30 April 2018

J Sainsbury plc

Full Year Unaudited results for the 52 weeks to 10 March 2018
Delivering at pace across the Group

Proposed combination with Asda

Today, Sainsbury's has separately announced a proposed combination with Asda to create a dynamic new player in UK retail

Financial highlights

- Underlying profit before tax £589 million, a return to growth; H2 profit increase of 11 per cent
- Strong cash generation with free cash flow of £432 million, up £113 million in the year
- Net debt reduced by £113 million to £1,364 million. Targeting to reduce net debt by a further £100 million in 2018/19
- Delivery of £185 million cost savings in the year, bringing the total to £540 million over three years, exceeding our original £500 million three year target. We will deliver further cost savings of at least £500 million over the next three years to 2020/21, starting with £200 million in savings this year
- Underlying earnings per share decreased six per cent to 20.4 pence per share, primarily reflecting the impact of a full year's consolidation of the additional shares issued at the HRG acquisition
- In line with our policy of paying a dividend that is covered 2.0 times by underlying earnings, we propose to pay a final dividend of 7.1 pence per share, an increase of eight per cent, bringing our full year dividend to 10.2 pence per share. The dividend is also covered 2.0 times by free cash flow
- Sainsbury's Bank profits of £69 million; expected to reduce to around £30 million next year
- Profit expectation for 2018/19 is in line with current market consensus of £629 million[1]

Strategic highlights

- Good food performance: transactions growing ahead of the market and an improving margin trend
- Convenience and Groceries Online sales up nearly eight per cent and nearly seven per cent respectively
- In the biggest retail change programme we have ever undertaken, we are transforming the way we work in our stores. We propose to simplify our structures and our operations and invest in technology to be more efficient and to improve customer service
- General Merchandise and Clothing, including Argos, continue to outperform a challenging market[2]
- 191 Argos stores open in Sainsbury's supermarkets; resulting in around 280 by the end of 2018/19, ahead of our plan to open 250 by March 2019. We will also deliver £160 million EBITDA synergies by March 2019, six months ahead of plan
- Nectar acquisition supports our strategy of knowing our customers better than anyone else

	2017/18	2016/17	Variance
Business Performance			
Group sales (inc VAT)	£31,735m	£29,112m	9.0%
Group like-for-like sales (inc VAT, ex fuel)			1.3%
Underlying profit before tax	£589m	£581m	1.4%
Underlying basic earnings per share	20.4p	21.8p	(6.4)%
Proposed final dividend	7.1p	6.6p	7.6%
Proposed full year dividend	10.2p	10.2p	-
Net debt (including perpetual securities)	£1,858m	£1,971m	£113m
Net debt (excluding perpetual securities)	£1,364m	£1,477m	£113m
Return on capital employed	8.4%	8.8%	

[1] Analyst consensus is available on our corporate website www.j-sainsbury.co.uk
[2] General Merchandise grew ahead of the market (BRC non-food non-clothing market, consistently gaining share. Clothing grew ahead of the market (Kantar Worldpanel, 52 weeks ending 18 March 2018)

	2017/18	2016/17
Statutory Reporting		
Group revenue (ex VAT, inc fuel)	£28,456m	£26,224m
Items excluded from underlying results	£(180)m	£(78)m
Profit before tax	£409m	£503m
Basic earnings per share	13.3p	17.5p

Mike Coupe, Group Chief Executive of J Sainsbury plc, said: "We have accelerated the rate of change and innovation across the Group and more customers are choosing to shop with us than ever before as a result. I am pleased to announce an increase in underlying profits before tax to £589 million, driven by delivery of Argos synergies, efficiency savings across the Group and improving food margin trends.

"We are focused on making Sainsbury's a destination of choice. We are clearly differentiated by the quality of our food and we have recently invested a further £150 million to lower prices. General Merchandise and Clothing are both performing ahead of the market and, in response to great customer feedback and financial returns, we are opening Argos stores in our supermarkets faster than we originally planned. We will also deliver £160 million EBITDA synergies by March 2019, six months ahead of plan.

"Sainsbury's Bank profits grew as we fully consolidated Argos Financial Services during the year. Looking to the year ahead, we expect lending margins to remain under pressure in a competitive market. Combined with new accounting standards and interest payments on the external capital we raised in November, we expect Bank profits to reduce significantly next year. We have decided to limit capital injections in the Bank to £110 million in 2018/19. We will take a cautious approach to unsecured lending while maintaining focus on mortgage growth.

"Our acquisition of Nectar supports our strategy of knowing our customers better than anyone else and I was pleased to welcome our Nectar colleagues to the Group in February.

"We continue to find ways to simplify our business and reduce costs. We have exceeded our original three year £500 million target and delivered a total of £540 million in savings. In addition, we will deliver at least £500 million of cost savings over the next three years to 2020/21. Net debt has reduced by £113 million to £1,364 million and we are targeting to reduce net debt by a further £100 million in 2018/19. I am optimistic about the year ahead."

Change of Directorate

Now that David Tyler has been Chairman for more than eight years, a search process has begun, led by Dame Susan Rice and the Nomination Committee, to find his successor as Non-Executive Chairman.

Dividend

In line with our policy of paying a dividend that is covered 2.0 times by underlying earnings, we propose to pay a final dividend of 7.1 pence per share, an increase of eight per cent, bringing our full year dividend to 10.2 pence per share.

Outlook

The market remains competitive. However, we are well placed to navigate the external environment and we remain focused on delivering our strategy. Despite the reduction in profits at Sainsbury's Bank, we are comfortable with current market consensus for 2018/19 UPBT of £629 million.[1]

[1] Analyst consensus is available on our corporate website www.j-sainsbury.co.uk

Fourth Quarter Trading Statement data for the 9 weeks to 10 March 2018

Like-for-like sales growth (including Argos in the base)	2016/17		2017/18						
	Q3	Q4	Q1	Q2	H1	Q3	Q4	H2	FY
Like-for-like sales (excl. fuel)	1.0%	0.3%	2.3%	0.6%	1.6%	1.1%	0.9%	1.1%	1.3%
Like-for-like sales (inc. fuel)	2.2%	0.9%	1.6%	0.9%	1.3%	1.2%	1.8%	1.4%	1.4%

Total sales growth (including Argos in base)	2016/17		2017/18						
	Q3	Q4	Q1	Q2	H1	Q3	Q4	H2	FY
Grocery	0.3%	0.3%	3.0%	1.4%	2.3%	2.3%	2.1%	2.3%	2.3%
General Merchandise	3.7%	1.5%	1.0%	(1.6)%	(0.1)%	(1.4)%	(1.2)%	(1.4)%	(0.8)%
Clothing	9.4%	5.2%	7.2%	6.3%	6.8%	1.0%	0.4%	0.8%	3.8%
Total Retail (excl. fuel and excl. impact of sale of Pharmacy)	**1.6%**	**0.7%**	**2.7%**	**0.9%**	**1.9%**	**1.2%**	**1.3%**	**1.2%**	**1.6%**

Total sales growth	2016/17		2017/18						
	Q3	Q4	Q1	Q2	H1	Q3	Q4	H2	FY
Total Retail (excl. fuel and excl. impact of sale of Pharmacy)	**33.1%**	**20.7%**	**24.4%**	**17.0%**	**21.2%**	**1.2%**	**1.3%**	**1.2%**	**10.6%**
Total Retail (excl. fuel)	31.6%	18.9%	22.9%	16.0%	19.9%	1.2%	1.3%	1.2%	10.0%
Total Retail (inc. fuel and excl. impact of sale of Pharmacy)	29.8%	18.2%	20.1%	14.8%	17.8%	1.4%	2.3%	1.7%	9.4%
Total Retail (inc. fuel)	28.6%	16.7%	18.9%	14.0%	16.8%	1.4%	2.3%	1.7%	8.9%

Notes

A. All sales figures contained in this trading statement are stated including VAT and in accordance with IFRIC 13
B. The sale of our Pharmacy business to LloydsPharmacy completed on 31 August 2016. The impact of this disposal is excluded from like-for-like sales for a period of one year from this date
C. Full year total retail sales growth is higher than the statutory accounts by 0.1 per cent due to the re-phasing of 2016/17 post-acquisition Argos sales into pre-acquisition quarters on a comparable basis

Strategic report

We are delivering the strategy we set out in November 2014. The market is competitive and the way customers shop continues to evolve. Our strategy is based on five pillars: knowing our customers better than anyone else; great products and services at fair prices; being there for our customers whenever and wherever; colleagues making the difference and our values making us different. To deliver this strategy we have prioritised four key areas of our business where we can differentiate ourselves, grow and create value:

Four key priorities

1. Further enhance our differentiated food proposition

- We are committed to offering competitive prices and recently invested a further £150 million to lower the price of 930 essential items
- Our share of transactions increased, with more customers choosing to shop at Sainsbury's than ever before
- Convenience and Online remain strong drivers of growth, with sales up nearly eight per cent and nearly seven per cent respectively
- We continue to invest in the quality of our food. We have re-launched 128 food ranges this year, covering 60 per cent of food sales

- Our *Slow Cook* range offers customers restaurant quality food. Our share of this growing market has increased from four per cent to 17 per cent and we are now the market leader
- Our gourmet *Supper Club* ready meal range, which launched in February, is a great example of the innovation in high quality food that differentiates us. It is performing well and growing share
- We are focused on making our stores attractive retail destinations. Innovative and exclusive partnerships enhance our food offer and give customers more choice. These include Godiva chocolates which are available exclusively to Sainsbury's customers in 500 stores and Patisserie Valerie handmade cakes and pastries which are available in 44 stores, including Click & Collect
- We have 59 Sushi Gourmet and Sushi Daily counters and we continue to work with selected concession partners such as Explore Learning, Specsavers, Timpsons and Crussh fit food and juice bars to maximise the use of space in our stores
- Customers value saving time and having more control over how much they spend. Our Smart Shop 'scan as you shop' technology is now in 60 supermarkets
- Our Same Day Groceries Online delivery option is now available to 40 per cent of the UK population
- We are transforming the way we work in our stores. We propose to simplify our structures and our operations and invest in technology to be more efficient and to improve customer service
- Our Nectar acquisition gives us the flexibility to trial and adapt our customer loyalty offer
- Our colleagues continue to deliver market-leading customer service and product availability. We have won the Grocer Gold Awards for Service and Availability for the past five years

2. Grow General Merchandise and Clothing and deliver synergies

- General Merchandise sales declined 0.8 per cent, outperforming the market and gaining market share[1]
- Clothing grew sales by nearly four per cent, with online growth of 45 per cent and outperformed the market[2]. *Tu* clothing can now be ordered from the Argos website for home delivery or to collect from over 1,000 Argos stores and collection points across the UK
- Strong Argos performance in key categories of Audio, Mobile and Video Games
- Argos *Fast Track* is a key point of difference and our unique Hub and Spoke model enables us to deliver customer orders quickly and conveniently. Argos is the only retailer in the UK that can deliver to 90 per cent of postcodes within four hours. *Fast Track* home deliveries increased by 28 per cent and *Fast Track* in-store collections by 45 per cent in the year
- Digital sales continue to grow and 60 per cent of sales now start online. Of those, 70 per cent are from mobile devices
- 191 Argos stores open in Sainsbury's supermarkets; resulting in around 280 by the end of 2018/19, ahead of our plan to open 250 by March 2019. We will also deliver £160 million EBITDA synergies by March 2019, six months ahead of plan
- Customers can pick up their Argos and *Tu* clothing from 192 collection points in our supermarkets. 155 of these are in supermarkets where customers can also collect eBay and DPD parcels. We also have 37 collection points in Sainsbury's Local stores.

3. Diversify and grow Sainsbury's Bank

- Sainsbury's Bank delivered £69 million profit, up 11 per cent, primarily reflecting the full consolidation of Argos Financial Services. Good sales growth across the product range was offset by a reduction in margins in the competitive unsecured lending market and a modest increase in bad debt charges, as expected
- While we remain confident in the Bank's potential to generate growth and healthy returns in the medium term, we expect Sainsbury's Bank profits to reduce significantly in the short term. We believe the banking market will remain competitive, with unsecured lending margins further impacted by cheap funding from the Bank of England's Term Funding Scheme. This year we are taking a cautious approach to unsecured lending and focusing on growing our mortgage book and our commission products. Together with the impacts of new accounting standards driving an additional £11 million impairment as a result of IFRS 9 adoption and the interest relating to the external capital we raised in November 2017, we expect this to result in profit of around £30 million in 2018/19
- Sainsbury's Bank Mortgages, launched in April 2017, have performed well. We have eight new broker partners and lending in excess of £275 million
- We have 1.9 million active Bank customers, up eight per cent

[1] BRC non-food non-clothing market, 52 weeks to 10th March 2018
[2] Kantar Worldpanel, 52 weeks ending 18 March 2018

- Credit Cards performed strongly, with 40 per cent year-on-year growth in new card sales; the Argos Card saw a 12 per cent increase in sales
- Following the launch of the new banking platform, we grew savings by 41 per cent
- Our insurance broker panel model, introduced in February 2017, has been popular with customers. Car Insurance new policy sales grew by 42 per cent and Home Insurance sales grew by 39 per cent
- Travel Money grew 26 per cent, increasing market share

4. Continue cost savings and maintain balance sheet strength

- Responding to changing customer shopping habits we are making transformational changes to our in-store operating model, and reducing costs throughout our store estate
- We have achieved cost savings of £540 million over the past three years, exceeding our original target of £500 million. We will deliver at least a further £500 million of cost savings over the next three years to 2020/21
- We achieved £185 million of these cost savings in 2017/18 across a number of areas including logistics, energy efficiency, store operations, procurement and marketing
- We have well-developed plans in place to deliver at least £500 million of cost savings over the next three years with £200 million of these savings to be achieved in 2018/19 as we continue to drive efficiencies and simplify the business
- Our balance sheet remains strong. We have reduced net debt by £113 million to £1,364 million (excluding perpetual securities) and we are targeting to reduce net debt by a further £100 million in 2018/19
- We continue to maintain high levels of liquidity, with facilities of £4.1 billion, of which only £2.5 billion was drawn down at the year end. We refinanced our revolving credit facility in October 2017, increasing it to £1.5 billion and extending its maturity. The ratio of lease adjusted net debt to earnings before interest, tax, depreciation and rent (EBITDAR) has improved to 3.2 times from 3.7 times a year ago
- We achieved strong underlying cash generation, with free cash flow of £432 million in 2017/18 compared to £319 million in 2016/17

Our values

Our values are integral to how we do business and enable us to drive lasting positive change in communities across the UK and overseas.

- Living healthier lives: 33,350 schools and clubs took part in our Active Kids scheme in 2017/18
- Sourcing with integrity: Through Sainsbury's Dairy Development Group's ten year partnership with over 260 dairy farmers we have achieved higher milk yields, improved animal welfare, and a price guarantee
- Respect for our environment: We have reduced packaging by 35 per cent since 2005 and we are working with WRAP to make plastic packaging recyclable
- Making a positive difference in the community: We generated £35 million in 2017/18 for charities, communities and good causes
- Great place to work: We were awarded Disability Confident Leader status by the Department for Work and Pensions for our work on disability and inclusivity – the largest retailer in the UK to achieve this status

Notes

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.

A results presentation for analysts and investors will be held on 30 April 2018 at 9.30am.

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 783 0906 (or +44 (0)1296 480 100 if you are unable to use the primary number). The pass code for the event is 471 558. 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.

Sainsbury's will issue Audited Preliminary Results for the year ended 10 March 2018 on 2 May and the 2018/19 First Quarter Trading Statement will be issued at 07:00 (BST) on 4 July 2018.

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MARKET CONTEXT

The Market

Economic conditions became more challenging for UK consumers during the last year. The devaluation of Sterling and higher commodity prices fed through to food and non-food prices from the start of our financial year, with the consequence that wage growth fell behind inflation for the first time in over three years. Higher inflation benefited food retail market growth, but the impact on disposable income of higher inflation saw non-food retail sales growth weaken over the course of the year. Combined with the impacts of wage inflation, online channel shift and other structural pressures on traditional non-food retailers, this is accelerating the process of consolidation in the non-food market.

Shopping habits and retail trends

Shopping habits continue to evolve as the UK consumer expects far greater choice and flexibility in how, when and where they shop for food, general merchandise and clothing, accessing a variety of channels.

In line with our expectations, consumers continue to shop more frequently across different channels and store formats, with convenience stores and online both showing strong growth. Discount and bargain retailers continue to open significant numbers of new stores and gain market share. These trends continue to place pressure on volumes through the core supermarket format. However, we anticipate that supermarkets will remain an important channel for groceries.

Consumers continue to move their general merchandise and clothing purchases online, accessing a wide choice of delivery and pick-up options. Click & Collect accounts for a significant proportion of UK online general merchandise and clothing sales, as the speed and ease of options continue to expand. Traditional store formats, particularly on the high street, are seeing footfall and sales decline as online participation grows.

In the future, retailers will need to offer a consistent and seamless experience to consumers and be able to rapidly fulfil their orders in a location and at a time that is most convenient to them.

Sainsbury's response to a changing market place

Our strategy reflects the changing marketplace and our business is well set to continue adapting to these changes. A strategy of being there for our customers whenever and wherever they choose to shop with us, allows us to be flexible in adapting to these changing customer needs. We have accelerated the rate of change and innovation across the Group and we are focused on satisfying more customer missions. We remain competitive on price across food, clothing and general merchandise and are focused on providing great value across a wide range of products, making targeted investments to lower prices so that consumers can make choices to suit their budgets.

We are clearly differentiated by the quality of our food and we are adapting our supermarkets to serve a wider variety of shopping missions. This includes the opening of Argos stores within Sainsbury's supermarkets, along with other quality third party offers such as Sushi Gourmet, Sushi Daily and Explore Learning.

Our General Merchandise and Clothing business is performing ahead of the market and we are opening Argos stores in our supermarkets faster than we originally anticipated. Argos has a unique Hub and Spoke distribution model that enables fulfilment of customer orders for collection or home delivery quickly, conveniently and efficiently.

Our combination of a strong online proposition with a wide availability of delivery and pick-up options continues to be popular with consumers. Our convenience store estate is made up of over 800 stores and is outperforming the market as we continue to review the range we offer our customers to ensure it is reflective of their changing needs and shopping missions.

We have delivered £540 million of cost savings over the last three years and we have targeted at least another £500 million of cost savings for the business for the next three years. Together with targeted £160 million EBITDA (£142 million EBIT) synergies from the acquisition of Argos and a focus on maintaining balance sheet strength, we are confident that we have the resources to remain highly competitive and to trade well through tougher market conditions.

STRATEGIC REPORT

Further enhance our differentiated food offer

Food has been the core of our business since 1869 and our customers trust in the quality and value of our offer. More people are shopping with us than ever before and our share of customer transactions increased.

Our strategic focus is to help our customers to live well for less, putting quality first and investing in our ranges. This year we improved 128 food ranges, covering 60 per cent of our food sales.

We are particularly strong in ranges where we offer customers quality and convenience as well as great value, such as *Taste the Difference, Deliciously FreeFrom* and *On the Go*. The strong trend towards gourmet quality ready meals led us to launch our *Supper Club* range in February and our restaurant quality *Slow Cook* range has become the market leader since its launch two years ago. The growth of these new food innovations shows customers trust both our high quality standards and our commitment to using the best ingredients while offering low prices.

We are using space innovatively in our larger supermarkets by partnering, often exclusively, with premium brands such as Godiva Belgian chocolates, available in 500 stores, and Patisserie Valerie, whose gateaux and pastries are popular with customers. Customers can buy the cakes over the counter in 31 stores, or order ahead for collection in an additional 13 stores. We work with selected concession partners to maximise our use of space and help make Sainsbury's an attractive retail destination. We have 59 Sushi Gourmet and Sushi Daily counters, as well as two Crussh fresh food and juice bars. Across our supermarket estate we are improving the layouts of our stores so that customers can shop quickly and conveniently. We are taking a disciplined approach to investing in stores, focusing on areas which matter most to customers.

We have been reducing cost from our end-to-end supply chain, working collaboratively with our suppliers to buy better for less. This has enabled us to invest a further £150 million in the price of 930 essential items so customers can be confident that they are getting great prices as well as great quality.

We are proposing to change the way we operate in stores and online. Improved systems are making us faster and more efficient with a simpler store management structure that will empower colleagues and improve service.

Convenience and Groceries Online continue to be strong drivers of growth, with sales up nearly eight per cent and nearly seven per cent respectively. Around 70 per cent of sales through our Convenience channel have been improved by ranging and merchandising activity. Sales through Convenience stores stand at around £2.7 billion. Groceries Online now offers Same Day delivery to 40 per cent of the UK population out of 102 stores and our Chop Chop one hour delivery service operates from seven stores in central London. Online Grocery orders can also be collected from over 100 stores. A new picking system, handsets and software have driven a 15 per cent improvement in pick-rate and we are achieving delivery punctuality of 97 per cent. Our popular Groceries Online app now accounts for around 20 per cent of food orders.

Our acquisition of Nectar allows us to explore innovative new ways to reward customer loyalty and supports our strategy of knowing our customers better than anyone else. We were pleased to welcome our Nectar colleagues to the Group in February.

Our colleagues continue to deliver excellent customer service and we have won the Grocer Gold Awards for Service and Availability for the past five years. We are proposing to invest £100 million to award store colleagues a market-leading rate of pay of £9.20 from September 2018, along with revised terms and conditions which will ensure consistency and fairness in contracts. We recognise that a small minority of colleagues will be adversely impacted by these proposals and have committed to additional payments for a period of 18 months for all those affected.

Grow General Merchandise and Clothing and deliver synergies

General Merchandise sales, including Argos, declined by 0.8 per cent and outperformed a challenging market.[1] General Merchandise performed strongly in key areas such as Audio, Mobiles and Video Games. Offering high street style at supermarket prices has made *Tu* clothing very popular with our customers. Sales grew nearly four per cent, outperforming the market, and Clothing now contributes close to £1 billion of annual sales to the Group. Over eight million customers regularly buy the range, making us the sixth largest clothing retailer in the UK by volume. We are strongly positioned in womenswear and childrenswear, with opportunities for growth in menswear, which now accounts for 15 per cent of clothing sales and is our fastest growing clothing category. Sales of clothing online have increased by 45 per cent. We are now making the *Tu* ranges easily accessible to Argos customers through the Argos website, available for home delivery or collection from over 1,000 Argos and Sainsbury's stores across the UK.

In the 18 months since we acquired Argos we have been rapidly integrating our two businesses. Joint range planning has enabled us to rationalise our product offer and give customers better overall choice and value. We have opened 191 Argos stores in Sainsbury's supermarkets and we expect to open around 90 more in the next financial year, bringing the total to around 280, ahead of our original schedule to open 250 Argos stores by March 2019. We are seeing strong like-for-like sales, with an uplift in grocery sales in supermarkets that have an Argos store.

Customers can pick up their Argos and *Tu* clothing from 192 collection points in our supermarkets. 155 of these are in supermarkets where customers can also collect eBay and DPD parcels. We also have 37 collection points in Sainsbury's Local stores.

We will deliver £160m EBITDA synergies by March 2019, six months ahead of plan. A key part of our strategy is to make it quick and convenient for customers to shop with us whenever and wherever they want. The Argos website is the third most visited retail website in the UK and online sales continue to grow, with 60 per cent of Argos sales originating online, over 70 per cent of which are generated through mobile devices.

Fast Track is a key point of difference for us, enabling us to leverage our unique Hub and Spoke model to deliver Argos orders quickly and conveniently. Customers have the choice of same day or next day *Fast Track* delivery or collection and this year *Fast Track* delivery increased by 28 per cent and *Fast Track* collection by 45 per cent. In November, we opened regional fulfilment centres in Reading and Birmingham.

Diversify and grow Sainsbury's Bank

Sainsbury's Bank profits increased by 11 per cent to £69 million, primarily due to the full year consolidation impact of Argos Financial Services. Good sales growth across the product range was offset by a reduction in margins in a competitive unsecured lending market and a modest increase in bad debt charges, as expected.

We have over 1.9 million active customers, an increase of eight per cent year on year. Over 81 per cent of insurance customers and 75 per cent of banking customers have, or are linked to, a Nectar card.

Credit Cards performed strongly, with 40 per cent growth in new Sainsbury's Bank card sales. The Argos Card saw a 12 per cent increase in sales and can now be used in both Argos and Sainsbury's, providing greater choice and convenience for customers. We launched our new, enhanced personal loan platform and around 70 per cent of all new personal lending goes to active Nectar card holders. New Savings account growth is up 41 per cent this year with growth in deposits up 21 per cent, which includes 32 per cent growth in ISA and Fixed Term deposits.

Since introducing our insurance broker panel model in February 2017, new policy sales in Car Insurance increased by 42 per cent and Home Insurance grew by 39 per cent. By working with a broader base of underwriting partners and looking at our data we have been able to offer more quotes to more Sainsbury's customers and give better discounts.

Our ATM estate grew by over five per cent to over 1,820 and we introduced 36 ATMs in high footfall Argos stores. £1 of every £11 dispensed from a LINK ATM transaction is from Sainsbury's Bank.

[1] General Merchandise grew ahead of the market (BRC non-food non-clothing market, consistently gaining share. Clothing beat the market (Kantar worldpanel, 52 weeks ending 18 March 2018)

Travel Money grew 26 per cent in a competitive market. This year we opened a further nine Travel Money bureaux, taking the total to 241 across the estate. As well as an in store service in convenient locations across the UK, we also offer an online home delivery service.

We expect the banking market to remain competitive and will take a cautious approach to unsecured lending in favour of a greater focus on growing our commission products and mortgage book. Together with the impact of new accounting standards and the interest related to the external capital we raised in November 2017, this will impact Sainsbury's Bank profits in the short term, but we are confident that this is the right decision for the business and remain confident in the potential of the Bank to generate growth and healthy returns in the medium term.

Continue cost savings and maintain balance sheet strength

We have made fundamental changes to our operations to be more efficient and customer-focused. Technology and digital innovations are also helping us to improve systems across our business, increasing efficiency and improving productivity. Through these operational efficiencies, we have exceeded our three year cost saving target and saved £540 million. We delivered cost savings of £185 million in 2017/18, £40 million above our target. Over the next three years to 2020/21 we will deliver a minimum of £500 million of cost savings. We plan to deliver £200 million of these savings in 2018/19 by simplifying our store management structures and operations and creating efficiencies to improve service for our customers.

We continue to maintain a strong balance sheet. We have reduced net debt by £113 million to £1,364 million and we are targeting to reduce net debt by a further £100 million in 2018/19. The reduction is a result of continued strong cash generation from retail operations, further working capital improvements and the acquisition of Nectar. This was partly offset by capital expenditure, capital injections into Sainsbury's Bank, adverse movements on US dollar derivatives and continued dividend payments. Group core retail capital expenditure at £495 million was lower than last year even with the addition of a full year of Argos core retail capital expenditure. It remains significantly lower than the average capital expenditure in the previous five years of £793 million. Our pension deficit has reduced by £589 million from £850 million last year to £261 million at the year end.

In the medium term our increased focus on cash will deliver adjusted net debt to adjusted EBITDAR (treating perpetual securities as debt) of less than three times and fixed charge above three times.

The Group has financing facilities of £4.1 billion, of which only £2.5 billion was drawn down at year end. The Group refinanced its syndicated committed revolving credit facility. The revised facility of £1.45 billion has three, four and five year tranches, with an initial final maturity for the longer dated tranche of April 2023. The refinancing is expected to drive annual interest savings of approximately £20 million.

We expect net finance costs of around £100 million in 2018/19 following final repayment of the secured loan due in 2018.

Financial Review of the full year unaudited results for the 52 weeks to 10 March 2018

Dear Shareholder, 2017/18 has been another year of significant change, with continued progress in delivering our strategic priorities, strong cash generation, cost saving and synergy outperformance, the consolidation of a full year of Argos, the acquisition of Nectar, and the return to like-for-like sales growth, all delivered in the context of a rapidly changing and competitive retail environment.

Sainsbury's underlying Group sales (including VAT) were up 9.0 per cent to £31,735 million mainly as a result of the impact of consolidating a full year of Argos. On a 52-week rolling basis Sainsbury's market share (as measured by Kantar) declined 27 basis points, due to further price investment and the continuing new store expansion from discounters, whose combined market share increased by 132 basis points. By contrast the 'big four' declined by 96 basis points. Our General Merchandise sales continued to outperform the market with strong growth in many of our key categories, as we maintained market share (as measured by the British Retail Consortium 'BRC') despite challenging market conditions.

During the year, we worked hard to protect our customers from the impact of cost price inflation and rising commodity prices by continuing to partner with our suppliers in looking at ways to reduce our sourcing and end-to-end supply chain costs. Against this backdrop we were pleased to record an improving food margin trend whilst General Merchandise margin remains under pressure in challenging market conditions. In 2017/18, retail underlying EBITDAR margin increased 4 basis points to 7.44 per cent and retail underlying operating margin declined 18 basis points to 2.24 per cent primarily as a result of the consolidation of a full year of Argos' results. Underlying profit before tax ('UPBT') increased by 1.4 per cent to £589 million (2016/17: £581 million). Profit before tax of £409 million (2016/17: £503 million) was down 18.7 per cent as a result of a £180 million charge recognised outside underlying results. This charge includes the proposed changes to our store operations that we have announced this year, Argos integration costs and Sainsbury's Bank transition costs. Cost savings of £185 million were delivered during the year resulting in a cumulative three-year total of £540 million, £40 million ahead of the target we set in 2014/15. We have well developed plans to deliver a further three-year cost saving target of £500 million by 2020/21 as we continue to simplify the business and we expect to achieve savings of around £200 million in 2018/19.

Sainsbury's Bank profits increased by 11 per cent to £69 million, primarily due to a full-year consolidation of Argos Financial Services results. Good sales growth across the product range was offset by a reduction in margins in the competitive unsecured lending market and an increase in bad debt charges, as expected. Next year, we expect lending margins to remain under pressure. Accordingly, we have decided to take a more cautious approach to unsecured lending and will focus on growing our mortgage book and our commission products. Together with the impacts of new accounting standards and the cost of the external capital we raised in November 2017, we expect Bank profits to reduce to around £30 million in 2018/19.

The balance sheet remains strong with a further reduction in net debt. Net debt was £1,364 million as at 10 March 2018 (11 March 2017: £1,477 million), a decrease of £113 million in the year, mainly as a result of continuing strong cash generation from our retail operations and further working capital improvements, offset by pension payments, capital expenditure and dividends paid. The Group has facilities of £4.1 billion with only £2.5 billion drawn at the end of the year.

The discount rate applied to the Group's pension schemes has been increased this year to use a revised approach that we believe better reflects expected yields on high quality corporate bonds over the duration of the Group's pension schemes. In addition, future mortality assumptions have been updated from CMI 2015 projections at 2017 year end to CMI 2017 projections. These changes have contributed to the reduction in our Group pension scheme IAS 19 accounting deficit (net of deferred tax) to £261 million (2016/17: £850 million deficit) as at 10 March 2018.

Underlying basic earnings per share decreased 6.4 per cent to 20.4 pence (2016/17: 21.8 pence), reflecting the full-year impact of the additional shares issued as a result of the Home Retail Group, ('HRG') acquisition. Basic earnings per share decreased 24.0 per cent to 13.3 pence (2016/17: 17.5 pence), lower than the underlying earnings per share due to the £180 million charge recognised outside of underlying results.

The Board has recommended a final dividend of 7.1 pence (2016/17: 6.6 pence), resulting in an unchanged full-year dividend of 10.2 pence per share (2016/17: 10.2 pence per share).

Unaudited summary income statement	**52 weeks to 10 March 2018 £m**	52 weeks to 11 March 2017 £m	Change %

Underlying group sales (including VAT)	**31,735**	29,112	9.0
Underlying retail sales (including VAT)	**31,220**	28,705	8.8
Underlying group sales (excluding VAT)	**28,453**	26,231	8.5
Underlying retail sales (excluding VAT)	**27,938**	25,824	8.2
Underlying operating profit			
Retail	**625**	626	(0.2)
Financial services	**69**	62	11.3
Total underlying operating profit	**694**	688	0.9
Underlying net finance costs[1]	**(119)**	(119)	-
Underlying share of post-tax profit from JVs[2]	**14**	12	16.7
Underlying profit before tax	**589**	581	1.4
Items excluded from underlying results	**(180)**	(78)	130.8
Profit before tax	**409**	503	(18.7)
Income tax expense	**(100)**	(126)	20.6
Profit for the financial period	**309**	377	(18.0)
Underlying basic earnings per share	**20.4p**	21.8p	(6.4)
Basic earnings per share	**13.3p**	17.5p	(24.0)
Dividend per share	**10.2p**	10.2p	-

1 Net finance costs including perpetual securities coupons before non-underlying finance movements.
2 The underlying share of post-tax profit from joint ventures and associates ('JVs') is stated before investment property fair value movements, non-underlying finance movements and profit on disposal of properties.

Group sales

Underlying group sales (including VAT, including fuel) increased by 9.0 per cent year-on-year, mainly as a result of the impact of consolidating a full year of Argos (2016/17: 27 weeks). Underlying retail sales (including VAT, including fuel) increased by 8.8 per cent. Including Argos in the base, retail sales (including VAT, excluding fuel) increased by 1.6 per cent due to an improved like-for-like performance. Fuel sales grew 2.6 per cent, largely driven by retail price inflation.

Total sales performance by category inc. Argos in base	**52 weeks to** **10 March 2018**
Grocery (exc. Pharmacy)	2.3%
General Merchandise	(0.8)%
Clothing	3.8%
Retail (exc. fuel and impact of sale of Pharmacy business)	**1.6%**
Fuel sales	2.6%
Retail (inc. fuel, exc. impact of sale of Pharmacy business)	**1.7%**

Grocery sales grew by 2.3 per cent driven by inflationary pressure across all food categories. A challenging General Merchandise market resulted in a sales decline of 0.8 per cent year-on-year. However, Clothing continued to perform well with sales growth of nearly four per cent year-on-year. We are the sixth biggest clothing retailer by volume.

Convenience growth was nearly eight per cent and Groceries Online sales growth was nearly seven per cent driven by order and basket size growth, supporting our ambition of becoming a multi-product, multi-channel retailer. There was sales growth across all Sainsbury's channels – Supermarkets, Convenience and Groceries Online.

Total sales performance by channel	52 weeks to 10 March 2018	52 weeks to 11 March 2017
Supermarkets	0.5%	(1.8)%
Convenience	7.5%	6.5%
Groceries Online	6.8%	8.2%

Retail like-for-like sales, excluding fuel, increased by 1.3 per cent in the year (2016/17: flat) mainly as a result of continued inflation.

Retail like-for-like sales performance inc. Argos in base	**52 weeks to 10 March 2018**	**52 weeks to 11 March 2017**
Like-for-like sales (exc. fuel)	1.3%	0.0%
Like-for-like sales (inc. fuel)	1.4%	0.5%

On a 52-week rolling basis, Sainsbury's market share (as measured by Kantar for the 52 weeks to 25 February 2018) declined 27 basis points due to continued price investment and the continuing store expansion from the discounters whose combined market share increased by 132 basis points. By contrast the 'big four' combined market share declined by 96 basis points.

Space

In 2017/18, Sainsbury's opened three new supermarkets (2016/17: six new supermarkets). Convenience continued to grow, with 24 new stores opened in 2017/18, including two Euro Garages stores, and 15 stores closed (2016/17: 41 stores opened and eight stores closed). Net of replacements, closures and disposals, closing Sainsbury's space was 23,209,000 sq. ft. (11 March 2017: 23,397,000 sq. ft.).

As at 10 March 2018, Argos had 844 stores and 192 collection points. Habitat had 16 stores.

Store numbers and retailing space	As at 11 March 2017	New stores	Disposals / closures	Extensions / refurbishments / downsizes	**As at 10 March 2018**
Supermarkets	605	3	-	-	**608**
Supermarkets area '000 sq. ft.[1]	21,512	80	-	(296)	**21,296**
Convenience[2]	806	24	(15)	-	**815**
Convenience area '000 sq. ft.	1,885	59	(32)	1	**1,913**
JS total store numbers	1,411	27	(15)	-	**1,423**
Argos stores[3]	715	1	(77)	-	**639**
Argos stores in Sainsbury's[3]	39	152	-	-	**191**
Argos in Homebase	57	-	(43)	-	**14**
Temporary stores	2	-	(2)	-	**-**
Argos total store numbers	813	153	(122)	-	**844**
Argos collection points[4]	37	194	(39)	-	**192**
Habitat	8	8	-	-	**16**

1 The net 296,000 sq. ft. reduction in Sainsbury's supermarket space is driven by 336,000 sq. ft. now belonging to Argos stores in Sainsbury's offset by 40,000 sq.ft of other space initiatives.
2 Includes Euro Garages stores.
3 Two Argos store openings have been reclassified as Argos stores in Sainsbury's to reflect their utilisation of the Sainsbury's store portfolio.
4 2016/17 included one Habitat collection point.

In 2018/19, Sainsbury's expects to open two new supermarkets and around 15 new convenience stores.

In 2018/19, Sainsbury's expects to open around 90 Argos stores in supermarkets (of which around 50 are relocations) resulting in around 280 Argos stores in supermarkets.

In 2018/19, Sainsbury's expects to close the remaining Argos stores within Homebase.

Retail underlying operating profit
Retail underlying operating profit decreased by 0.2 per cent to £625 million (2016/17: £626 million), reflecting continued investment in the customer offer, cost inflation and the consolidation of the Argos first half operating loss, partly offset by cost savings of £185 million and cumulative EBITDA synergies of £87 million (EBIT of £82 million).

Retail underlying operating margin declined by 18 basis points year-on-year to 2.24 per cent (2016/17: 2.42 per cent), equivalent to a 17 basis point decline at constant fuel prices, as a result of the consolidation of Argos sales.

Retail underlying operating profit	**52 weeks to 10 March 2018**	52 weeks to 11 March 2017	Change	Change at constant fuel prices
Retail underlying operating profit (£m)[1]	**625**	626	(0.2)%	
Retail underlying operating margin (%)[2]	**2.24**	2.42	(18)bps	(17)bps
Retail underlying EBITDAR (£m)[3]	**2,078**	1,912	8.7%	
Retail underlying EBITDAR margin (%)[4]	**7.44**	7.40	4bps	8bps

1 Retail underlying earnings before interest, tax and Sainsbury's underlying share of post-tax profit from joint ventures.
2 Retail underlying operating profit divided by underlying retail sales excluding VAT.
3 Retail underlying operating profit before rent of £740 million and underlying depreciation and amortisation of £713 million.
4 Retail underlying EBITDAR divided by underlying retail sales excluding VAT.

In 2018/19, Sainsbury's expects cost inflation of around three per cent. We have well-developed plans to deliver at least £500 million of cost savings over the next three years with £200 million of these savings to be achieved in 2018/19 as we continue to drive efficiencies and simplify the business.

In 2018/19, Sainsbury's expects a depreciation and amortisation cost of around £700 million.

Our 2018/19 full-year underlying profit expectation for the combined Group remains in line with current market consensus (2018/19 UPBT consensus estimate of £629 million, as published on 5 March 2018 on www.j-sainsbury.co.uk/investors/analyst-consensus).

Acquisition of Nectar
On 1 February 2018, Sainsbury's acquired all Nectar businesses and related assets required for the full and independent operation of the Nectar Loyalty programme, including the remaining 50 per cent share of its joint venture with Aimia Inc., Insight 2 Communication LLP. The consideration of £39 million generated goodwill of £147 million. The transaction supports Sainsbury's strategy of knowing its customers better than anyone else.

Synergies arising from the acquisition of Argos
In 2017/18, Sainsbury's achieved £87 million of cumulative EBITDA synergies (£82 million EBIT), of which £80 million were incremental to the 2016/17 full year. As part of the transaction to acquire Home Retail Group ('HRG'), Sainsbury's initially announced that the Group expected to achieve a cumulative £160 million of EBITDA synergies (£142 million EBIT) by the end of the first half of 2019/20. Due to the acceleration of some of this activity, we later announced that we expect to deliver these in 2018/19 (six months early).

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

£m	FY 2016/17	FY 2017/18	FY 2018/19e	Total
EBITDA synergies (incremental year-on-year)	**7**	**80**	**73**	**160**
EBIT synergies (incremental year-on-year)	**6**	**76**	**60**	**142**
Exceptional costs	**(27)**	**(75)**	**(28)**	**(130)**
Exceptional capital expenditure	**(18)**	**(80)**	**(42)**	**(140)**

In 2018/19, we expect incremental EBITDA synergies of £73 million (£60 million EBIT), resulting in total EBITDA synergies of £160 million (£142 million EBIT) since acquisition (six months early). Argos integration costs are expected to be around £30 million; integration capital expenditure is expected to be around £40 million in 2018/19.

Homebase separation
HRG announced on 18 January 2016 that the sale of Homebase would give rise to £75 million of additional exceptional costs in relation to the transaction, separation and restructuring. Up to the date of the acquisition, HRG had incurred £30 million of these costs; a further £4 million was incurred to 11 March 2017 and £10 million in 2017/18.

It is currently anticipated that the total exceptional costs will now only be £45 million, a reduction of £30 million from the original estimate.

Sainsbury's Bank

Sainsbury's Bank results 12 months to 28 February	**2018**	2017	Change
Underlying revenue (£m)	**515**	407	27%
Interest payable (£m)	**(64)**	(60)	7%
Total income (£m)	**451**	347	30%
Underlying operating profit (£m)	**69**	62	11%
Cost:income ratio (%)	**70**	72	200bps
Active customers (m) – Bank	**1.92**	1.77	8%
Active customers (m) – AFS	**1.95**	1.84	6%
Net interest margin (%)[1]	**4.9**	4.4	50bps
Bad debt as a percentage of lending (%)[2]	**1.3**	0.8	(50)bps
CET 1 capital ratio (%)[3]	**14.1**	13.3	80bps
Customer lending (£m)[4]	**5,691**	4,599	24%

1 Net interest receivable divided by average interest-bearing assets. Excluding AFS, net interest margin was 3.6 per cent (2016/17: 3.9 per cent).
2 Bad debt expense divided by gross lending. Excluding AFS, bad debt as a percentage of lending was 0.9 per cent (2016/17: 0.6 per cent).
3 Common equity tier 1 capital divided by risk-weighted assets.
4 Amounts due from customers at the Balance Sheet date in respect of loans, mortgages, credit cards and store cards net of provisions.

Sainsbury's Bank total income increased by 30 per cent year-on-year to £451 million mainly as a result of the full-year consolidation impact of Argos Financial Services ('AFS'). The consolidation also contributed to the 11 per cent increase year-on-year in Sainsbury's Bank underlying operating profit to £69 million.

Sainsbury's Bank cost:income ratio has improved by 200 basis points driven by sales growth across all products partially offset by an increase in administrative expenses. The number of Sainsbury's Bank active customers increased by eight per cent year-on-year to 1.92 million (2016/17: 1.77 million).
Net interest margin increased by 50 basis points year-on-year to 4.9 per cent (2016/17: 4.4 per cent) reflecting the acquisition of AFS that operates a higher risk and return operating model. Excluding AFS, net interest margin was 3.6 per cent, a decrease of 30 basis points year-on-year reflecting the increasingly competitive unsecured lending market. The acquisition also contributed towards the adverse movement in bad debt levels as a percentage of lending to 1.3 per cent (2016/17: 0.8 per cent). Excluding AFS, bad debt as a percentage of lending was in line with expectations at 0.9 per cent.

The CET 1 capital ratio increased by 80 basis points year-on-year to 14.1 per cent (2016/17: 13.3 per cent), reflecting the additional funds contributed during the year from the Parent. Loan balances increased by 24 per cent to £5,691 million, mainly due to growth across personal loans, credit cards and mortgages.

In November 2017, Sainsbury's Bank further diversified its funding through the issue of £175 million of fixed rate reset callable subordinated Tier 2 notes.

We have decided to take a more cautious approach to unsecured lending next year and margins will reduce in a competitive market. Combined with new accounting standards and interest payments on the external capital we raised in November, we expect Sainsbury's Bank profits to reduce to around £30 million in 2018/19.

Capital injections into the Bank are expected to be £110 million in 2018/19 and are expected to average £100 million per year from 2019/20 onwards. This is to cover card and loan platforms, regulatory capital and growth in loan, card and mortgage balances.

Sainsbury's Bank transition costs are expected to be around £55 million and transition capital costs are expected to be around £5 million.

Underlying net finance costs

Underlying net finance costs remained flat year-on-year at £119 million (2016/17: £119 million), as the impact of loan refinancing costs was offset by lower average net debt.

Sainsbury's expects net finance costs of around £100 million in 2018/19 following final repayment of the secured loan due in 2018.

Items excluded from underlying results

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

Items excluded from underlying results	**52 weeks to 10 March 2018 £m**	52 weeks to 11 March 2017 £m
Property related	**12**	36
Argos integration and Homebase separation	**(85)**	(53)
Sainsbury's Bank transition	**(38)**	(60)
Impact of the acquisition of Nectar UK	**2**	-
Divestments	**-**	15
Restructuring costs	**(85)**	(33)
Other	**14**	17
Items excluded from underlying results	**(180)**	(78)

- Property-related items for the year comprise profit on disposal of properties and investment property fair value movements.
- Argos integration costs for the year of £75 million were part of the previously announced £130 million required over three years in order to achieve the EBITDA synergies of £160 million. Homebase separation and restructuring costs were £10 million.
- Sainsbury's Bank transition costs of £38 million (2016/17: £60 million) were part of the previously announced costs incurred in transitioning to a new, more flexible banking platform.
- Restructuring costs in the year of £85 million relate to changes to our store colleague structures and working practices.

Taxation

The income tax charge was £100 million (2016/17: £126 million), with an underlying tax rate of 24.1 per cent (2016/17: 23.2 per cent) and an effective tax rate of 24.4 per cent (2016/17: 25.0 per cent).

The underlying tax rate was higher year-on-year, despite the statutory corporation tax rate being lower than the prior year. However, in the prior year there was the benefit of a one per cent revaluation of underlying deferred tax balances, whereas there was no such revaluation in 2017/18. The effective tax rate in 2017/18 was increased by the tax impact of property disposals and some non-tax deductible exceptional costs. In 2017/18 there was no benefit of a revaluation of non-underlying deferred tax balances.

In 2018/19, 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 to 20.4 pence (2016/17: 21.8 pence) reflecting the full-year impact of the additional shares issued as a result of the HRG acquisition and a slightly higher underlying tax rate. Basic earnings per share decreased to 13.3 pence (2016/17: 17.5 pence), more than the fall in underlying basic earnings per share, mainly as a result of the £180 million charge for items excluded from underlying results (2016/17: £78 million charge).

Dividends
The Board has recommended a final dividend of 7.1 pence per share (2016/17: 6.6 pence). This will be paid on 13 July 2018 to shareholders on the Register of Members at the close of business on 8 June 2018, subject to approval by shareholders at the AGM. In line with the Group's policy to keep the dividend covered two times by underlying earnings, this will result in an unchanged full-year dividend of 10.2 pence (2016/17: 10.2 pence).

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

Net debt and retail cash flows
Group net debt includes the capital injections into 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 10 March 2018, net debt was £1,364 million (11 March 2017: £1,477 million), a decrease of £113 million.

Unaudited summary cash flow statement	Retail 52 weeks to 10 March 2018 £m	Retail 52 weeks to 11 March 2017 £m
Adjusted retail operating cash flow before changes in working capital[1]	**1,214**	1,179
Decrease in working capital	**196**	61
Cash generated from retail operations[2]	**1,410**	1,240
Retirement benefit obligations	**(151)**	(112)
Net interest paid	**(105)**	(108)
Corporation tax paid	**(72)**	(87)
Net cash generated from retail operating activities[3]	**1,082**	933
Cash capital expenditure before strategic capital expenditure[4]	**(542)**	(588)
Proceeds from disposal of property, plant and equipment	**54**	55
Bank capital injections	**(190)**	(130)
Dividends and distributions received from JVs net of capital injections	**28**	49
Retail free cash flow[5]	**432**	319
Dividends paid on ordinary shares	**(212)**	(230)
Exceptional pension contributions	**-**	(199)
Strategic capital expenditure	**(80)**	(92)
Acquisition of subsidiaries	**135**	457
Repayment of borrowings including finance leases	**(174)**	(211)
Other	**(2)**	6
Net increase in cash and cash equivalents	**99**	50
Decrease in borrowings including finance leases	**174**	211
Acquisition movements	**(15)**	39
Fair value, other non-cash and net interest movements	**(145)**	49
Movement in net debt	**113**	349
Opening net debt	**(1,477)**	(1,826)
Closing net debt	**(1,364)**	(1,477)
Closing net debt (inc. perpetual securities as debt)	**(1,858)**	(1,971)

1 Excludes working capital, pension contributions and exceptional pension contributions
2 Excludes pension contributions and exceptional pension contributions.
3 Excludes the exceptional pension contributions.
4 Excludes Argos integration capital expenditure.
5 Retail free cash flow restated to reflect capital injections made to Sainsbury's Bank and dividends and distributions received from joint ventures net of capital injections.

Adjusted operating cash flow before changes in working capital increased by £35 million year-on-year to £1,214 million (2016/17: £1,179 million) and working capital improved by £196 million. Capital expenditure before strategic capital expenditure was £542 million (2016/17: £588 million) driven by a reduction in Sainsbury's core retail capital expenditure partially offset by a full year's Argos core retail capital expenditure. Bank capital injections of £190 million were made in the year (2016/17: £130 million) together with retirement benefit obligation payments of £151 million (2016/17: £112 million).

Free cash flow increased by £113 million in the year to £432 million (2016/17: £319 million). Free cash flow was used to fund dividends and repay debt. Dividends of £212 million were paid in the year, which are covered 2.0 times by free cash flow (2016/17: 1.4 times). Strategic capital expenditure was £12 million favourable year-on-year as no freehold purchases were made in the current year (2016/17: £74 million purchase of Chiswick), partly offset by Argos integration capital expenditure.

Fair value, other non-cash and interest movements of £145 million were primarily driven by a reduction in the value of US Dollar foreign exchange derivatives held to mitigate the Group's exposure to fluctuations in US Dollar denominated purchases. The weighted average hedge rate ('WAHR') at 10 March 2018 was below the spot rate generating an unrealised fair value loss (2016/17: unrealised profit as the WAHR at 11 March 2017 was above the spot rate).

As at 10 March 2018, Sainsbury's had drawn debt facilities of £2.5 billion (including the perpetual securities) and undrawn committed credit facilities of £1.45 billion. The Group also held £85 million of uncommitted facilities, which was undrawn as at 10 March 2018.

On 17 October 2017 the Group refinanced its syndicated committed revolving credit facility. The revised facility of £1.45 billion has three, four and five-year tranches with an initial final maturity for the longer dated tranche of April 2023.

Sainsbury's expects 2018/19 year-end net debt to reduce by around £100 million. We expect net debt to reduce over the medium term.

Sainsbury's expects adjusted net debt to EBITDAR (treating the perpetual securities as debt) to reduce below three times in the medium term.

Sainsbury's expects fixed charge cover of over three times in the medium term.

Capital expenditure

Core retail capital expenditure was £495 million (2016/17: £547 million). Retail capital expenditure (including Argos integration capital expenditure) was £575 million (2016/17: £639 million).

In 2018/19, 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 £550 million. Core retail capital expenditure is expected to be around £550 million per annum over the medium term.

We expect Argos integration capital expenditure to be around £40 million.

Financial ratios

Key financial ratios	**As at 10 March 2018**	As at 11 March 2017

Return on capital employed (%)[1]	**8.4**	8.8
Return on capital employed (exc. pension deficit) (%)[1]	**7.7**	8.0
Adjusted net debt to EBITDAR[2]	**3.2 times**	3.7 times
Interest cover[3]	**5.9 times**	5.9 times
Fixed charge cover[4]	**2.5 times**	2.6 times
Gearing[5]	**18.4%**	21.5%
Gearing (exc. pension deficit) [6]	**17.8%**	19.1%

Key financial ratios (with perpetual securities treated as debt)[7]		
Adjusted net debt to EBITDAR	**3.5 times**	4.0 times
Gearing	**26.9%**	30.9%
Gearing (exc. pension deficit)	**25.9%**	27.3%

Key financial ratios (with perpetual securities coupons excluded from net underlying finance costs)		
Interest cover[8]	**7.4 times**	7.3 times
Fixed charge cover[9]	**2.6 times**	2.7 times

1 The 14 point period includes the opening capital employed as at 11 March 2017 and the closing capital employed for each of the 13 individual four-week periods to 10 March 2018.
2 Net debt of £1,364 million plus capitalised lease obligations of £5,683 million, divided by Group underlying EBITDAR of £2,181 million, calculated for a 52-week period to 10 March 2018. Perpetual securities treated as equity.
3 Underlying profit before interest and tax divided by underlying net finance costs, where interest on perpetual securities is included in underlying finance costs.
4 Group underlying EBITDAR divided by net rent and underlying net finance costs, where interest on perpetual securities is included in underlying finance costs.
5 Net debt divided by net assets. Perpetual securities treated as equity.
6 Net debt divided by net assets, excluding pension deficit. Perpetual securities treated as equity.
7 On a statutory basis, the perpetual securities are accounted for as equity on the Balance Sheet. Treating the perpetual securities, net of transaction fees, as debt increases net debt to £1,858 million, and reduces net assets to £6,917 million.
8 Underlying profit before interest and tax divided by underlying net finance costs, where interest on perpetual securities is excluded from underlying finance costs.
9 Group underlying EBITDAR divided by net rent and underlying net finance costs, where interest on perpetual securities is excluded from underlying finance costs.

Property value

As at 10 March 2018, Sainsbury's estimated market value of properties, including our 50 per cent share of properties held within property joint ventures, was £10.5 billion (11 March 2017: £10.3 billion). The £0.2 billion increase was a result of a small yield movement.

Defined benefit pensions

At 10 March 2018, the retirement benefit obligation for the Group was £261 million (including Argos, the unfunded obligation and adjusting for associated deferred tax). The £589 million decrease in the deficit from 11 March 2017 was driven by a rise in the discount rate from 2.70 per cent to 2.80 per cent, and updates to future mortality assumptions. The discount rate has been increased this year to use a revised approach that the Group believes better reflects expected yields on high quality corporate bonds over the duration of the Group's pension schemes. Mortality assumptions have been updated from CMI 2015 projections at the 2017 year end to CMI 2017 projections.

Following agreement of the valuation of both schemes, the Group is committed to make annual contributions of £124 million to the schemes (Sainsbury's scheme: £84 million; Argos scheme: £40 million). The next triennial valuations are for the March 2018 year-ends for both schemes and will need to be completed by June 2019.

Retirement benefit obligations	**Sainsbury's As at 10 March 2018 £m**	**Argos As at 10 March 2018 £m**	**Group As at 10 March 2018 £m**	Group As at 11 March 2017 £m
Present value of funded obligations	**(8,744)**	**(1,284)**	**(10,028)**	(10,854)
Fair value of plan assets	**8,669**	**1,215**	**9,884**	9,920
Additional liability due to minimum funding requirements (IFRIC 14)	**-**	**(78)**	**(78)**	-
Pension deficit	**(75)**	**(147)**	**(222)**	(934)
Present value of unfunded obligations	**(21)**	**(14)**	**(35)**	(40)
Retirement benefit obligations	**(96)**	**(161)**	**(257)**	(974)
Deferred income tax (liability)/asset	**(38)**	**34**	**(4)**	124
Net retirement benefit obligations	**(134)**	**(127)**	**(261)**	(850)