9 November 2016

J Sainsbury plc

Interim Results for the 28 weeks to 24 September 2016

Delivering against strategy, with a strong platform for growth

- Like-for-like transaction growth across all channels and total volume growth
- Differentiated food proposition offering customers market-leading choice, quality and value
- General Merchandise sales growth of nearly five per cent
- Clothing sales growth of nearly one per cent in a challenging market
- Acquisition of Home Retail Group plc ('HRG') accelerates our strategy:
    - c.250 Argos digital stores in supermarkets over the next three years
    - 30 Argos digital stores and 200 digital collection points in supermarkets by Christmas
    - Confident of delivering £160 million synergy target over three years
- On track to deliver £500m cost savings target by 2017/18
- New three-year £500m cost savings target from 2018/19
- Net debt reduced by £485 million from March 2016 to £1.3 billion[(1)]
- Interim dividend of 3.6 pence per share
- New Sainsbury's Group provides a strong platform for growth, with four key priorities:
    - Further enhance our differentiated food proposition
    - Grow Clothing and General Merchandise and deliver synergies by integrating Argos
    - Diversify and grow Sainsbury's Bank
    - Continue cost savings and maintain balance sheet strength

Commenting on the Interim Results 2016, Mike Coupe, Group Chief Executive of J Sainsbury plc, said: "Two years ago we set out our strategy to make our customers' lives easier, offering great quality and service at fair prices, serving our customers whenever and wherever they want. We have made good progress delivering this in challenging market conditions.

"We have invested in the quality of our products while reducing prices on everyday items, delivering volume growth and outperforming the market in customer service and availability. To meet growing demand for home delivery groceries in London, we opened a new online fulfilment centre. By Christmas we will open 30 Argos digital stores and create a further 30 Argos digital collection points in our supermarkets. These will form part of a rollout of 200 new digital collection points where customers can collect *Tu* clothing, eBay and DPD parcels.

"We achieved like-for-like transaction growth across all our channels and remain on track to deliver our three-year £500 million cost saving programme by the end of 2017/18. We will also deliver £500 million of cost savings over three years from 2018/19. We continue to benefit from a strong balance sheet, with net debt reduced by £485 million from March 2016 to £1.3 billion and we are committed to paying an affordable dividend, fixed at 2.0 times cover for the full year. Consistent with our policy to pay an interim dividend of 30 per cent of the previous full year dividend, our interim dividend will be 3.6 pence per share."

Mike Coupe added: "The acquisition of HRG accelerates our strategy to give customers choice, convenience, speed and flexibility in when, where and how they shop. Food will always be at our heart and we are strengthening our Clothing, General Merchandise and Financial Services offers to realise the potential of the Group. The combination of our products, services, customer data and fast delivery networks gives us a strong platform for growth and enables us to deliver clear synergies."

Outlook

The market remains competitive and pricing pressures continue to impact margins. The full impact of the devaluation of sterling on retail prices is as yet uncertain. However, we are well placed to navigate the external environment and remain focussed on delivering our strategy.

Financial highlights

	28 weeks to 24 September 2016	28 weeks to 26 September 2015	% Total Change
Business Performance			
Underlying Group sales (inc VAT)	£13,923m	£13,641m	2.1%
Like-for-Like sales (inc VAT, ex fuel) (Sainsbury's only)			(1.0)%
Underlying profit before tax[(2)]	£277m	£308m	(10.1)%
Underlying basic earnings per share[(3)]	11.2p	12.0p	(6.7)%
Return on capital employed (excluding pension fund deficit)[(4)]	8.0%	8.5%	(57)bps
Statutory Reporting*			
Group sales (ex VAT, inc fuel)	£12,642m	£12,419m	1.8%
Items excluded from underlying results	£95m	£31m	
Profit before tax	£372m	£339m	9.7%
Basic earnings per share	14.8p	13.6p	8.8%
Interim dividend	3.6p	4.0p	(10.0)%

**Variation between Business Performance and Statutory Reporting is due to items excluded from underlying results*

- Our full year underlying profit expectation for the combined group remains in line with current market consensus (which includes Argos)[1]
- We expect Sainsbury's second half underlying profit (excluding the impact of Argos) to be lower than that achieved in the first half, as a result of continued price investment and a step up in cost inflation in the second half
- Argos is expected to deliver an underlying profit contribution to the Group of £55m-£75m[2] in the second half
- We expect full year 2016/17 net debt to be around £1.5bn, mainly as a result of the HRG acquisition

Strategic and operational highlights

We know our customers better than anyone else

- Recognising that our customers want a clearer and simpler shopping experience, we have removed multi-buys and our Brand Match scheme and we are investing in lower regular prices. Promotional participation is down from 37 per cent two years ago to 24 per cent[3]. Customer satisfaction scores continue to improve[4]

Great products and services at fair prices

- Our programme to invest in the quality of 3,000 Sainsbury's branded food products is on track, including launching a new *On the Go* range of sandwiches, sushi and salads and a leading *Deliciously FreeFrom* range which is a newly expanded range of allergen-free fresh, frozen and ambient lines such as lasagne, pizzas and dairy-free alternatives to cheese
- General Merchandise sales growth of nearly five per cent driven by seasonal items and popular ranges such as our design-led bedding and homeware
- Our Clothing business grew by nearly one per cent in a challenging market and continues to gain market share; we are the UK's sixth largest clothing retailer by volume[5]
- With the acquisition of Argos, we are now a market leader in toys, small domestic appliances, electricals and homeware
- We have successfully built and deployed Sainsbury's Bank's new banking platforms and transferred all savings customers and ATMs

1 2016/17 UPBT consensus estimate (including Argos) of £573m, as published on 1 November 2016 on www.j-sainsbury.co.uk/investor-centre/analyst-consensus
2 Before synergies and Homebase disposal impacts
3 Nielsen Homescan, % Spend on deal (Total Business, four week data up to 24 September 2016)
4 CSI Data – Customer Satisfaction Tracking Q1 and Q2 2016/17
5 Kantar Worldpanel for the 52 weeks to 28 February 2016

There for our customers

- There are now 22 Argos digital stores in our supermarkets and we will have 30 by Christmas
- By the end of November there will be 30 Argos digital collection points. These will form part of the rollout of 200 new digital collection points where customers can collect *Tu* clothing, eBay and DPD parcels
- Convenience sales growth of over six per cent; this business contributes around £2.4 billion of annualised sales
- We opened 16 new convenience stores and are trialling six Sainsbury's Locals in a franchise partnership with Euro Garages in service stations
- Groceries Online grew eight per cent and contributes around £1.3 billion of annualised sales. We opened an online fulfilment centre in East London to meet increasing demand in London
- A same-day groceries online delivery offer will be available from 30 stores across the country by Christmas and we are trialling one-hour deliveries
- Our new Nine Elms flagship store in London highlights the benefits to our customers of the HRG acquisition. Nine Elms hosts an Argos digital store, a Habitat, Sushi Gourmet, Lloyds Pharmacy, Explore Learning and Starbucks

Colleagues make the difference

- We increased the standard rate of pay of Sainsbury's store colleagues by four per cent this year, the same rate as last year and we continue to pay well above the National Living Wage
- We continue to win awards for high levels of customer service, including the industry-leading Grocer Gold Customer Service and Availability Awards for the past four years
- Including Argos, nearly 195,000 colleagues now work across the Group and we will create approximately 1,000 net retail roles within Argos stores over the next three years

Our values make us different

- In September we were awarded a Gold accreditation by Investors In People for the third time, making us the largest employer to have reached the Gold standard and the only retailer to achieve three Gold awards
- As part of our £10 million investment over five years in our *Waste less, Save more* campaign we have launched 16 trials to help families reduce food waste in Swadlincote, our test-bed town
- We published our corporate food waste figures within our operations, reporting an overall reduction of 9.4 per cent year-on-year
- We have increased our food donation partnerships by 300 per cent year-on-year and now have more than 1,100 charity food donation partners
- Over 8,000 schools took part in our Active Kids Paralympic Challenge, giving more than 2.5 million children the opportunity to engage in Paralympic sports such as sitting volleyball
- We received the highest possible score from the World Wildlife Fund's Palm Oil Buyers' Scorecard, reflecting our ongoing commitment to sourcing palm oil sustainably

Notes:

1. Net debt excludes the net debt of Financial Services and is calculated as the sum of current available for sale assets, current net derivatives, net cash and cash equivalents, loans, non-current finance lease obligations and non-current net derivatives. Refer to Alternative Performance Measures disclosure on page 57
2. Underlying profit before tax: Profit before tax before any profit or loss on the disposal of properties, investment property fair value movements, non-underlying finance movements, IAS 19 pension financing element and defined benefit pension scheme expenses, acquisition adjustments and one-off items that are material and infrequent in nature, but after the coupons on the perpetual subordinated capital securities and perpetual subordinated convertible bonds. Refer to Alternative Performance Measures disclosure on page 57
3. Underlying basic earnings per share: Underlying profit attributable to ordinary shareholders, net of attributable taxation, divided by the weighted average number of ordinary shares in issue during the year, excluding those held by the Employee Share Ownership Plan ESOP trusts, which are treated as cancelled. Refer to Alternative Performance Measures disclosure on page 57
4. Return on capital employed: Underlying profit before interest and tax, divided by the average of opening and closing capital employed (net assets before net debt). In light of the acquisition of HRG on 2 September 2016 and the disproportionate impact this has on the ROCE calculation (using a two point average for Capital Employed and the inclusion of only three weeks of 'return') a calculation based on a 14 point average has been used. Refer to Alternative Performance Measures disclosure on page 57
5. Certain statements made in this announcement are forward-looking statements. Such statements are based on current expectations and are subject to a number of risks and uncertainties that could cause actual events or results to differ materially from any expected future events or results referred to in these forward-looking statements. They appear in a number of places throughout this announcement 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 business we operate. Unless otherwise required by applicable law, regulation or accounting standard, we do not undertake any obligation to update or revise any forward-looking statements, whether as a result of new information, future developments or otherwise
6. J Sainsbury plc will report its 2016/17 Third Quarter Trading Statement at 07:00 (GMT) on 11 January 2017.

A results presentation for analysts and investors will be held at 09:30 on 9 November 2016.

To view the slides of the results presentation and the webcast: We recommend that you register for this event in advance. To do so, visit www.j-sainsbury.co.uk and follow the on-screen instructions. To participate in the live event, please go to the website from 09:00 on the day of the announcement, where there will be further instructions. An archive of the webcast will be available later in the day.

To listen to the results presentation: To listen to the live results presentation by telephone, please dial 0800 678 1161 (or +44 (0)1296 311 600 if you are unable to use the primary number). The pass code for the event is 597 417. A transcript of the presentation and an archive recording of this event will be available later in the day at www.j-sainsbury.co.uk

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Market context

The market

Conditions have remained positive for UK consumers in recent months, with wage growth higher than inflation. Consistent with most of the post-recession period of real wage growth and higher consumer confidence, spending has been strongest in higher ticket discretionary categories such as eating out, holidays and new car sales. Retail sales data suggest that money-saving behaviours adopted during the recession have remained, with consumers spending cautiously and waiting more often for sale periods to make purchases in general merchandise and clothing categories. Market growth in the grocery sector remains subdued, but slightly improved, with deflation easing modestly and some evidence of improved volumes.

Following the vote to leave the European Union, we may see changes in coming months to all aspects of this consumer backdrop, with wage growth already easing. The impact of the devaluation of sterling on retail prices is as yet uncertain. As ever, we will aim to remain competitive on price and our price position today, across food, clothing and general merchandise is as competitive as ever.

Shopping habits

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

Within the grocery sector, customers are continuing to shop more frequently and more widely across different channels and store formats. Convenience stores and online retail continue to show strong growth. Discount retailers continue to open significant numbers of new stores and gain market share, but at reduced rates. In line with our expectations, this further reduces volumes through the supermarket format. However, we continue to expect supermarkets to remain the key channel for groceries and we are adapting our supermarket stores to reflect changing customer needs and better serve a wider variety of shopping purposes.

Within general merchandise and clothing, traditional store formats, particularly on the high street, continue to see footfall and sales declines as online participation grows. However, the combination of a strong online proposition and a wide choice of delivery and pick-up options is proving to be popular with consumers, with click and collect accounting for a significant proportion of UK online clothing and general merchandise sales.

Future retail trends

Across all retail categories, customers' expectations of retailers will continue to rise, in terms of how and when they are able to shop, how quickly retailers are able to fulfil their orders, and customers' ability to determine how they receive their goods. Technology raises customers' expectations, but should also help retailers to meet them efficiently. Price transparency, another product of technology, brings challenges to some retail models but, over time, is removing price as a point of differentiation in favour of quality and service. Retailers will succeed through efficiently offering competitive prices, differentiated, high quality product ranges and services and a range of flexible and convenient delivery options.

We know our customers better than anyone else

To achieve our goal of being the most trusted retailer where people love to work and shop, it is vital that we understand what our customers want. To increase our knowledge in this key area, we have a data driven approach that gives us an enhanced, holistic understanding of our customers, enabling us to meet their needs more effectively. We have designed and delivered two key customer data systems that mean we can meet the individual needs of our customers, serve them better and run more efficient marketing campaigns.

Quality and competitive pricing remain key factors in customers' shopping decisions and we have never been more competitive on price. In February, we announced the removal of multi-buys on the majority of our food products, in favour of lower regular prices. This was completed on the vast majority of food products in June, two months ahead of schedule. Customers are now shopping more frequently and often buying fewer items. This, combined with growing awareness of the cost of food waste and careful management of household budgets, has led to a trend away from multiple product purchasing and customers have told us they prefer the increased choice, flexibility and simplicity we now offer. We continue to invest in lowering the price of everyday items. For example, we reduced 335g broccoli from 50 pence to 40 pence, 3 x large onions from £1.00 to 80 pence, 1.35kg whole chicken from £3.50 to £2.95 and 46 x Little Ones newborn nappies from £3.75 to £2.50. We also replaced Brand Match with lower regular prices after the vast majority of our customers said that price and flexibility was more important to them. Promotional participation is down from 37 per cent two years ago, to 24 per cent and customer price satisfaction scores continue to improve.

The Nectar scheme remains an important source of loyalty and customer insight, with nearly 14 million Nectar card holders shopping with us through all our channels. We aim to reward loyal customers with campaigns that save them money and offer them great rewards.

Great products and services at fair prices

Quality food

We continue to invest significantly in lowering the price of everyday items and are more competitive on price than we have ever been. Though like-for-like food sales declined in the half, we continued to grow volume and increase the number of customer transactions by offering customers a winning combination of quality, choice and fair prices. The quality of Sainsbury's branded food products is a key differentiator and we continue to invest in improving and expanding our food ranges. Our programme to improve 3,000 of the food lines that really matter to our customers will be complete by the end of the calendar year.

We invest strategically in food categories that are growing in popularity and gaining market share. For example, we launched our new *On the Go* range of breakfast, lunch and snacking lines in September. Customers are responding well to our new and improved ranges. The food to go market is worth around £16 billion and we have invested £8 million in improving the range, introducing new sandwich and bread lines, salads, sushi and breakfast options, as well as reviewing and improving the taste and freshness of our existing range. We also introduced new products to our *Deliciously Freefrom range,* which now incorporates fresh lasagne, frozen pizza and ambient lines such as new pasta ranges, offering customers more variety, improved products and market-leading allergen information on the packaging. The market for these products is growing. The innovative milk-free alternatives to cheese have also been well-received by vegans and customers looking for an alternative to dairy.

Growth opportunities in clothing and general merchandise

Sainsbury's general merchandise sales grew by nearly five per cent, driven by a particularly strong performance in seasonal events this summer and we also increased our market share. We have a clothing business of scale and sales grew by almost one per cent in a declining market this summer and we continue to increase our market share, retaining our position as the sixth largest clothing retailer in the UK by volume. We continue to invest in our clothing ranges, launching a new Admiral Performance range for men in August and Tu Premium for women in September.

We acquired HRG in September, making us one of the UK's largest food and non-food retailers, offering customers a choice of over 90,000 products across a diverse range of categories – food, clothing, general merchandise and financial services. We have now merged our clothing and general merchandise businesses with Argos and Habitat, creating a £6 billion turnover business that is a market leader in the key categories of toys and small domestic appliances and is second in the market for electricals and homeware.

Financial Services

Sainsbury's Bank became wholly owned by Sainsbury's in 2014 and at that time we set out on a transformation. Our goal was to build a new, more flexible banking platform, continue to deliver strong trading performance, grow customer numbers and offer Sainsbury's customers great financial products and services at fair prices. We are well on track with our plan and over the past two years we have grown customer numbers by 8 per cent to over 1.7 million.

We have successfully built and deployed a new banking platform, with savings customers the first to transition smoothly on to the new system in September. Savings customers are now enjoying enhanced features, and customer service has been brought in-house with the creation of the Bank's first dedicated contact centre. We have also migrated all ATMs, another important milestone in our transformation project. This added additional security features and revenue generating ATM advertising. In the half, we installed a further 30 ATMs, taking our total to nearly 1,700 as at the middle of October. We expect to introduce our new loans platform by the end of 2017. We are assessing our options for cards following the acquisition of HRG and the opportunity to create a common cards operating model.

Sainsbury's Bank continues to deliver a good trading performance. Credit Card sales have grown 13 per cent year-on-year, driven by best buy products in the Purchase and Balance Transfer markets. By focussing on providing market leading Personal Loans in an increasingly competitive market where rates are at historic lows, volumes increased by two per cent year-on-year. To enhance our offer to customers taking overseas trips, we linked Travel Money and Travel Insurance with a promotion which helped increase overall Travel Insurance sales by 23 per cent year-on-year. Our Travel Money sales grew by 33 per cent year-on-year. The Bank played a critical role in the recent acquisition of HRG, successfully obtaining full UK Regulatory permissions and expanding the Bank's savings portfolio which provided around £500 million of the transactional funding. Following the acquisition of HRG, Argos Financial Services is now integrated into Sainsbury's Bank.

We have made good progress with our Mortgage proposition development and remain on course to re-launch into the mortgage market during the first half of 2017. We also plan to launch new Home and Car Insurance options for our customers in 2017 with a panel of insurers. This will enable Sainsbury's Bank to offer good quality insurance products to a wider range of Sainsbury's customers at the most competitive prices for them.

There for our customers

The way people shop is changing – customers increasingly want choice, convenience, flexibility and fast delivery. Our acquisition of HRG will enable us to accelerate our strategy to be a multi-product, multi-channel retailer with fast delivery networks, able to serve our customers whenever and wherever they want to shop with us. Argos is a leading home delivery service in the UK, with a unique capability that enables us to offer four-hour delivery or convenient fast track collect in-store options on approximately 20,000 products to over 90 per cent of households. So, whether customers want to shop in a store or online, opt for home delivery or Click & Collect, we will make it fast, easy and convenient for them.

Supermarkets
Our customers do the majority of their shopping in our supermarkets, and will continue to do so for the foreseeable future. Two years ago we identified that, although we have a structurally advantaged portfolio, we would still have some under-utilised space in 25 per cent of our supermarkets over the next five years. We are making good progress on using this space to extend our clothing and general merchandise offer and to introduce Argos and other carefully selected concession partners, giving customers complementary products and services, as well as more choice and convenience. Over one third of the space in our flagship 'supermarket of the future' in Nine Elms, south-west London, is dedicated to clothing and general merchandise and offers customers a broad range of products and services including an Argos digital store, Habitat, Lloyds Pharmacy, Sushi Gourmet, Starbucks and an Explore Learning Centre. Customers can park easily and do their grocery shopping, choose a new outfit, buy an item for the home and enjoy a meal, all under one roof.

The estimated market value of properties, including our 50 per cent share of properties held within property joint ventures, is £10.3 billion. The £0.3 billion decrease during the year was due to a small decline in market rental values and a small yield shift. We are maximising the value of our property assets and working with joint venture partners to develop new residential and commercial opportunities while also adding trading space to our estate. Our £500 million development at Nine Elms launched in August 2016 with a new Sainsbury's supermarket, 645 apartments, shops and offices. We are also developing plans for replacement stores at Whitechapel and Ilford which will provide 1,242 homes and new jobs. Our replacement store proposal at Selly Oak will also include 418 student accommodation units. We are investing in the right infrastructure to support the growth of our business and to help us serve our customers better. We operate 24 distribution centres to service our supermarkets, convenience stores and online businesses.

Argos, Habitat and the potential of combined businesses
Argos is a digital retail leader and is the second most visited retail website in the UK, with nearly one billion website visits each year. 50 per cent of Argos sales originate online, with 75 per cent of orders fulfilled in-store. In October 2015, Argos introduced Fast Track, a market-leading nationwide proposition offering approximately 20,000 products for immediate store collection or same-day home delivery to approximately over 90 per cent of UK mainland households. In addition to this, Argos offers a leading express two-man home delivery service providing large item delivery across a broad range of products and contact centres to provide customers with personalised service. Argos's digital capabilities, market leading product offer and innovative delivery options will be of great benefit to Sainsbury's customers.

We aim to have an Argos presence in all our stores over the next few years. After a successful trial, we will have 30 Argos digital stores in our supermarkets in time for Christmas, giving customers the choice of making an instant purchase in-store via tablets, or to reserve online for easy same-day collection. The ten Argos digital stores that have been trading for over a year are delivering strong double-digit like-for-like sales as customer awareness increases. Around 60 per cent of Argos digital customers also shop in the main store, generating a halo effect on sales of between one to two per cent.

By the end of November there will be 30 Argos digital collection points. These will form part of the rollout of 200 new digital collection points where customers can collect Tu clothing, eBay and DPD parcels. Over the coming months, we will have seven Habitat stores, offering Habitat's well-designed, affordable products for the home.

Convenience
The trend for shopping locally and buying smaller quantities more frequently continues and convenience store sales grew over six per cent, generating annualised sales of approximately £2.4 billion. We have maintained our disciplined approach to new space, opening 16 new stores, which takes the number of convenience stores in our estate to 783. We opened the first of six trial franchise shops with Euro Garages which will see Sainsbury's Locals attached to their petrol filling stations. This will offer customers greater access to Sainsbury's products in new locations.

Groceries Online
Groceries Online now contributes approximately £1.3 billion in annualised sales. This half, sales grew eight per cent and the number of orders grew by over 12 per cent. Our grocery Click & Collect service, located in over 130 stores, has proved popular, attracting new customers and offering existing ones another quick and convenient way to shop.

We will continue to pick online grocery orders from our supermarkets across the UK and it makes good commercial, operational and logistical sense to do so. In addition, to address the growing demand for Groceries Online in the densely populated London area, we have opened a new, 185,000 square foot online fulfilment centre in Bromley-by-Bow, East London, which has recruited 500 people to date and is expected to recruit a further 430 colleagues by 2020. This will help us keep pace with demand and enable us to fulfil an additional 25,000 orders in London each week.

Delivery options
To meet customer demand for a fast and flexible offer, we successfully trialled a same-day online grocery service with home delivery or Click & Collect options, which we will extend to 30 stores by Christmas. In addition, our innovative one-hour delivery service enables customers in Pimlico and Wandsworth in London, to order up to 20 items via our newly-launched Groceries Online App and have them delivered by bicycle within one hour. We are the first UK supermarket to offer this type of service.

Netto
Following a comprehensive review of the business we, together with our partner Dansk Supermarked, decided to end our joint venture of Netto trial stores. We believe it makes better commercial sense for us to focus on delivering our strategy within our core business and to maximise the opportunities that arise from our acquisition of HRG.

Colleagues making the difference

Our colleagues provide customers with industry-leading service and aim to exceed customer expectations every day.

In recognition of the critical role they play, we increased 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. Following our acquisition of HRG, we welcomed colleagues from Argos and Habitat to our business and now employ nearly 195,000 colleagues, all focused on giving excellent service to our customers. We are extending colleague discount on Sainsbury's, Argos and Habitat products to all colleagues, reflecting the new make-up of the Sainsbury's Group.

We expect to create around 1,000 net additional Argos retail roles over the next three years as a result of the HRG acquisition and, to achieve our vision of making shopping easier for customers whenever and wherever they want to shop, we are creating 150 in-house digital and technology jobs in Manchester and we have recruited 10 software development apprentices for our London-based Digital Lab.

As a result of colleagues' hard work, we have won the Grocer Gold Awards for both Customer Service and Availability for the past four years.

Our values make us different

Our Sustainability Plan focuses on the issues that are most important to our customers, colleagues and stakeholders and where we can make a really positive impact. Our five values, outlined below, underpin our strategy, make good business sense and give us a competitive advantage.

Living healthier lives
As of today, over 8,000 schools have signed up to take part in the Active Kids Paralympic Challenge, a partnership between Sainsbury's, The Youth Sport Trust and Paralympic GB. This gives more than 2.5 million children the opportunity to take part in and increase their understanding of Paralympic sports.

Sourcing with integrity
We have received the highest possible score from the World Wildlife Fund's Palm Oil Buyers Scorecard, reflecting our ongoing commitment to sourcing palm oil sustainably and over 98 per cent of the palm oil used in our own-brand products is certified sustainable.

We are committed to sourcing our raw materials sustainably. This includes sourcing timber from credibly-certified forests or verified recycled sources. As members of WWF's Global Forest & Trade Network in the UK, we have also committed to transparent communication on how we procure our forest products and a significant 93 per cent of the wood used in our own-brand products is now from recycled or FSC or PEFC certified sources, with full chain of custody.

Respect for our environment
We now have 16 Waste less, Save more trials in Swadlincote, south Derbyshire, where we are working with the community to help households reduce food waste at home. We are testing a range of initiatives to establish the most effective ways to reduce household food waste, before sharing our learnings nationwide.

Our corporate food waste numbers for 2014/15 and 2015/16 show that we are making a positive impact, reducing food waste in our operations by 9.4 per cent year-on-year. We now have more than 1,100 Food Donation charity partnerships operating across 77 per cent of our stores, a significant increase over the last year, which means more food is getting to those who need it most. Though this is good progress, we recognise there is much more to do and we will continue to improve operational efficiency throughout our supply chain and build more Food Donation Partnerships across our stores.

Making a positive difference to our community
We saw a 442 per cent increase in customer engagement during our Local Charity campaign this year, due to initiatives such as the launch of a new website and new in-store voting mechanisms. More than 1.9 million people voted for the local charity of their choice this year, compared to 350,000 last year. Over 1,200 of our stores support a local charity.

We supported the Royal British Legion in the commemoration of the start of the Battle of the Somme. New products including commemorative Somme pin badges and Remembrance Rosebushes have raised more than £30,000 for RBL since July 2016.

A great place to work
In September, we were awarded Gold accreditation by Investors in People for the third time. 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 evaluated how we listen and act on colleague feedback, develop and support our colleagues to learn and how we spot talent.

In September, we welcomed ten apprentices onto the new Software Developer programme in our rapidly growing Digital and Technology team, three of whom are existing Sainsbury's colleagues. This includes three women, which is 20 per cent above the industry standard for women who started on IT apprenticeships in England last year.

Financial Review

The first half of 2016/17 has been a significant period in Sainsbury's history, which culminated in the acquisition of Home Retail Group plc ('HRG') on 2 September 2016, around three weeks before the end of the half. From an underlying trading perspective therefore, this has not had a significant impact on the financial results, with £235 million of Argos sales (excluding VAT, £281 million including VAT) and £1 million of underlying profit before tax consolidated into the Group Income Statement. The acquisition has, however, been fully consolidated within the Balance Sheet.

Sainsbury's continues to operate in a competitive trading environment with sustained food price deflation impacting margins. Over the first half, retail underlying EBITDAR margin declined nine basis points to 7.49 per cent and retail underlying operating margin declined 24 basis points to 2.47 per cent. On a 52-week rolling basis Sainsbury's market share (as measured by Kantar) declined only six basis points, despite continued price investment and the continuing pace of new store expansion from the discounters. However, there was like-for-like transaction number growth across all channels – supermarkets, convenience and groceries online – and total volume growth.

Sainsbury's underlying Group sales (including VAT) were up 2.1 per cent to £13,923 million and broadly flat when excluding the impact of HRG. Underlying profit before tax ('UPBT') declined by 10.1 per cent to £277 million (2015/16: £308 million), however profit before tax of £372 million (2015/16: £339 million) was up 9.7 per cent as a result of a £95 million profit recognised outside of underlying results – mainly due to property profits and the sale of the Pharmacy business to LloydsPharmacy.

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 now gives us the opportunity to launch into the mortgage market in 2017. Argos Financial Services ('AFS') also transferred to the Bank at the end of the first half, 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. This refinancing has enabled the Group to repay 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 synergies we are confident of achieving, 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 also just under £1.1 billion, resulting in goodwill of just £18 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 and high levels of liquidity. Net debt at £1.3 billion (£1.8 billion treating the perpetual securities as debt) has reduced £485 million since year-end, mainly as a result of the cash acquired from the HRG transaction and improved retail working capital. Although some of this will reverse before year-end, we still expect a significant reduction in year-end net debt to £1.5 billion (£2.0 billion treating the perpetual securities as debt). The Group has facilities of £4.0 billion with only £2.8 billion drawn at the end of the first half. We have concluded the Sainsbury's pension scheme triennial valuation and recovery payments will increase by £6 million to £84 million. 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 IAS19 accounting deficit (net of deferred tax) to just under £1.1 billion, and the acquired HRG pension scheme deficit (net of deferred tax) is £249 million as at 24 September 2016.

Underlying basic earnings per share decreased 6.7 per cent to 11.2 pence (2015/16: 12.0 pence), lower than the reduction in underlying profit before tax due to a favourable tax rate. Basic earnings per share increased 8.8 per cent to 14.8 pence (2015/16: 13.6 pence), higher than the underlying earnings per share due to the £95 million profit recognised outside of underlying results.

The Board has approved an interim dividend of 3.6 pence (2015/16: 4.0 pence) in line with our policy of paying 30 per cent of the prior year's full-year dividend as an interim dividend.

Summary income statement[1]

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	Change %	52 weeks to 12 March 2016 £m
Underlying Group sales (including VAT)	**13,923**	13,641	2.1	25,829
Retail sales (including VAT, including fuel)	**13,750**	13,475	2.0	25,502
Retail sales (including VAT, excluding fuel)			2.4	
Group sales (excluding VAT)	**12,642**	12,419	1.8	23,506
Retail sales (excluding VAT, including fuel)	**12,469**	12,248	1.8	23,168
Retail sales (excluding VAT, excluding fuel)			2.1	
Underlying operating profit				
Retailing	**308**	332	(7.2)	635
Financial services – Sainsbury's Bank	**29**	34	(14.7)	65
Total underlying operating profit	**337**	366	(7.9)	700
Underlying net finance costs[2]	**(65)**	(62)	(4.8)	(121)
Underlying share of post-tax profit from JVs[3]	**5**	4	25.0	8
Underlying profit before tax	**277**	308	(10.1)	587
Items excluded from underlying results	**95**	31	206.5	(39)
Profit before tax	**372**	339	9.7	548
Income tax expense	**(73)**	(75)	2.7	(77)
Profit for the financial period	**299**	264	13.3	471
Underlying basic earnings per share	**11.2p**	12.0p	(6.7)	24.2p
Basic earnings per share[4]	**14.8p**	13.6p	8.8	23.9p
Dividend per share	**3.6p**	4.0p	(10.0)	12.1p
Interim dividend (£m)	**78**	77	1.3	

1 Retail sales include Argos sales of £281 million including VAT and £235 million excluding VAT, and an underlying profit contribution of £1 million.
2 Net finance costs including perpetual securities coupons before non-underlying finance movements and the IAS 19 pension financing charge.
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.
4 Basic earnings per share is calculated based on profit attributable to ordinary shareholders using the weighted average shares in issue.

Retail sales

Retail sales (including VAT, excluding fuel) increased by 2.4 per cent, including a 0.9 per cent contribution from new Sainsbury's space (excluding extensions and replacements), a 2.5 per cent contribution from Argos and a Sainsbury's like-for-like ('LFL') sales decline of 1.0 per cent.

Retail sales growth (including VAT)

	28 weeks to 24 September 2016 %	28 weeks to 26 September 2015 %	52 weeks to 12 March 2016 %
Sainsbury's like-for-like sales	**(1.0)**	(1.6)	(0.9)
Sainsbury's net new space (excluding extensions and replacements)[1]	**0.9**	1.5	1.3
Contribution from Argos	**2.5**	-	-
Sales growth (excluding fuel)	**2.4**	(0.1)	0.4
Impact of fuel	**(0.4)**	(1.9)	(1.6)
Sales growth (including fuel)	**2.0**	(2.0)	(1.2)

1 Includes the impact of the disposal of the Pharmacy business.

LFL sales, excluding fuel, declined by 0.8 per cent in the first quarter, and by 1.1 per cent in the second quarter, driven by continued food price deflation. On a 52-week rolling basis, our market share (as measured by Kantar) declined marginally, by six basis points, to 16.4 per cent, despite total volume and transaction growth.

Including the impact of fuel sales, retail sales including VAT reduces by 0.4 per cent to 2.0 per cent. The dilutive effect of Argos sales resulted in a negative contribution from fuel in the half despite fuel sales growth of 0.3 per cent (driven by volume growth of 6.1 per cent partly offset by retail price deflation).

Our multi-channel strategy enables customers to shop whenever, wherever and however they want. The convenience business grew sales by over six per cent, ahead of the market. Groceries online grew by eight per cent year-on-year, with order growth of 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.

Space

The contribution from Sainsbury's net new space of 0.9 per cent (excluding extensions and replacements, and the impact of Argos) was in line with Sainsbury's expectations. In the first half of 2016/17, Sainsbury's opened two new supermarkets, of which one was a replacement store (2015/16: four new supermarkets, of which two were replacements) and completed four supermarket refurbishments (2015/16: four supermarket refurbishments). Convenience continues to grow, with 16 new stores opened during the half (2015/16: 37 stores). Six convenience stores were closed (2015/16: three stores) and one was refurbished (2015/16: four stores).

Net of replacements, closures and disposals, closing Sainsbury's space of 23,291,000 sq ft was 1.0 per cent higher than last year (26 September 2015: 23,049,000 sq ft).

The contribution from net new space (excluding extensions, replacements and the disposal of the Pharmacy business) is expected to be around 0.8 per cent in 2016/17 with a first half contribution of 1.0 per cent and a second half contribution of 0.7 per cent. The impact of the disposal of the Pharmacy business reduces this to 0.3 per cent in 2016/17, with a first half contribution of 0.9 per cent and a negative second half contribution of 0.3 per cent.

In 2016/17, Sainsbury's expects to deliver five new supermarkets and around 40 new convenience stores.

Sainsbury's Store numbers and retailing space

28 weeks to 24 September 2016	**Supermarkets**		**Convenience**		**Total**	
	Number	Area 000 sq ft	Number	Area 000 sq ft	**Number**	**Area 000 sq ft**
At 12 March 2016	601	21,402	773	1,800	**1,374**	**23,202**
New stores	2	84	16	38	**18**	**122**
Disposals/closures	(1)	(25)	(6)	(11)	**(7)**	**(36)**
Extensions/refurbishments/downsizes	-	4	-	(1)	**-**	**3**
At 24 September 2016	**602**	**21,465**	**783**	**1,826**	**1,385**	**23,291**
Memorandum:						
Refurbishments/downsizes	4	4	1	(1)	**5**	**3**

In addition, as at 24 September 2016, Argos had 843 stores (including Habitat), of which 177 were digital stores. This includes 95 concessions within Homebase, which are expected to close in the next 12 months following the disposal of Homebase in February 2016.

Argos and Habitat Store numbers

	Argos stores	Argos in Sainsbury's	Argos in Homebase	Habitat[1]	Other[2]	**Total**
At 24 September 2016	725	15	95	4	4	**843**

1 Three Habitat stores and one Habitat store in Argos.
2 Three collection points and one convenience store.

In 2016/17 Sainsbury's expects to open around 35 Argos digital stores in supermarkets, resulting in around 45 Argos digital stores in supermarkets by the end of the year. In addition, we expect to open four Argos pop-up stores in the second half of 2016/17 and seven Habitat stores within supermarkets in 2016/17.

Around 35 Argos stores located in Homebase stores will close in the second half, with the remaining stores closing in the first half of 2017/18.

Retail underlying operating profit
Retail underlying operating profit decreased by 7.2 per cent to £308 million (2015/16: £332 million), reflecting lower LFL sales, investment in the customer offer and cost inflation. This was partly offset by cost savings of £65 million.

Retail underlying operating margin declined by 24 basis points year-on-year to 2.47 per cent (2015/16: 2.71 per cent), equivalent to a 26 basis points decline at constant fuel prices. Retail underlying EBITDAR margin decreased by nine basis points to 7.49 per cent, or a 15 basis points decline to 7.43 per cent at constant fuel prices.

Retail underlying operating profit

	28 weeks to 24 September 2016	28 weeks to 26 September 2015	Change	Change at constant fuel prices	52 weeks to 12 March 2016
Retail underlying operating profit (£m)[1]	**308**	332	(7.2)%		635
Retail underlying operating margin (%)[2]	**2.47**	2.71	(24)bps	(26)bps	2.74
Retail underlying EBITDAR (£m)[3]	**934**	928	0.6%		1,755
Retail underlying EBITDAR margin (%)[4]	**7.49**	7.58	(9)bps	(15)bps	7.58

1 Underlying earnings before interest, tax, Sainsbury's Bank underlying operating profit and Sainsbury's underlying share of post-tax profit from JVs.
2 Retail underlying operating profit divided by retail sales excluding VAT.
3 Retail underlying operating profit before rent, depreciation and amortisation.
4 Retail underlying EBITDAR divided by retail sales excluding VAT.

In 2016/17, Sainsbury's expects cost inflation at the lower end of the two to three per cent range, with a step up in the second half as a result of the four per cent wage increase for store colleagues effective from 28 August 2016. We expect efficiency savings of around £120 million in 2016/17. 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 introducing a further three year £500 million cost saving target from 2018/19 onwards.

We will remain competitive on price in the market. Our full year underlying profit expectation for the combined group remains in line with current market consensus, which includes Argos[1]. We expect Sainsbury's second half underlying profit (excluding the impact of Argos) to be lower than that achieved in the first half, as a result of continued price investment and a step up in cost inflation in the second half.

1 2016/17 UPBT consensus estimate (including Argos) of £573m, as published on 1 November 2016 on www.j-sainsbury.co.uk/investor-centre/analyst-consensus.

Argos acquisition impact on retail underlying profit
On 2 September 2016, Sainsbury's completed the acquisition of HRG. Argos contributed £281 million of sales (including VAT) and £1 million of underlying profit before tax to retail performance since the point of acquisition.

Previously HRG analysed their business as Argos, Homebase, financial services, central activities and interest income. Homebase has now been sold. The financial services elements of HRG will now be included within the Group's financial services segment, and guidance on the effect of this will now be 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 and known as 'Argos'.

The consolidation of Argos is expected to add an underlying profit contribution in the second half of between £55 million and £75 million before synergies and Homebase Transitional Services Agreement impact. The full year Argos underlying profit contribution is expected to be between £30 million to £50 million before synergies and Homebase disposal costs, however the first half loss of £26 million is not consolidated.

As announced as part of the transaction to acquire HRG, the Group expect to achieve synergies of £160 million in the third full year post acquisition. The £160 million of synergies are derived from three areas:

Synergies from concessions - £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 over the same three year time period. 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 expected phasing of the synergies, exceptional costs and exceptional capital expenditure is shown below:

£m	H1 2016/17	H2 2016/17e	FY 2016/17e	FY 2017/18e	FY 2018/19e	H1 2019/20e	Total
Synergies (incremental year-on-year)	-	0-5	0-5	55-60	65	35	160
Exceptional costs	(6)	(9)	(15)	(60)	(40)	(15)	(130)
Exceptional capex	(5)	(15)	(20)	(55)	(45)	(20)	(140)

Synergies are expected to be up to £5 million in the second half of 2016/17.

Homebase Transitional Services Agreement ('TSA')

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 £2 million in the period to the 24 September 2016.

Further costs of £10 million in relation to this are anticipated in the second half.

To support the transition, a TSA was entered into on 17 January 2016 to govern the provision of the key transitional services to Wesfarmers Limited in advance of the completion of the sale of Homebase on 27 February 2016.

As previously reported by HRG, the business will continue to provide the transitional services for a period of time not likely to exceed 18 months from inception. The cost reduction programme to minimise the overhang of the transitional costs continues to perform well. Upon completion approximately £10 million of overhead costs from providing the services under the TSA will have to be absorbed by HRG. It is expected that this will impact from the second half of the 2017/18 financial year.

Of the original 18 services provided, HRG and Homebase have served notice on 14, nine of which have ceased to be provided. The remaining four services include information systems, contact centre, distribution and two-man home delivery.

In addition, over a period of approximately 18 months, all Argos stores within Homebase stores will be removed. As previously reported by HRG this is expected to result in a reduction in Argos' underlying profit of approximately £10 million. All Habitat stores within Homebase stores closed in advance of the Sainsbury's acquisition of HRG.

We expect the cumulative combined impact of the TSA and the closure of Argos stores within Homebase to be up to £5 million in 2016/17, £10 million in 2017/18 and £20 million from 2018/19 onward.

Supplier arrangements

The two types of supplier arrangements that involve a level of judgement or estimation are:

- Fixed amounts – these are agreed with suppliers primarily to support in-store activity including promotions, such as utilising specific space.

- Supplier rebates – these are typically agreed on an annual basis, aligned with the financial year, with the rebate amount linked to pre-agreed targets such as sales volumes.

Within the Group, supplier rebate amounts are offset against cost of sales with fixed amounts offset against either cost of sales or administrative expenses. Total supplier arrangements have reduced by £75 million to £102 million (2015/16: £177 million). The year-on-year reduction has been driven by the conscious decision to move away from supplier arrangements and towards a reduction in the base cost of goods. The analysis below includes the consolidation of HRG, where relevant.

Supplier arrangements[1]	**28 weeks to 24 September 2016 £m**	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Fixed amounts			
Cost of sales	**73**	109	302
Admin expenses	**2**	-	-
Total Fixed amounts	**75**	109	302
Supplier rebates	**27**	68	69
Total supplier arrangements	**102**	177	371

1 Supplier rebates do not include material estimation.

Of the above amounts, the following was outstanding and held on the balance sheet at 24 September 2016:

Supplier arrangements	**As at 24 September 2016 £m**	As at 26 September 2015 £m	As at 12 March 2016 £m
Within current trade receivables			
Supplier arrangements due	**34**	8	6
Within current trade payables			
Supplier arrangements due	**10**	16	39
Accrued supplier arrangements	**11**	16	25

£30 million of the increase in trade receivables supplier arrangements due is as a result of the HRG acquisition and subsequent consolidation of balances.

Financial services - Sainsbury's Bank

Sainsbury's Bank results[1]
6 months to 31 August

	2016	2015	Change %
Revenue (£m)	**173**	166	4.2
Interest payable (£m)	**(29)**	(27)	7.4
Total income (£m)	**144**	139	3.6
Underlying operating profit (£m)	**29**	34	(14.7)
Net interest margin (%)[2]	**3.8**	3.9	(10)bps
Bad debt as a percentage of lending (%)[3]	**0.5**	0.3	(23)bps
Tier one capital ratio (%)[4]	**14.4**	14.0	32bps

1 Results are excluding the impact of Argos Financial Services due to Sainsbury's Bank consolidation being six months to 31 August 2016.
2 Net interest receivable divided by average interest-bearing assets.
3 Bad debt expense divided by gross lending.
4 Tier 1 capital divided by risk-weighted assets.

Sainsbury's Bank delivered an underlying operating profit of £29 million, a 14.7 per cent decrease year-on-year. This decrease was mainly as a result of the investment required to enter the mortgage market and the impact of reduced interchange fees.

Net interest margin decreased by ten basis points year-on-year to 3.8 per cent (31 August 2015: 3.9 per cent) driven by the diversification of the Bank's funding sources to include a greater mix of longer-term wholesale funds. Bad debt levels as a percentage of lending increased to 0.5 per cent (31 August 2015: 0.3 per cent) reflecting growth in lending and higher loss rates on pre-prime loans. The Tier 1 capital ratio increased by 32 basis points year-on-year to 14.4 per cent (31 August 2015: 14.0 per cent), reflecting capital injections in support of the transfer of the Argos Financial Services ('AFS') business to Sainsbury's Bank.

Migration of our savings customers took place successfully in September 2016 and migration of ATMs was also completed. We now expect to introduce our new loans platform by the end of 2017, and are assessing our options for cards following the acquisition of HRG and the opportunity to create a common cards operating model. We are still planning to launch our new mortgage offer in the first half of 2017.

In the first half, customer deposits increased by 15.6 per cent reflecting the additional funding raised at 31 August 2016 in advance of acquiring AFS. 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 £681 million, offset by provision of £66 million resulting in a 9.7 per cent provision as a percentage of receivables.

In 2016/17 underlying operating profit is expected to be around ten per cent lower year-on-year due to investment required to enter the mortgage market and the impact of reduced interchange fees. A small second half contribution from AFS will be offset by the ongoing cost of increased customer deposits used to refinance the AFS loan book.

Capital injections to the Bank in the first half of 2016/17 were £100 million as a result of the transfer of AFS into the Bank. Capital injections are expected to be £20 million in the second half, taking full year capital injections to £120 million.

Property and other joint ventures ('JV')

Sainsbury's underlying share of post-tax profit from its JV with British Land was £7 million (2015/16: £8 million). Its underlying share of post-tax profit from the JV with Land Securities was £nil (2015/16: £1 million).

An investment property fair value decrease of £14 million was recognised within the share of post-tax profit from the JVs in the income statement (2015/16: £14 million decrease), mainly driven by average property yields of the JVs increasing to 5.3 per cent, or 14 basis points higher than the prior year (2015/16: 5.1 per cent).

Sainsbury's recognised a net £2 million share of loss (2015/16: net £5 million share of loss) from the other start-up JVs: I^2C and Netto (2015/16 includes Telecoms). On 2 July 2016 it was announced that the Netto JV would be closed and it ceased trading on 30 July 2016.

In 2016/17, Sainsbury's expects the share of profit from the property JVs to be slightly lower year-on-year. Sainsbury's share of loss from the continuing start-up JVs is expected to be slightly lower year-on-year following the decision to close Netto.

Underlying net finance costs

Underlying net finance costs increased by £3 million year-on-year to £65 million (2015/16: £62 million), as a result of the perpetual securities coupons, offset by lower interest costs as a result of lower net debt.

Underlying net finance costs[1]	**28 weeks to 24 September 2016 £m**	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Underlying finance income	**9**	9	19
Interest costs	**(65)**	(71)	(132)
Perpetual securities coupons	**(13)**	(4)	(15)
Capitalised interest	**4**	4	7
Underlying finance costs	**(74)**	(71)	(140)
Underlying net finance costs	**(65)**	(62)	(121)

1 Finance income/costs before financing fair value movements and the IAS 19 pension financing charge.

Sainsbury's expects underlying net finance costs in 2016/17 to be slightly lower year-on-year as a result of lower average net debt. Capitalised interest is expected to be similar year-on-year.

Items excluded from underlying results

Items excluded from underlying results totalled a profit of £95 million (2015/16: £31 million profit). Profit on disposal of properties of £113 million for the first half includes £111 million of profit on the completion of the Nine Elms store, which is a mixed-use development opened in August. Investment property fair value decreased by £14 million and the non-underlying finance movements of £12 million mainly relate to a gain recognised in fixed price power purchase agreements due to an increase in forecast forward energy prices. The increase in perpetual securities was due to the comparative not including an amount for the full prior period, as they were issued on 30 July 2015.

Items excluded from underlying results

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Profit on disposal of properties	**113**	94	101
Investment property fair value movements	**(14)**	(14)	(18)
Non-underlying finance movements	**12**	(4)	(22)
IAS 19 pension financing charge and scheme expenses	**(10)**	(15)	(28)
Perpetual securities coupons	**13**	4	15
Acquisition adjustments	**1**	1	3
One-off items	**(20)**	(35)	(90)
Total items excluded from underlying results	**95**	31	(39)

The loss in one-off items of £20 million (2015/16: £35 million loss) is mainly driven by:

- A £98 million profit recognised on disposal of the Pharmacy business to Celesio A.G, owners of LloydsPharmacy
- Costs of £16 million relating to Sainsbury's Bank's transition to a new, more flexible banking programme
- A £22 million charge relating to the one-off legal and advisory fees in relation to the acquisition of HRG
- £30 million of impairment charges and onerous contracts relating to lease exit and break costs and movements in the market value of land
- A £23 million charge related to the closure of Netto as a result of writing off Sainsbury's investment in the joint venture, other closure costs, increased lease exit and break costs
- A Homebase separation and restructuring charge of £2 million in the three week period of consolidating HRG, part of the previously announced £75 million on the sale of Homebase
- Argos integration costs of £6 million were incurred in the first half, part of the previously announced £130 million required over the three years in order to achieve the synergies of £160 million
- Internal restructuring costs of £19 million were incurred in the first half

One-off items

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Disposal of Pharmacy business	**98**	-	(3)
Sainsbury's Bank transition costs	**(16)**	(25)	(59)
HRG acquisition costs	**(22)**	-	(12)
Impairment and onerous contract charge	**(30)**	3	(1)
Netto closure	**(23)**	-	-
Homebase separation and restructuring costs	**(2)**	-	-
Argos integration costs	**(6)**	-	-
Internal restructuring	**(19)**	(13)	(15)
Total one-off items	**(20)**	(35)	(90)

In 2016/17, Sainsbury's Bank costs for transitioning to a new, more flexible banking platform are expected to be around £40 million (capital costs relating to the transition are expected to be around £40 million).

No further property profits are expected in the second half.

The sale of the Pharmacy business was completed on 1 September 2016, and no further profits are expected in the second half.

In 2016/17, Argos integration costs are expected to be around £15 million. In addition, Argos exceptional integration capital expenditure is expected to be around £20 million. Both part of the previously announced £130 million exceptional integration costs and £140 million exceptional capital expenditure required.

Taxation

The income tax charge was £73 million (2015/16: £75 million), with an underlying tax rate of 21.3 per cent (2015/16: 25.3 per cent) and an effective tax rate of 19.6 per cent (2015/16: 22.1 per cent). The underlying rate is lower than last year, mainly due to falls in the statutory corporate tax rate being applied to deferred tax balances in the current year but not in the prior year.

Underlying tax rate 28 weeks to 24 September 2016	**Profit £m**	**Tax £m**	**Rate %**
Underlying profit before tax, and tax thereon	277	(59)	21.3
Adjustments (and tax thereon) for:			
Items excluded from underlying results and revaluation of deferred tax balances	95	(14)	
Profit before tax, and tax thereon	**372**	**(73)**	**19.6**

In 2016/17, 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 6.7 per cent to 11.2 pence (2015/16: 12.0 pence) reflecting the fall in underlying profits and the effect of additional shares issued during the year, as a result of the HRG acquisition, partly offset by a lower underlying tax rate year-on-year.

The weighted average number of shares in issue was 1,953.4 million (2015/16: 1,920.0 million), an increase of 33.4 million shares or 1.7 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 weighted average number of shares in the first half by 32.2 million and will increase the full year weighted average number of shares by 130.3 million. In 2017/18, the full effect of the weighted average number of shares will be 261.1 million.

Basic earnings per share was 14.8 pence (2015/16: 13.6 pence). The basic earnings per share was higher than the underlying basic earnings per share due to the items excluded from underlying results.

Underlying earnings per share 28 weeks to 24 September 2016	**2016 pence per share**	2015 pence per share
Basic earnings per share attributable to ordinary shareholders	**14.8**	13.6
Adjustments (net of tax) for:		
Items excluded from underlying results and revaluation of deferred tax balances	**(3.6)**	(1.6)
Underlying basic earnings per share attributable to ordinary shareholders[1]	**11.2**	12.0

1 Underlying EPS calculation is based on underlying profit after tax attributable to ordinary shareholders. Therefore the coupons on the perpetual securities are not added back.

Dividends

The Board has approved an interim dividend of 3.6 pence per share (2015/16: 4.0 pence), equivalent to 30 per cent of the previous full year dividend. This will be paid on 4 January 2017 to shareholders on the Register of Members at the close of business on 18 November 2016.

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 through a cash and shares offer, comprising 55 pence per share and 0.321 shares in J Sainsbury plc for each share held of HRG. This resulted in total consideration of £1,093 million.

Consideration fair value at acquisition date	£m
Cash of £447 million (being £0.55 per existing share); based on HRG's share capital of 813,445,001 shares	**447**
£3 million in relation to the existing HRG share scheme awards and options	**3**
261 million new J Sainsbury plc shares at a share price of £2.461 (2 September 2016)	**643**
Total	**1,093**

The fair value of assets acquired at that date was £1,075 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 £138 million of other net assets. The fair value of assets acquired was less than the fair value of the consideration by £18 million, which has been treated as goodwill.

Fair value of net assets acquired At 2 September 2016 (provisional)	£m
Fixed assets	**274**
Intangible assets[1]	**326**
Inventories	**816**
Trade and other receivables	**141**
Deferred tax assets	**41**
Amounts due from financial services customers (loan book)	**615**
Other financial assets	**60**
Cash and cash equivalents[2]	**548**
Total assets acquired	**2,821**
Trade and other payables[2]	**(1,203)**
Provisions	**(89)**
Retirement benefit obligations	**(454)**
Total liabilities acquired	**(1,746)**
Net identifiable assets acquired at fair value	**1,075**
Goodwill arising on acquisition	**18**
Purchase consideration transferred	**1,093**

1 Intangible assets include a brand of £179 million relating to the Argos brand name, and reflect its fair value at the acquisition date. It is estimated to have a useful economic life of ten years.
2 Cash and cash equivalents and trade and other payables acquired are both presented gross of the capital return of £226 million.

Financing

The Group's key financing objectives are to diversify funding sources, to minimise refinancing risk and to maintain appropriate contingent liquidity. As at 24 September 2016, the Group had drawn debt facilities of £2.3 billion, undrawn but committed borrowing facilities of £1.15 billion at its disposal and £500 million of perpetual securities.

The principal elements of the Group's drawn debt facilities comprise two long-term loans of £718 million due 2018 and £761 million due 2031, both secured over property assets. In addition, the Group has further secured loans of £200 million due August 2019 and €50 million due 30 September 2016, a five year £450 million Convertible Bond due November 2019, £81 million of hire purchase facilities and £77 million of finance lease obligations.

On 18 March 2016, Sainsbury's entered into an amendment and restatement agreement in respect of the Revolving Credit Facility ('RCF') and on 16 May 2016, extended the final maturity date of the first tranche, Facility (A), of £500 million, from May 2018 to May 2019. The second tranche, £650 million Facility (B), matures in May 2020. The facility is secured against supermarket properties, and contains no financial covenants. As at 24 September 2016, £nil was drawn from either Facility.

Net debt and 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 24 September 2016, net debt was £1,341 million (12 March 2016: £1,826 million), a decrease of £485 million since year-end. This decrease was primarily driven by the acquired HRG cash balance, and a decrease in Retail working capital.

Net debt bridge	**£m**
12 March 2016 net debt	**(1,826)**
Retail operating cash flow before changes in working capital and exceptional pension contributions	553
Cash outflow on acquisition of HRG	(447)
Cash acquired on acquisition, net of capital return to HRG shareholders[1, 2]	322
Impact of Argos loan book transfer and refinancing	504
Retail working capital movements	239
Net cash used in other investing activities	(325)
Exceptional pension contributions (including HRG)	(199)
Dividends	(151)
Other items including interest and tax paid offset by FV and other cash movements	(11)
24 September 2016 net debt	**(1,341)**

1 This excludes £20 million of cash acquired that relates to AFS.
2 Capital return £226 million.

If the perpetual securities were treated as debt, net debt would increase from £1,341 million to £1,835 million (12 March 2016: £2,320 million).

Retail operating cash flows before changes in working capital and exceptional pension contributions decreased by 9.9 per cent to £553 million (2015/16: £614 million).

The total impact of the HRG transaction included £504 million net impact of the Argos loan book refinancing, £548 million of cash and cash equivalents acquired, partly offset by the £447 million cash consideration and the £226 million capital return to HRG shareholders.

The £239 million decrease in retail working capital from 12 March 2016 was mainly due to an increase in trade and other payables as a result of the timing of key payment runs at half year as compared to year-end.

Net cash used in other investing activities of £325 million included £307 million of expenditure on Property, Plant and Equipment, and £47 million on intangible assets, partly offset by £15m of disposal proceeds received and other cash movements of £14 million.

Exceptional pension contributions of £199 million include the planned £125 million cash payment made in August 2016 to the Sainsbury's defined benefit pension scheme and £74 million of payments made to the HRG pension scheme in September 2016.

Dividends of £151 million in relation to the final dividend of 8.1 pence per share for the 2015/16 year were paid in the period.

Included within other items were corporation and interest tax paid, dividends on perpetual securities, investments in JV's partly offset by consolidation of the HRG derivative, dividends received and fair value and other non-cash movements.

Summary cash flow statement

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Retail operating cash flow before changes in working capital (before exceptional pension contributions)	**553**	614	1,126
Decrease in retail working capital	**239**	191	23
Retail cash generated from operations	**792**	805	1,149
Bank operating cash flow before changes in working capital	**27**	18	29
Decrease/(increase) in Sainsbury's Bank working capital	**226**	(323)	(429)
Group cash generated from operations	**1,045**	500	749
Interest paid	**(49)**	(65)	(108)
Corporation tax paid	**(51)**	(63)	(124)
Net cash from operating activities	**945**	372	517
Proceeds from sale of Pharmacy business	**-**	-	125
Acquisition of subsidiaries, excluding cash acquired	**(447)**	-	-
Cash acquired from HRG transaction	**548**	-	-
Capital return to HRG shareholders	**(226)**	-	-
Sainsbury's Bank refinancing of Argos loan book	**(504)**	-	-
Retail refinancing of Argos loan book	**504**	-	-
Net cash used in other investing activities	**(325)**	(313)	(525)
Proceeds from issue of shares	**3**	7	8
Purchase of own shares	**-**	-	(20)
Proceeds from issue of perpetual securities	**-**	247	247
Proceeds from issue of convertible bonds	**-**	247	247
Repayment of borrowings	**(86)**	(293)	(372)
Exceptional pension contributions	**(199)**	(125)	(125)
Dividends paid	**(151)**	(157)	(234)
Dividends paid on perpetual securities	**(20)**	-	(4)
Increase/(decrease) in cash and cash equivalents	**42**	(15)	(136)
Elimination of net increase in Sainsbury's Bank cash and cash equivalents	**255**	238	316
Decrease in debt	**112**	280	353
Fair value and other non-cash movements	**76**	(17)	(16)
Movement in net debt	**485**	486	517

Group cash generated from operations increased by 109 per cent to £1,045 million (2015/16: £500 million), mainly due to a decrease in Group working capital of £465 million (2015/16: £132 million increase) driven by the movement in Sainsbury's Bank working capital.

The £226 million decrease in Sainsbury's Bank working capital was driven by additional customer deposits raised to fund the acquisition of AFS and the diversification of the Bank's holdings of liquid assets, partly offset by an increase in customer lending due to competitive propositions across personal loans and credit cards.

Borrowings of £86 million were repaid during the period in relation to Eddystone and Longstone debt and hire purchase finance lease repayments.

Sainsbury's expects 2016/17 year-end net debt to reduce to around £1.5 billion (£2.0 billion treating the perpetual securities as debt) mainly as a result of the HRG acquisition. Sainsbury's expects a small improvement in retail working capital. We expect net debt to reduce over the medium term.

Retail capital expenditure

Sainsbury's core retail capital expenditure decreased by £64 million year-on-year to £237 million (2015/16: £301 million). Core retail capital expenditure as a percentage of retail sales (including fuel, including VAT) was 1.7 per cent (2015/16: 2.2 per cent).

Sainsbury's opened two supermarkets (including one temporary replacement store at Redhill) during the first half (2015/16: four supermarkets) and 16 new convenience stores (2015/16: 37 convenience stores).

During the half, no extensions were completed (2015/16: no extensions), five refurbishments (2015/16: eight refurbishments) consisting of four supermarkets (2015/16: four supermarkets) and one convenience store (2015/16: 4 convenience stores).

Net retail capital expenditure was £315 million (2015/16: £298 million), mainly as a result of the purchase of a freehold at Chiswick, where there may be future potential for a mixed use development and £5 million Argos integration capital expenditure.

Retail capital expenditure	**28 weeks to 24 September 2016 £m**	28 weeks to 26 September 2015 £m[1]	52 weeks to 12 March 2016 £m
New store development	**39**	107	207
Extensions and refurbishments	**46**	98	183
Other – including supply chain and Digital & Technology	**152**	96	152
Core retail capital expenditure	**237**	301	542
Acquisition of freehold and trading properties[2]	**74**	1	-
Debtor/creditor movements	**(1)**	(4)	1
Argos integration capital expenditure	**5**	-	-
Net retail capital expenditure	**315**	298	543
Capex/sales ratio (%)[3]	**1.7**	2.2	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 2016/17, 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.

Sainsbury's depreciation in 2016/17 is expected to increase by around £20 million year-on-year primarily due to investment in Digital and Technology that is depreciated over a shorter lifetime.

Return on capital employed

In light of the acquisition of HRG on 2 September 2016 and the disproportionate impact this has on the ROCE calculation (using a two point average for Capital Employed and the inclusion of only three weeks of 'return') a calculation based on a 14 point average has been used with comparatives also restated.

The return on capital employed ('ROCE') on the 14 point average basis over the 52 weeks to 24 September 2016 was 8.4 per cent (2015/16: 9.2 per cent), a year-on-year decrease of 79 basis points. Excluding the retirement benefit obligation (net of deferred tax) from capital employed, ROCE over the 52 weeks to 24 September 2016 was 8.0 per cent (2015/16: 8.5 per cent), 57 basis points lower than for the 52 weeks to 26 September 2015. ROCE decline was mainly due to the fall in underlying operating profit.

Return on capital employed (14 point average)[1]	**52 weeks to 24 September 2016**	52 weeks to 26 September 2015
Total underlying operating profit (£m)	**671**	725
Underlying share of post-tax profit from JVs (£m)	**9**	4
Underlying profit before interest and tax (£m)	**680**	729
Average capital employed (£m)	**8,087**	7,921
Return on capital employed (%)	**8.4**	9.2
Return on capital employed (exc. pension fund deficit) (%)	**8.0**	8.5
52 week ROCE movement	**(79)bps**	
52 week ROCE movement (exc. pension fund deficit)	**(57)bps**	

1 The 14 point period average includes the opening capital employed as at 26 September 2015 and the closing capital employed for each of the 13 individual periods to 24 September 2016.

Summary balance sheet

Shareholders' funds as at 24 September 2016 were £6,494 million (12 March 2016: £6,365 million), an increase of £129 million, mainly attributable to the acquisition of HRG, partly offset by increases in trade and other payables and an increased retirement benefit obligation.

Net debt was £485 million lower than at 12 March 2016, driven by the acquisition of HRG, reduced capital expenditure and a decrease in retail working capital.

Sainsbury's Bank net assets at 31 August 2016 of £764 million (29 February 2016: £650 million) have been consolidated and separately identified.

Accounting for the perpetual securities as equity, adjusted net debt to EBITDAR was 4.0 times (2015/16: 4.0 times). Adjusted net debt to EBITDAR is expected to reduce by year-end as additional Argos EBITDAR is included in the calculation (first half 2016/17 calculation currently includes the full impact of capitalised leases with almost no EBITDAR contribution due to only three weeks of performance consolidated). Interest cover reduced to 5.3 times (2015/16: 6.0 times) due to lower underlying profit before tax. Fixed charge cover reduced to 2.6 times (2015/16: 2.7 times). Gearing decreased during the half to 20.6 per cent (12 March 2016: 28.7 per cent) as a result of the reduction in net debt following the HRG acquisition. Excluding the pension deficit, gearing decreased to 17.2 per cent (12 March 2016: 27.0 per cent).

Treating the perpetual securities as debt, adjusted net debt to EBITDAR increases to 4.3 times. Gearing increases to 30.6 per cent and gearing excluding the pension deficit increases to 25.1 per cent. Excluding the coupons from underlying net finance costs, interest cover increases to 6.6 times and fixed charge cover increases to 2.7 times.

Summary balance sheet (Sainsbury's Bank separated)	**Group**	Group	Group	Group
	As at 24 September 2016 £m	Movement since 12 March 2016 £m	As at 26 September 2015 £m	As at 12 March 2016 £m
Land and buildings (freehold & long leasehold)	**7,155**	177	7,015	6,978
Land and buildings (short leasehold)	**859**	39	799	820
Fixtures and fittings	**1,993**	67	1,910	1,926
Property, plant and equipment	**10,007**	283	9,724	9,724
Other non-current assets	**1,014**	278	772	736
Inventories	**1,909**	941	1,013	968
Trade and other receivables	**507**	169	373	338
Sainsbury's Bank assets[1]	**5,359**	828	4,368	4,531
Cash and cash equivalents	**874**	297	622	577
Debt	**(2,215)**	188	(2,479)	(2,403)
Net debt	**(1,341)**	485	(1,857)	(1,826)
Trade and other payables and provisions	**(5,054)**	(1,218)	(3,954)	(3,836)
Retirement benefit obligations, net of deferred tax	**(1,312)**	(923)	(473)	(389)
Sainsbury's Bank liabilities[1]	**(4,595)**	(714)	(3,755)	(3,881)
Net assets	**6,494**	129	6,211	6,365

1 As at 31 August 2016, 31 August 2015 and 29 February 2016.

Key Financial ratios (with perpetual securities accounted for as equity)	**As at 24 September 2016**	As at 26 September 2015	As at 12 March 2016
Adjusted net debt to EBITDAR[1]	**4.0 times**	4.0 times	4.0 times
Interest cover[2]	**5.3 times**	6.0 times	5.9 times
Fixed charge cover[3]	**2.6 times**	2.7 times	2.7 times
Gearing[4]	**20.6%**	29.9%	28.7%
Gearing (excluding pension deficit)[5]	**17.2%**	27.8%	27.0%

Key Financial ratios (with perpetual securities treated as debt)[6]			
Adjusted net debt to EBITDAR	**4.3 times**	4.3 times	4.3 times
Gearing	**30.6%**	41.1%	39.5%
Gearing (excluding pension deficit)	**25.1%**	38.0%	37.1%

Key Financial ratios (with perpetual securities coupons excluded from net underlying finance costs)[7]			
Interest cover	**6.6 times**	6.4 times	6.7 times
Fixed charge cover	**2.7 times**	2.7 times	2.8 times

1 Net debt of £1,341 million plus capitalised lease obligations of £5,988 million (5.5 per cent discount rate), divided by Group underlying EBITDAR of £1,836 million, calculated for a 52 week period to 24 September 2016.
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 £1,835 million, and reduces net assets to £6,000 million.
7 Excluding the perpetual securities coupons, underlying net finance costs reduces to £52 million.

As at 24 September 2016, 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 during the half was mainly due to a reduction in market rental values and a small yield movement. The summary balance sheet discloses Sainsbury's Bank assets and liabilities separately to aid interpretation. A summary balance sheet is also presented with Sainsbury's Bank consolidated by line.

Summary balance sheet (Sainsbury's Bank consolidated)	**Group As at 24 September 2016 £m**	Group Movement since 12 March 2016 £m	Group As at 26 September 2015 £m	Group As at 12 March 2016 £m
Land and buildings (Freehold & long leasehold)	**7,156**	175	7,017	6,981
Land and buildings (Short leasehold)	**859**	39	799	820
Fixtures and fittings	**2,032**	69	1,938	1,963
Property, plant and equipment	**10,047**	283	9,754	9,764
Other non-current assets	**3,202**	454	2,548	2,748
Inventories	**1,909**	941	1,013	968
Trade and other receivables	**3,327**	1,076	2,290	2,251
Sainsbury's Bank cash and cash equivalents	**311**	(255)	644	566
Cash and cash equivalents	**874**	297	622	577
Debt	**(2,215)**	188	(2,479)	(2,403)
Net debt	**(1,341)**	485	(1,857)	(1,826)
Trade and other payables and provisions	**(9,649)**	(1,932)	(7,708)	(7,717)
Retirement benefit obligations, net of deferred tax	**(1,312)**	(923)	(473)	(389)
Net assets	**6,494**	129	6,211	6,365

Defined benefit pensions

As at 24 September 2016, the Group's post-tax pension deficit was £1,312 million which comprises the Sainsbury's pension scheme and the HRG pension scheme.

The Sainsbury's pension scheme post-tax pension deficit was £1,063 million, an increase of £674 million since the year-end (12 March 2016: £389 million). The increase in the deficit was mainly driven by a fall in the discount rate since the year-end from 3.65 per cent to 2.20 per cent.

As at 24 September 2016, the HRG pension scheme post-tax pension deficit was £249 million.

The Sainsbury's defined benefit pension scheme was subject to a triennial valuation at March 2015. This was carried out by Willis Towers Watson plc, the Scheme's independent actuary. 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. Sainsbury's made two cash payments in August 2015 and August 2016 of £125 million, and will increase overall committed contributions by £6 million per annum to £84 million (including property partnership payments) until March 2021. The next valuation date is effective from March 2018.

The HRG defined benefit pension scheme was subject to a triennial valuation as at 31 March 2015. This was carried out by Willis Towers Watson plc, the Scheme's independent actuary. 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. Since the valuation, the scheme has received £50 million in relation to the Homebase sale (£24 million of which was paid after the acquisition) and £50 million from Sainsbury's. Contributions have been agreed at £40 million per annum until October 2021. The next valuation date is effective from March 2018.

Retirement benefit obligations

	HRG As at 24 September 2016 £m	**Sainsbury's As at 24 September 2016 £m**	**Group As at 24 September 2016 £m**	Group As at 26 September 2015 £m	Group As at 12 March 2016 £m
Present value of funded obligations	**(1,479)**	**(9,826)**	**(11,305)**	(7,470)	(7,625)
Fair value of plan assets	**1,183**	**8,633**	**9,816**	6,971	7,235
Pension deficit	**(296)**	**(1,193)**	**(1,489)**	(499)	(390)
Present value of unfunded obligations	**(16)**	**(23)**	**(39)**	(16)	(18)
Retirement benefit obligations	**(312)**	**(1,216)**	**(1,528)**	(515)	(408)
Deferred income tax asset	**63**	**153**	**216**	42	19
Net retirement benefit obligations	**(249)**	**(1,063)**	**(1,312)**	(473)	(389)

Group income statement (unaudited)
for the 28 weeks to 24 September 2016

	Note	**28 weeks to 24 September 2016 £m**	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Revenue	5	**12,642**	12,419	23,506
Cost of sales		**(11,877)**	(11,662)	(22,050)
Gross profit		**765**	757	1,456
Administrative expenses		**(527)**	(428)	(850)
Other income		**219**	94	101
Operating profit		**457**	423	707
Finance income	6	**24**	9	19
Finance costs	6	**(73)**	(82)	(167)
Share of post-tax loss from joint ventures and associates		**(36)**	(11)	(11)
Profit before tax		**372**	339	548
Analysed as:				
Underlying profit before tax		**277**	308	587
Profit on disposal of properties	4	**113**	94	101
Investment property fair value movements	4	**(14)**	(14)	(18)
Non-underlying finance movements	4	**12**	(4)	(22)
IAS 19 pension financing charge and scheme expenses	4	**(10)**	(15)	(28)
Perpetual securities coupons	4	**13**	4	15
Acquisition adjustments	4	**1**	1	3
One-off items	4	**(20)**	(35)	(90)
		372	339	548
Income tax expense	7	**(73)**	(75)	(77)
Profit for the financial period		**299**	264	471

Earnings per share	8	**Pence per share**	Pence per share	Pence per share
Basic		**14.8**	13.6	23.9
Diluted		**13.7**	12.9	22.5
Underlying basic		**11.2**	12.0	24.2
Underlying diluted		**10.4**	11.4	22.8

The notes on pages 35 to 54 form an integral part of these Condensed Consolidated Interim Financial Statements.

Group statement of comprehensive income (unaudited)
for the 28 weeks to 24 September 2016

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Profit for the financial period	**299**	264	471
Items that will not be reclassified subsequently to the income statement:			
Remeasurement on defined benefit pension schemes	**(869)**	69	121
Current tax relating to items not reclassified	**27**	-	-
Deferred tax relating to items not reclassified	**118**	(10)	(36)
	(724)	59	85
Items that may be reclassified subsequently to the income statement:			
Currency translation differences	**2**	-	2
Available-for-sale financial assets fair value movements			
Attributable to Group	**3**	(1)	(1)
Items reclassified from available-for-sale assets reserve	**(1)**	-	-
Cash flow hedges effective portion of fair value movements			
Attributable to Group	**72**	(12)	4
Attributable to joint ventures and associates	**-**	-	1
Items reclassified from cash flow hedge reserve	**(29)**	4	7
Deferred tax relating to items that may be reclassified	**8**	-	3
	55	(9)	16
Total other comprehensive (expense)/income for the financial period (net of tax)	**(669)**	50	101
Total comprehensive (expense)/income for the financial period	**(370)**	314	572

The notes on pages 35 to 54 form an integral part of these Condensed Consolidated Interim Financial Statements.

Group balance sheet (unaudited)
at 24 September 2016

	Note	**24 September 2016 £m**	26 September 2015 £m	12 March 2016 £m
Non-current assets				
Property, plant and equipment		**10,047**	9,754	9,764
Intangible assets		**696**	344	329
Investments in joint ventures and associates		**284**	353	327
Available-for-sale financial assets	12	**389**	182	340
Other receivables		**68**	85	103
Amounts due from Financial Services customers		**1,768**	1,581	1,649
Derivative financial instruments	12	**17**	17	17
		13,269	12,316	12,529
Current assets				
Inventories		**1,909**	1,013	968
Trade and other receivables		**788**	600	508
Amounts due from Financial Services customers		**2,415**	1,690	1,695
Available-for-sale financial assets	12	**124**	-	48
Derivative financial instruments	12	**136**	45	51
Cash and bank balances	10b	**1,185**	1,266	1,143
		6,557	4,614	4,413
Non-current assets held for sale		**30**	38	31
		6,587	4,652	4,444
Total assets		**19,856**	16,968	16,973
Current liabilities				
Trade and other payables		**(4,251)**	(3,281)	(3,077)
Amounts due to Financial Services customers and other deposits		**(3,766)**	(3,256)	(3,173)
Borrowings		**(227)**	(177)	(223)
Derivative financial instruments	12	**(40)**	(46)	(43)
Taxes payable		**(90)**	(125)	(158)
Provisions		**(152)**	(42)	(46)
		(8,526)	(6,927)	(6,720)
Non-current liabilities held for sale		**-**	(4)	(4)
		(8,526)	(6,931)	(6,724)
Net current liabilities		**(1,939)**	(2,279)	(2,280)
Non-current liabilities				
Other payables		**(308)**	(248)	(269)
Amounts due to Financial Services customers and other deposits		**(633)**	(375)	(582)
Borrowings		**(2,113)**	(2,314)	(2,190)
Derivative financial instruments	12	**(48)**	(45)	(69)
Deferred income tax liability		**(82)**	(244)	(237)
Provisions		**(124)**	(85)	(129)
Retirement benefit obligations	13	**(1,528)**	(515)	(408)
		(4,836)	(3,826)	(3,884)
Net assets		**6,494**	6,211	6,365
Equity				
Called up share capital		**625**	550	550
Share premium account		**1,118**	1,114	1,114
Capital redemption reserve		**680**	680	680
Merger reserve		**568**	-	-
Other reserves		**205**	133	155
Retained earnings		**2,802**	3,239	3,370
Total equity before perpetual securities		**5,998**	5,716	5,869
Perpetual securities		**496**	495	496
Total equity		**6,494**	6,211	6,365

The notes on pages 35 to 54 form an integral part of these Condensed Consolidated Interim Financial Statements.

Group cash flow statement (unaudited)
for the 28 weeks to 24 September 2016

	Note	**28 weeks to 24 September 2016 £m**	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Cash flows from operating activities				
Cash generated from operations	10a	**846**	375	624
Interest paid		**(49)**	(65)	(108)
Corporation tax paid		**(51)**	(63)	(124)
Net cash generated from operating activities		**746**	247	392
Cash flows from investing activities				
Purchase of property, plant and equipment		**(307)**	(360)	(646)
Purchase of intangible assets		**(47)**	(30)	(34)
Proceeds from disposal of property, plant and equipment		**15**	68	109
Receipt of advance disposal proceeds		**-**	-	125
Acquisition of subsidiaries net of cash acquired		**101**	-	-
Capital return to Home Retail Group plc shareholders	3	**(226)**	-	-
Share issue costs on acquisition of Home Retail Group plc		**(3)**	-	-
Investment in joint ventures		**(16)**	(6)	(18)
Disposal of subsidiaries		**-**	-	(1)
Interest received		**9**	8	19
Dividends received		**23**	7	46
Net cash used in investing activities		**(451)**	(313)	(400)
Cash flows from financing activities				
Proceeds from issuance of ordinary shares		**3**	7	8
Drawdown of short-term borrowings		**448**	-	-
Repayment of short-term borrowings		**(448)**	(95)	(95)
Repayment of long-term borrowings		**(64)**	(176)	(238)
Proceeds from issue of perpetual capital securities		**-**	247	247
Proceeds from issue of perpetual convertible bonds		**-**	247	247
Purchase of own shares		**-**	-	(20)
Repayment of capital element of obligations under finance lease payments		**(17)**	(17)	(30)
Interest elements of obligations under finance lease payments		**(4)**	(5)	(9)
Dividends paid on ordinary shares		**(151)**	(157)	(234)
Dividends paid on perpetual securities		**(20)**	-	(4)
Net cash (used in)/generated from financing activities		**(253)**	51	(128)
Net increase/(decrease) in cash and cash equivalents		**42**	(15)	(136)
Net opening cash and cash equivalents		**1,140**	1,276	1,276
Closing cash and cash equivalents	10b	**1,182**	1,261	1,140

The notes on pages 35 to 54 form an integral part of these Condensed Consolidated Interim Financial Statements.

Group statement of changes in equity (unaudited)
for the 28 weeks to 24 September 2016

	Called up share capital £m	Share premium account £m	Capital redemption and other reserves £m	Merger reserve £m	Retained earnings £m	Total equity before perpetual securities £m	Perpetual securities £m	Total equity £m
At 12 March 2016	**550**	**1,114**	**835**	**-**	**3,370**	**5,869**	**496**	**6,365**
Profit for the period	**-**	**-**	**-**	**-**	**297**	**297**	**2**	**299**
Other comprehensive income/(expense)	**-**	**-**	**55**	**-**	**(724)**	**(669)**	**-**	**(669)**
Total comprehensive income/(expense) for the period ended 24 September 2016	**-**	**-**	**55**	**-**	**(427)**	**(372)**	**2**	**(370)**
Transactions with owners:								
Dividends paid	**-**	**-**	**-**	**-**	**(155)**	**(155)**	**-**	**(155)**
Acquisition of subsidiaries (note 3)	**75**	**-**	**-**	**568**	**(3)**	**640**	**-**	**640**
Distributions to holders of perpetual subordinated convertible bonds (net of tax)	**-**	**-**	**-**	**-**	**-**	**-**	**(2)**	**(2)**
Amortisation of convertible bond equity component	**-**	**-**	**(5)**	**-**	**5**	**-**	**-**	**-**
Share-based payment (net of tax)	**-**	**-**	**-**	**-**	**21**	**21**	**-**	**21**
Purchase of own shares[1]	**-**	**-**	**-**	**-**	**(9)**	**(9)**	**-**	**(9)**
Allotted in respect of share option schemes	**-**	**4**	**-**	**-**	**-**	**4**	**-**	**4**
At 24 September 2016	**625**	**1,118**	**885**	**568**	**2,802**	**5,998**	**496**	**6,494**

1 Purchase of own shares in the year of £9 million relate to Home Retail Group treasury shares that converted to 0.321 J Sainsbury plc shares as part of the acquisition on 2 September 2016.

	Called up share capital £m	Share premium account £m	Capital redemption and other reserves £m	Retained earnings £m	Total equity before perpetual securities £m	Perpetual securities £m	Total equity £m
At 15 March 2015	548	1,108	826	3,057	5,539	-	5,539
Profit for the period	-	-	-	262	262	2	264
Other comprehensive (expense)/income	-	-	(9)	59	50	-	50
Total comprehensive (expense)/ income for the period ended 26 September 2015	-	-	(9)	321	312	2	314
Transactions with owners:							
Dividends paid	-	-	-	(157)	(157)	-	(157)
Issue of perpetual subordinated capital securities and perpetual subordinated convertible bonds	-	-	-	-	-	495	495
Distributions to holders of perpetual subordinated convertible bonds (net of tax)	-	-	-	-	-	(2)	(2)
Amortisation of convertible bond equity component	-	-	(4)	4	-	-	-
Share-based payment (net of tax)	-	-	-	14	14	-	14
Purchase of own shares	-	-	-	-	-	-	-
Allotted in respect of share option schemes	2	6	-	-	8	-	8
At 26 September 2015	550	1,114	813	3,239	5,716	495	6,211

The notes on pages 35 to 54 form an integral part of these Condensed Consolidated Interim Financial Statements.

Group statement of changes in equity (continued) (unaudited)

	Called up share capital	Share premium account	Capital redemption and other reserves	Retained earnings	Total equity before perpetual securities	Perpetual securities	Total equity
	£m	£m	£m	£m	£m	£m	£m
At 15 March 2015	548	1,108	826	3,057	5,539	-	5,539
Profit for the year	-	-	-	452	452	19	471
Other comprehensive income			16	85	101	-	101
Total comprehensive income for the year ended 12 March 2016	-	-	16	537	553	19	572
Transactions with owners:							
Dividends paid	-	-	-	(234)	(234)	-	(234)
Issue of perpetual subordinated capital securities and perpetual subordinated convertible bonds (net of tax)	-	-	-	-	-	496	496
Distributions to holders of perpetual subordinated convertible bonds (net of tax)	-	-	-	-	-	(19)	(19)
Amortisation of convertible bond equity component	-	-	(7)	7	-	-	-
Share-based payment (net of tax)	-	-	-	23	23	-	23
Purchase of own shares	-	-	-	(20)	(20)	-	(20)
Allotted in respect of share option schemes	2	6	-	-	8	-	8
At 12 March 2016	550	1,114	835	3,370	5,869	496	6,365

The notes on pages 35 to 54 form an integral part of these Condensed Consolidated Interim Financial Statements.

Notes to the Condensed Consolidated Interim Financial Statements (unaudited)

1 General information

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 Condensed Consolidated Interim Financial Statements are unaudited but have been reviewed by the auditors whose report is set out on page 56. The financial information presented herein does not amount to statutory accounts within the meaning of Section 434 of the Companies Act 2006. The Annual Report and Financial Statements 2016 have been filed with the Registrar of Companies. The Independent Auditors' report on the Annual Report and Financial Statements 2016 was unqualified and did not contain a statement under Section 498 of the Companies Act 2006.

The financial period represents the 28 weeks to 24 September 2016 (comparative financial period 28 weeks to 26 September 2015; prior financial year 52 weeks to 12 March 2016). The financial information comprises the results of the Company and its subsidiaries (the 'Group') and the Group's interests in joint ventures and associates.

The Group's principal activities are food, clothing and general merchandise retailing and retail financial services.

2 Basis of preparation

The Interim Results, comprising the Condensed Consolidated Interim Financial Statements and the Interim Management Report, have been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority and with IAS 34 'Interim Financial Reporting' as adopted by the European Union.

The financial information contained in the Interim Results is presented in sterling, rounded to the nearest million (£m) unless otherwise stated.

The financial information contained in the Condensed Consolidated Interim Financial Statements should be read in conjunction with the Annual Report and Financial Statements 2016, which were prepared in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the European Union. 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 the annual report for the year ended on 12 March 2016 other than the adoption of the accounting standards set out below which have not had any impact on the interim financial statements. The prior year interim diluted and underlying diluted earnings per share has been amended (refer to note 8).

The preparation of interim financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates.

In preparing these Condensed Consolidated Interim Financial Statements, the significant judgements made by management in applying the group's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the Consolidated Financial Statements for the year ended 12 March 2016, with the exception of the following items:

- Taxes on income in the interim periods are accrued using the tax rate that would be applicable to expected total annual earnings, also taking into account the impact of "discrete items" in the interim period.
- As a result of the acquisition of Home Retail Group plc on 2 September 2016, significant estimation has been exercised in determining the fair value of the net assets acquired.

2 Basis of preparation (continued)

Sainsbury's Bank plc has been consolidated for six months to 31 August 2016 (26 September 2015: six months to 31 August 2015, 12 March 2016: twelve months to 29 February 2016). Adjustments have been made for the effects of significant transactions or events that occurred between this date and the Group's balance sheet date.

The Directors are satisfied that the Group has sufficient resources to continue in operation for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the 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.

- Amendments to IFRS 11, 'Joint arrangements' on accounting for acquisitions of interests in joint operations
- Amendments to IAS 16, 'Plant, property and equipment' and IAS 38, 'Intangible assets' on acceptable methods of depreciation and amortisation
- Amendments to IAS 27, 'Consolidated and separate financial statements' which allows entities to equity account for joint ventures and associates in their separate financial statements
- Annual improvements 2012 – 2014

3 Acquisition of Home Retail Group plc

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 acquisition date £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.	**447**
£3 million in relation to the contractual requirement to settle certain existing HRG share scheme awards and options	**3**
261 million new J Sainsbury plc shares of $28^{4}/_{7}$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.	**643**
Total	**1,093**

Home Retail Group's activities mainly comprise general merchandise related retailing. The acquisition is expected to accelerate Sainsbury's growth strategy in Clothing and General Merchandise retailing 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 £18 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.

3 Acquisition of Home Retail Group plc (continued)

The provisional assets and liabilities recognised as a result of the acquisition are as follows:

Fair value of net assets acquired as at 2 September 2016 (provisional)	**£m**
Fixed assets	**274**
Intangible assets	**326**
Inventories	**816**
Trade and other receivables	**141**
Deferred tax assets	**41**
Amounts due from Financial Services customers (the "loan book")	**615**
Other financial assets[1]	**60**
Cash and cash equivalents[2]	**548**
Total assets acquired	**2,821**
Trade and other payables[2]	**(1,203)**
Provisions	**(89)**
Defined benefit obligations	**(454)**
Total liabilities acquired	**(1,746)**
Net identifiable assets acquired at fair value	**1,075**
Goodwill arising on acquisition	**18**
Purchase consideration transferred	**1,093**

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 and are transferred to 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 £73 million.

(c) Amounts due from Financial Services customers (the "loan book")

The gross fair value of the loan book is £681 million against which a provision for impairment of £(66) million is held. This is inclusive of a fair value uplift of £20 million.

(d) Revenue and profit contribution

From the date of acquisition, Home Retail Group has contributed £235 million of revenue excluding VAT, £1 million of underlying profit before tax and a statutory loss before tax of £(5m) 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 £14,432 million, Group underlying profit before tax would have been £259 million and Group profit before tax would have been £279 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.

3 Acquisition of Home Retail Group plc (continued)

(e) Acquisition-related costs

Acquisition-related costs (included in administrative expenses and recognised outside of underlying profit) amount to £22 million in the current period (12 March 2016: £12 million) (see note 4). In addition £3 million of costs relating to the issuance of J Sainsbury plc shares have been recognised directly within equity.

(f) Cash impact of acquisition

	£m
Cash consideration	(447)
Cash acquired	548
Acquisition of subsidiaries, net of cash acquired (included in cash flow statement)	**101**
Capital return to shareholders of Home Retail Group plc (see below)	(226)
Net cash impact of acquisition	**(125)**

(g) 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.

4 Non-GAAP performance measures

Certain items recognised in reported profit or loss before tax can vary significantly from year to year and therefore create volatility in reported earnings which does not reflect the Group's underlying performance. Similarly, whilst defined benefit pension scheme expenses may not vary significantly, they no longer relate to the Group's ongoing activities given the closure of the defined benefit pension scheme to future accrual. The Directors believe that the 'underlying revenue', 'underlying profit before tax' ('UPBT') and 'underlying diluted and basic earnings per share' measures presented provide a clear and consistent presentation of the underlying performance of Sainsbury's ongoing business for shareholders. Underlying profit is not defined by IFRS and therefore may not be directly comparable with the 'adjusted' profit measures of other companies. The adjusted items are:

- Profit/loss on disposal of properties (included within other income);
- Investment property fair value movements - these reflect the difference between the fair value of an investment property at the reporting date and its carrying amount at the previous reporting date;
- Non-underlying finance movements – these are fair value gains and losses on non-derivative financial assets and liabilities carried at amortised cost, on derivatives relating to financing activities and on hedged items in fair value hedges, as well as the discount unwind on provisions relating to non-underlying items;
- The financing element of IAS 19 'Employee Benefits' and defined benefit scheme expenses;
- Coupons on 'perpetual securities' (perpetual subordinated capital securities and perpetual subordinated convertible bonds) – the coupons on the perpetual securities 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 (see note 12);
- Acquisition adjustments – these reflect the adjustments arising from the Sainsbury's Bank and Home Retail Group acquisitions, including the fair value unwind and amortisation of acquired intangibles; and
- One-off items – these are items which are material and infrequent in nature and do not relate to the Group's underlying performance (see tables below).

4 Non-GAAP performance measures (continued)

The adjustments made to reported profit before tax to arrive at underlying profit before tax are:

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Underlying profit before tax	**277**	308	587
Profit on disposal of properties[1]	**113**	94	101
Investment property fair value movements	**(14)**	(14)	(18)
Non-underlying finance movements[2]	**12**	(4)	(22)
IAS 19 pension financing charge and scheme expenses[3]	**(10)**	(15)	(28)
Perpetual securities coupons[4]	**13**	4	15
Acquisition adjustments	**1**	1	3
One-off items	**(20)**	(35)	(90)
Total adjustments	**95**	31	(39)
Profit before tax	**372**	339	548

1 Profit/(loss) on disposal of properties for the 28 weeks to 24 September 2016 comprised £116 million for the Group (26 September 2015: £94 million, 12 March 2016: £100 million) and £(3) million for the joint ventures (26 September 2015: £nil, 12 March 2016: £1 million).

2 Non-underlying finance movements for the 28 weeks to 24 September 2016 comprised £13 million for the Group (26 September 2015: £(3) million, 12 March 2016: £(20) million) and £(1) million for the joint ventures (26 September 2015: £(1) million, 12 March 2016: £(2) million).

3 Comprises pension financing charge for the 28 weeks to 24 September 2016 of £(8) million (26 September 2015: £(12) million, 12 March 2016: £(22) million) and defined benefit scheme expenses of £(2) million (26 September 2015: £(3) million, 12 March 2016: £(6) million).

4 The coupons on the 'perpetual securities' (perpetual subordinated capital securities and 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.

Acquisition adjustments

Acquisition adjustments of £1 million (26 September 2015: £1 million, 12 March 2016: £3 million) comprise the following:

	28 weeks to 24 September 2016 £m	**28 weeks to 26 September 2015 £m**	**52 weeks to 12 March 2016 £m**
Acquisition adjustments arising on purchase of HRG			
Cost of sales	**(2)**	-	-
Administrative expenses	**3**	-	-
Total Home Retail Group acquisition adjustments	**1**	-	-
Acquisition adjustments arising on purchase of Sainsbury's Bank			
Revenue	**3**	5	11
Cost of sales	**-**	1	2
Administrative expenses (intangible amortisation)	**(3)**	(5)	(10)
Total Sainsbury's Bank acquisition adjustments	**-**	1	3
Total acquisition adjustments	**1**	1	3

4 Non-GAAP performance measures (continued)

One-off items

One-off items of £(20) million (26 September 2015: £(35) million, 12 March 2016: £(90) million) comprise the following:

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Net gain/(transaction costs) on disposal of pharmacy business	**98**	-	(3)
Impairment and onerous contract (charge)/reversal	**(30)**	3	(1)
Sainsbury's Bank transition costs	**(16)**	(25)	(59)
Home Retail Group acquisition costs	**(22)**	-	(12)
Argos integration costs	**(6)**	-	-
Homebase separation and restructuring costs	**(2)**	-	-
Netto closure costs	**(23)**	-	-
Internal restructuring costs	**(19)**	(13)	(15)
	(20)	(35)	(90)

5 Segment reporting

The Group's businesses are organised into three operating segments:

- Retail (Food and Clothing & General Merchandise);
- Financial Services (Sainsbury's Bank and Argos Financial Services); and
- Property Investments (The British Land Company PLC joint venture and Land Securities Group PLC joint venture).

Management have 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. All material operations and assets are in the UK. The 28 weeks to 24 September 2016 includes 3 weeks of Home Retail Group results (from 2 September 2016) – the second half will contain a full 24 weeks.

Revenue from operating segments is measured on a basis consistent with the revenue number disclosure in the income statement. Revenue is generated by the sale of goods and services.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

The Operating Board assesses the performance of all segments on the basis of underlying profit before tax. The reconciliation provided below reconciles underlying operating profit from each of the segments disclosed to profit before tax.

5 Segment reporting (continued)

28 weeks to 24 September 2016	Retail £m	Financial Services £m	Property Investment £m	Group £m
Segment revenue				
Retail sales to external customers	**12,469**	**-**	**-**	**12,469**
Inter-segmental elimination[1]	**(3)**	**-**	**-**	**(3)**
Financial services sales to external customers	**-**	**173**	**-**	**173**
Underlying revenue	**12,466**	**173**	**-**	**12,639**
Acquisition adjustment fair value unwind[2]	**-**	**3**	**-**	**3**
Revenue	**12,466**	**176**	**-**	**12,642**
Underlying operating profit	**308**	**29**	**-**	**337**
Underlying finance income	**9**	**-**	**-**	**9**
Underlying finance costs[3]	**(74)**	**-**	**-**	**(74)**
Underlying share of post-tax (loss)/profit from joint ventures and associates	**(2)**	**-**	**7**	**5**
Underlying profit before tax	**241**	**29**	**7**	**277**
Non-underlying income				**95**
Profit before tax				**372**
Income tax expense				**(73)**
Profit for the financial period				**299**
Assets	**14,213**	**5,359**	**-**	**19,572**
Investment in joint ventures and associates	**6**	**-**	**278**	**284**
Segment assets	**14,219**	**5,359**	**278**	**19,856**
Segment liabilities	**(8,767)**	**(4,595)**	**-**	**(13,362)**

1 The inter-segmental elimination relates to commissions received from Financial Services, the other side of which is cost of sales in the Financial Services segment, not shown in the above
2 Represents fair value unwind on loans and advances to customers resulting from the Sainsbury's Bank acquisition.
3 The coupons on the perpetual securities 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 4.

28 weeks to 26 September 2015	Retail £m	Financial Services £m	Property Investment £m	Group £m
Segment revenue				
Retail sales to external customers	12,248	-	-	12,248
Financial services sales to external customers	-	166	-	166
Underlying revenue	12,248	166	-	12,414
Acquisition adjustment fair value unwind[1]	-	5	-	5
Revenue	12,248	171	-	12,419
Underlying operating profit	332	34	-	366
Underlying finance income	9	-	-	9
Underlying finance costs[2]	(71)	-	-	(71)
Underlying share of post-tax (loss)/profit from joint ventures and associates	(5)	-	9	4
Underlying profit before tax	265	34	9	308
Non-underlying income				31
Profit before tax				339
Income tax expense				(75)
Profit for the financial period				264
Assets	12,247	4,368	-	16,615
Investment in joint ventures and associates	11	-	342	353
Segment assets	12,258	4,368	342	16,968
Segment liabilities	(7,002)	(3,755)	-	(10,757)

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 4.

5 Segment reporting (continued)

52 weeks to 12 March 2016	Retail £m	Financial Services £m	Property Investments £m	Group £m
Segment revenue				
Retail sales to external customers	23,168	-	-	23,168
Financial services to external customers	-	327	-	327
Underlying revenue	23,168	327	-	23,495
Acquisition adjustment fair value unwind[1]	-	11	-	11
Revenue	23,168	338	-	23,506
Underlying operating profit	635	65	-	700
Underlying finance income	19	-	-	19
Underlying finance costs[2]	(140)	-	-	(140)
Underlying share of post-tax (loss)/profit from joint ventures and associates	(7)	-	15	8
Underlying profit before tax	507	65	15	587
Non-underlying expense				(39)
Profit before tax				548
Income tax expense				(77)
Profit for the financial year				471
Assets	12,115	4,531	-	16,646
Investment in joint ventures and associates	16	-	311	327
Segment assets	12,131	4,531	311	16,973
Segment liabilities	(6,727)	(3,881)	-	(10,608)

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 4.

6 Finance income and finance costs[1,2]

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Interest on bank deposits and other financial assets	**9**	9	19
Other finance income:			
Retail finance fair value movements[3]	**15**	-	-
Finance income	**24**	9	19
Borrowing costs:			
Secured borrowings	**(44)**	(47)	(88)
Unsecured borrowings	**(16)**	(16)	(30)
Obligations under finance leases	**(4)**	(5)	(9)
Provisions – amortisation of discount	**(3)**	(3)	(5)
	(67)	(71)	(132)
Other finance costs:			
Interest capitalised – qualifying assets	**4**	4	7
Retail finance fair value movements[3]	**-**	(3)	(20)
IAS 19 pension financing charge	**(8)**	(12)	(22)
Interest expense on Pharmacy sale advance proceeds	**(2)**	-	-
	(6)	(11)	(35)
Finance costs	**(73)**	(82)	(167)

1 Financial Services interest income is reported in revenue and interest expense reported in cost of sales, and therefore not included in this note.
2 The coupons on the perpetual securities (included within underlying profit – see note 4) are accounted for as dividends in accordance with IAS 32: 'Financial Instruments: Presentation' and hence are not a finance cost.
3 Retail finance fair value movements include fair value gains/(losses) on derivative financial instruments not designated in a hedging relationship of £15 million (26 September 2015: £(3) million, 12 March 2016: £(20) million).

7 Income tax expense

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Current tax expense	**61**	55	88
Deferred tax expense/(credit)	**12**	20	(11)
Total income tax expense in income statement	**73**	75	77
Underlying tax rate	**21.3%**	25.3%	20.8%
Effective tax rate	**19.6%**	22.1%	14.1%

	£m	£m	£m
Income tax expense on underlying profit	**59**	78	122
Income tax expense/(credit) on non-underlying items (including revaluation of non-underlying deferred tax balances)	**14**	(3)	(45)
Total income tax expense in income statement	**73**	75	77

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 has been substantively enacted in the interim period, 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.

8 Earnings per share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders of the parent by the weighted average number of ordinary shares in issue during the year, excluding those held by the Employee Share Ownership Plan trusts, 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 calculated by excluding the effect of any profit or loss on disposal of properties, investment property fair value movements, non-underlying finance movements, IAS 19 pension financing and defined benefit pension scheme expenses, acquisition adjustments and one-off items that are material and infrequent in nature. This alternative measure of earnings per share is presented to reflect the Group's underlying trading performance. All operations are continuing for the periods presented.

8 Earnings per share (continued)

	28 weeks to 24 September 2016 million	28 weeks to 26 September 2015 million	52 weeks to 12 March 2016 million
Weighted average number of ordinary shares in issue	**1,953.4**	1,920.0	1,920.8
Weighted average number of dilutive share options	**13.4**	15.2	14.6
Weighted average number of dilutive senior convertible bonds	**136.3**	130.0	131.4
Weighted average number of dilutive subordinated perpetual convertible bonds[1]	**74.3**	17.9	41.4
Total number of ordinary shares for calculating diluted earnings per share	**2,177.4**	2,083.1	2,108.2

	£m	£m	£m
Profit for the financial year (net of tax)	**299**	264	471
Less profit attributable to:			
Holders of perpetual capital securities	**(7)**	(1)	(8)
Holders of perpetual convertible bonds	**(3)**	(1)	(4)
Profit for the financial year attributable to ordinary shareholders of the parent[2]	**289**	262	459

	£m	£m	£m
Profit for the financial period attributable to ordinary shareholders of the parent	**289**	262	459
Add interest on senior convertible bonds (net of tax)	**6**	6	11
Add coupon on subordinated perpetual convertible bonds, net of tax	**3**	1	4
Diluted earnings for calculating diluted earnings per share	**298**	269	474

	£m	£m	£m
Profit from continuing operations attributable to ordinary shareholders of the parent	**289**	262	459
Adjustments for non-underlying items (note 4)	**(95)**	(31)	39
Tax (including revaluation of deferred tax balances) on non-underlying items	**14**	(3)	(45)
Add back coupons on perpetual securities (net of tax)[3]	**10**	2	12
Underlying profit after tax attributable to ordinary shareholders of the parent	**218**	230	465
Add interest on senior convertible bonds (net of tax)	**6**	6	11
Add coupon on subordinated perpetual convertible bonds (net of tax)	**3**	1	4
Diluted underlying profit after tax attributable to ordinary shareholders of the parent	**227**	237	480

	pence per share	pence per share	pence per share
Basic earnings	**14.8**	13.6	23.9
Diluted earnings	**13.7**	12.9	22.5
Underlying basic earnings	**11.2**	12.0	24.2
Underlying diluted earnings	**10.4**	11.4	22.8

1 The prior year interim weighted average number of dilutive subordinated perpetual convertible bonds has been amended. This has the effect of increasing both the diluted earnings per share and underlying diluted earnings per share by 0.3 pence per share. This is as a result of applying a more accurate weighted average calculation to the relevant shares.

2 Profit attributable to ordinary shareholders of the parent is calculated in accordance with IAS 33, 'Earnings per share'.

3 Underlying earnings per share calculation is based on underlying profit after tax attributable to ordinary shareholders. Therefore the coupons on the perpetual securities are added back.

9 Dividend on ordinary shares

	28 weeks to 24 September 2016	28 weeks to 26 September 2015	52 weeks to 12 March 2016
Amounts recognised as distributions to ordinary shareholders in the period:			
Dividend per share (pence)	**8.1**	8.2	12.2
Total dividend charge (£m)	**155**	157	234

Post the half-year, an interim dividend of 3.6 pence per share (26 September 2015: 4.0 pence per share) has been approved by the Board of Directors for the financial year ending 11 March 2017, resulting in a total interim dividend of £78 million (26 September 2015: £77 million). The interim dividend was approved by the Board on 8 November 2016 and as such has not been included as a liability at 24 September 2016.

10 Notes to the cash flow statement

(a) Reconciliation of operating profit to cash generated from operations

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Profit before tax	**372**	339	548
Net finance costs	**49**	73	148
Share of post-tax loss of joint ventures	**36**	11	11
Operating profit	**457**	423	707
Adjustments for:			
Depreciation expense	**310**	294	559
Amortisation expense	**17**	14	25
Non-cash acquisition adjustments[1]	**(2)**	(6)	(13)
Financial services impairment losses on loans and advances	**9**	5	15
Profit on disposal of properties	**(116)**	(94)	(100)
Net gain on disposal of Pharmacy business	**(98)**	-	-
Impairment/(release) of property, plant and equipment	**11**	(12)	(9)
Foreign exchange differences	**(17)**	5	24
Share-based payment expense	**21**	15	23
Retirement benefit obligations[2]	**(211)**	(137)	(201)
Operating cash flows before changes in working capital	**381**	507	1,030
Changes in working capital:			
(Increase)/decrease in inventories	**(127)**	(35)	12
Increase in investment securities	**(111)**	-	(202)
Increase in trade and other receivables	**(172)**	(97)	(25)
Increase in amounts due from financial services customers and other deposits	**(230)**	(258)	(318)
Increase/(decrease) in trade and other payables	**453**	283	(16)
Increase/(decrease) in amounts due to financial services customers and other deposits	**643**	(29)	95
Increase in provisions and other liabilities	**9**	4	48
Cash generated from operations	**846**	375	624

1 This excludes £3 million (26 September 2015: £5 million, 12 March 2016: £10 million) amortisation on acquired intangibles included within amortisation expense in this note.

2 The adjustment for retirement benefit obligations reflects the difference between the defined benefit pension scheme expenses of £2 million (26 September 2015: £2 million, 12 March 2016: £6 million) and the cash contributions of £(213) million made by the Group to the defined benefit scheme (26 September 2015: £(139) million, 12 March 2016: £(207) million).

10 Notes to the cash flow statement (continued)

(b) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise the following:

	24 September 2016 £m	26 September 2015 £m	12 March 2016 £m
Cash in hand and bank balances	**303**	674	374
Money market funds and deposits	**767**	352	480
Deposits at central banks	**115**	120	269
Treasury bills	**-**	120	20
Cash and bank balances	**1,185**	1,266	1,143
Bank overdrafts	**(3)**	(5)	(3)
Net cash and cash equivalents	**1,182**	1,261	1,140

11 Analysis of net debt[1,2]

	At 24 September 2016			At 26 September 2015		
	Retail	**Financial Services**	**Group**	Retail	Financial Services	Group
	£m	**£m**	**£m**	£m	£m	£m
Non-current assets						
Interest bearing available-for-sale financial assets	**38**	**-**	**38**	36	-	36
Available-for-sale investment securities	**-**	**192**	**192**	-	-	-
Derivative financial instruments	**12**	**5**	**17**	16	1	17
	50	**197**	**247**	52	1	53
Current assets						
Cash and cash equivalents	**874**	**311**	**1,185**	622	644	1,266
Interest bearing available-for-sale financial assets	**-**	**124**	**124**	-	-	-
Derivative financial instruments	**136**	**-**	**136**	45	-	45
	1,010	**435**	**1,445**	667	644	1,311
Current liabilities						
Bank overdrafts	**(3)**	**-**	**(3)**	(5)	-	(5)
Borrowings	**(190)**	**-**	**(190)**	(142)	-	(142)
Finance leases	**(34)**	**-**	**(34)**	(30)	-	(30)
Derivative financial instruments	**(36)**	**(4)**	**(40)**	(45)	(1)	(46)
	(263)	**(4)**	**(267)**	(222)	(1)	(223)
Non-current liabilities						
Borrowings	**(1,989)**	**-**	**(1,989)**	(2,156)	-	(2,156)
Finance leases	**(124)**	**-**	**(124)**	(158)	-	(158)
Derivative financial instruments	**(25)**	**(23)**	**(48)**	(40)	(5)	(45)
	(2,138)	**(23)**	**(2,161)**	(2,354)	(5)	(2,359)
Total net debt	**(1,341)**	**605**	**(736)**	(1,857)	639	(1,218)

1 The Group's definition of net debt excludes Financial Services' own net debt balances.
2 The perpetual securities are accounted for as equity in accordance with IAS 32 'Financial Instruments: Presentation' and therefore not included within net debt.

11 Analysis of net debt (continued)

	At 12 March 2016		
	Retail	Financial Services	Group
	£m	£m	£m
Non-current assets			
Interest bearing available-for-sale financial assets	35	-	35
Available-for-sale investment securities	-	156	156
Derivative financial instruments	13	4	17
	48	160	208
Current assets			
Cash and cash equivalents	577	566	1,143
Interest bearing available-for-sale financial assets	-	48	48
Derivative financial instruments	51	-	51
	628	614	1,242
Current liabilities			
Bank overdrafts	(3)	-	(3)
Borrowings	(182)	-	(182)
Finance leases	(38)	-	(38)
Derivative financial instruments	(41)	(2)	(43)
	(264)	(2)	(266)
Non-current liabilities			
Borrowings	(2,053)	-	(2,053)
Finance leases	(137)	-	(137)
Derivative financial instruments	(48)	(21)	(69)
	(2,238)	(21)	(2,259)
Total net debt	(1,826)	751	(1,075)

A reconciliation of opening to closing net debt is provided in the Financial Review on page 22.

Borrowings

On 16 May 2016, the Group extended the maturity on one tranche of its secured corporate £1,150 million syndicated revolving credit facility. The facility is structured on a dual tranche basis with a £500 million Facility (A) due May 2019 (extended from May 2018) and a £650 million Facility (B) due May 2020.

As at 24 September 2016, £nil had been drawn under the Facility (26 September 2015: £nil; 12 March 2016: £nil).

Sainsbury's Bank

As at 24 September 2016, Sainsbury's Bank had £15 million of Bank of England Indexed Long-Term Repo facility (ILTR), which was fully collateralised by a combination of £20 million Treasury Assets and Personal Loans (26 September 2015: £nil).

As at 24 September 2016, Sainsbury's Bank had pledged the rights to a pool of Bank-issued customer loans in exchange for £260 million of Treasury Bills (under the Bank of England Funding for Lending Scheme). These Treasury Bills can then be converted to cash as a source of future funding to the Bank.

12 Financial instruments

Carrying amount versus fair values

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 value 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.

12 Financial instruments (continued)

At 24 September 2016	Carrying amount £m	Fair value £m
Financial assets		
Amounts due from Sainsbury's Bank customers[1]	**4,183**	**4,166**
Financial liabilities[2]		
Loans due 2018[3]	**(732)**	**(770)**
Loans due 2031	**(780)**	**(927)**
Bank overdrafts	**(3)**	**(3)**
Revolving credit facility due 2019	**-**	**-**
Bank loans due 2016	**(44)**	**(44)**
Bank loans due 2019	**(200)**	**(200)**
Senior convertible bond due 2019	**(423)**	**(470)**
Finance lease obligations	**(158)**	**(158)**
Amounts due to Sainsbury's Bank customers	**(4,399)**	**(4,381)**

1 Includes £1,881 million accounted for as a fair value hedge.
2 The perpetual securities are accounted for as equity in accordance with IAS 32 'Financial instruments: Presentation' and therefore are not a financial liability.
3 Includes £183 million accounted for as a fair value hedge.

At 26 September 2015	Carrying amount £m	Fair value £m
Financial assets		
Amounts due from Sainsbury's Bank customers[1]	3,271	3,280
Financial liabilities[2]		
Loans due 2018[3]	(829)	(892)
Loans due 2031	(818)	(987)
Bank overdrafts	(5)	(5)
Revolving credit facility due 2018	-	-
Bank loans due 2016	(37)	(37)
Bank loans due 2019	(200)	(200)
Senior convertible bond due 2019	(414)	(450)
Finance lease obligations	(188)	(188)
Amounts due to Sainsbury's Bank customers	(3,631)	(3,631)

1 Includes £1,776 million accounted for as a fair value hedge.
2 The perpetual securities are accounted for as equity in accordance with IAS 32 'Financial instruments: Presentation' and therefore are not a financial liability.
3 Includes £211 million accounted for as a fair value hedge.

12 Financial instruments (continued)

At 12 March 2016	Carrying amount £m	Fair value £m
Financial assets		
Amounts due from Sainsbury's Bank customers[1]	3,344	3,337
Financial liabilities[2]		
Loans due 2018[3]	(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 Sainsbury's Bank customers and banks	(3,755)	(3,757)

1 Includes £2,705 million accounted for as a fair value hedge.
2 The perpetual securities are accounted for as equity in accordance with IAS 32 'Financial instruments: Presentation' and therefore are not a financial liability.
3 Includes £206 million accounted for as a fair value hedge.

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).

At 24 September 2016	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Available-for-sale financial assets[1]				
Interest bearing financial assets	**-**	**38**	**-**	**38**
Other financial assets	**12**	**-**	**145**	**157**
Investment securities	**316**	**-**	**-**	**316**
Financial assets				
Derivative financial assets	**-**	**153**	**-**	**153**
Financial liabilities				
Derivative financial liabilities	**-**	**(71)**	**(17)**	**(88)**

At 26 September 2015	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Available-for-sale financial assets[1]				
Interest bearing financial assets	-	36	-	36
Other financial assets	-	-	144	144
Financial assets at FVTPL				
Derivative financial assets	-	62	-	62
Financial liabilities at FVTPL				
Derivative financial liabilities	-	(73)	(18)	(91)

1 Available-for-sale financial assets also includes £2 million in relation to unlisted equity investments which are carried at cost as the fair value cannot be reliably measured and has been excluded from the fair value hierarchy table above.

12 Financial instruments (continued)

At 12 March 2016	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
Available-for-sale financial assets[1]				
Interest bearing financial assets	-	35	-	35
Other financial assets	-	-	146	146
Investment securities	203	-	1	204
Financial assets at FVTPL				
Derivative financial assets	-	68	-	68
Financial liabilities at FVTPL				
Derivative financial liabilities	-	(78)	(34)	(112)

1 Available-for-sale financial assets also includes £2 million in relation to unlisted equity investments which are carried at cost as the fair value cannot be reliably measured and has been excluded from the fair value hierarchy table above.

Reconciliation of Level 3 fair value measurements of financial assets:

Details of the determination of Level 3 fair value measurements are set out below:

28 weeks to 24 September 2016	**Available-for-sale financial assets £m**	**Derivative financial liabilities £m**	**Investment Securities £m**	**Total £m**
Opening balance	**146**	**(34)**	**1**	**113**
Included in finance income/(cost) in the income statement	**-**	**17**	**(1)**	**16**
Included in other comprehensive income	**(1)**	**-**	**-**	**(1)**
Total Level 3 financial assets and liabilities	**145**	**(17)**	**-**	**128**

28 weeks to 26 September 2015	Available-for-sale financial assets £m	Derivative financial liabilities £m	Total £m
Opening balance	145	(14)	131
Included in finance cost in the Group income statement	-	(4)	(4)
Included in other comprehensive income	(1)	-	(1)
Total Level 3 financial assets	144	(18)	126

52 weeks to 12 March 2016	Available-for-sale financial assets £m	Derivative financial liabilities £m	Investment Securities £m	Total £m
Opening balance	145	(14)	-	131
Included in finance cost in the Group income statement	-	(20)	-	(20)
Included in other comprehensive income	1	-	1	2
Total Level 3 financial assets and liabilities	146	(34)	1	113

12 Financial instruments (continued)

Available-for-sale other financial assets

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 0.6 per cent per annum (26 September 2015 0.8 per cent; 12 March 2016: 0.6 per cent) and a discount rate of nine per cent (26 September 2015 nine per cent; 12 March 2016: nine per cent). 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:

	24 September 2016		26 September 2015	
	Change in discount rate +/- 1.0%	**Change in growth rate +/- 1.0%**	Change in discount rate +/- 1.0%	Change in growth rate +/- 1.0%
	£m	**£m**	£m	£m
Available-for-sale assets	**(9)/9**	**14/(13)**	(10)/11	16/(15)

	12 March 2016	
	Change in discount rate +/- 1.0%	Change in growth rate +/- 1.0%
	£m	£m
Available-for-sale assets	(9)/10	15/(14)

Derivative financial liabilities – power purchase agreement

The Group has entered into several long-term fixed-price power purchase agreements with independent producers. Included within derivative financial instruments is a net liability of £(17) million relating to these agreements at 24 September 2016 (within derivative financial liabilities at 26 September 2015: £(18) million; at 12 March 2016: £(34) million). 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 back 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:

	24 September 2016		26 September 2015	
	Change in volume +/- 20.0%	**Change in electricity forward price +/- 20.0%**	Change in volume +/- 20.0%	Change in electricity forward price +/- 20.0%
	£m	**£m**	£m	£m
Derivative financial instruments	**(4)/4**	**7/(7)**	(4)/4	8/(8)

	12 March 2016	
	Change in volume +/- 20.0%	Change in electricity forward price +/- 20.0%
	£m	£m
Derivative financial instruments	(7)/7	13/(14)

13 Retirement benefit obligations

Retirement benefit obligations relate to a defined benefit scheme, 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 employees of Sainsbury's and Home Retail Group. The Sainsbury's Scheme was closed to new employees in 2002 and closed to future accrual in 2013. The Home Retail Group scheme was closed to new members and future accrual in 2013. The assets of both Schemes are held separately from the Group's assets.

The Sainsbury's defined benefit pension scheme was subject to a Trustee's triennial valuation at 14 March 2015. This was carried out by Willis Towers Watson, the Scheme's independent actuary. 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.

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, the Scheme's independent actuary. 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.

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.

The Consumer Price Index ('CPI') rather than the Retail Price Index ('RPI') has been used as the basis for inflationary increases to pensions in cases where this is permitted by the Schemes' rules.

The amounts recognised in the balance sheet, based on valuations performed by KPMG, are as follows:

	24 September 2016			26 September 2015	12 March 2016
	Total Group	**Home Retail Group[1]**	**Sainsbury's**		
	£m	**£m**	**£m**	£m	£m
Present value of funded obligations	**(11,305)**	**(1,479)**	**(9,826)**	(7,470)	(7,625)
Fair value of plan assets	**9,816**	**1,183**	**8,633**	6,971	7,235
	(1,489)	**(296)**	**(1,193)**	(499)	(390)
Present value of unfunded obligations	**(39)**	**(16)**	**(23)**	(16)	(18)
Retirement benefit obligations	**(1,528)**	**(312)**	**(1,216)**	(515)	(408)
Deferred income tax asset	**216**	**63**	**153**	42	19
Net retirement benefit obligations	**(1,312)**	**(249)**	**(1,063)**	(473)	(389)

1 Home Retail Group plc acquired on 2 September 2016 (refer to note 3)

The retirement benefit obligations and the associated deferred income tax balance are shown within different line items on the face of the balance sheet.

The principal actuarial assumptions used at the balance sheet date are as follows:

	24 September 2016	26 September 2015	12 March 2016
	%	%	%
Discount rate	**2.20**	3.80	3.65
Inflation rate - RPI	**2.95**	3.20	3.15
Inflation rate - CPI	**1.95**	2.20	2.15
Future pension increases	**1.80 – 2.85**	2.00 – 3.05	1.90 – 3.00

13 Retirement benefit obligations (continued)

The amounts recognised in the income statement in respect of the IAS 19 charges for the defined benefit schemes are as follows:

	24 September 2016 £m	26 September 2015 £m	12 March 2016 £m
Excluded from underlying profit before tax:			
Interest cost on pension scheme liabilities	**(150)**	(142)	(266)
Interest income on plan assets	**142**	130	244
IAS 19 pension financing charge (note 6)	**(8)**	(12)	(22)
Defined benefit pension scheme expenses	**(2)**	(3)	(6)
Total IAS 19 income statement expense (excluded from underlying profit before tax (note 4))	**(10)**	(15)	(28)

The movement in the Group's defined benefit obligations are as follows:

	£m
Pension deficit at 12 March 2016	**(408)**
Acquisition of Home Retail Group plc (note 3)	(454)
Remeasurement losses	(869)
Net interest cost	(8)
Pension scheme expenses	(2)
Contributions by employer	213
Pension deficit at 24 September 2016	**(1,528)**

Cash contributions

Cash contributions in the period include a £125 million special contribution to the Sainsbury's defined benefit scheme, a £24 million special contribution to the Home Retail Group defined benefit scheme in relation to the capital return (see note 3) and a £50 million special contribution paid to the Home Retail Group defined benefit scheme as a result of the acquisition.

Following agreement of the triennial valuations, the Group's committed contributions into the Sainsbury's defined benefit scheme (including distributions from the Sainsbury's Property Scottish Partnership) have increased by £6 million to £84 million per year until March 2021. The committed contributions into the Home Retail Group defined benefit scheme have been agreed at £40 million per annum until October 2021.

14 Capital expenditure and commitments[1]

In the financial period, there were additions to property, plant and equipment of £376 million (26 September 2015: £345 million) and additions to intangible assets of £41 million (26 September 2015: £37 million).

In the financial period, there were disposals of property, plant and equipment with a net book value of £20 million (26 September 2015: £25 million), disposals of assets held for sale with a net book value of £25 million (26 September 2015: £1 million) and disposals of intangible assets with a net book value of £nil (26 September 2015: £nil).

At 24 September 2016, capital commitments contracted, but not provided for by the Group, amounted to £181 million (26 September 2015: £195 million).

1 Property, plant and equipment and intangible assets acquired as part of the acquisition of Home Retail Group plc are excluded.

15 Related party transactions

The Group's related parties are its joint ventures as disclosed in its Annual Report and Financial Statements 2016.

Transactions with joint ventures and associates
For the 28 weeks to 24 September 2016, the Group entered into various transactions with joint ventures and associates as set out below:

	28 weeks to 24 September 2016 £m	28 weeks to 26 September 2015 £m	52 weeks to 12 March 2016 £m
Management services received	**-**	-	(1)
Management services provided	**3**	1	4
Revenue received from joint ventures	**16**	16	33
Dividend income received	**22**	7	46
Investment in joint ventures and associates	**(16)**	(6)	(18)
Rental expenses paid	**(28)**	(32)	(65)

Balances arising from transactions with joint ventures and associates

	24 September 2016 £m	26 September 2015 £m	12 March 2016 £m
Receivables			
Other receivables	**20**	29	28
Loans due from joint ventures	**3**	2	3
Payables			
Other payables	-	-	(1)
Loans due to joint ventures	**(5)**	(5)	(5)

16 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 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.

Principal risks and uncertainties

Risk is an inherent part of doing business. The J Sainsbury plc Board has overall responsibility for the management of the principal risks and internal control of the Company. The Board has identified the following principal potential risks to the successful operation of the business. These risks, along with the events in the financial markets and their potential impacts on the wider economy, remain those most likely to affect the Group in the second half of the year.

- Business continuity and major incidents response
- Business strategy and change
- Colleague engagement, retention and capability
- Data security
- Environment and sustainability
- Financial and treasury risk
- Health and safety – people and product
- Trading environment and competitive landscape

The Principal Risks and Uncertainties have been reviewed with consideration given to the acquisition of the Home Retail Group plc in September 2016. The above Principal Risks remain unchanged from those reported in the Group's Annual Report and Financial Statements 2016. For detail of these risks, please refer to pages 36 to 38 of the J Sainsbury plc Annual Report and Financial Statements 2016, a copy of which is available on the Group's corporate website www.j-sainsbury.co.uk.

Due to the acquisition of Home Retail Group plc, there is an additional risk that relates to the integration activities required. The combined Group's success will be dependent upon its ability to integrate the two businesses. There will be challenges associated with the integration and there is a risk that the synergies expected from the acquisition may not be fully achieved. Through the integration programme, the required activities to mitigate this risk are being taken.

The risk associated with the political and regulatory environment was reviewed following the result of the EU referendum and decision for the UK to leave the EU. The level of risk remains the same due to the ongoing political and economic uncertainty.

Statement of Directors' responsibilities

The Directors confirm that this set of Condensed Consolidated Interim Financial Statements has been prepared in accordance with IAS 34 'Interim Financial Reporting' as adopted by the European Union, and that the Interim Management Report herein includes a fair review of the information required by DTR 4.2.7R and DTR 4.2.8R.

The Directors of J Sainsbury plc are listed in the J Sainsbury plc Annual Report and Financial Statements 2016.

By order of the Board

Mike Coupe
Chief Executive
8 November 2016

Ed Barker
Interim Chief Financial Officer
8 November 2016

Independent review report to J Sainsbury plc

Introduction

We have been engaged by the Company to review the condensed set of financial statements in the interim financial report for the 28 weeks ended 24 September 2016 which comprises the Group income statement, Group statement of comprehensive income, the Group balance sheet, the Group cash flow statement, and the Group statement of changes in equity and the related explanatory notes. We have read the other information contained in the interim financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with guidance contained in International Standard on Review Engagements (UK and Ireland) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, for our work, for this report, or for the conclusions we have formed.

Directors' Responsibilities

The interim financial report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the interim financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 2, the annual financial statements of the group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this interim financial report has been prepared in accordance with International Accounting Standard 34, ‘Interim Financial Reporting’, as adopted by the European Union.

Our Responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the interim financial report based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the interim financial report for the 28 weeks ended 24 September 2016 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Ernst & Young LLP
London
8 November 2016

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 Sainsbury's. 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**
Underlying Group sales	Total sales less acquisition adjustment fair value unwind on Sainsbury's Bank.	*A reconciliation of this measure can be found in note 5 of the accounts.*
Like for like sales	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.	*A reconciliation of like-for-like sales is provided on page 14 of the Financial Review.*
Underlying profit before tax	Profit before tax from continuing operations before any profit or loss on the disposal of properties, investment property fair value movements, non-underlying finance movements, the financing element of IAS 19 and defined benefit pension scheme expenses, acquisition adjustments and one-off items that are material and infrequent in nature, but after the coupons on perpetual securities.	*A reconciliation of underlying profit before tax is provided in note 4 to the accounts.*
Retail underlying operating profit	Underlying earnings before interest, tax, Sainsbury's Bank operating profit and Sainsbury's underlying share of post-tax profit from JVs.	*A reconciliation of these measures can be found in note 5 of the accounts.*
Underlying basic earnings per share	Earnings per share using underlying profit as described above.	*A reconciliation of underlying earnings per share is included in note 8 to the accounts.*
Operating cash flow	Cash generated from operations after changes in working capital.	*A reconciliation is provided in note 10 to the accounts.*
Net debt	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 11 of the accounts.*
Gearing	Net debt divided by net assets.	*Net assets as per the Group balance sheet.*
EBITDAR and underlying EBITDAR	Earnings before interest, tax, depreciation, amortisation and rent. Underlying EBITDAR uses underlying earnings.	*A reconciliation is provided on page 14 of the Financial Review.*
Core retail capital expenditure	Capital expenditure excludes Sainsbury's Bank, Argos exceptional capital expenditure, proceeds from sale and leasebacks and capital relating to the acquisition of freehold and trading properties	*A calculation of this is provided in the financial review on page 24.*
Lease adjusted net debt / underlying EBITDAR	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 26.*
Retail operating cash flow	Retail cash generated from operations after changes in working capital	*A reconciliation of retail operating cash flow is provided on page 23 of the Financial Review.*
Return on capital employed	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 25 of the Financial Review.*