be made to the Scheme. Of this total, £26 million was paid during Home Retail Group's year ending 28 February 2016. Following the capital return to shareholders associated with the Homebase sale, the final cash contribution of £24 million was made to the Scheme in September following the acquisition of Home Retail Group by Sainsbury's.

### Unfunded pension liabilities

The unfunded pension liabilities are unwound when each employee reaches retirement and takes their pension from the Group payroll or is crystallised in the event of an employee leaving or retiring and choosing to take the provision as a one-off cash payment.

### IFRIC 14

IFRIC 14 is the interpretation that details when a company can recognise any pension surplus that exists. Furthermore, if the company has a funding commitment in excess of the IAS 19 deficit, then IFRIC 14 requires recognition of this excess in those circumstances when the surplus that would result on fulfilling that commitment cannot be recognised. A surplus may be recognised either because of an unconditional right to a refund to the company, or on grounds of a future contribution reduction where schemes are still open to future accrual.

For the Sainsbury's pension scheme, management is of the view that it has an unconditional right to a refund of surplus under IFRIC 14. As such no adjustment has been made for potential additional liabilities.

Based on the net deficit of the Home Retail Group Pension Scheme as at 11 March 2017 and the committed payments under the Schedule of Contributions signed on 2 September 2016, there is no notional surplus and therefore no additional balance sheet liability in respect of a 'minimum funding requirement' to be recognised at 11 March 2017.

#### a) Income statement

The amounts recognised in the income statement are as follows:

|   | 2017<br>£m   | 2016<br>£m |
|---|--------------|------------|
| Excluded from underlying profit before tax:               |              |            |
| Interest cost on pension liabilities <sup>1</sup>         | <b>(292)</b> | (266)      |
| Interest income on plan assets                            | <b>276</b>   | 244        |
| Total included in finance costs (note 6)                  | <b>(16)</b>  | (22)       |
| Defined benefit pension scheme expenses                   | <b>(8)</b>   | (6)        |
| Total excluded from underlying profit before tax (note 3) | <b>(24)</b>  | (28)       |
| <b>Total income statement expense</b>                     | <b>(24)</b>  | (28)       |

1 Includes interest of £1 million for the unfunded pension scheme (2016: £1 million).

## 29 Retirement benefit obligations continued

### b) Other comprehensive income

Re-measurement of the retirement benefit obligations have been recognised as follows:

|   | 2017<br>£m     | 2016<br>£m |
|---|----------------|------------|
| Return on plan assets, excluding amounts included in interest | <b>1,182</b>   | (16)       |
| Actuarial (losses)/gains arising from changes in:             |                |            |
| Finance assumptions <sup>1</sup>                              | <b>(2,005)</b> | 103        |
| Demographic assumptions <sup>2</sup>                          | <b>320</b>     | –          |
| Experience  | <b>96</b>      | 34         |
| Total actuarial (losses)/gains                                | <b>(1,589)</b> | 137        |
| Total re-measurements   | <b>(407)</b>   | 121        |

1 Includes £3 million loss for the unfunded pension scheme (2016: £2 million loss).

2 Includes £1 million gain for the unfunded pension scheme (2016: £nil).

### c) Balance sheet

The amounts recognised in the balance sheet are as follows:

|   | Sainsbury's<br>2017<br>£m | Home Retail<br>Group<br>2017<br>£m | Group<br>2017<br>£m | Group<br>2016<br>£m |
|---|---------------------------|------------------------------------|---------------------|---------------------|
| Present value of funded obligations       | <b>(9,441)</b>            | <b>(1,413)</b>                     | <b>(10,854)</b>     | (7,625)             |
| Fair value of plan assets                 | <b>8,708</b>              | <b>1,212</b>                       | <b>9,920</b>        | 7,235               |
|   | <b>(733)</b>              | <b>(201)</b>                       | <b>(934)</b>        | (390)               |
| Present value of unfunded obligations     | <b>(23)</b>               | <b>(17)</b>                        | <b>(40)</b>         | (18)                |
| <b>Retirement benefit obligations</b>     | <b>(756)</b>              | <b>(218)</b>                       | <b>(974)</b>        | (408)               |
| Deferred income tax asset (note 7)        | <b>77</b>                 | <b>47</b>                          | <b>124</b>          | 19                  |
| <b>Net retirement benefit obligations</b> | <b>(679)</b>              | <b>(171)</b>                       | <b>(850)</b>        | (389)               |

The retirement benefit obligation and the associated deferred income tax balance are shown within different line items on the face of the balance sheet.

The movements in the Group's net defined benefit obligation are as follows:

|  | 2017<br>£m   | 2016<br>£m |
|--|--------------|------------|
| As at the beginning of the year                | <b>(408)</b> | (708)      |
| Acquisition of Home Retail Group plc (note 31) | <b>(454)</b> | –          |
| Interest cost                                  | <b>(16)</b>  | (22)       |
| Remeasurement (losses)/gains                   | <b>(407)</b> | 121        |
| Pension scheme expenses                        | <b>(8)</b>   | (6)        |
| Contributions by employer                      | <b>319</b>   | 207        |
| <b>As at the end of the year</b>               | <b>(974)</b> | (408)      |

The movements in the retirement benefit obligations (including unfunded obligations) are as follows:

|  | 2017<br>£m      | 2016<br>£m |
|--|-----------------|------------|
| As at the beginning of the year                | <b>(7,643)</b>  | (7,696)    |
| Acquisition of Home Retail Group plc (note 31) | <b>(1,587)</b>  | –          |
| Interest cost                                  | <b>(292)</b>    | (267)      |
| Remeasurement (losses)/gains                   | <b>(1,589)</b>  | 138        |
| Benefits paid                                  | <b>217</b>      | 182        |
| <b>As at the end of the year</b>               | <b>(10,894)</b> | (7,643)    |

Analysed as:

|                                |                 |         |
|--------------------------------|-----------------|---------|
| Retirement benefit obligations | <b>(10,854)</b> | (7,625) |
| Unfunded obligations           | <b>(40)</b>     | (18)    |

## 29 Retirement benefit obligations continued

The movements in the fair value of plan assets are as follows:

|  | 2017<br>£m   | 2016<br>£m   |
|--|--------------|--------------|
| As at the beginning of the year                | 7,235        | 6,988        |
| Acquisition of Home Retail Group plc (note 31) | 1,133        | –            |
| Interest income on plan assets                 | 276          | 244          |
| Pension scheme expenses                        | (8)          | (6)          |
| Remeasurement gains/(losses)                   | 1,182        | (16)         |
| Contributions by employer                      | 319          | 207          |
| Benefits paid                                  | (217)        | (182)        |
| <b>As at the end of the year</b>               | <b>9,920</b> | <b>7,235</b> |

### Risks associated with the Group's defined benefit pension schemes

The defined benefit schemes expose the Group to a number of risks as detailed below:

| Risk                          | Description   | Mitigation  |
|-------------------------------|---|---|
| <b>Asset volatility</b>       | Returns on assets that vary from the discount rate create funding level volatility. Both schemes hold a significant proportion of growth assets such as equities and real estate. Whilst growth assets are expected to outperform corporate bond yields over the long term this might not always occur in the short term. | All equities are invested passively across global indices. All other assets are invested actively and are widely diversified to reduce returns risk and enhance returns.  |
| <b>Currency</b>               | The schemes' liabilities are sterling based whereas the majority of assets are denominated in foreign currencies.   | Currency hedging programmes in both schemes help dampen returns volatility caused by the fluctuation of sterling against other leading currencies.  |
| <b>Changes in bond yields</b> | A decrease in bond yields, which in turn drive the discount rate, will increase the present value of the schemes' liabilities for accounting purposes.  | A significant proportion of assets are held in corporate bonds that provide a hedge against falling bond yields. Furthermore significant levels of interest rate hedging within the schemes' liability hedging portfolios through interest rate derivatives serve to protect against falling bond yields. A buy-in policy in the HRG scheme transfers a proportion of interest rate risk to an insurer. |
| <b>Inflation</b>              | The majority of the schemes' liabilities are linked to UK price inflation indices (to a maximum of five per cent per year).   | The Sainsbury's scheme's liability hedging portfolios hedge significant proportions of inflation liabilities by holding index linked bonds and inflation rate derivatives. The schemes' equities provide a natural hedge for inflation. A buy-in policy in the HRG scheme transfers a proportion of inflation risk to an insurer.   |
| <b>Longevity</b>              | Beneficiaries living longer than expected could increase the schemes' liabilities.  | A buy-in policy in the HRG scheme transfers some longevity risk to an insurer.  |
| <b>Operational</b>            | Poor administration of benefits may result in an increased defined benefit obligation in future years.  | The schemes' benefits administrators have agreed service level agreements and controls are carefully monitored.   |

## 29 Retirement benefit obligations continued

The major categories of plan assets are as follows:

|                                 | Quoted<br>2017<br>£m | Unquoted <sup>1</sup><br>2017<br>£m | Quoted<br>2016<br>£m | Unquoted<br>2016<br>£m |
|---------------------------------|----------------------|-------------------------------------|----------------------|------------------------|
| <b>Equity</b>                   |                      |                                     |                      |                        |
| Public                          | 1,987                | –                                   | 1,671                | –                      |
| Private                         | –                    | 267                                 | –                    | 206                    |
| <b>Bonds</b>                    |                      |                                     |                      |                        |
| Government bonds                | 1,272                | –                                   | 811                  | –                      |
| Corporate bonds                 | 3,483                | (60)                                | 2,725                | (38)                   |
| Emerging market bonds           | 419                  | –                                   | 268                  | –                      |
| <b>Derivatives<sup>2</sup></b>  | –                    | 519                                 | –                    | 756                    |
| <b>Alternatives</b>             |                      |                                     |                      |                        |
| Real estate                     | 58                   | 524                                 | –                    | 309                    |
| Private debt                    | –                    | 436                                 | –                    | 206                    |
| Diversified growth              | 185                  | –                                   | –                    | –                      |
| Insurance policies <sup>3</sup> | –                    | 357                                 | –                    | –                      |
| Other                           | 102                  | 59                                  | –                    | 1                      |
| Cash and cash equivalents       | 390                  | (78)                                | 343                  | (23)                   |
|                                 | <b>7,896</b>         | <b>2,024</b>                        | 5,818                | 1,417                  |

### Notes

1 Certain unquoted fixed interest securities, private equity and debt investments, property investments and hedge funds are stated at fair value. These fair values may differ from their realisable values due to the absence of liquid markets in these investments.

2 Swap contract derivatives outstanding at the year-end are stated at the net present value of future discounted cash flows of each leg of the swap.

3 Insurance policies of £357 million refers to a buy-in policy held by the HRG scheme. The income from this policy exactly matches the amount and timing of all of the benefits payable for the insured pensioner members. Therefore the fair value of the insurance policy has been calculated to be the present value of the related obligations.

Of the above assets, £3,230 million are denominated in sterling and £6,690 million are denominated in overseas currencies.

### d) Assumptions

The principal actuarial assumptions used at the balance sheet date are as follows:

|                          | 2017<br>%   | 2016<br>%   |
|--------------------------|-------------|-------------|
| Discount rate            | 2.70        | 3.65        |
| Inflation rate – RPI     | 3.30        | 3.15        |
| Inflation rate – CPI     | 2.30        | 2.15        |
| Future pension increases | 2.00 – 3.15 | 1.90 – 3.00 |

The discount rate is based on the yield on AA-rated sterling corporate bonds appropriate to the term of the Schemes' liabilities.

The life expectancy for members aged 65 years at the balance sheet date is as follows:

|                  | Sainsbury's<br>(Main<br>scheme)<br>2017 | Sainsbury's<br>(Executive<br>scheme)<br>2017 | HRG<br>2017 | Sainsbury's<br>(Main<br>scheme)<br>2016 | Sainsbury's<br>(Executive<br>scheme)<br>2016 |
|------------------|---|--|-------------|---|--|
| Male pensioner   | 21.5                                    | 24.8   | 22.6        | 22.7                                    | 25.2   |
| Female pensioner | 24.3                                    | 26.0   | 25.0        | 25.5                                    | 26.4   |

The life expectancy at age 65 for members aged 45 years at the balance sheet date is as follows:

|                  | Sainsbury's<br>(Main<br>scheme)<br>2017 | Sainsbury's<br>(Executive<br>scheme)<br>2017 | HRG<br>2017 | Sainsbury's<br>(Main<br>scheme)<br>2016 | Sainsbury's<br>(Executive<br>scheme)<br>2016 |
|------------------|---|--|-------------|---|--|
| Male pensioner   | 23.3                                    | 26.5   | 24.4        | 24.6                                    | 27.0   |
| Female pensioner | 26.3                                    | 27.9   | 26.9        | 27.4                                    | 28.3   |

The weighted average duration of the defined benefit obligation at the end of the reporting period is 22 years for Sainsbury's and 25 years for HRG (2016: 21 years for Sainsbury's).

## 29 Retirement benefit obligations continued

### e) Sensitivities

An increase of 0.5 per cent in the discount rate would decrease the retirement benefit obligations by £1,095 million. A decrease of 0.5 per cent in the discount rate would increase the retirement benefit obligations by £1,270 million.

An increase of 0.5 per cent in the inflation rate would increase the retirement benefit obligations by £850 million. A decrease of 0.5 per cent in the inflation rate would decrease the retirement benefit obligations by £796 million. This sensitivity includes the effect of inflation on the Scheme's pension increases.

An increase of one year to the life expectancy would increase the retirement benefit obligations by £381 million.

The sensitivities are based on management's best estimate of a reasonably anticipated change. The sensitivities are calculated using the same methodology used to calculate the retirement benefit obligation, by considering the change in the retirement benefit obligation for a given change in assumption. The net retirement benefit obligation is the difference between the retirement benefit obligation and the fair value of plan assets. Changes in the assumptions may occur at the same time as changes in the fair value of plan assets. There has been no change in the calculation methodology since the prior period.

## 30 Share-based payments

### Accounting policies

The Group provides benefits to employees (including Directors) of the Group in the form of equity-settled and cash-settled share-based payment transactions, whereby employees render services in exchange for shares, rights over shares or the value of those shares in cash terms.

For equity-settled share-based payments, the fair value of the employee services rendered is determined by reference to the fair value of the shares awarded or options granted, excluding the impact of any non-market vesting conditions. All share options are valued using an option-pricing model (Black-Scholes or Monte Carlo). This fair value is charged to the income statement over the vesting period of the share-based payment scheme.

For cash-settled share-based payments, the fair value of the employee services rendered is determined at each balance sheet date and the charge recognised through the income statement over the vesting period of the share-based payment scheme, with the corresponding increase in accruals.

The value of the charge is adjusted in the income statement over the remainder of the vesting period to reflect expected and actual levels of options vesting, with the corresponding adjustments made in equity and accruals.

The grant by the Company of options over its equity instruments to the employees of subsidiary undertakings in the Group is treated as a capital contribution. The fair value of employee services received, measured by reference to the grant date fair value, is recognised over the vesting period as an increase to investment in subsidiary undertakings, with a corresponding credit to equity.

The Group recognised £32 million (2016: £23 million) of employee costs (note 28) related to share-based payment transactions made during the financial year. Of these, £nil (2016: £nil) were cash-settled.

The Group operates a number of share-based payment schemes as set out below:

### a) Savings-Related Share Option Scheme (Sharesave)

The Group operates a Savings-Related Share Option Scheme, which is open to all UK employees with more than three months' continuous service. This is an approved HMRC scheme and was established in 1980. Under Sharesave, participants remaining in the Group's employment at the end of the three-year or five-year savings period are entitled to use their savings to purchase shares in the Company at a stated exercise price. Employees leaving for certain reasons are able to use their savings to purchase shares within six months of their leaving.

A reconciliation of Sharesave option movements is shown below:

|   | 2017<br>Number of<br>options<br>million | 2017<br>Weighted<br>average<br>exercise<br>price<br>pence | 2016<br>Number of<br>options<br>million | 2016<br>Weighted<br>average<br>exercise price<br>pence |
|---|---|---|---|--|
| Outstanding at the beginning of the year  | 59.0                                    | 234   | 55.0                                    | 254  |
| Granted                                   | 27.1                                    | 184   | 20.0                                    | 195  |
| Forfeited                                 | (16.7)                                  | 249   | (13.0)                                  | 253  |
| Exercised                                 | (2.6)                                   | 249   | (3.0)                                   | 244  |
| Expired                                   | (0.3)                                   | 208   | –                                       | 218  |
| <b>Outstanding at the end of the year</b> | <b>66.5</b>                             | <b>210</b>  | 59.0                                    | 234  |
| Exercisable at the end of the year        | 5.7                                     | 301   | 7.6                                     | 277  |
| Exercisable price range                   |   | <b>185 to 332</b>   |   | 195 to 332   |

The weighted average share price for options exercised over the year was 269 pence (2016: 266 pence). The weighted average remaining contractual life of options outstanding at 11 March 2017 was 2.4 years (2016: 2.3 years).

### 30 Share-based payments continued

Options granted during the year were valued using the Black-Scholes option-pricing model. No performance conditions were included in the fair value calculations. The fair value per option granted during the year and the assumptions used in the calculation are as follows:

|  |                         | 2017        | 2016 |
|--|-------------------------|-------------|------|
| Share price at grant date (pence)                  |                         | <b>231</b>  | 243  |
| Exercise price (pence)                             |                         | <b>185</b>  | 195  |
| Expected volatility                                | – 3 year period (%)     | <b>29.9</b> | 26.6 |
|  | – 5 year period (%)     | <b>25.5</b> | 24.1 |
| Option life  | – 3 year period (years) | <b>3.2</b>  | 3.2  |
|  | – 5 year period (years) | <b>5.2</b>  | 5.2  |
| Expected dividends (expressed as dividend yield %) |                         | <b>4.9</b>  | 5.1  |
| Risk-free interest rate                            | – 3 year period (%)     | <b>0.8</b>  | 1.6  |
|  | – 5 year period (%)     | <b>1.6</b>  | 2.1  |
| Fair value per option                              | – 3 year period (pence) | <b>49</b>   | 48   |
|  | – 5 year period (pence) | <b>45</b>   | 45   |

The expected volatility is based on the standard deviation of the Group's share price for the period immediately prior to the date of grant of award, over the period identical to the vesting period of the award, adjusted for management's view of future volatility of the share price.

As part of the acquisition of Home Retail Group plc (HRG) colleagues had the option to roll over their HRG Save As You Earn (SAYE) options to J Sainsbury plc SAYE option or let their HRG options vest. Therefore the above outstanding SAYE options include the rollover options. The calculation of the fair value per option rolled over has not been included within the table above.

#### b) Long-Term Incentive Plan

Under the Long-Term Incentive Plan, shares are conditionally awarded to the senior managers in the Company. The core awards are calculated as a percentage of the participants' salaries and scaled according to grades.

Performance is measured at the end of the three-year performance period. If the required performance conditions have been met, the awards vest and 50 per cent of the award will be released. Subject to participants remaining in employment for a further year, the balance will then be released one year after the vesting date. Options granted to acquire the award of shares will expire two years from the vesting date. Dividends will accrue on the shares that vest in the form of additional shares.

The core award can grow by up to four times, dependent on the level of performance. Straight-line vesting will apply if performance falls between two points. Awards are structured as nil cost options.

A reconciliation of the number of shares conditionally allocated is shown below:

|   | 2017<br>million | 2016<br>million |
|---|-----------------|-----------------|
| Outstanding at the beginning of the year  | <b>5.4</b>      | 6.1             |
| Conditionally allocated                   | <b>2.5</b>      | 2.2             |
| Forfeited                                 | <b>(1.7)</b>    | (2.2)           |
| Released to participants                  | <b>(0.4)</b>    | (0.7)           |
| <b>Outstanding at the end of the year</b> | <b>5.8</b>      | 5.4             |

The weighted average remaining contractual life of share options outstanding at 11 March 2017 was 1.8 years (2016: 1.7 years).

Details of shares conditionally allocated at 11 March 2017 are set out below:

| Date of conditional award         | 2017<br>million | 2016<br>million |
|-----------------------------------|-----------------|-----------------|
| 19 May 2011 (2011 Value Builder)  | –               | 0.2             |
| 16 May 2013 (2013 Future Builder) | –               | 1.4             |
| 15 May 2014 (2014 Future Builder) | <b>1.6</b>      | 1.7             |
| 14 May 2015 (2015 Future Builder) | <b>1.9</b>      | 2.1             |
| 12 May 2016 (2016 Future Builder) | <b>2.3</b>      | –               |
|                                   | <b>5.8</b>      | 5.4             |

### 30 Share-based payments continued

Options to acquire the award of shares were valued using the Black-Scholes option-pricing model. No performance conditions were included in the fair value calculations. The fair value per option granted during the year and the assumptions used in the calculation are as follows:

|                                   | 2017       | 2016 |
|-----------------------------------|------------|------|
| Share price at grant date (pence) | <b>265</b> | 276  |
| Option life (years)               | <b>4.2</b> | 4.2  |
| Fair value per option (pence)     | <b>265</b> | 276  |

During the year, a total number of 0.4 million shares were exercised (2016: 1.4 million shares). The weighted average share price during the year for options exercised was 272 pence (2016: 238 pence).

#### c) Deferred Share Award

The Deferred Share Award targets a diverse range of financial and strategic scorecard measures. These are intended to reward the top managers in the Company, including Executive Directors, for driving the short-term objectives that will directly lead to building the sustainable, long-term growth of the Company. Awards are structured as nil cost options.

Share-based awards are made to participants subject to performance against a basket of measures. At least 50 per cent of the awards are based on the delivery of financial performance and returns to shareholders. The balance is based on measures which will assess the Company's performance relative to its competitors as well as key strategic goals.

Performance against the target is measured over one financial year. Any shares awarded are deferred for a further two years to ensure that management's interests continue to be aligned with those of shareholders. The shares are subject to forfeiture if the participant resigns or is dismissed. Dividends accrue on the shares that vest in the form of additional shares.

A reconciliation of the number of shares granted over the year is shown below:

|   | 2017<br>million | 2016<br>million |
|---|-----------------|-----------------|
| Outstanding at the beginning of the year  | <b>2.2</b>      | 2.5             |
| Granted                                   | <b>2.2</b>      | 1.2             |
| Lapsed                                    | <b>(0.1)</b>    | (0.3)           |
| Exercised                                 | <b>(1.3)</b>    | (1.2)           |
| <b>Outstanding at the end of the year</b> | <b>3.0</b>      | 2.2             |

The number of shares allocated at the end of the year is set out below:

|             | 2017<br>million | 2016<br>million |
|-------------|-----------------|-----------------|
| 16 May 2013 | –               | 0.1             |
| 15 May 2014 | –               | 1.2             |
| 14 May 2015 | <b>0.9</b>      | 0.9             |
| 13 May 2016 | <b>2.1</b>      | –               |
|             | <b>3.0</b>      | 2.2             |

The weighted average remaining contractual life of share options outstanding at 11 March 2017 was 1.7 years (2016: 1.4 years). The weighted average share price during the year for options exercised was 269 pence (2016: 268 pence).

### 30 Share-based payments continued

#### d) Bonus Share Award

The bonus arrangements for our senior managers and supermarket store managers include corporate and personal performance targets. A profit gateway is in place where a certain level of underlying profit before tax must be achieved before any bonus related to the corporate element of the bonus is released.

60 per cent of the bonus is paid in cash and 40 per cent awarded in shares. They are automatically released after three financial years. Shares are subject to forfeiture if the participant resigns or is dismissed.

Dividends accrue on these shares and are released at the end of the three-year retention period.

A reconciliation of the number of shares granted over the year is shown below:

|   | 2017<br>million | 2016<br>million |
|---|-----------------|-----------------|
| Outstanding at the beginning of the year  | 8.9             | 10.2            |
| Granted                                   | 6.3             | 3.7             |
| Exercised                                 | (3.8)           | (4.0)           |
| Lapsed                                    | (0.5)           | (1.0)           |
| <b>Outstanding at the end of the year</b> | <b>10.9</b>     | <b>8.9</b>      |

The number of shares allocated at the end of the year is set out below:

|             | 2017<br>million | 2016<br>million |
|-------------|-----------------|-----------------|
| 16 May 2013 | –               | 3.1             |
| 15 May 2014 | 2.7             | 3.0             |
| 14 May 2015 | 2.5             | 2.8             |
| 13 May 2016 | 5.7             | –               |
|             | <b>10.9</b>     | <b>8.9</b>      |

The weighted average remaining contractual life of share options outstanding at 11 March 2017 was 1.5 years (2016: 1.1 years). The weighted average share price during the year for options exercised was 277 pence (2016: 269 pence).

### 31 Acquisition of Home Retail Group plc

#### Accounting policies for business combinations

The Group applies the acquisition method of accounting for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair value of identifiable assets transferred, the liabilities incurred and the equity interests issued by the Group at the acquisition date. Acquisition-related costs are expensed as incurred.

On 2 September 2016, the Group acquired 100 per cent of the issued share capital of Home Retail Group plc (HRG), a listed company based in the United Kingdom, by means of a Scheme of Arrangement under Part 26 of the Act for a consideration of £1,093 million. The full analysis of the consideration is shown below:

| Form of consideration  | Consideration fair value at<br>acquisition date<br>£m |
|--|---|
| Cash of £447 million (being 55p per existing share); fair value is based on Home Retail Group plc's share capital of 813,445,001 shares in existence as at the acquisition date  | <b>447</b>  |
| £3 million in relation to the contractual requirement to settle certain existing HRG share scheme awards and options   | <b>3</b>  |
| 261 million new J Sainsbury plc shares of 28 <sup>1</sup> / <sub>7</sub> p nominal value each were issued (being 0.321 new J Sainsbury plc shares per existing Home Retail Group plc share); fair value of the consideration is based on a J Sainsbury plc share price of £2.4610 as of 2 September 2016 | <b>643</b>  |
| <b>Total</b>   | <b>1,093</b>  |

### 31 Acquisition of Home Retail Group plc continued

Home Retail Group's activities mainly comprise General Merchandise related retail. The acquisition is expected to accelerate Sainsbury's growth strategy in General Merchandise & Clothing retail as well as its online presence. The combination brings together two of the UK's leading retail businesses with complementary product offers through an integrated, multi-channel proposition.

None of the goodwill recognised of £58 million is expected to be deductible for income tax purposes. This was calculated as the difference between the fair value of consideration paid and the fair value of net assets acquired as set out in the following table.

The provisional assets and liabilities recognised as a result of the acquisition are as follows:

| Fair value of net assets acquired (provisional)                 | £m             |
|---|----------------|
| Fixed assets  | <b>262</b>     |
| Intangible assets   | <b>322</b>     |
| Inventories   | <b>810</b>     |
| Trade and other receivables                                     | <b>146</b>     |
| Deferred tax assets   | <b>45</b>      |
| Amounts due from Financial Services customers (the 'loan book') | <b>615</b>     |
| Other financial assets <sup>1</sup>                             | <b>59</b>      |
| Cash and cash equivalents <sup>2</sup>                          | <b>548</b>     |
| <b>Total assets acquired</b>                                    | <b>2,807</b>   |
| Trade and other payables <sup>2</sup>                           | <b>(1,214)</b> |
| Provisions  | <b>(104)</b>   |
| Defined benefit obligation                                      | <b>(454)</b>   |
| <b>Total liabilities acquired</b>                               | <b>(1,772)</b> |
| <b>Net identifiable assets acquired at fair value</b>           | <b>1,035</b>   |
| Goodwill arising on acquisition                                 | <b>58</b>      |
| <b>Purchase consideration transferred</b>                       | <b>1,093</b>   |

1 Other financial assets includes £9 million of J Sainsbury plc shares (converted from Home Retail Group plc own shares at the point of acquisition). On consolidation these become J Sainsbury plc own shares in the consolidated statement of changes in equity.

2 Cash and cash equivalents and trade and other payables acquired are both presented gross of the capital return of £226 million.

In accordance with IFRS 3 'Business Combinations', the acquisition accounting will be finalised within 12 months of the acquisition date of 2 September 2016.

#### a) Intangible assets

Intangible assets include a brand of £179 million relating to the Argos brand name. This reflects its fair value at the acquisition date and is estimated to have a useful economic life of ten years.

#### b) Trade and other receivables

Trade and other receivables include £40 million of trade receivables, against which a bad debt provision of £(1) million is held. Also included are prepayments and accrued income of £29 million, and other debtors of £78 million.

#### c) Amounts due from Financial Services customers (the 'loan book')

The loan book fair value of £615 million includes a fair value increase of £20 million and a provision for impairment of £(66) million.

#### d) Revenue and profit contribution

From the date of acquisition, Home Retail Group has contributed £2,661 million of revenue excluding VAT, £77 million of underlying profit before tax and a statutory profit before tax of £54 million to the Group. If the acquisition date had been on the first day of the financial year, Group revenues for the period would have been £28,013 million, Group underlying profit before tax would have been £563 million and Group profit before tax would have been £361 million. These amounts have been calculated using the Group's accounting policies. The information is provided for illustrative purposes only and is not indicative of the results of the combined Group that would have occurred had the purchase actually been made at the beginning of the year, or indicative of the future results of the combined Group.

#### e) Acquisition-related costs

Acquisition-related costs (included in administrative expenses and recognised outside of underlying profit) amount to £22 million in the current year (2016: £12 million) (see note 3). In addition £3 million of costs relating to the issuance of J Sainsbury plc shares have been recognised directly within equity.

#### f) Capital return

Prior to the acquisition of Home Retail Group plc, it was announced that Home Retail Group plc shareholders would be entitled to a £226 million capital return comprising the following:

- 25.0 pence per share, reflecting the £200 million return to shareholders in respect of the sale of Homebase by Home Retail Group plc on 29 February 2016; and
- 2.8 pence per share (totalling £26 million) in lieu of a final dividend in respect of Home Retail Group plc's financial year ended 27 February 2016.

This was recorded as a liability in the net assets acquired above within trade and other payables. The full amount was paid on 12 September 2016.

### 31 Acquisition of Home Retail Group plc continued

#### g) Cash impact of acquisition

|  | £m           |
|--|--------------|
| Cash consideration   | <b>(447)</b> |
| Cash acquired  | <b>548</b>   |
| <b>Acquisition of subsidiaries, net of cash acquired (per cash flow statement)</b> | <b>101</b>   |

#### h) Hindsight adjustments

The provisional fair values acquired are different from those reported at the half-year due to hindsight adjustments as permitted under IFRS 3 'Business Combinations'. The goodwill arising as a result of the acquisition has therefore increased from £18 million, as reported at the half-year, to £58 million.

### 32 Operating lease commitments

#### Accounting policies

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership to the Group. All other leases are classified as operating leases. For property leases, the land and building elements are treated separately to determine the appropriate lease classification.

#### a) Operating leases

Assets leased under operating leases are charged directly to the income statement on a straight-line basis over the lease term.

#### b) Sale and leaseback

A sale and leaseback transaction is one where a vendor sells an asset and immediately reacquires the use of that asset by entering into a lease with the buyer.

For sale and finance leasebacks, any apparent profit or loss from the sale is deferred and amortised over the lease term. For sale and operating leasebacks, generally the assets are sold at fair value, and the profit or loss from the sale is recognised immediately in the income statement.

#### c) Leases with predetermined fixed rental increases

The Group has a number of leases with predetermined fixed rental increases. These rental increases are accounted for on a straight-line basis over the term of the lease.

#### d) Operating lease income

Operating lease income consists of rentals from sub-tenant agreements and is recognised as earned on a straight-line basis over the lease term.

The Group leases various retail stores, offices, depots and equipment under non-cancellable operating leases. The leases have varying terms, escalation clauses and renewal rights.

The Group's future minimum lease payments under operating leases are as follows:

|  | 2017<br>£m    | 2016<br>£m |
|--|---------------|------------|
| Aggregate future minimum lease payments: |               |            |
| Within one year                          | <b>760</b>    | 614        |
| In the second to fifth years inclusive   | <b>2,615</b>  | 2,245      |
| After five years                         | <b>7,117</b>  | 7,209      |
|  | <b>10,492</b> | 10,068     |

Further analysis of the Group's future minimum lease payments after five years is as follows:

|   | 2017<br>£m   | 2016<br>£m |
|---|--------------|------------|
| Aggregate future minimum lease payments:        |              |            |
| Greater than five years but less than ten years | <b>1,924</b> | 1,866      |
| Greater than ten years but less than 15 years   | <b>1,253</b> | 1,281      |
| After 15 years                                  | <b>3,940</b> | 4,062      |
|   | <b>7,117</b> | 7,209      |

The commercial terms of the Group's operating leases vary, however they commonly include either a market rent review or an index linked rent review (with a cap and collar). The timing of when rent reviews take place differs for each lease. The Group has pre-emption rights over a minor number of properties, which provides the Group with the right of first refusal to purchase the property in the event the landlord chooses to sell. The option price payable for the asset in each instance is normally referenced to current market value prevailing at the point of pre-emption.

For the purposes of calculating adjusted net debt, the total value of the Group's capitalised operating lease commitments is £5,938 million (2016: £5,500 million).

### 32 Operating lease commitments continued

The Group sublets certain leased properties:

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| Aggregate future minimum lease receipts: |            |            |
| Within one year                          | <b>39</b>  | 35         |
| In the second to fifth years inclusive   | <b>119</b> | 119        |
| After five years                         | <b>116</b> | 124        |
|  | <b>274</b> | 278        |

### 33 Capital commitments

The Group has entered into contracts totalling £107 million (2016: £173 million) for future capital expenditure in relation to property, plant and equipment and £11 million (2016: £6 million) for intangible assets not provided for in the financial statements.

### 34 Financial commitments

Sainsbury's Bank has off balance sheet commitments to extend credit to customers of £98 million (2016: £77 million).

### 35 Contingent liabilities

The Group has a contingent liability for indemnities arising from the disposal of subsidiaries. No provision has been recognised on the basis that any potential liability arising is not considered probable. It is not possible to quantify the impact of this liability with any certainty.

Along with other retailers, the Group is subject to claims in respect of pay rates across supermarket and distribution centre workers. There is also a potential obligation in respect of holiday pay on voluntary overtime. The Group is keeping these matters under close review but considers the likelihood of payout to be remote.

### 36 Related party transactions

#### a) Key management personnel

The key management personnel of the Group comprise members of the J Sainsbury plc Board of Directors and the Operating Board. The key management personnel compensation is as follows:

|                                   | 2017<br>£m | 2016<br>£m |
|-----------------------------------|------------|------------|
| Short-term employee benefits      | 10         | 7          |
| Post-employment employee benefits | 1          | 1          |
| Share-based payments              | 6          | 4          |
|                                   | <b>17</b>  | 12         |

Nine key management personnel had credit card balances with Financial Services (2016: ten). These arose in the normal course of business and were immaterial to the Group and the individuals. Five key management personnel held saving deposit accounts with Financial Services (2016: five). These balances arose in the normal course of business and were immaterial to the Group and the individuals.

#### b) Joint ventures and associates

##### Transactions with joint ventures and associates

For the 52 weeks to 11 March 2017, the Group entered into various transactions with joint ventures and associates as set out below:

|  | 2017<br>£m | 2016<br>£m |
|--|------------|------------|
| Management services received                     | –          | (1)        |
| Management services provided                     | 8          | 4          |
| Income share received from joint ventures        | 29         | 33         |
| Dividends and distributions received             | 65         | 46         |
| Proceeds from repayment of loan to joint venture | 2          | –          |
| Investment in joint ventures and associates      | (18)       | (18)       |
| Rental expenses paid                             | (57)       | (65)       |

##### Year-end balances arising from transactions with joint ventures and associates

|                               | 2017<br>£m | 2016<br>£m |
|-------------------------------|------------|------------|
| <b>Receivables</b>            |            |            |
| Other receivables             | 12         | 28         |
| Loans due from joint ventures | 3          | 3          |
| <b>Payables</b>               |            |            |
| Other payables                | –          | (1)        |
| Loans due to joint ventures   | (5)        | (5)        |

Loans with joint ventures are non-interest bearing and repayable on demand.

#### c) Retirement benefit obligations

As discussed in note 29, the Group has entered into an arrangement with the Pension Scheme Trustee as part of the funding plan for the actuarial deficit in the Scheme. Full details of this arrangement are set out in note 29 to these financial statements.

### 37 Details of related undertakings

All companies listed below are owned by the Group and all interests are in the ordinary share capital, except where otherwise indicated. All subsidiaries have been consolidated.

#### a) Subsidiary undertakings

The Group holds a majority of the voting rights of the following undertakings:

| Entity   | Country of Incorporation | Interest | Holding  | Address*                      |
|--|--------------------------|----------|----------|-------------------------------|
| ARG Personal Loans Limited                                   | UK                       | 100%     | Indirect | Avebury                       |
| ARG Services Limited   | UK                       | 100%     | Indirect | 33 Holborn                    |
| Argos (Asia) Limited   | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Argos (Hong Kong) Limited                                    | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Argos Best Sellers Limited                                   | UK                       | 100%     | Indirect | 33 Holborn                    |
| Argos Business Solutions Limited                             | UK                       | 100%     | Indirect | Avebury                       |
| Argos Card Transactions Limited                              | UK                       | 100%     | Indirect | 33 Holborn                    |
| Argos Direct Limited   | UK                       | 100%     | Indirect | 33 Holborn                    |
| Argos Distributors (Ireland) Limited                         | Ireland                  | 100%     | Indirect | Unit 7, Ashbourne Retail Park |
| Argos Extra Limited  | UK                       | 100%     | Indirect | 33 Holborn                    |
| Argos Holdings Limited                                       | UK                       | 100%     | Indirect | Avebury                       |
| Argos Limited  | UK                       | 100%     | Indirect | Avebury                       |
| Argos Retail Group (Asia) Limited                            | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Argos Retail Group (Hong Kong) Limited                       | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Argos Retail Group Limited                                   | UK                       | 100%     | Indirect | 33 Holborn                    |
| Argos Superstores Limited                                    | UK                       | 100%     | Indirect | 33 Holborn                    |
| Argos Surbs Investments Limited                              | UK                       | 100%     | Indirect | Avebury                       |
| Avebury (Asia) Limited                                       | Hong Kong                | 100%     | Indirect | Suite 1608-1613, Tower 6      |
| Barleygold Limited   | UK                       | 100%     | Indirect | 50 Bedford Street             |
| Bed Store & More Limited                                     | UK                       | 100%     | Indirect | 33 Holborn                    |
| Bells Stores Limited   | UK                       | 100%     | Direct   | 33 Holborn                    |
| BLSSP (PHC 7) Limited  | UK                       | 100%     | Direct   | 33 Holborn                    |
| Braemar Castle Limited                                       | UK                       | 100%     | Direct   | 33 Holborn                    |
| Brand Leaders Limited  | UK                       | 100%     | Indirect | 33 Holborn                    |
| Chad Valley Limited  | UK                       | 100%     | Indirect | 33 Holborn                    |
| Clearance Bargains Limited                                   | UK                       | 100%     | Indirect | 33 Holborn                    |
| Cliffrange Limited   | UK                       | 100%     | Indirect | 33 Holborn                    |
| Coolidge Investments Limited                                 | UK                       | 100%     | Indirect | 33 Holborn                    |
| Financial Recovery Services Limited                          | UK                       | 100%     | Indirect | Avebury                       |
| First Stop Stores Limited                                    | UK                       | 100%     | Indirect | 33 Holborn                    |
| Flint Castle Limited   | UK                       | 100%     | Direct   | 33 Holborn                    |
| Global (Guernsey) Limited                                    | Guernsey                 | 100%     | Indirect | Maison Trinity                |
| Habitat Retail Limited                                       | UK                       | 100%     | Indirect | Avebury                       |
| Holborn UK Investments Limited                               | UK                       | 100%     | Direct   | 33 Holborn                    |
| Home Retail (Asia) Limited                                   | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Home Retail (Hong Kong) Limited                              | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Home Retail Group (Asia) Limited                             | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Home Retail Group (Cyprus) Limited                           | Cyprus                   | 100%     | Indirect | Michalaki Karaoli, 8          |
| Home Retail Group (Finance) LLP                              | UK                       | 100%     | Indirect | Avebury                       |
| Home Retail Group (Guernsey) LP                              | Guernsey                 | 100%     | Indirect | Maison Trinity                |
| Home Retail Group (Hong Kong) Limited                        | Hong Kong                | 100%     | Indirect | Units C & D 5/F, D2 Place Two |
| Home Retail Group (Jersey) Limited                           | Jersey                   | 100%     | Indirect | 44 Esplanade                  |
| Home Retail Group (UK) Limited                               | UK                       | 100%     | Indirect | Avebury                       |
| Home Retail Group Card Services Limited                      | UK                       | 100%     | Indirect | Avebury                       |
| Home Retail Group Holdings (Overseas) Limited                | UK                       | 100%     | Indirect | 33 Holborn                    |
| Home Retail Group Insurance Services Limited                 | UK                       | 100%     | Indirect | Avebury                       |
| Home Retail Group Limited                                    | UK                       | 100%     | Indirect | Avebury                       |
| Home Retail Group Nominees Limited                           | UK                       | 100%     | Indirect | 33 Holborn                    |
| Home Retail Group Pension Scheme Nominees Limited            | UK                       | 100%     | Indirect | Avebury                       |
| Home Retail Group Procurement Consultancy (Shanghai) Limited | China                    | 100%     | Indirect | Room 02-04, 12/F., Tower 1    |
| Home Retail Group UK Service Company Limited                 | UK                       | 100%     | Indirect | 33 Holborn                    |
| Home Store & More Limited                                    | UK                       | 100%     | Indirect | 33 Holborn                    |
| J Sainsbury Common Investment Fund Limited                   | UK                       | 100%     | Indirect | 33 Holborn                    |

\*See full address on page 177.

## 37 Details of related undertakings continued

| Entity   | Country of Incorporation | Interest | Holding  | Address*  |
|--|--------------------------|----------|----------|---|
| J Sainsbury Distribution Limited                             | UK                       | 100%     | Direct   | 33 Holborn  |
| J Sainsbury Limited  | Ireland                  | 100%     | Direct   | Riverside One                                     |
| J Sainsbury Pension Scheme Trustees Limited                  | UK                       | 100%     | Direct   | 33 Holborn  |
| J Sainsbury Trustees Limited                                 | UK                       | 100%     | Indirect | 33 Holborn  |
| Jacksons Stores 2002 Limited                                 | UK                       | 100%     | Indirect | 33 Holborn  |
| Jacksons Stores Limited                                      | UK                       | 100%     | Direct   | 33 Holborn  |
| JS Information Systems Limited                               | UK                       | 100%     | Direct   | 33 Holborn  |
| JS Insurance Limited   | Isle of Man              | 100%     | Direct   | Third Floor, St George's Court                    |
| JSD (London) Limited   | UK                       | 100%     | Indirect | 33 Holborn  |
| Jungle Online  | UK                       | 100%     | Indirect | 33 Holborn  |
| Jungle.com Holdings Limited                                  | UK                       | 100%     | Indirect | 33 Holborn  |
| Jungle.com Limited   | UK                       | 100%     | Indirect | 33 Holborn  |
| Nash Court (Kenton) Limited                                  | UK                       | 100%     | Indirect | 33 Holborn  |
| Premier Incentives Limited                                   | UK                       | 100%     | Indirect | 33 Holborn  |
| Ramheath Properties Limited                                  | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury Bridgeco Holdco Limited                            | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury Holdco A Limited                                   | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury Holdco B Limited                                   | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury Propco A Limited                                   | UK                       | 100%     | Indirect | 33 Holborn  |
| Sainsbury Propco B Limited                                   | UK                       | 100%     | Indirect | 33 Holborn  |
| Sainsbury Propco C Limited                                   | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury Propco D Limited                                   | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury Property Investments Limited                       | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury's Asia (Shanghai) Limited                          | Hong Kong                | 100%     | Indirect | 27/F Standard Chartered Tower                     |
| Sainsbury's Asia Limited                                     | Hong Kong                | 100%     | Indirect | 27/F Standard Chartered Tower                     |
| Sainsbury's Bank plc   | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury's Basingstoke Limited                              | UK                       | 100%     | Indirect | 33 Holborn  |
| Sainsbury's Commercial Consulting (Dongguan) Company Limited | China                    | 100%     | Indirect | Room 302, Zhixing International Commerce Building |
| Sainsbury's Convenience Stores Limited                       | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsburys Corporate Director Limited                        | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury's Intermediate Holdings Limited                    | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury's Limited  | Ireland                  | 100%     | Direct   | Riverside One                                     |
| Sainsbury's Limited  | UK                       | 100%     | Direct   | No.2 Lochrin Square                               |
| Sainsbury's Manor GP Limited                                 | UK                       | 100%     | Direct   | Hurlawcreek Road                                  |
| Sainsbury's Manor II Property Limited                        | UK                       | 100%     | Direct   | Hurlawcreek Road                                  |
| Sainsbury's Manor Property Limited                           | UK                       | 100%     | Direct   | Hurlawcreek Road                                  |
| Sainsbury's Planet Limited                                   | UK                       | 100%     | Direct   | 33 Holborn  |
| Sainsbury's Supermarkets Ltd                                 | UK                       | 100%     | Direct   | 33 Holborn  |
| Software Warehouse Holdings Limited                          | UK                       | 100%     | Indirect | 33 Holborn  |
| Stamford House (Jersey) Limited                              | Jersey                   | 100%     | Direct   | Queensway House                                   |
| Stamford House Investments Limited                           | UK                       | 100%     | Indirect | 33 Holborn  |
| Stamford Properties One Limited                              | UK                       | 100%     | Direct   | 33 Holborn  |
| Stamford Properties Three Limited                            | UK                       | 100%     | Direct   | 33 Holborn  |
| Stamford Properties Two Limited                              | UK                       | 100%     | Direct   | 33 Holborn  |
| Stanhope Finance Limited                                     | UK                       | 100%     | Indirect | 33 Holborn  |
| Tintagel Castle Limited                                      | UK                       | 100%     | Direct   | 33 Holborn  |
| Town Centre Retail (Bicester) Limited                        | UK                       | 100%     | Indirect | 33 Holborn  |

\*See full address on page 177.

### 37 Details of related undertakings continued

#### b) Associated undertakings

The Group has a participating interest in the following undertakings:

| Entity  | Country of Incorporation | Interest                  | Holding  | Address*            |
|---|--------------------------|---------------------------|----------|---------------------|
| Arcus FM Limited                                  | UK                       | Preference Shares         | Indirect | Enterprise House    |
| Arcus Solutions Limited                           | UK                       | Preference Shares         | Indirect | Enterprise House    |
| PXS Limited                                       | UK                       | 85,000 B Shares           |          | One New Change      |
| Tamar Energy Limited                              | UK                       | 2,000,000 Investor shares | Indirect | 150 Waterloo Road   |
| BL Sainsbury Superstores Limited                  | UK                       | 50%                       | Indirect | York House          |
| Hedge End Park Limited                            | UK                       | 50%                       | Direct   | 33 Holborn          |
| Harvest 2 GP Limited                              | UK                       | 50%                       | Indirect | 100 Victoria Street |
| Insight 2 Communication LLP                       | UK                       | 50%                       | Indirect | 80 Strand           |
| Harvest 2 Limited Partnership                     | UK                       | 50%                       | Indirect | 100 Victoria Street |
| Harvest Development Management Limited            | UK                       | 50%                       | Indirect | 100 Victoria Street |
| Harvest GP Limited                                | UK                       | 50%                       | Indirect | 100 Victoria Street |
| Netto Limited                                     | UK                       | 50%                       | Direct   | 33 Holborn          |
| Sainsbury's Property Scottish Partnership         | UK                       | 33%                       | Indirect | Hurlawcrook Road    |
| Sainsbury's Property Scottish Limited Partnership | UK                       | 10%                       | Indirect | Hurlawcrook Road    |
| Manor II Property Scottish Partnership            | UK                       | 0.01%                     | Indirect | Hurlawcrook Road    |
| Manor Property Scottish Partnership               | UK                       | 0.01%                     | Indirect | Hurlawcrook Road    |
| Manor Scottish Limited Partnership                | UK                       | 0.01%                     | Indirect | Hurlawcrook Road    |

#### c) Undertakings other than subsidiaries and associated undertakings

The direct or indirect holder of 100 per cent of the voting interests in the following undertakings is an associate of the Group:

| Entity                             | Country of Incorporation | Interest | Holding  | Address*     |
|------------------------------------|--------------------------|----------|----------|--------------|
| B.L.C.T. (10775) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| B.L.C.T. (11546) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| B.L.C.T. (20720) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| B.L.C.T. (27255) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| B.L.C.T. (38775) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| B.L.C.T. (39150) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| B.L.C.T. (39214) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| B.L.C.T. (39215) Limited           | Jersey                   | 50%      | Indirect | 47 Esplanade |
| BL Crawley                         | Jersey                   | 50%      | Indirect | 47 Esplanade |
| BL Superstores Finance PLC         | UK                       | 50%      | Indirect | York House   |
| BL Superstores (Funding) Limited   | UK                       | 50%      | Indirect | York House   |
| BLS Non Securitised 2012 1 Limited | UK                       | 50%      | Indirect | York House   |
| BLS Non-Securitised 2012 2 Limited | UK                       | 50%      | Indirect | York House   |
| BLSSP (Cash Management) Limited    | UK                       | 50%      | Indirect | York House   |
| BLSSP (Lending) Limited            | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 1 2010) Limited         | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 1 2012) Limited         | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 1) Limited              | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 10) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 11) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 12) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 14) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 16) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 17) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 18) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 19) Limited             | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 2 2010) Limited         | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 2) Limited              | UK                       | 50%      | Indirect | York House   |
| BLSSP (PHC 20) Limited             | UK                       | 50%      | Indirect | York House   |

\*See full address on page 177.

**37 Details of related undertakings continued**

| Entity                             | Country of Incorporation | Interest | Holding  | Address*            |
|------------------------------------|--------------------------|----------|----------|---------------------|
| BLSSP (PHC 21) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 22) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 23) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 24) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 25) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 26) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 28) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 3) Limited              | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 32) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 33) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 34) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 35) Limited             | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 4) Limited              | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 5) Limited              | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 6) Limited              | UK                       | 50%      | Indirect | York House          |
| BLSSP (PHC 9) Limited              | UK                       | 50%      | Indirect | York House          |
| British Land Superstores           | UK                       | 50%      | Indirect | York House          |
| Clarendon Property Company         | UK                       | 50%      | Indirect | York House          |
| Harvest 2 Selly Oak Limited        | UK                       | 50%      | Indirect | 100 Victoria Street |
| Harvest Nominee No. 1 Limited      | UK                       | 50%      | Indirect | 100 Victoria Street |
| Harvest Nominee No. 2 Limited      | UK                       | 50%      | Indirect | 100 Victoria Street |
| Pencilscreen Limited               | UK                       | 50%      | Indirect | York House          |
| Selected Land and Property Company | UK                       | 50%      | Indirect | York House          |
| Ten Fleet Place                    | UK                       | 50%      | Indirect | York House          |
| Vyson                              | UK                       | 50%      | Indirect | York House          |

**d) Overseas branches**

The Group has the following branches overseas.

| Entity  | Country | Holding  | Address*   |
|---|---------|----------|--|
| Sainsbury's Asia Limited – Bangladesh Liason Office                                   | India   | Indirect | Level 10, Simpletree Anarkali                      |
| Sainsbury's Asia Limited – India Branch Office  | India   | Indirect | Unit No. 1, 1st Floor, Ambience Corporate Tower II |
| Sainsbury's Commercial Consulting (Dongguan) Company Limited – Shanghai Branch Office | China   | Indirect | Suite 2202-2205, 22F., Raffles City                |

**e) Companies in liquidation**

| Entity                                    | Country of Incorporation | Interest | Holding  | Address*          |
|---|--------------------------|----------|----------|-------------------|
| Global Media Vault Limited                | UK                       | 100%     | Indirect | 33 Holborn        |
| Home Retail Group (India) Private Limited | India                    | 100%     | Indirect | Paradigm Wing A   |
| J Sainsbury (Overseas) Limited            | UK                       | 100%     | Direct   | 33 Holborn        |
| J Sainsbury Holdings                      | Ireland                  | 100%     | Indirect | Riverside One     |
| JS Finance Corporation                    | Ireland                  | 100%     | Indirect | Riverside One     |
| L&B (No 26) Limited                       | UK                       | 100%     | Indirect | 50 Bedford Street |
| Mobile by Sainsbury's Limited             | UK                       | 100%     | Indirect | 33 Holborn        |
| Portfolio Investments Ltd                 | UK                       | 100%     | Indirect | 33 Holborn        |
| RECO Property Limited                     | UK                       | 100%     | Indirect | 33 Holborn        |
| Romford Developments Limited              | UK                       | 50%      | Indirect | 33 Holborn        |
| S. W. Dewsbury Limited                    | UK                       | 100%     | Direct   | 33 Holborn        |
| Sainsbury's Entertainment Ltd             | UK                       | 100%     | Indirect | 33 Holborn        |
| Sainsbury's Holborn Property              | UK                       | 100%     | Indirect | 33 Holborn        |
| Savacentre Limited                        | UK                       | 100%     | Direct   | 33 Holborn        |
| Stamford Properties (Dorking) Limited     | UK                       | 100%     | Indirect | 33 Holborn        |
| Stamford Properties Four Limited          | UK                       | 100%     | Direct   | 33 Holborn        |
| Stockdale Land (Bicester) Limited         | UK                       | 100%     | Indirect | 33 Holborn        |

\*See full address on page 177.

### 37 Details of related undertakings continued

| Address  | Full Address  |
|--|---|
| 100 Victoria Street                                | 100 Victoria Street, London, SW1E 5JL, United Kingdom   |
| 27/F Standard Chartered Tower                      | 27/F Standard Chartered Tower, Millennium City 1, 388 Kwun Tong Road, Kwun, Hong Kong   |
| 33 Holborn   | 33 Holborn, London, EC1N 2HT, United Kingdom  |
| 150 Waterloo Road                                  | 3rd Floor, 150 Waterloo Road, London, SE1 8SB, United Kingdom   |
| 44 Esplanade                                       | 44 Esplanade, St Helier, Jersey, JE4 9WG, Channel Islands   |
| 47 Esplanade                                       | 47 Esplanade, St Helier, Jersey, JE1 0BD, Channel Islands   |
| 50 Bedford Street                                  | 50 Bedford Street, Belfast, BT2 7FN, United Kingdom   |
| 80 Strand  | 80 Strand, 6th Floor, London, WC2R 0NN, United Kingdom  |
| Avebury  | Avebury, 489-499 Avebury Boulevard, Milton Keynes, MK9 2NW, United Kingdom  |
| No.2 Lochrin Square                                | No.2 Lochrin Square, 96 Fountainbridge, Edinburgh, EH3 9QA, United Kingdom  |
| Enterprise House                                   | Enterprise House, 168-170 Upminster Road, Upminster, Essex, RM14 2RB, United Kingdom  |
| Level 10, Simpletree Anarkali                      | Level 10, Simpletree Anarkali, 89 Gulshan Avenue Plet 03, Block – CWS(A), Dhaka – 1212 Bangladesh   |
| Maison Trinity                                     | Maison Trinity, Trinity Square, St Peter Port, GY1 4AT, Guernsey, Channel Islands   |
| One New Change                                     | One New Change, London, EC4M 9AF, United Kingdom  |
| Michalaki Karaoli, 8                               | Michalaki Karaoli, 8, Anemomylos Building, 4th Floor, Flat/Office 401, P.C. 1504, Nicosia, Cyprus   |
| Paradigm Wing A                                    | Paradigm Wing A, 1st Floor, Mindspace, Malad (West), Mumbai, 400 064, India   |
| Room 02-04, 12/F., Tower 1                         | Room 02-04, 12/F., Tower 1, Kerry Everybright City Phase III – Enterprise Centre, No. 128 West Tian Mu Road, Ahzbei, Shanghai, 200070, Shanghai, People's Republic of China |
| Room 302, Zhixing International Commerce Building  | Room 302, Zhixing International Commerce Building, Park Road, Changping Town, Dongguan City, Guangdong province, People's Republic of China.                                |
| Riverside One                                      | Riverside One, Sir John Rogerson's Quay, Dublin 2, Republic of Ireland  |
| Queensway House                                    | Queensway House, Hilgrove Street, St. Helier, JE1 1ES, Jersey, Channel Islands  |
| Hurlawcrook Road                                   | Scottish Commercial Office, Hurlawcrook Road, Langlands Park Industrial Estate, East Kilbride, G75 0QH, United Kingdom  |
| Units C & D 5/F, D2 Place Two                      | Units C & D 5/F, D2 Place Two, No 15 Cheung Shun Street, Cheung Sha Wan, Kowloon, Hong Kong, Hong Kong  |
| Unit 7, Ashbourne Retail Park                      | Unit 7, Ashbourne Retail Park, Ballybin Road, Ashbourne, Republic of Ireland  |
| Unit No. 1, 1st Floor, Ambiance Corporate Tower II | Unit No. 1, 1st Floor, Ambiance Corporate Tower II, Ambiance Island, NH-8, Gurgaon – 122011, Haryana, India   |
| Suite 1608-1613, Tower 6                           | Suite 1608-1613, Tower 6, The Gateway, 9 Canton Road, Tsim Sha Tsui, Kowloon, Hong Kong   |
| Suite 2202-2205, 22F., Raffles City                | Suite 2202-2205, 22F., Raffles City, 268 Xi Zang Middle Road, Shanghai 200001, People's Republic of China   |
| York House   | York House, 45 Seymour Street, London, W1H 7LX, United Kingdom  |
| Third Floor, St George's Court                     | Third Floor, St George's Court, Upper Church Street, Douglas, IM1 1EE, Isle of Man  |

## Five year financial record

### Five year financial record

|   | 2017          | 2016   | 2015   | 2014   | 2013   |
|---|---------------|--------|--------|--------|--------|
| <b>Financial results (£m)</b>   |               |        |        |        |        |
| <b>Underlying sales (including VAT, including fuel, including Financial Services)</b> | <b>29,112</b> | 25,829 | 26,122 | 26,353 | 25,632 |
| <b>Underlying operating profit</b>  |               |        |        |        |        |
| Retail  | <b>626</b>    | 635    | 720    | 873    | 831    |
| Financial Services  | <b>62</b>     | 65     | 62     | 6      | –      |
|   | <b>688</b>    | 700    | 782    | 879    | 831    |
| Underlying net finance costs <sup>1</sup>   | <b>(119)</b>  | (121)  | (107)  | (111)  | (111)  |
| Underlying share of post-tax profit from joint ventures                               | <b>12</b>     | 8      | 6      | 30     | 38     |
| <b>Underlying profit before tax<sup>1, 2</sup></b>                                    | <b>581</b>    | 587    | 681    | 798    | 758    |
| (Decrease)/increase on previous year (%)  | <b>(1.0)</b>  | (13.8) | (14.7) | 5.3    | 6.5    |
| <b>Retail underlying operating margin (%)<sup>3</sup></b>                             | <b>2.42</b>   | 2.74   | 3.07   | 3.65   | 3.57   |
| <b>Earnings per share</b>   |               |        |        |        |        |
| Underlying (pence)  | <b>21.8</b>   | 24.2   | 26.4   | 32.8   | 30.8   |
| (Decrease)/increase on previous year (%)  | <b>(9.9)</b>  | (8.3)  | (19.5) | 6.5    | 9.6    |
| Proposed dividend per share (pence) <sup>4</sup>                                      | <b>10.2</b>   | 12.1   | 13.2   | 17.3   | 16.7   |

1 Net finance costs before non-underlying finance movements, IAS 19 pension financing charge but after accrued coupons on the perpetual securities.

2 Profit/(loss) before tax from continuing operations before non-underlying items as described in note 3.

3 Retail operating profit margin based on retail sales excluding Value Added Tax, including fuel, excluding Financial Services.

4 Total proposed dividend to ordinary shareholders in relation to the financial year.

# Company balance sheet

At 11 March 2017 and 12 March 2016

|   | Note | 2017<br>£m     | 2016<br>£m |
|---|------|----------------|------------|
| <b>Non-current assets</b>                       |      |                |            |
| Investments in subsidiaries                     | 2    | <b>5,757</b>   | 4,500      |
| Investments in joint ventures and associates    | 3    | <b>10</b>      | 33         |
| Available-for-sale financial assets             | 4    | <b>39</b>      | 35         |
| Other receivables                               | 5    | <b>1,716</b>   | 1,531      |
| Derivative financial instruments                | 12   | <b>6</b>       | 22         |
|   |      | <b>7,528</b>   | 6,121      |
| <b>Current assets</b>                           |      |                |            |
| Trade and other receivables                     | 5    | <b>1,042</b>   | 1,195      |
| Derivative financial instruments                | 12   | <b>19</b>      | 32         |
| Cash and cash equivalents                       |      | <b>300</b>     | 338        |
|   |      | <b>1,361</b>   | 1,565      |
| Assets held for sale                            |      | <b>–</b>       | 1          |
|   |      | <b>1,361</b>   | 1,566      |
| <b>Total assets</b>                             |      | <b>8,889</b>   | 7,687      |
| <b>Current liabilities</b>                      |      |                |            |
| Trade and other payables                        | 6    | <b>(375)</b>   | (157)      |
| Borrowings                                      | 7    | <b>(1)</b>     | (40)       |
| Derivative financial instruments                | 12   | <b>(17)</b>    | (35)       |
| Taxes payable                                   |      | <b>(31)</b>    | (21)       |
|   |      | <b>(424)</b>   | (253)      |
| <b>Net current assets</b>                       |      | <b>937</b>     | 1,313      |
| <b>Non-current liabilities</b>                  |      |                |            |
| Other payables                                  | 6    | <b>(587)</b>   | (692)      |
| Borrowings                                      | 7    | <b>(625)</b>   | (616)      |
| Derivative financial instruments                | 12   | <b>(4)</b>     | (13)       |
| Deferred income tax liability                   | 9    | <b>–</b>       | –          |
| Provisions                                      | 8    | <b>(2)</b>     | (2)        |
|   |      | <b>(1,218)</b> | (1,323)    |
| <b>Net assets</b>                               |      | <b>7,247</b>   | 6,111      |
| <b>Equity</b>                                   |      |                |            |
| Called up share capital                         | 10   | <b>625</b>     | 550        |
| Share premium account                           | 10   | <b>1,120</b>   | 1,114      |
| Capital redemption reserve                      | 10   | <b>680</b>     | 680        |
| Merger reserve                                  | 10   | <b>568</b>     | –          |
| Other reserves                                  | 10   | <b>28</b>      | 31         |
| Retained earnings                               | 11   | <b>3,730</b>   | 3,240      |
| <b>Total equity before perpetual securities</b> |      | <b>6,751</b>   | 5,615      |
| Perpetual capital securities                    |      | <b>248</b>     | 248        |
| Perpetual convertible bonds                     |      | <b>248</b>     | 248        |
| <b>Total equity</b>                             |      | <b>7,247</b>   | 6,111      |

The notes on pages 181 to 185 form an integral part of these financial statements.

The financial statements on pages 179 to 185 were approved by the Board of Directors on 2 May 2017, and are signed on its behalf by:

**Mike Coupe** Chief Executive

**Kevin O'Byrne** Chief Financial Officer

# Company statement of changes in equity

for the 52 weeks to 11 March 2017

|  | Note    | Called up share capital<br>£m | Share premium account<br>£m | Capital redemption and other reserves<br>£m | Merger reserve<br>£m | Retained earnings<br>£m | Total equity before perpetual securities<br>£m | Perpetual capital securities<br>£m | Perpetual convertible bonds<br>£m | Total equity<br>£m |
|--|---------|-------------------------------|-----------------------------|---|----------------------|-------------------------|--|------------------------------------|-----------------------------------|--------------------|
| <b>At 13 March 2016</b>  |         | <b>550</b>                    | <b>1,114</b>                | <b>711</b>                                  | <b>–</b>             | <b>3,240</b>            | <b>5,615</b>                                   | <b>248</b>                         | <b>248</b>                        | <b>6,111</b>       |
| Profit for the period  | 11      | –                             | –                           | –   | –                    | 682                     | 682  | 12                                 | 6                                 | 700                |
| Other comprehensive income   | 10      | –                             | –                           | 5   | –                    | –                       | 5  | –                                  | –                                 | 5                  |
| <b>Total comprehensive income for the year ended 11 March 2017</b>   |         | <b>–</b>                      | <b>–</b>                    | <b>5</b>                                    | <b>–</b>             | <b>682</b>              | <b>687</b>                                     | <b>12</b>                          | <b>6</b>                          | <b>705</b>         |
| Transactions with owners:  |         |                               |                             |   |                      |                         |  |                                    |                                   |                    |
| Dividends  | 11      | –                             | –                           | –   | –                    | (232)                   | (232)  | –                                  | –                                 | (232)              |
| Acquisition of subsidiaries  | 10, 11  | 75                            | –                           | –   | 568                  | (3)                     | 640  | –                                  | –                                 | 640                |
| Adjustment to consideration in respect of share options  | 11      | –                             | –                           | –   | –                    | 3                       | 3  | –                                  | –                                 | 3                  |
| Distribution to holders of perpetual securities (net of tax)   |         | –                             | –                           | –   | –                    | –                       | –  | (12)                               | (6)                               | (18)               |
| Amortisation of convertible bond equity component  | 10, 11  | –                             | –                           | (8)   | –                    | 8                       | –  | –                                  | –                                 | –                  |
| Allotted in respect of share option schemes  | 10, 11  | –                             | 6                           | –   | –                    | 32                      | 38   | –                                  | –                                 | 38                 |
| <b>At 11 March 2017</b>  |         | <b>625</b>                    | <b>1,120</b>                | <b>708</b>                                  | <b>568</b>           | <b>3,730</b>            | <b>6,751</b>                                   | <b>248</b>                         | <b>248</b>                        | <b>7,247</b>       |
| At 15 March 2015   |         |                               |                             |   |                      |                         |  |                                    |                                   |                    |
|  |         | 548                           | 1,108                       | 720   | –                    | 2,085                   | 4,461  | –                                  | –                                 | 4,461              |
| Profit for the period  | 11      | –                             | –                           | –   | –                    | 1,360                   | 1,360  | 13                                 | 6                                 | 1,379              |
| Other comprehensive income   | 10      | –                             | –                           | (2)   | –                    | –                       | (2)  | –                                  | –                                 | (2)                |
| Total comprehensive income for the period ended 12 March 2016  |         | –                             | –                           | (2)   | –                    | 1,360                   | 1,358  | 13                                 | 6                                 | 1,377              |
| Transactions with owners:  |         |                               |                             |   |                      |                         |  |                                    |                                   |                    |
| Dividends  | 11      | –                             | –                           | –   | –                    | (234)                   | (234)  | –                                  | –                                 | (234)              |
| Issue of perpetual subordinated capital securities and perpetual subordinated convertible bonds (net of tax) |         | –                             | –                           | –   | –                    | –                       | –  | 248                                | 248                               | 496                |
| Distributions to holders of perpetual subordinated convertible bonds (net of tax)                            |         | –                             | –                           | –   | –                    | –                       | –  | (13)                               | (6)                               | (19)               |
| Amortisation of convertible bond equity component  | 10, 11  | –                             | –                           | (7)   | –                    | 7                       | –  | –                                  | –                                 | –                  |
| Allotted in respect of share option schemes  | 10, x11 | 2                             | 6                           | –   | –                    | 22                      | 30   | –                                  | –                                 | 30                 |
| <b>At 12 March 2016</b>  |         | <b>550</b>                    | <b>1,114</b>                | <b>711</b>                                  | <b>–</b>             | <b>3,240</b>            | <b>5,615</b>                                   | <b>248</b>                         | <b>248</b>                        | <b>6,111</b>       |

The notes on pages 181 to 185 form an integral part of these financial statements.

# Notes to the Company financial statements

## 1 Basis of preparation

The parent company's financial statements are prepared in accordance with United Kingdom Accounting Standards, in particular Financial Reporting Standard 101 Reduced Disclosure Framework (FRS 101) and the Companies Act 2006. FRS 101 sets out a reduced disclosure framework for a 'qualifying entity' as defined in the Standard, which addresses the financial reporting requirements and disclosure exemptions in the individual financial statements of qualifying entities that otherwise apply the recognition measurement and disclosure requirements of International Financial Reporting Standards (IFRS) as adopted by the European Union.

These are the first financial statements of the Company prepared in accordance with FRS 101. The Company's transition date to FRS 101 is 13 March 2016. FRS 101 sets out amendments to IFRS as adopted by the European Union that are necessary to achieve compliance with the Companies Act and related regulations. These amendments had no impact on the Statement of Comprehensive Income, Balance Sheet or Statement of Changes in Equity for the Company for the year ended 11 March 2017.

The financial year represents the 52 weeks to 11 March 2017 (prior financial year 52 weeks to 12 March 2016).

The disclosure exemptions adopted by the Company in accordance with FRS 101 are as follows:

- The requirements of IAS 7 to present a cash flow statement.
- The requirements of paragraph 17 of IAS 24, 'Related Party Transactions', to disclose information related to key management personnel, and the requirements of IAS 24 to disclose related party transactions between two or more members of a group for wholly owned subsidiaries.
- The requirements of paragraphs 30 and 31 of IAS 8 to disclose information assessing the possible impact of new standards issued but which are not yet effective.
- The requirements of IFRS 7 and IFRS 13 for disclosure of financial instruments and fair values.

The financial statements are presented in sterling, rounded to the nearest £million unless otherwise stated. They have been prepared on the going concern basis under the historical cost convention, except for derivative financial instruments and available-for-sale financial assets that have been measured at fair value.

The Directors have taken advantage of the exemption available under Section 408 of the Companies Act 2006 and not presented an Income Statement nor a Statement of Comprehensive Income for the Company alone. The profit after tax for the Company for the year was £682 million (2016: £1,360 million).

## 2 Investments in subsidiaries

### Accounting policies

Investments in subsidiaries are carried at cost less any impairment loss in the financial statements of the Company.

|   | 2017<br>£m   | 2016<br>£m |
|---|--------------|------------|
| <b>Shares in subsidiaries</b>                     |              |            |
| At 13 March 2016                                  | 4,500        | 7,630      |
| Additions   | 1,257        | 160        |
| Disposals   | –            | (3,294)    |
| Release of provision for diminution of investment | –            | 4          |
| <b>At 11 March 2017</b>                           | <b>5,757</b> | 4,500      |

Additions in the year predominantly relate to the acquisition of Home Retail Group.

During the prior year a number of subsidiaries were liquidated as part of a corporate simplification project. This resulted in dividends received of £5,307 million and a subsequent disposal of subsidiaries of £3,294 million.

## 3 Investments in joint ventures and associates

### Accounting policies

Investments in joint ventures and associates are carried at cost less any impairment loss in the financial statements of the Company.

|   | Company<br>shares at<br>cost<br>2017<br>£m | Company<br>shares at cost<br>2016<br>£m |
|---|--|---|
| <b>At 13 March 2016</b>                         | <b>33</b>                                  | 18                                      |
| Additions                                       | 16   | 15                                      |
| Provision for diminution in value of investment | (39)                                       | –                                       |
| <b>At 11 March 2017</b>                         | <b>10</b>                                  | 33                                      |

A provision of £39 million (2016: £nil) was made against investments in joint ventures where the carrying amounts exceeded the recoverable amount.

#### 4 Available-for-sale financial assets

##### Accounting policies

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories (of fair value through profit or loss, loans and receivables). They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date. Subsequent to initial recognition at fair value plus transaction costs, these assets are recorded at fair value at each period end with the movements recognised in other comprehensive income until derecognition or impaired, at which time the cumulative gain or loss previously recognised in other comprehensive income is recycled to the income statement. Dividends on AFS equity instruments are recognised in the income statement when the entity's right to receive payment is established. Interest on AFS debt instruments is recognised using the effective interest method.

|                                   | 2017<br>£m | 2016<br>£m |
|-----------------------------------|------------|------------|
| <b>Non-current</b>                |            |            |
| Interest bearing financial assets | <b>39</b>  | 35         |

#### 5 Other receivables

##### Accounting policies

Receivables are recognised initially at fair value, and subsequently at amortised cost using the effective interest rate method, less provision for impairment.

|                                 | 2017<br>£m   | 2016<br>£m |
|---------------------------------|--------------|------------|
| <b>Non-current</b>              |              |            |
| Amounts owed by Group companies | <b>1,716</b> | 1,531      |
| <b>Current</b>                  |              |            |
| Amounts owed by Group companies | <b>1,038</b> | 1,189      |
| Prepayments and accrued income  | <b>4</b>     | 6          |
|                                 | <b>1,042</b> | 1,195      |

#### 6 Trade and other payables

##### Accounting policies

Payables are recognised initially at fair value, and subsequently at amortised cost using the effective interest rate method.

|                                | 2017<br>£m | 2016<br>£m |
|--------------------------------|------------|------------|
| <b>Current</b>                 |            |            |
| Amounts owed to Group entities | <b>346</b> | 125        |
| Other payables                 | <b>29</b>  | 32         |
|                                | <b>375</b> | 157        |
| <b>Non-current</b>             |            |            |
| Amounts owed to Group entities | <b>587</b> | 692        |

#### 7 Borrowings

|                           | 2017<br>Current<br>£m | 2017<br>Non-current<br>£m | 2017<br>Total<br>£m | 2016<br>Current<br>£m | 2016<br>Non-current<br>£m | 2016<br>Total<br>£m |
|---------------------------|-----------------------|---------------------------|---------------------|-----------------------|---------------------------|---------------------|
| Bank loans due 2016       | –                     | –                         | –                   | 39                    | –                         | 39                  |
| Bank loans due 2019       | –                     | <b>199</b>                | <b>199</b>          | –                     | 199                       | 199                 |
| Convertible bond due 2019 | <b>1</b>              | <b>426</b>                | <b>427</b>          | 1                     | 417                       | 418                 |
| <b>Total borrowings</b>   | <b>1</b>              | <b>625</b>                | <b>626</b>          | 40                    | 616                       | 656                 |

## 8 Provisions

### Accounting policies

Provisions are recognised when there is a present legal or constructive obligation as a result of a past event, for which it is probable that an outflow of economic benefit will be required to settle the obligation, and where the amount of the obligation can be reliably estimated. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

|                                    | Onerous leases and onerous contracts<br>£m | Disposal provision<br>£m | Total<br>£m |
|------------------------------------|--|--------------------------|-------------|
| At 13 March 2016 and 12 March 2017 | 1  | 1                        | 2           |
| At 15 March 2015                   | 3  | 1                        | 4           |
| Utilisation of provision           | (2)  | –                        | (2)         |
| At 12 March 2016                   | 1  | 1                        | 2           |

|               | 2017<br>£m | 2016<br>£m |
|---------------|------------|------------|
| Disclosed as: |            |            |
| Current       | –          | –          |
| Non-current   | 2          | 2          |
|               | 2          | 2          |

## 9 Taxation

### Accounting policies

Deferred tax is accounted for on the basis of temporary differences arising from differences between the tax base and accounting base of assets and liabilities.

Deferred tax is recognised for all temporary differences, except to the extent where it arises from the initial recognition of an asset or a liability in a transaction that is not a business combination and, at the time of transaction, affects neither accounting profit nor taxable profit. It is determined using tax rates (and laws) that have been enacted or substantively 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 tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Deferred tax is charged or credited to the income statement, except when it relates to items charged or credited directly to equity or other comprehensive income.

Deferred tax is provided on temporary differences associated with investments in subsidiaries, branches and joint ventures except where the Company is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

|  | Capital losses<br>£m | Rolled over capital gains<br>£m | Total<br>£m |
|--|----------------------|---------------------------------|-------------|
| At 13 March 2016   | 22                   | (22)                            | –           |
| Rate change adjustment to income statement                                     | (1)                  | 1                               | –           |
| <b>At 11 March 2017</b>  | <b>21</b>            | <b>(21)</b>                     | <b>–</b>    |
| At 15 March 2015   | 25                   | (25)                            | –           |
| Rate change adjustment to income statement                                     | (3)                  | 3                               | –           |
| At 12 March 2016   | 22                   | (22)                            | –           |
|  |                      | 2017<br>£m                      | 2016<br>£m  |
| Total deferred income tax liabilities  |                      | (21)                            | (22)        |
| Total deferred income tax assets   |                      | 21                              | 22          |
| <b>Net deferred income tax liability recognised in non-current liabilities</b> |                      | –                               | –           |

## 10 Share capital and reserves

### Accounting policies

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

### Share capital, share premium and merger reserve

|  | 2017<br>million | 2016<br>million | 2017<br>£m   | 2016<br>£m |
|--|-----------------|-----------------|--------------|------------|
| <b>Called up share capital</b>                             |                 |                 |              |            |
| Allotted and fully paid ordinary shares 28 $\frac{1}{2}$ p | <b>2,188</b>    | 1,924           | <b>625</b>   | 550        |
| <b>Share premium account</b>                               |                 |                 |              |            |
| Share premium  |                 |                 | <b>1,120</b> | 1,114      |

The movements in the called up share capital, share premium and merger reserve accounts are set out below:

|   | Number of<br>ordinary<br>shares<br>million | Ordinary<br>shares<br>£m | Share<br>premium<br>account<br>£m | Merger<br>reserve<br>£m |
|---|--|--------------------------|-----------------------------------|-------------------------|
| At 13 March 2016                            | 1,924                                      | 550                      | <b>1,114</b>                      | –                       |
| Acquisition of subsidiaries <sup>1</sup>    | 261  | 75                       | –                                 | <b>568</b>              |
| Allotted in respect of share option schemes | 3  | –                        | 6                                 | –                       |
| <b>At 11 March 2017</b>                     | <b>2,188</b>                               | <b>625</b>               | <b>1,120</b>                      | <b>568</b>              |
| At 15 March 2015                            | 1,919                                      | 548                      | 1,108                             | –                       |
| Allotted in respect of share option schemes | 5  | 2                        | 6                                 | –                       |
| At 12 March 2016                            | 1,924                                      | 550                      | <b>1,114</b>                      | –                       |

1 261 million new J Sainsbury plc shares of 28 $\frac{1}{2}$ p nominal value each were issued (being 0.321 new J Sainsbury plc shares per existing Home Retail Group plc share); fair value of the consideration is based on a J Sainsbury plc share price of £2.4610 as at 2 September 2016. This is accounted for as £75 million in share capital, plus the premium arising from the consideration in excess of the nominal amount of shares issued of £568 million, which is recognised in the merger reserve as the transaction qualified for merger relief.

### Capital redemption and other reserves

|   | Available-<br>for-sale assets<br>£m | Cash flow<br>hedge reserve<br>£m | Convertible<br>bond reserve<br>£m | Total other<br>reserves<br>£m | Capital<br>redemption<br>reserve<br>£m | Merger<br>reserve<br>£m |
|---|-------------------------------------|----------------------------------|-----------------------------------|-------------------------------|--|-------------------------|
| At 13 March 2016  | 6                                   | (4)                              | 29                                | 31                            | 680                                    | –                       |
| Acquisition of subsidiaries   | –                                   | –                                | –                                 | –                             | –                                      | <b>568</b>              |
| Available-for-sale financial assets fair value movements (net of tax)   | 4                                   | –                                | –                                 | 4                             | –                                      | –                       |
| Cash flow hedges effective portion of fair value movements (net of tax) | –                                   | (1)                              | –                                 | (1)                           | –                                      | –                       |
| Items reclassified from cash flow hedge reserve                         | –                                   | 2                                | –                                 | 2                             | –                                      | –                       |
| Amortisation of convertible bond – equity component                     | –                                   | –                                | (8)                               | (8)                           | –                                      | –                       |
| <b>At 11 March 2017</b>   | <b>10</b>                           | <b>(3)</b>                       | <b>21</b>                         | <b>28</b>                     | <b>680</b>                             | <b>568</b>              |
| At 15 March 2015  | 8                                   | (4)                              | 36                                | 40                            | 680                                    | –                       |
| Available-for-sale financial assets fair value movements (net of tax)   | (2)                                 | –                                | –                                 | (2)                           | –                                      | –                       |
| Cash flow hedges effective portion of fair value movements (net of tax) | –                                   | (2)                              | –                                 | (2)                           | –                                      | –                       |
| Items reclassified from cash flow hedge reserve                         | –                                   | 2                                | –                                 | 2                             | –                                      | –                       |
| Amortisation of convertible bond – equity component                     | –                                   | –                                | (7)                               | (7)                           | –                                      | –                       |
| At 12 March 2016  | 6                                   | (4)                              | 29                                | 31                            | 680                                    | –                       |

The available-for-sale assets reserve represents the fair value gains and losses on the available-for-sale financial assets held by the Company. The cash flow hedge reserve represents the cumulative effective fair value gains and losses on cash flow hedges in the Company.

The convertible bond reserve represents the equity component of the £450 million convertible bond issued in November 2014.

The capital redemption reserve arose on the redemption of B shares. Shareholders approved a £680 million return of share capital, by way of a B share scheme, at the Company's Extraordinary General Meeting on 12 July 2004. The final redemption date for B shares was 18 July 2007 and all transactions relating to the B shares have now been completed.

## 11 Retained earnings

|   | 2017<br>£m   | 2016<br>£m   |
|---|--------------|--------------|
| Beginning of the year                                   | 3,240        | 2,085        |
| Acquisition of subsidiaries                             | (3)          | –            |
| Adjustment to consideration in respect of share options | 3            | –            |
| Profit for the year                                     | 682          | 1,360        |
| Dividends paid  | (232)        | (234)        |
| Allotted in respect of share option schemes             | 32           | 22           |
| Amortisation of convertible bond – equity component     | 8            | 7            |
| <b>End of the year</b>                                  | <b>3,730</b> | <b>3,240</b> |

## 12 Derivative financial instruments

The fair value of derivative financial instruments has been disclosed in the balance sheet as follows:

|              | 2017<br>Asset<br>£m | 2017<br>Liability<br>£m | 2016<br>Asset<br>£m | 2016<br>Liability<br>£m |
|--------------|---------------------|-------------------------|---------------------|-------------------------|
| Non-current  | 6                   | (4)                     | 22                  | (13)                    |
| Current      | 19                  | (17)                    | 32                  | (35)                    |
| <b>Total</b> | <b>25</b>           | <b>(21)</b>             | 54                  | (48)                    |

The fair value and notional amount of derivatives analysed by hedge type are as follows:

|   | 2017             |                |                  |                | 2016             |                |                  |                |
|---|------------------|----------------|------------------|----------------|------------------|----------------|------------------|----------------|
|   | Asset            |                | Liability        |                | Asset            |                | Liability        |                |
|   | Fair value<br>£m | Notional<br>£m |
| <b>Fair value hedges</b>                                |                  |                |                  |                |                  |                |                  |                |
| Interest rate swaps                                     | 6                | 160            | –                | –              | 14               | 206            | –                | –              |
| <b>Cash flow hedges</b>                                 |                  |                |                  |                |                  |                |                  |                |
| Interest rate swaps                                     | –                | –              | (4)              | 100            | –                | –              | (4)              | 100            |
| <b>Derivatives not in a formal hedging relationship</b> |                  |                |                  |                |                  |                |                  |                |
| Interest rate swaps                                     | 17               | 341            | (15)             | 295            | 30               | 386            | (27)             | 327            |
| Inflation rate swaps                                    | 2                | 400            | (2)              | 400            | 10               | 400            | (10)             | 400            |
| Cross currency and foreign exchange swaps               | –                | –              | –                | –              | –                | –              | (7)              | 71             |
| <b>Total</b>  | <b>25</b>        | <b>901</b>     | <b>(21)</b>      | <b>795</b>     | 54               | 992            | (48)             | 898            |

## Additional shareholder information

### Financial calendar

|   |                  |
|---|------------------|
| Ex-dividend date                                    | 11 May 2017      |
| Record date   | 12 May 2017      |
| Last date for return of revocation of DRIP mandates | 16 June 2017     |
| Q1 Trading Statement                                | 4 July 2017      |
| Annual General Meeting                              | 5 July 2017      |
| Payment date and DRIP share purchase                | 7 July 2017      |
| Interim results announced                           | 8 November 2017* |
| Q3 Trading Statement                                | 10 January 2018* |
| Preliminary Results announced                       | 2 May 2018*      |
| Annual General Meeting                              | 11 July 2018*    |

\*provisional dates

The interim dividend was paid on 4 January 2017.

### Shareholder profiles

End of year information as at 11 March 2017

|                           | 2017                 | 2016          |
|---------------------------|----------------------|---------------|
| Number of shareholders    | <b>133,332</b>       | 113,101       |
| Number of shares in issue | <b>2,188,149,787</b> | 1,924,077,194 |

### By size of holding

|                      | Shareholders % |       | Shares %     |       |
|----------------------|----------------|-------|--------------|-------|
|                      | 2017           | 2016  | 2017         | 2016  |
| 500 and under        | <b>69.13</b>   | 63.58 | <b>0.47</b>  | 0.42  |
| 501 to 1,000         | <b>11.23</b>   | 11.94 | <b>0.51</b>  | 0.53  |
| 1,001 to 10,000      | <b>17.98</b>   | 22.35 | <b>3.01</b>  | 3.69  |
| 10,001 to 100,000    | <b>1.24</b>    | 1.63  | <b>1.85</b>  | 2.33  |
| 100,001 to 1,000,000 | <b>0.29</b>    | 0.35  | <b>6.12</b>  | 7.20  |
| Over 1,000,000       | <b>0.13</b>    | 0.15  | <b>88.04</b> | 85.83 |
|                      | <b>100</b>     | 100   | <b>100</b>   | 100   |

### By category of shareholder

|                        | Shareholders % |       | Shares %     |      |
|------------------------|----------------|-------|--------------|------|
|                        | 2017           | 2016  | 2017         | 2016 |
| Individuals            | <b>96.47</b>   | 92.82 | <b>5.26</b>  | 5.67 |
| Insurance companies    | <b>0.06</b>    | 0.06  | <b>0.03</b>  | 0.03 |
| Banks and Nominees     | <b>3.18</b>    | 6.85  | <b>93.59</b> | 92.1 |
| Investment Trusts      | <b>0.03</b>    | 0.03  | <b>0.01</b>  | 0.04 |
| Pension Funds          | <b>0.01</b>    | 0.01  | <b>0.01</b>  | 0    |
| Other Corporate Bodies | <b>0.25</b>    | 0.23  | <b>1.1</b>   | 2.16 |
|                        | <b>100</b>     | 100   | <b>100</b>   | 100  |

### Annual General Meeting (AGM)

The AGM will be held at 11.00am on Wednesday, 5 July 2017 at The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE. The Notice of the Meeting and the proxy card for the meeting are enclosed with this report.

### Registrars

For information about the AGM, shareholdings, dividends and to report changes to personal details, shareholders should contact:

Computershare Investor Services PLC  
The Pavilions  
Bridgwater Road  
Bristol BS99 6ZZ  
Telephone: 0370 702 0106

Please remember to tell Computershare if you move house or change bank details or if there is any other change to your account information.

You can view and manage your shareholding online at [www.investorcentre.co.uk](http://www.investorcentre.co.uk). You will require your 11 character Shareholder Reference Number (SRN) to log in. Your SRN starts with the letter C or G and is followed by ten numbers. It can be found on share certificates and dividend confirmations.

### Dividends

Having your dividends paid directly into your bank or building society account is a more secure way than receiving your dividend by cheque. If you would prefer your dividends to be paid directly into your bank or building society account further information is available from Computershare Investor Services (address and telephone number above). You will still receive an annual dividend confirmation detailing each dividend to enable you to complete your tax return.

### Dividend Reinvestment Plan (DRIP)

The Company has a DRIP, which allows shareholders to reinvest their cash dividends in the Company's shares bought in the market through a specially arranged share dealing service. No new shares are allotted under this DRIP and approximately 30,086 shareholders participate. Full details of the DRIP and its charges, together with mandate forms, are available from the Registrars. Alternatively, you can elect to join the DRIP by registering on [www.investorcentre.co.uk](http://www.investorcentre.co.uk).

### Annual Dividend Confirmations

The Company sends out an Annual Dividend Confirmation (ADC) in relation to dividend payments. This means that those shareholders receiving their dividend direct into their bank account will receive an ADC once a year detailing all payments made throughout that year.

### Shareholder communications Company website

J Sainsbury plc Interim and Annual Reports, and results announcements are available via the internet on our website at [www.j-sainsbury.co.uk](http://www.j-sainsbury.co.uk). As well as providing share price data and financial history, the site also provides background information about the Company, regulatory and news releases, and current issues.

### Electronic shareholder communications

The Company encourages all shareholders to receive their shareholder communications electronically in order to reduce the impact on the environment. To do this go to [www.investorcentre.co.uk/etreeuk/jsainsbury](http://www.investorcentre.co.uk/etreeuk/jsainsbury). For each email registration by a Sainsbury's shareholder, a donation will be made to the Woodland Trust, the UK's leading woodland conservation charity. By registering with the eTree programme you will be giving the Company permission to send all shareholder documents to you via email with a link to a secure website.

Alternatively, the Company has set up a facility for shareholders to take advantage of electronic communications. The service allows you to:

- view the Annual Report and Financial Statements on the day it is published;
- receive electronic notification of the availability of future shareholder information (you must register your email for this service);
- check the balance and current value of your shareholding and view your dividend history; and,
- submit your vote online prior to a general meeting.

To register visit [www.investorcentre.co.uk](http://www.investorcentre.co.uk). You will need your 11 character SRN which can be found on your share certificate or recent dividend confirmation – the number is often preceded by the letter C or G.

### Shareholder security

Shareholders are advised to be very wary of any unsolicited advice, offers to buy shares at a discount or offers of free company annual reports. If you receive any unsolicited investment advice, whether over the telephone, through the post or by email:

- make sure you get the name of the person and organisation;
- check that they are properly authorised by the FCA before getting involved by visiting <https://register.fca.org.uk/>; and,
- report the matter to the FCA either by calling 0800 111 6768 or by completing an online form at [www.fca.org.uk/consumers/report-scam-unauthorised-firm](http://www.fca.org.uk/consumers/report-scam-unauthorised-firm)

Details of any share dealing facilities that the Company endorses will be included in Company mailings.

More detailed information on this or similar activity can be found on the FCA website [www.scamsmart.fca.org.uk](http://www.scamsmart.fca.org.uk)

### Share dealing services

To buy or sell your J Sainsbury plc ordinary shares, please visit your stockbroker or a high street bank who will usually be able to assist you. Alternatively, you may consider using:

- The Share Centre Ltd who offer a postal dealing service. They can be contacted at The Share Centre, PO Box 2000, Oxford Road, Aylesbury, Buckinghamshire HP21 8ZB. Telephone: 01296 414141 or Freephone 08000 282812 and quote Sainsbury's; or,
- Computershare who offer a telephone and internet facility which gives shareholders the opportunity to trade at a known price. The telephone service is available from 8.00am to 4.30pm, Monday to Friday, excluding bank holidays, on telephone number 0370 703 0084. The internet share dealing service gives shareholders the option to submit instructions to trade online. More information can be found by visiting [www-uk.computershare.com/Investor/ShareDealing](http://www-uk.computershare.com/Investor/ShareDealing).

Further information and detailed terms and conditions are available on request by calling either provider.

### American Depositary Receipts (ADRs)

The Company has a sponsored Level I ADR programme for which The Bank of New York Mellon acts as depositary. The ADRs are traded on the over-the-counter (OTC) market in the US under the symbol JSIAY, where one ADR is equal to four ordinary shares. All enquiries relating to ADRs should be addressed to:

BNY Mellon  
Shareowner Services  
PO Box 30170  
College Station  
TX 77842-3170

Toll Free Telephone # for domestic callers: 1-888-269-2377

International callers can call: +1-201-680-6825

Website: [www.mybnymdr.com](http://www.mybnymdr.com)

Email: [shrrelations@bnymellon.com](mailto:shrrelations@bnymellon.com)

### ShareGift

If you have only a small number of shares which would cost more for you to sell than they are worth, you may wish to consider donating them to the charity ShareGift (Registered Charity 1052686) which specialises in accepting such shares as donations. The relevant stock transfer form may be obtained from Computershare Investor Services PLC. There are no implications for Capital Gains Tax purposes (no gain or loss) on gifts of shares to charity. It is also possible to obtain income tax relief. Further information about ShareGift may be obtained on 020 7930 3737 or from [www.sharegift.org](http://www.sharegift.org).

### Tax information – Capital Gains Tax (CGT)

For CGT purposes, the market value of J Sainsbury plc ordinary shares on 31 March 1982 adjusted for all capital adjustments was 91.99 pence and B shares 10.941 pence.

CGT information on historic Home Retail Group corporate actions can be found in the Investor Section on our website [www.j-sainsbury.co.uk/investor-centre](http://www.j-sainsbury.co.uk/investor-centre).

### Share capital consolidation

The original base cost of shares apportioned between ordinary shares of 28 <sup>4</sup>/<sub>7</sub> pence and B shares is made by reference to the market value of each class of shares on the first day for which a market value is quoted after the new holding came into existence. The market value for CGT purposes of any share or security quoted on the Stock Exchange Daily Official List is generally the lower of the two quotations on any day plus one quarter of the difference between the values.

On Monday, 19 July 2004 the values were determined as follows:

New ordinary shares 257.5 pence

B shares 35 pence

Historic share capital consolidation information relating to Home Retail Group can be found in the Investor Section on our website [www.j-sainsbury.co.uk/investor-centre](http://www.j-sainsbury.co.uk/investor-centre).

## Key contacts and advisers

### General contact details

For general enquiries about Sainsbury's Bank call: 0808 540 5060

For any customer enquiries please contact, for Sainsbury's, our Sainsbury's Customer Careline by calling: 0800 636 262 and for Sainsbury's Argos, the Argos helpline by calling: 0345 640 2020

### Registered office

J Sainsbury plc  
33 Holborn  
London EC1N 2HT  
Registered number 185647

### Investor relations

James Collins  
Head of Investor Relations  
J Sainsbury plc  
Store Support Centre  
33 Holborn  
London EC1N 2HT  
investorrelations2@sainsburys.co.uk

### Registrar

Computershare Investor Services PLC  
The Pavilions  
Bridgwater Road  
Bristol BS99 6ZZ  
Telephone: 0370 702 0106

[www.investorcentre.co.uk](http://www.investorcentre.co.uk)

### Auditors

Ernst & Young LLP  
1 More London Place  
London SE1 2AF

### Solicitors

Linklaters LLP  
One Silk Street  
London EC2Y 8HQ

### Stockbrokers

UBS  
5 Broadgate  
London  
EC2M 2QS

Morgan Stanley  
25 Cabot Square  
Canary Wharf  
London E14 4QA

### Cautionary statement

Certain statements included in this Annual Report are forward looking and are therefore subject to risks, assumptions and uncertainties that could cause actual results to differ materially from those expressed or implied because they relate to future events. These forward-looking statements include, but are not limited to, statements relating to the Company's expectations. Forward-looking statements can be identified by the use of relevant terminology including the words: 'believes', 'estimates', 'anticipates', 'expects', 'intends', 'plans', 'goal', 'target', 'aim', 'may', 'will', 'would', 'could' or 'should' or, in each case, their negative or other variations or comparable terminology and include all matters that are not historical facts. They appear in a number of places throughout this Annual Report and include statements regarding our intentions, beliefs or current expectations and those of our officers, Directors and employees concerning, amongst other things, our results of operations, financial condition, liquidity, prospects, growth, strategies and the businesses we operate. Consequently, our actual future financial condition, performance and results could differ materially from the plans, goals and expectations set out in our forward-looking statements. The Company undertakes no obligation to publicly update any forward-looking statement, whether as a result of new information, future events or otherwise.

## Alternative performance measures

In response to the Guidelines on Alternative Performance Measures (APMs) issued by the European Securities and Markets Authority (ESMA), we have provided additional information on the APMs used by the Group. The Directors use the below APMs as they are critical to understanding the financial performance and financial health of the Group. As they are not defined by International Financial Reporting Standards they may not be directly comparable with other companies who use similar measures. All APMs relate the current period's results and comparative periods where provided.

| APM  | Definition   | Reconciliation  |     |              |            |            |
|--|--|---|-----|--------------|------------|------------|
| <b>Cash flows and net debt</b>             |  |   |     |              |            |            |
| <b>Cash flow items in Financial Review</b> | To help the reader understand cash flows of the business a summarised cash flow statement is included within the financial review. As part of this a number of line items have been combined. The cash flow in note 4 of the accounts includes a reference to show what has been combined in these line items. |   | Ref | 2017<br>£m   | 2016<br>£m |            |
|  |  | Net interest  | A   | <b>(108)</b> | (102)      |            |
|  |  | Property related including strategic capital expenditure                              | B   | <b>28</b>    | 155        |            |
|  |  | HRG acquisition and AFS loan book refinancing   | C   | <b>457</b>   | –          |            |
|  |  | Repayment of borrowings   | D   | <b>(211)</b> | (363)      |            |
|  |  | Other   | E   | <b>(10)</b>  | (31)       |            |
| <b>Free cash flow</b>                      | Net cash generated from retail operations, adjusted for exceptional pension contributions, after cash capital expenditure but before strategic capital expenditure.  | <b>Reconciliation of free cash flow</b>   |     |              | 2017<br>£m | 2016<br>£m |
|  |  | Cash generated from retail operations   |     | <b>929</b>   | 1,024      |            |
|  |  | Add back: exceptional pension contribution  |     | <b>199</b>   | 125        |            |
|  |  | Net interest paid   |     | <b>(108)</b> | (102)      |            |
|  |  | Corporation tax   |     | <b>(87)</b>  | (124)      |            |
|  |  | Retail purchase of property, plant and equipment and intangibles                      |     | <b>(622)</b> | (593)      |            |
|  |  | Retail purchase of intangible assets  |     | <b>(58)</b>  | (34)       |            |
|  |  | Add back: Strategic capital expenditure   |     | <b>92</b>    | –          |            |
|  |  | Free cash flow  |     | <b>345</b>   | 296        |            |
| <b>Operating cash flow</b>                 | Cash generated from operations after changes in working capital.   | A reconciliation is provided in notes 4 and 25 to the accounts.                       |     |              |            |            |
| <b>Retail operating cash flow</b>          | Retail cash generated from operations after changes in working capital   | A reconciliation of retail operating cash flow is provided in note 4 of the accounts. |     |              |            |            |
| <b>Core retail capital expenditure</b>     | Capital expenditure excludes Sainsbury's Bank, Argos exceptional capital expenditure, proceeds from sale and leasebacks and strategic capital expenditure  | A calculation of this is provided in the financial review on page 52.                 |     |              |            |            |
| <b>Net debt</b>                            | Net debt excludes the net debt of Financial Services and is calculated as: current available for sale assets + current net derivatives + net cash and cash equivalents + loans + non-current finance lease obligations + non-current net derivatives.  | A reconciliation of net debt is provided in note 26 of the accounts.                  |     |              |            |            |
| <b>Gearing</b>                             | Net debt divided by net assets.  | Net assets as per the Group balance sheet.  |     |              |            |            |

| APM  | Definition   | Reconciliation   |
|--|--|--|
| <b>Income statement</b>                            |  |  |
| <b>Like-for-like sales</b>                         | Year-on-year growth in sales including VAT, excluding fuel, excluding Financial Services, for stores that have been open for more than one year.   | A reconciliation of like-for-like sales is provided on page 47 of the Financial Review   |
| <b>Underlying profit before tax</b>                | Profit or loss before tax before any items recognised which, by virtue of their size and or nature, do not reflect the Group's underlying performance.   | A reconciliation of underlying profit before tax is provided in note 3 to the accounts.  |
| <b>Retail underlying operating profit</b>          | Underlying earnings before interest, tax, Financial Services operating profit and Sainsbury's underlying share of post-tax profit from JVs.  | A reconciliation of these measures can be found in note 4 of the accounts.               |
| <b>Underlying basic earnings per share</b>         | Earnings per share using underlying profit as described above.   | A reconciliation of underlying earnings per share is included in note 8 to the accounts. |
| <b>EBITDAR and underlying EBITDAR</b>              | Earnings before interest, tax, depreciation, amortisation and rent. Underlying EBITDAR uses underlying earnings.   | A reconciliation is provided on page 48 of the Financial Review.                         |
| <b>Other</b>                                       |  |  |
| <b>Lease adjusted net debt/ underlying EBITDAR</b> | Net debt plus capitalised lease obligations (5.5% discount rate) divided by Group underlying EBITDAR   | A reconciliation of this is provided in the financial review on page 53.                 |
| <b>Return on capital employed</b>                  | Return on Capital Employed is calculated as Return divided by average Capital Employed. Return is defined as Underlying Profit before interest and tax. Capital Employed is defined as Net assets excluding Net debt. The average is calculated on a 14 point basis. | A calculation of this is provided on page 53 of the Financial Review.                    |

# Glossary

**Active Kids** – Our nationwide scheme to help inspire school children to take more exercise and to eat more healthily. Launched in 2005, Active Kids is open to all nursery, primary and secondary schools as well as Scouts and Girl Guides in the UK. [www.sainsburys.co.uk/activekids](http://www.sainsburys.co.uk/activekids)

**Annual General Meeting (AGM)** – This year the AGM will be held on Wednesday 5 July 2017 at The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE at 11.00am.

**Argos Financial Services** – ARG Personal Loans Limited; Home Retail Group Card Services Limited; and Home Retail Group Insurance Services Limited.

**basics** – Sainsbury's entry level own-brand range of products.

**bps** – Basis points.

**by Sainsbury's** – Core own label brand.

**Click & Collect** – Service which allows customers to place general merchandise and grocery orders online for collection in-store.

**CMBS** – Commercial Mortgage Backed Securities.

**Corporate Responsibility and Sustainability (CR&S)** – The need to act responsibly in managing our impact on a range of stakeholders: customers, colleagues, investors, suppliers, the community and the environment.

**CPI** – Consumer Price Index.

**Dividend cover** – Underlying profit after tax from continuing operations attributable to ordinary shareholders divided by total value of dividends declared during the year.

**Earnings Per Share (EPS)** – Earnings attributable to ordinary shareholders of the parent divided by the weighted average number of ordinary shares in issue during the year, excluding those held by ESOP Trusts, which are treated as cancelled.

**Fairtrade** – The Fairtrade label is an independent consumer label that guarantees a fair deal for marginalised workers and small scale farmers in developing countries. Producers receive a minimum price that covers the cost of production and an extra premium that is invested in the local community. [www.fairtrade.org.uk](http://www.fairtrade.org.uk)

**Fair value** – The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

**FTSE4Good** – The FTSE Group, an indexing company, runs the FTSE4Good index series to measure the performance of companies that meet corporate responsibility standards, and to facilitate investment in those companies. [www.ftse.com/products/indices/FTSE4Good](http://www.ftse.com/products/indices/FTSE4Good)

**FVTPL** – Fair value through profit or loss. Method of valuing a financial instrument where changes in fair value are recognised directly in the income statement.

**Group** – The Company and its subsidiaries.

**IFRIC** – International Financial Reporting Interpretations Committee.

**IFRSs** – International Financial Reporting Standard(s).

**Joint venture (JV)** – A business jointly owned by two or more parties.

**Kantar Worldpanel (Kantar)** – An independent third party providing data on the UK Grocery Market.

**Live Well for Less** – Sainsbury's customer commitment to continue to help people live the life they want to live, with quality products at fair prices.

**LTIP** – Long-Term Incentive Plan.

**MSC** – Marine Stewardship Council.

**Nectar** – One of the most popular loyalty schemes in the UK, of which Sainsbury's is a partner.

**Non-controlling interest** – The equity in a subsidiary not attributable, directly or indirectly, to the Company.

**OFT** – Office of Fair Trading.

**PRA** – Prudential Regulation Authority.

**Real discount rate** – Discount rate less inflation rate.

**RPI** – Retail Price Index.

**Taste the Difference** – Sainsbury's premium own-brand range of products.

**Total Shareholder Return (TSR)** – The growth in value of a shareholding over a specified period, assuming that dividends are reinvested to purchase additional units of the stock.

**Tu** – Sainsbury's own label clothing range.



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